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June 20, 2018

Via Hand Delivery and Electronic Mail

Hon. Aida Camacho-Welch, Secretary
NJ Board of Public Utilities
44 South Clinton Ave.
3rd Floor, Suite 314
P.O. Box 350
Trenton, NJ 08625-0350

**RE: In the Matter of the Petition of Elizabethtown Gas Company for Authorization Through June 30, 2021; (i) to Make, Execute, and Issue a Term Loan Agreement to Provide Initial Financing for Elizabethtown Gas Company; (ii) to Make, Execute, and Issue a First Mortgage Indenture and Any Appropriate Supplemental Mortgage Indentures; and (iii) to Make, Execute, and Issue First Mortgage Bonds Or Other Evidences of Indebtedness
BPU Docket No. GF18050512**

Dear Secretary Camacho-Welch:

Please accept for filing an original and ten copies of these comments filed on behalf of the Division of Rate Counsel ("Rate Counsel") regarding the above-referenced matter.

Enclosed is one additional copy. Please date stamp the copy as "filed" and return it to the courier. Thank you for your consideration and attention to this matter.

I. BACKGROUND

A. Petition

On May 8, 2018, Elizabethtown Gas Company (“Elizabethtown”, “the Company” or “Petitioner”) filed a Petition (“Petition”) for authorization to: (a.) enter into a \$530 million term loan agreement (anticipated to be for a term of up to two years); (b.) establish a First Mortgage Indenture (and, if needed, supplemental indentures) to allow for the further insurance of First Mortgage Bonds; and (c.) issue of up to \$800 million in total long-term debt.¹ The requested authority would cover the time period from the issuance of a Board order in this docket until June 30, 2021, or a period of about three years.

On May 30, 2018, Petitioner filed an Amended Petition (“Amended Petition”) stating that the \$530 million term loan would be for a period of less than one year and therefore would be classified as short-term debt. This amendment reflects a revised financing plan for the proposed short-term term loan as described in Paragraphs 8 through 10 of the Amended Petition.

B. Proposed Acquisition

Elizabethtown Gas (“ETG”) is a division of Pivotal Utilities Holdings, Inc. (“Pivotal”) which provides natural gas utility service to approximately 288,000 customers in seven New Jersey Counties. Pivotal itself is a wholly-owned subsidiary of Southern Company Gas and ultimately a third-tier subsidiary of Southern Company. South Jersey Industries, Inc. (“SJI”) recently entered into an agreement with Southern Company to acquire substantially all of the assets of Elizabethtown Gas (the “Acquisition”).² In order to effectuate the Acquisition transaction, SJI established ETG Acquisition Corporation as a wholly-owned subsidiary.³ ETG Acquisition Corporation, in turn, would purchase ETG’s assets, free of debt. Under the terms of the Acquisition agreement, none of ETG’s current debt will be included in the transaction.⁴ At Closing, ETG Acquisition Corporation would change its name to Elizabethtown Gas Company.⁵ Absent the debt issue authority sought in the instant Petition, post-Closing Elizabethtown would have no debt, nor will it have any funds to use for working capital, capital investments, or to operate the utility.⁶ The \$530 million short-term term loan is part of a plan to finance the Acquisition along with other SJI sources of funding.

¹ The request for \$800 million long-term debt issuance authority is a ceiling amount inclusive of the \$530 million term loan and its expected refinancing within the one-year term.

² The Acquisition matter is presently pending before the Board. On December 21, 2017, SJI and other corporate entities filed Verified Joint Petition for approval of the Acquisition. In that docket, the financing plan for the Acquisition and the corporate restructuring arrangements for the proposed new entity are subject to review and approval by the Board. See I/M/O Acquisition of Elizabethtown Gas, BPU Dkt. No. GM17121309.

³ Amended Petition, p. 2.

⁴ Amended Petition, p. 2.

⁵ Amended Petition, p. 2. Elizabethtown will become a wholly owned subsidiary of SJI Utilities, Inc. a New Jersey corporation that SJI will form as part of the Acquisition.

⁶ Amended Petition, p. 3.

C. Financing Proposal

The Amended Petition provides some limited information on the requested \$800 million of financing authority. Elizabethtown proposes that the proceeds from the \$530 million short-term term loan will be used to fund part of the Acquisition. In turn, the \$530 million short-term term loan will be replaced by a like amount of long-term First Mortgage Bonds within six months of Acquisition closing (i.e., with that refinancing occurring by approximately the end of 2018).⁷ The remaining \$270 million of requested long-term debt could be in the form of First Mortgage Bonds or potentially other types of debt instruments.⁸ Some portion or all of this debt would be used to fund ongoing construction spending, redeem short-term debt and for other corporate purposes over the time period through June 2021.

The long-term debt will be for terms of one to up to forty years, with the exact timing of issuances not known at this time, depending on market conditions.⁹ The new long-term debt could be sold through either a public issuance or private placement.¹⁰ Elizabethtown anticipates that interest rates on the long-term debt will not exceed 10 percent but will provide advance notice to the Office of the Economist in the event that market conditions indicate an interest rate above 10 percent.¹¹ In Paragraph 23, page 6, of the Amended Petition, Elizabethtown provides a maximum yield spread table relative to U.S. Treasury securities, with a maximum yield spread for long-term debt with maturities in excess of 20 years of 485 basis points. Elizabethtown proposes to provide advance notice to the Office of the Economist if actual yield spread is expected to exceed the specified maximum listed in that table.¹²

II. RATE COUNSEL ANALYSIS

The instant Petition for debt issuance authority is both highly unusual and of critical importance to Elizabethtown's gas utility customers. This is a petition for a utility company that does not presently exist but will be established upon the Closing of the Acquisition. As noted above, at the present time, Elizabethtown Gas is a division of Pivotal Utilities Holding, Inc. The new corporate subsidiary, to be named Elizabethtown Gas Company, will be established at the Closing on the Acquisition by SJI of the present Elizabethtown assets. Upon Closing, the new utility will have no debt at all, since the pre-existing Elizabethtown debt would be extinguished as part of the Acquisition transaction. Typically, utilities issue large amounts of new debt gradually over time in order to refund their maturing debt and for capital expansion purposes, often replacing the temporary financing of capital spending by short-term debt. In this unusual case, the vast majority of the debt issue authority is for the purpose of financing the Acquisition

⁷ S-ETG-FIN-5.

⁸ S-ETG-FIN-2.

⁹ Amended Petition, p. 1.

¹⁰ Amended Petition, Paragraph 21, pp. 5-6.

¹¹ Amended Petition, Paragraph 22, p. 6

¹² Elizabethtown proposes to issue bonds within the confines of a Market Yield Spread Table and notify the Board's Office of the Economist if market conditions require a greater yield spread. Amended Petition, p. 6; S-ETG-FIN-3. Further, Elizabethtown anticipates that the interest rates borne by the bonds will not exceed 10 percent. *Id.* Elizabethtown will also notify the Board's Office of the Economist if market conditions require an interest rate greater than 10 percent. *Id.*

itself, with only about a quarter to a third (\$270 million) of the \$800 million total for capital expansion and other utility purposes over the next three years.

This Petition is also unusual as it is effectively a proposal for the complete recapitalization of Elizabethtown, with most of its debt to be issued at one time or within a very short amount of time. This complete recapitalization therefore creates "timing risk" concern for debt issuance. Instead of the utility's outstanding debt (and maturities) being spread out over a period of many years, as is typically the case, Elizabethtown's debt outstanding and, therefore, its embedded cost of debt largely will reflect market conditions at a single point in time. The cover letter to the Amended Petition presents steps that the Elizabethtown intends to take in order to mitigate that risk. Specifically, Elizabethtown will take a \$530 million draw on the short-term term loan at Closing, but it will move very quickly to refinance this short-term debt with long-term debt in the form of First Mortgage Bonds within six months of Closing. Moreover, Elizabethtown intends to lock in the interest rate on that new long-term debt within three months of Closing. As Elizabethtown expects such a Closing by July 2018, this means the Company's new embedded cost of debt could be determined as soon as sometime this autumn.

With some clarification, Rate Counsel is generally supportive of the Company's intended risk mitigation approach of expeditiously locking in its embedded cost of debt and recapitalization going forward. Utilities are presently encountering a gradually rising interest rate environment with the Federal Reserve pursuing a normalization of its monetary policy and recent announcements of its intention to gradually increase short-term interest rates. Long-term interest rates have also risen somewhat above their near historic lows from a year ago, but for credit worthy utilities (such as Elizabethtown and South Jersey Gas); long-term interest rates remain quite attractive. At the present time, 30-year Treasury rates remain around a very low 3.1 percent with long-term utility debt generally yielding about 4 to 4.5 percent. Thus, the Company can mitigate the market timing risk by moving ahead with its permanent debt financing as quickly as practicable while debt issuance conditions remain favorable. In that regard, it is important that the long-term debt issued be secured debt (as proposed by Elizabethtown) and that the new entity, Elizabethtown Gas Company, be adequately capitalized with equity capital, as well as debt, to establish and maintain strong credit ratings for the new long-term debt.

As a technical matter, the Petition reserves the right to issue long-term debt for terms ranging from 1 to 40 years. In order to mitigate the cost of capital risk, and given current market conditions, Rate Counsel recommends that the new secured long-term debt issued to refinance the short-term loan be for a term no less than 10 years and preferably for 30 years. This will help promote the long-term stability of the Company's embedded cost of debt to be used for ratemaking.

III. RECOMMENDATION

Rate Counsel does not object to Elizabethtown's request for authority to issue debt to finance the Acquisition, namely, the issuance of a total of up to \$800 million in long-term debt through June 30, 2021 and the establishment of a First Mortgage Bond Indenture (and if needed supplemental indentures), with \$530 million of the up to \$800 million be used for the prompt refinancing of the short-term term debt with First Mortgage Bonds. However, given the unique circumstances described above, such approval of this Petition must be expressly conditioned on the Board's approval of the underlying Acquisition transaction itself in BPU Docket No. GM17121309, including all conditions accompanying such Board approval, and the actual Closing of the Acquisition transaction. Rate Counsel further recommends that after Closing on the Acquisition and issuance of the short-term term loan the Company proceed as expeditiously as practicable to refinance the short-term term loan with secured long-term debt in order to prudently recapitalize Elizabethtown and protect its customers from potential instability in capital markets.

Rate Counsel further notes that the Elizabethtown has provided to the Office of the Economist a proposed order in this docket that lists 17 conditions of approval and/or reservations of rights in the form of ordering paragraphs. Rate Counsel recommends that 16 of those 17 ordering paragraphs be adopted as proposed, without modification, and included in any Board order approving the Petition. However, Rate Counsel recommends that the first of the Petitioner's 17 conditions be modified to also reference the proposed short-term term debt, to read as follows:

1. Petitioner will issue the short-term term loan debt and the various series of Bonds in compliance with this Order. No further Order of this Board shall be necessary for Petitioner to complete the series of Bond transactions or other issuances of indebtedness payable no more than 12 months from the dates thereof if the conditions of this order are met.

The recommended 17 conditions, including Rate Counsel's modified Paragraph 1, are appended hereto as Attachment A. With these 17 ordering paragraphs, along with Rate Counsel's recommendation that the approval of this Petition be expressly conditioned on Board approval of the underlying Acquisition itself (and all accompanying approval conditions) and prompt refinancing with secured debt of the short-term term debt, Rate Counsel believes that the interests of Elizabethtown Gas customers will be adequately protected.

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Notwithstanding these recommendations, Rate Counsel reserves its right to take appropriate positions regarding financing matters, cost of capital and the setting of rates in current and future proceedings that involve the Petitioner.

Respectfully submitted,

Stefanie A. Brand
DIRECTOR, DIVISION OF RATE COUNSEL

By: 
Felicia Thomas-Friel, Esq.
Deputy Rate Counsel

cc: Service List (via electronic and USPS regular mail)

ATTACHMENT A

1. Petitioner will issue the short-term term loan debt and the various series of Bonds in compliance with this Order. No further Order of this Board shall be necessary for Petitioner to complete the series of Bond transactions or other issuances of indebtedness payable no more than 12 months from the dates thereof if the conditions of this order are met.

2. With respect to each issue and sale of any Bonds which may be made through competitive bidding, and not registered under the Securities Act, Petitioner shall provide this Board with the following material for informational purposes, as soon as, and in no event later than 24 hours prior to the time for the receipt of bids (which materials may be provided by mail or by facsimile transmission and confirmed by mail): (a) a statement in respect of bidding for the Bonds which shall specify (i) the date and time for receipt of bids for the Bonds, (ii) the principal amount of the Bonds, (iii) the series designation of the Bonds, (iv) the minimum and maximum percentage of principal amount which may be specified in the bid as the purchase price for the Bonds, (v) the term of the Bonds, (vi) the terms and conditions, if any, upon which the Bonds may be redeemed, whether at the option of the Petitioner, pursuant to any sinking fund or improvement fund for the Bonds, or otherwise, and (vii) such other provisions as may be established by Petitioner with respect to the terms and conditions of the Bonds and the bidding thereof; and (b) an assessment of the then current financial markets applicable to the Bonds which shall include (i) data with respect to recent sales of comparable securities of other utilities, (ii) interest rate spreads between United State Treasury Bonds and utility securities comparable to the Bonds, (iii) the anticipated number of bidders for the Bonds, (iv) the anticipated range of the yield of the Bonds based upon current market conditions, and (v) such other information as Petitioner shall deem relevant to assess the expected sale of the Bonds and the reasonableness of the annual cost of money.

3. If competitive bidding procedures are utilized, and: (a) at least three independent bids for the purchase of Bonds are received, (b) Petitioner accepts the bid which produces the most advantageous financial terms to Petitioner and (c) the price to Petitioner in such bid is no less than 97% of principal amount and no more than 102% of principal amount, Petitioner may, without further Order of the Board, issue and sell the Bonds in accordance with the terms and conditions contained in such accepted bid. If (x) only one or two bids are received for the Bonds, or (y) Petitioner proposes to accept the bid which does not produce the most advantageous financial terms to the Petitioner or (z) the accepted bid provides for a price to the Petitioner of less than 97% of principal amount or more than 102% of principal amount, the proposed issuance and sale of the Bonds shall not be consummated until a further Order of the Board authorizing such issuance and sale has been entered.

4. If Bonds are sold pursuant to competitive bidding, Petitioner shall furnish the Board in writing as soon as practicable after accepting the bid for

Bonds, the names of all principal bidders together with the interest rate, the annual cost of money to Petitioner, the price to the public, if applicable, the percentage yield and the price to Petitioner applicable to each bid.

5. While it is anticipated that the interest rates to be borne by the Bonds will not exceed ten percent (10%), if market conditions require an interest rate greater than ten percent (10%), Petitioner will notify the Office of the Economist of the Board at least fourteen (14) days prior to the issuance of any Bonds if this falls within the Market Yield Spread Table approved by this Order. If the rate exceeds the approved range, Petitioner shall seek Board approval as described below.

6. Whether the Bonds are sold in an offering that is registered under the Securities Act, or sold on a competitively bid basis, Petitioner shall not issue Bonds at coupon rates in excess of those that would result from the Market Yield Spread Table set forth in this Order. In the event that market conditions change, Petitioner may file an updated Market Yield Spread Table for Board approval, before issuing Bonds with coupon rates that are not within the Market Yield Spread Table set forth herein.

7. Petitioner shall telephonically notify the Chief Economist prior to its issuance of Bonds, whether issued in an offering registered under the Securities Act or not, and will supply the following for informational purposes only: (a) principal amount or amounts of the Bonds proposed to be sold; (b) anticipated maturity ranges; (c) actual current yields of United States Treasury securities; (d) range of estimated coupon spreads over United States Treasury securities; (e) data, as available, with respect to recent sales of comparable Bonds of other utilities; and (f) such other information as Petitioner shall deem relevant to assess the reasonableness of the expected sale of the Bonds. Further, within seven (7) business days after the issuance and sale of any Bonds, Petitioner will provide the Chief Economist such information as was available at the time of sale upon which Petitioner based its decision to sell, such as market data with respect to utilities with similar credit ratings that have issued comparable securities.

8. Petitioner shall, as promptly as is practicable following the end of each month during which the Bonds are sold, file with the Board a statement which shall set forth the Bond transactions concluded during such month including the names of the agents and details of the transactions with the agents. Such statement shall also set forth (a) the principal amount, maturity date, redemption provisions, commissions and the interest rate spread over comparable United State Treasury securities for any Bonds sold and (b) the principal amount of the Bonds remaining authorized for issuance and sale in this Docket.

9. Petitioner shall furnish the Board with copies of each Note Indenture, similar indenture, and supplemental indenture, as executed.

10. Petitioner shall furnish this Board with copies of all final and complete documents as executed and filed with other regulatory agencies, including the SEC.

11. Petitioner shall semi-annually file with this Board, a statement setting forth: (a) the amount of Bonds issued pursuant to this order; and (b) details with respect to the disbursement of proceeds from such issuances.

12. This Order shall not be construed as a certification that the securities authorized to be offered for sale will be represented by tangible or intangible assets of commensurate value or investment costs.

13. This Order shall not effect nor in any way limit the exercise or authority of this Board, or of this State, in any future petition or in any proceeding with respect to rates, franchises, services, financing, capitalization, depreciation, or any other matters affecting the Petitioner.

14. This Order shall not be construed as directly or indirectly fixing, for any purpose whatsoever, any value of the tangible or intangible assets now owned or hereafter to be owned by Petitioner.

15. Petitioner should undertake financing in a manner that achieves the lowest reasonable cost of capital to customers.

16. Petitioner is obligated to use a prudent mix of capital to finance its utility operations and investments.

17. The authority granted in this Order shall become null and void and of no effect with respect to any portion thereof which is not exercised by June 30, 2021.

In the Matter of the Petition of
Elizabeth Gas Company for
Authorization Through June 30, 2021;
(1) to Make, Execute and Issue a Term
Loan Agreement to Provide Initial
Financing for Elizabethtown Gas
Company; (ii) to Make, Execute and
Issue a First Mortgage Indenture and
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