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April 28, 2023

<u>Via Electronic Mail</u>
Sherri L. Golden, Secretary
New Jersey Board of Public Utilities
44 South Clinton Avenue, 1st Floor
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Re: I/M/O the Petition of Elizabethtown Gas Company to Issue Long-Term Debt and Security Therefor and for Authority to Issue and Sell Short-Term Indebtedness, all Through December 31, 2025
BPU Docket No. GF23020063

Dear Secretary Golden:

Please accept for filing in the above-referenced matter the New Jersey Division of Rate Counsel's ("Rate Counsel") comments concerning Elizabethtown Gas Company's ("ETG" or "the Company") February 6, 2023 petition to the New Jersey Board of Public Utilities ("Board") requesting authorization to issue up to $1.4 billion of long-term debt and up to $300 million of short-term debt at any one time through December 31, 2025.

Consistent with the Order issued by the Board in connection with <u>In the Matter of the New Jersey Board of Public Utilities' Response to the COVID-19 Pandemic for a Temporary Waiver of the Requirements for Certain Non-Essential Obligations</u>, BPU Dkt. No. EO20030254, dated March 19, 2020, these comments are being electronically filed with the Secretary of the Board and with ETG. No paper copies will follow.

A. Background

ETG, a regulated public utility with local offices in Union, New Jersey, is engaged in the transmission, distribution, transportation, and sale of natural gas in Hunterdon, Mercer, Middlesex, Morris, Sussex, Union, and Warren counties, New Jersey. ETG serves approximately 300,000 customers.

On February 6, 2023, ETG filed a petition ("Petition") and supporting documents with the Board essentially requesting the following authorizations:

- To issue and sell in one or more series up to $1.4 billion of long-term debt securities.
- To redeem, refinance, or defease any or all of its outstanding long-term indebtedness as long as it is financially advantageous to do so; and
- To issue, renew or extend up to $300,000 million of short-term debt at any one time.[1]

ETG is a subsidiary of South Jersey Industries, Inc. ("SJI"). On February 1, 2023, NJ Boardwalk Holdings LLC ("Boardwalk") acquired SJI. As of December 31, 2022, ETG had 14 issues of outstanding long-term debt totaling $925 million.[2] Each outstanding long-term debt issue, however, contains a "change-in-control" redemption provision.[3] As a result of the Boardwalk acquisition, ETG anticipates that its current debt holders will redeem all outstanding long-term debt issues. Thus, the Company will utilize the net proceeds from the issuance of new long-term debt to retire short-term debt, including a bridge loan issued because of the change-in-control redemption of existing long-term

[1] Petition, pages 1-2.
[2] ETG response to RCR-A-8 and Attachment RCR-A-8.1.
[3] Id.

debt, to fund new capital expenditure requirements, to fund gas supply acquisitions, and for other general corporate purposes.[4]

By its Petition, ETG also requests authorization to issue up to $300 million of short-term debt at any one time. ETG requests Board authorization to accomplish the financings contemplated in the Petition at any time through December 31, 2025.[5]

B. <u>Rate Counsel Analysis</u>

Exhibit D(2) to ETG's Petition presents a table showing 14 issues of long-term debt that are currently outstanding totaling $925 million. Each issue contains a change-in-control redemption provision.[6] The interest rates on these issues range from 2.260% to 4.520%.[7] The maturity dates range from December 2028 to November 2060.[8]

ETG anticipates that change-in-control redemption provisions will be exercised on all of its outstanding long-term debt.[9] ETG believes there is a strong economic incentive for debt holders to exercise the change-in-control redemption provisions.[10] The Company states that its existing debt portfolio is well below its Fair Market Value and that its current weighted average interest coupon rate is approximately 1.7% lower than the current coupon rate for similar issuances.[11] Thus, it is in the bond holders' financial interest to exercise the change-in-control redemption provisions, according to ETG.

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[4] Petition, pages 2-3.
[5] Petition, page 15.
[6] ETG's response to RCR-A-8.
[7] <u>Id</u>.
[8] <u>Id</u>.
[9] ETG's response to RCR-A-9.
[10] ETG's response to RCR-A-11.
[11] <u>Id</u>.

In the instant Petition, ETG seeks the Board's authorization to issue and sell up to $1.4 billion aggregate principal amount of indebtedness with maturities of not less than twelve months. This financing cap is intended to provide $925 million to refinance debt subject to the change-in-control redemption provisions plus an additional $475 million to finance new capital expenditures planned for the years 2023 through 2025, at approximately $150 million per year.[12]

ETG's need for the requested financing authority seems almost self-evident. As of March 29, 2023, $830 million out of the $925 million issues outstanding with change-in-control redemption provisions have been tendered for redemption.[13] Thus, at least $830 million of new long-term debt will be necessary to simply replace the existing debt that will be redeemed. Additional new long-term debt beyond the $830 million also will be necessary to assist ETG in financing its 2023 – 2025 capital expenditures.[14]

As to ETG's creditworthiness, Standard and Poor's ("S&P") has rated ETG's senior securities A- since at least 2018.[15] On February 25, 2022, S&P renewed ETG's A- credit rating but also put the Company on a "negative watch" for potential downgrading due to the merger proceeding.[16] Thereafter, on February 10, 2023, S&P once again renewed ETG's A- credit rating but revised the negative watch to a "positive watch" for potential upgrading due to "strong insulating measures and ring-fencing commitments" contained in the Merger Agreement.[17]

[12] ETG's response to RCR-A-6 and Attachment RCR-A-6.1.
[13] ETG's response to RCR-A-29.
[14] ETG's response to RCR-A-17 and Attachment RCR-A-17.1 (Confidential).
[15] ETG's response to RCR-A-4.
[16] Id.
[17] Id.

ETG's financial results over the past few years have been adequate to service its debt requirements. For the years 2020 through 2022, ETG's interest coverage ratios have been 3.0, 2.8, and 2.5 respectively.[18] ETG's mortgage indenture contains certain financial covenants related to additional debt issuance. Specifically, the Company's net earnings ratio must not be less than two times the annual interest requirement.[19] ETG's 2022 net earnings ratio was 4.7 times; its pro forma ratio for 2023 is projected to be 3.4 times.[20] Both earnings ratios are well above the minimum 2.0 times requirement. Further, ETG's mortgage indenture requires that the debt to asset value ratio not exceed 70%.[21] ETG projects its debt to asset value ratio will be 64% following the projected refinancings.[22] Thus, barring any unforeseen financial deterioration, ETG should have the creditworthiness and the financial capability to meet its ongoing and future debt service obligations.

Long-term debt financing is an integral part of ETG's overall financing objective. In ETG's last base rate proceeding, BPU Docket No. GR211212544, the Board approved a capital structure for ETG consisting of 48% long-term debt and 52% common equity.[23] ETG's target capital structure, however, is 35% long-term debt and 65% common equity, excluding the goodwill adjustments.[24] As of December 31, 2022, ETG's capital structure was 39% long-term debt and 61% common equity, excluding the goodwill adjustments.[25]

[18] ETG's response to RCR-A-22 and Attachment RCR-A-22.1.
[19] ETG's response to RCR-A-21.
[20] Id.
[21] Id.
[22] Id.
[23] ETG's response to RCR-A-14.
[24] ETG's response to RCR-A-15. Rate Counsel notes that this target capital structure has not been approved, and will be subject to regulatory review in a future base rate or other appropriate proceeding.
[25] ETG's response to RCR-A-18 and Attachment RCR-A-18.1.

The additional long-term debt contemplated in the Petition should reduce the discrepancy between ETG's current capital structure and the one approved in ETG's last base rate proceeding.[26]

The refinancing of ETG's existing long-term debt comes with a significant price tag. The Company estimates that its annual interest expense will increase approximately $17.5 million, and its weighted cost of long-term debt will increase by 1.9% following the refinance.[27] The hold harmless provisions in the Merger Agreement, however, were designed to protect against ETG passing these cost increases onto its customers. Thus, a cost increase for ETG's customers is not a relevant consideration in this proceeding. The hold harmless considerations will be addressed in ETG's next base rate proceeding.

ETG's Petition also seeks the Board's authorization to issue short-term debt, i.e., debt with maturities of less than 365 days, not to exceed $300 million at any one time, through December 31, 2025. Presently, ETG, along with SJI and South Jersey Gas Company, is a party to a single, five-year revolving credit agreement under which ETG may make short-term loans not to exceed $300 million at any time.[28] However, because issuances of new short-term loans after the initial issuance of such loans may be deemed renewals or extensions, ETG seeks approval for such renewals or extensions.[29] In addition, ETG also intends to issue other short-term debt obligations prior to December 31, 2025.[30]

ETG relies on short-term debt, from time to time, for several corporate purposes including funding its working capital requirements, purchasing natural gas, paying for

[26] ETG's response to S-ETG-14.
[27] ETG's response to RCR-A-13.
[28] Petition, page 12.
[29] Id.
[30] Id.

state income and other taxes, and temporarily funding long-term debt including maturities.[31] While it is not uncommon for ETG to have in excess of $100 million of short-term debt outstanding, the Company's short-term borrowings never exceeded $180 million in the period January 2020 through February 2023.[32] The ability to issue short-term debt is an important element of ETG's overall financial strategy. Moreover, ETG is not seeking to increase its existing short-term debt limit.

C. <u>Rate Counsel Recommendation</u>

Rate Counsel has carefully reviewed the Petition and is not opposed to its approval. The Company is engaged in the transmission, distribution, transportation, and sale of natural gas to approximately 300,000 customers in its New Jersey service territory. The proposed financing is necessary and appropriate as part of the Company's overall strategy to provide safe, adequate, and reliable service to its New Jersey customers. Barring unforeseen and unanticipated circumstances, the proposed long-term and short-term debt issues should not jeopardize ETG's financial integrity. Moreover, the Company's 2023-2025 financing and capital structure objectives are consistent with the capital structure contained in ETG's most recent base rate proceeding in BPU Docket No. GR211212544. Based on ETG's recent financial performance, however, it appears that the Company has sufficient income to meet additional debt service interest requirements without jeopardizing its ability to provide safe, adequate, and reliable service to its New Jersey customers.

[31] Petition, pages 11-12.
[32] ETG's response to RCR-A-20 and Attachment RCR-A-20.1.

Even though Rate Counsel is generally supportive of the authorizations sought in the Petition, approval of the Petition should not include an authorization to include in rate base any specific assets that will be acquired as a result of this financing. Nor should the Board's authorization in this Petition be construed as acceptance for future ratemaking purposes of the resulting capital structure and capital costs. The determination of any assets to be included in rate base and the ratemaking impact of serving customers, including the impact of the transaction(s) on ETG's capital costs as well as the hold harmless provisions included in the Merger Agreement will be addressed in future base rate proceedings.

Rate Counsel recommends that a Board order approving the Company's Petition contain the following language:

1. With respect to each debt issuance, ETG shall provide the following material for information purposes as soon as it is available and in no event later than twenty-four (24) hours prior to the anticipated time for the pricing: (1) a statement with respect to the indicative pricing for the debt issuance and the terms thereof which shall specify (i) the anticipated date and timing for the pricing of the new issuance, (ii) the aggregate principal amount of the new issuance, (iii) the terms and conditions upon which the new issuance may be redeemed, whether at the option of ETG, pursuant to any mandatory provisions, or otherwise, and (iv) such other provisions as may be established by ETG with respect to the terms and conditions of the new issuance and the pricing therefore; (2) an assessment of the then current financial markets applicable to the issuance, including, (i) data with respect to recent sales of comparable securities of other utilities, if any, (ii) data with respect to current yields on certain outstanding long-term notes of ETG, (iii) anticipated compensation to and the names of the underwriters for the new issuance, (iv) the anticipated range of the yield of the new issuance based upon current market conditions, and (v) such other information ETG deems relevant to assess the expected new issuance and the reasonableness of the effective cost of money rate thereof.

2. If (1) the interest rate of any series of new issuance, in relation to U.S. Treasury securities, does not exceed the range set forth in the Petition, and (2)

the compensation to the underwriters with respect to any series does not exceed 1.0% of the aggregate principal amount of the new issuance, ETG may effect new issuance transactions without further Order of the Board. If either the interest rate or the compensation to the underwriters exceeds such amounts, the proposed issuance shall not be consummated until a further Order of the Board authorizing such new issuance transactions has been entered.

3. ETG shall, as promptly as is practical after acceptance of an offer for, and the pricing of, any new issuance, notify the Office of the Chief Economist and Rate Counsel in writing of the action to be taken and include a statement setting forth the compensation to and the names of the underwriters, and, as applicable, the aggregate principal amount of new issuance, the interest rate of the new issuance, and any other material provision with respect to the terms and conditions of the new issuance.

4. ETG shall furnish the Board with copies of executed documents filed with other regulatory agencies, if any, relating to the new issuance.

5. The new issuances authorized herein shall not be redeemed at a premium prior to maturity without further Board approval, unless the estimated present value savings derived from the difference between interest or dividend payments on a new issue of comparable securities and those securities refunded is on an after-tax basis greater than the estimated present value of all redemption, tendering and issuing costs, assuming an appropriate discount rate.

6. ETG shall furnish the Board with copies of all executed amendments and/or supplements, if any, of the ETG’s Mortgage and Deed of Trust, or any successor mortgage thereto.

7. ETG shall furnish the Board with copies of all final documents as executed and filed with other regulatory agencies, including the SEC, if any, relating to the new issuances.

8. The Board’s Order in this proceeding shall not be construed as certification that the securities authorized to be offered for sale will be represented by tangible or intangible assets of commensurate value or investment costs.

9. The Board’s Order in this proceeding shall not be construed as directly or indirectly fixing, for any purpose whatsoever, any value of any tangible or intangible assets now owned or hereafter to be owned by ETG.

10. The Board’s Order in this proceeding shall not affect nor in any way limit the exercise of the authority of the Board, Rate Counsel, or the State of New

Jersey, in any future ETG proceedings with respect to rates, franchise, service, financing (including method of sale of securities), accounting, capitalization or any other matters affecting the Petition.

11. The authority granted in the Board's Order in this proceeding shall become null and void and of no effect with respect to any portion thereof that is not exercised by December 31, 2025.

12. The Board's Order in this proceeding shall not constitute pre-approval of any cost or authorization for rate recovery. All capital costs are subject to review in ETG's next base rate proceeding.

These provisions will satisfy Rate Counsel's concern that the Board's approval is limited to the transactions as described herein, does not imply authorization to include any specific assets or amounts in rate base, does not imply authorization for any other ratemaking treatment, and does not establish any precedent with regard to approval of future financing petitions.

Respectfully Submitted,

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In the Matter of the Petition of
Elizabethtown Gas Company To Issue
Long-Term Debt and Security Therefor
and for Authority to Issue and Sell Short
Term Indebtedness, all Through
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