Palmetto Promise's Research Significantly Undervalues Santee Cooper

January 11, 2021

The Santee Cooper Ad Hoc Committee of the House has requested our review of inputs they received from the Palmetto Promise Institute and Clemson Economics Associates, and a piece jointly submitted by the South Carolina Small Business Chamber of Commerce and the Gullah Geechee Chamber of Commerce. This writing responds to the first two of these inputs – we will respond to the joint Chamber submission in a separate writing. Both the Santee Cooper enabling statute and Act 135 restrict certain activities by Santee Cooper related to a sale. We have and we will continue to operate within those restrictions and have consulted with outside legal counsel to ensure our response to the Committee's direct request is not violative thereof.

Palmetto Promise Institute has published false and misleading information regarding Santee Cooper including a number of significant, fundamental errors that, if left unchallenged, will lead to misunderstanding and undervaluation of this important state asset. It is critically important that decisions about Santee Cooper, whatever they may be, are made using true and accurate information, and thus we provide the following.

Santee Cooper's rates are the lowest of the majors, not the highest in South Carolina.

In earlier writings, PPI stated that Santee Cooper's rates were "the highest in the state," but clearly they erred because they compared the rates of Santee Electric Cooperative to the state average, not Santee Cooper. They now recognize this error and indicate it was a result of simply "transposing two rates," and have corrected the error "….in journalistic best practice….", but the damage has been done. This is inexcusably faulty work, and both false and misleading.

The only valid way to compare residential rates between utilities is to use the "average residential customer" (defined in South Carolina and confirmed by the Office of Regulatory Staff as using 1000 kilowatt hours a month of energy), and compute the bills they would receive, averaged over a year, on the standard residential rate plans of the utilities being compared. In this instance the utilities being compared would be the Dukes, Dominion, and Santee Cooper. Total bills are the basis of this comparison, as that is the only thing meaningful to the customer – the total amount that comes out of their pockets. Using this approach, and 2020 rate levels, the results are Dominion $122.98, Duke Progress $122.59, Duke Carolinas $120.54, and Santee Cooper $110.78. Santee Cooper is clearly the lowest.

PPI attaches as Appendix B a residential rate comparison used by ORS in the Dominion rate case. This document does not accurately compare rates of Santee Cooper to those of Dominion, Duke Progress and Duke Energy Carolinas. Electric rates have a base component and adjustable components. The ORS document only uses customer charges and base rates for Santee Cooper and ignores the impacts of our fuel adjustment, demand sales adjustment and economic development sales adjustment, all of which lower our annual energy charge significantly (to $110.78 in 2020 for a 1,000 kwh/month residential customer). Footnote 3 on the Appendix only states that the fuel adjustment clause and the demand sales adjustment were excluded, but the economic development sales adjustment is missing as well (EDR is a small amount, but still should have been included or footnoted).

By contrast, the ORS document used projected adjustments, including fuel, to the current rates of Dominion and the Dukes, once again providing an apples to oranges analysis that does not favor Santee Cooper.

We firmly stand by the original comparison of 2020 rates, showing Santee Cooper as having the lowest residential rates in South Carolina for a 1,000 kwh/month customer when compared to Dominion and the Dukes.

<u>Santee Cooper is NOT underinvesting in the utility system but in fact maintains one of the most reliable electric utilities in the U.S. as validated by third-party experts</u>.

PPI claims that Santee Cooper is underinvesting in the system by comparing Santee Cooper's capital expenditures to those of Duke, Dominion and NextEra. All three of these companies hold large non-utility businesses and they also operate large retail distribution utilities. *The majority of Santee Cooper's electricity is delivered at high voltage and at wholesale to customers, including Central and municipalities, and thus Santee Cooper doesn't have a distribution system for those loads – the co-ops and municipalities that Santee Cooper serves are their own distribution utilities. These comparisons are thus apples to oranges*. The proper method to gauge whether a utility is investing in the system is whether annual capital expenditures exceed the rate of depreciation, which is the case in Santee Cooper's Reform Plan. Further, and most importantly, as part of the Act 95 process the State Department of Administration retained global engineering firm Black & Veatch to review the Santee Cooper system. *Black & Veatch concluded that the Santee Cooper system is well maintained, that Santee Cooper has an excellent history of operating the assets, and that the operating expense and capital expenditure forecasts in the Reform Plan are appropriate.* Dr. Grace, of Clemson Economics Associates, says "Unfortunately we have not been given access to the Black and Veatch reviews; I cannot confirm sound infrastructure without doing so. Once I have been granted access to the report, if there is no cause for concern, we would be glad to strike this question from our list of concerns." The Black & Veatch report is posted in full at www.santeecooper.com/progress, and we invite Dr. Grace to review it there.

Finally, Santee Cooper consistently ranks among the top utilities across the U.S. for safety and reliability. According to the most recent U.S. Energy Information Administration data, Santee Cooper's distribution reliability ranks a stellar 4th in the country compared to over 550 investor-owned utilities and co-ops. A utility with this track record is clearly and properly investing in the system. PPI's underinvesting conclusion is false, without a factual basis, and is intentionally misleading.

<u>Santee Cooper is NOT "underfunded</u>".

In an earlier writing, Dr. Grace of CEA claims that Santee Cooper is "underfunded" but leaves the reader to define what that means. In her most recent revised writing, she clarifies that when she said "underfunded," she meant that Santee Cooper would need to borrow some new money for capital expenditures, specifically between now and 2029. In other words, Santee Cooper was not generating enough funds internally to pay for all of its capital expenditures without borrowing.

Financing a going concern utility such as Santee Cooper is a combination of paying off old debt related to old assets and borrowing new debt for new assets, all at the same time. As long as the company is paying off more old debt than it is borrowing new, total debt goes <u>down</u>, not <u>up</u>. That is precisely the case with Santee Cooper as Dr. Grace shows in a chart on page 2 of her submission, but fails to mention. Total debt outstanding declines by nearly $2 billion over this time, per the chart she shows, even though some level of new borrowings are assumed. Santee Cooper never said otherwise. It is false and misleading to not recognize and point out that total debt is going down, not up.

Why is there a need for new borrowings? A going concern needs new wire, towers, meters, bucket trucks, environmental upgrades, etc. for both replacement purposes as well as to serve new growth. These are generally long-lived utility assets, and typically are financed over their lives through borrowing to some degree in order to spread out the repayment for this equipment over the customers that actually use it.

Santee Cooper finances the equipment it uses to provide reliable electric service through a combination of internally generated funds and borrowings, in a proportion consistent with industry standards. To say we are "underfunded" as Dr. Grace defines it, meaning we have some new money borrowing needs, is to argue in favor of financing our equipment needs with 100% internally generated funds. Customer prices would have to rise substantially for that to occur, and of course it would be grossly unfair as today's customers would be asked to pay for equipment that a customer 20 years from now would be using.

Santee Cooper is not underfunded, its capitalization practices are consistent with industry standards, and its debt is going <u>down</u> substantially over time, not up. It is false and misleading to say otherwise.

<u>**Santee Cooper's debt is NOT $13.001 billion.**</u>

The outstanding debt on Santee Cooper's balance sheet as of 12/31/2020 (i.e. after the recent refinancing/financing) was $6.8 billion, not $13.001 billion as stated in the PPI piece. PPI's statement is simply false and misleading. The repayment of that debt is spread out over time to reflect, as aforementioned, the life of the assets being financed. As we have pointed out, Santee Cooper has been paying off substantial amounts of debt early.

The bond indebtedness of Santee Cooper, like its peers in the public power industry, is structured like a home mortgage, with level payments over time, comprised of a changing mix of principal and interest. "Debt service coverage" is the most important financial metric for public power entities, and measures the number of times such an entity can cover its P&I after payment of all operating, maintenance, fuel, and other cash expenses. Santee Cooper's financial metrics, including debt service coverage, earn it an "A" rating from the rating agencies – aligning with the top 4% of all ratings for investor-owned utilities nationally and thus we are pleased to hear that PPI finally acknowledges in its revised report "…the strong ratings Santee Cooper traditionally receives from the credit rating agencies."

<u>**Santee Cooper is substantially solvent and highly liquid.**</u>

The PPI and CEA pieces completely omit any reference at all to Santee Cooper solvency and liquidity, and by omission present an incomplete and very misleading financial picture. As of the end of 2020, Santee Cooper had approximately 150 days of "cash on hand" and approximately 345 days of liquidity (i.e. available cash and available credit lines.) An A-rated utility enterprise normally targets 90 days of cash on hand, which Santee Cooper materially exceeds. Santee Cooper, in other words, carries enough cash on hand to meet its remaining Cook Settlement obligations ($135 million – the first payment of $65 million was made on September 25, 2020) without violating the 90 day target. In addition, Santee Cooper has recently put aside $85 million to retire an extraordinary debt principal amount due in 2023. More than ample solvency, and pre-funding of known obligations such as these, are essential actions taken, along with litigation settlements, to substantially de-risk the company. These factors are fundamental to a proper financial analysis of this institution, and their omission by PPI is intentionally misleading.

In closing, Santee Cooper:

1. has the lowest rates of the major utilities in the state,
2. is <u>not</u> underinvesting in the system,
3. is <u>not</u> "underfunded",
4. does not have $13 billion in debt,
5. is decreasing its debt,
6. is highly solvent and liquid,
7. has extinguished all nuclear-related litigation, and thus
8. enjoys strong "A" ratings from major rating agencies

The proper valuation of Santee Cooper should reflect these facts. The picture painted by PPI undervalues Santee Cooper, intentional or otherwise.