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BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

**In re: Standard offer Contract for
the purchase of firm capacity and
energy from a qualifying facility
between Panda-Kathleen, L.P.
and Florida Power Corporation.**

Docket No. 950110-EI

**Submitted for filing:
January 24, 1996**

**REBUTTAL TESTIMONY OF
BRIAN A. MORRISON**

ON BEHALF OF

FLORIDA POWER CORPORATION

**Unredacted Version - Contains
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DOCUMENT NUMBER - DATE

00844 JAN 24 1996

FILED - RECORDS/REPORTING

FLORIDA POWER CORPORATION
DOCKET No. 950110-EI

**REBUTTAL TESTIMONY OF
BRIAN A. MORRISON**

1 **Q. Please state your name and business address.**

2 A. Brian A. Morrison, 800 Third Avenue, Suite 2300, New York, NY
3 10022.

4

5 **Q. By whom are you employed and in what capacity?**

6 A. I am employed by Morrison & Kibbey Ltd. as a Managing Director.

7

8 **Q. What type of an organization is Morrison & Kibbey, Ltd.?**

9 A. Morrison & Kibbey Ltd. is an investment banking firm.

10

11 **Q. What specifically do you do for Morrison & Kibbey?**

12 A. Like my other partners, I am responsible for assisting our clients in
13 developing new corporate financing strategies and the implementation
14 of these strategies.

15

16 **Q. Please describe your educational and business background.**

17 A. Education

18 1971-1975 Georgetown University BS - Mathematics

19 Scholarships: George F. Baker Trust

20 Francis Ouimet Foundation

1 1977-1979 Harvard Business School MBA - Finance
2 Scholarships: George F. Baker Trust
3 Danforth Memorial Fellowship

4 Business

5 1993-Present Morrison & Kibbey Ltd. Managing Director
6 1986-1993 Hicks Morrison & Co. Managing Director
7 1985-1986 Amvest Capital Corp. Senior Vice President
8 1982-1985 Dean Witter Reynolds First Vice President
9 1979-1982 Shearson/American
10 Express Assist. Vice President
11 1976-1978 Citibank, N.A.

12 A copy of my resume is attached as Exhibit No. ___ (BAM-1).
13

14 **Q. Have you worked in the area of financing of cogeneration projects?**

15 **A. Yes extensively.**
16

17 **Q. In what capacity?**

18 **A. In our role acting as financial advisor and placement agent we have**
19 **developed and/or implemented financing plans for over 40 power**
20 **projects representing in excess of 1,350 MW of generating capacity.**
21

22 **Q. For how many cogeneration projects have you worked on financing?**

23 **A. 16, totalling over 540 MW.**
24

25 **Q. What is the purpose of your testimony?**

1 A. The purpose of my testimony is to rebut the direct testimony pre-filed
2 by Panda-Kathleen, L.P., that stated that "Panda's ability to meet the
3 construction start date of January 1, 1996, and the in-service date of
4 January 1, 1997, has been jeopardized solely as a result of Florida
5 Power's actions in attempting to disown the contract." (Emphasis
6 added.) Testimony of Ralph Killian, page 37, lines 9-13.

7
8 **Q. On what do you base the testimony contained herein?**

9 A. I based my testimony on my review of the Panda/Florida Power Standard
10 Offer Contract, the Commission's Rule 25-17.0832, F.A.C., documents
11 produced by Panda in discovery, and on my direct experiences in
12 representing numerous private power developers in assisting in the
13 development and implementation of various types of project financing
14 structures.

15
16 **Q. Are you familiar with Panda's corporate structure as it pertains to this**
17 **proceeding?**

18 A. Yes. Three corporate entities appear in the documents: Panda-Kathleen,
19 L.P.; Panda-Kathleen Corporation; and, Panda Energy Corporation.
20 Florida Power entered into a Standard Offer Contract with Panda-
21 Kathleen, L.P., a Delaware Limited Partnership. Panda-Kathleen
22 Corporation is the general partner to Panda-Kathleen, L.P. and is a
23 subsidiary of the parent corporation, Panda Energy Corporation. Except
24 where my testimony pertains specifically to one of these entities, I will
25 refer to these various Panda corporations as Panda.

1 **Q. Are you aware that Panda-Kathleen, L.P., has failed to meet the**
2 **construction start date of January 1, 1996?**

3 **A. Yes.**
4

5 **Q. Are you also aware that on January 25, 1995, Florida Power filed a**
6 **Petition for Declaratory Statement with the Florida Public Service**
7 **Commission raising issues of the interpretation and application of Rule**
8 **25-17.0832, F.A.C., with respect to the Panda/Florida Power Standard**
9 **Offer Contract?**

10 **A. Yes.**
11

12 **Q. Based on your review of documents and your experience in the financing**
13 **of the development of power facilities, was Panda-Kathleen, L.P.'s,**
14 **failure to meet the construction start date "solely the result of Florida**
15 **Power's actions?"**

16 **A. No.**
17

18 **Q. What reasons would you cite for Panda-Kathleen, L.P.'s failure to meet**
19 **its construction start date?**

20 **A. Panda was experiencing difficulty in a number of areas prior to January**
21 **25, 1995. I've outlined below some of the issues that lenders were**
22 **aware of and expressed concern about regarding the Panda-Kathleen**
23 **project. The first issues involved the regulatory issues of whether**
24 **Florida Power would be required to purchase power in excess of 74.9**
25 **MW under the Panda/Florida Power Standard Offer Contract and the**

1 Commission's Cogeneration Rules, and whether Florida Power would
2 have to make capacity payments to Panda after 20 years under that
3 same contract. Second, Panda-Kathleen, L.P., had been unable to
4 secure an independent thermal host and had decided to use a subsidiary
5 of Panda Energy Corporation to build and operate the thermal host for
6 its own facility. Finally, the economics of the project in general lead to
7 Panda-Kathleen, L.P., "mothballing" the project for a period of time.
8 These issues would lead any lender to more carefully analyze both the
9 project and the financial condition of the developer.
10

11 **Q. Please describe the steps typically followed by the developer of a**
12 **cogeneration project in obtaining financing for the project.**

13 **A. Typically, a developer will have completely finalized the site acquisition,**
14 **the power purchase agreement, the outstanding permit issues, the fuel**
15 **supply, the equipment configuration, the Engineering Procurement &**
16 **Construction contract, the insurance policies and the thermal contract,**
17 **if any.**

18
19 **Q. Based on the documents produced by Panda which you have reviewed,**
20 **at what stage in the process of obtaining financing was Panda-Kathleen,**
21 **L.P., on January 24, 1995?**

22 **A. Based upon my review of the documents provided, there still seemed to**
23 **be a significant number of items to be resolved in all of the**
24 **mentioned areas which would be of concern to any institutional**
25 **lender from a due diligence standpoint. One of the potential investors,**

1 Calpine, citing among other issues the overall economics of the project
2 and the distilled water plant issues, informed the Kathleen Project Team
3 on January 23, 1995, that it had dropped out of the project as Panda-
4 Kathleen Corporation's equity partner. As to the other lenders, I did not
5 see detailed term sheets or indications of interest from Morgan Stanley
6 or ABB Capital which outlined their specific intent on providing financing
7 to this project at this time under certain terms and conditions.
8

9 **Q. In terms of the time required to obtain financing, was this project on**
10 **track to obtain the necessary financing in order to meet the contractual**
11 **milestones for commencing construction and commencing operation?**

12 **A. No. In order to meet the commercial operations date of January 1,**
13 **1997, Panda-Kathleen, L.P.'s, management readily admits that the**
14 **financing for the project needed to be in place before December 31,**
15 **1994.**

16
17 **Q. To your knowledge, was Panda-Kathleen, L.P.'s, financing for the**
18 **project in place by that date?**

19 **A. No. Lenders were still conducting due diligence without having issued**
20 **a firm commitment to the fund project.**

21
22 **Q. Do you believe that Panda-Kathleen, L.P., would have been able to**
23 **obtain financing after January 24, 1995, if Florida Power had not filed**
24 **the Petition for Declaratory Statement on January 25, 1995?**

1 A. No. The regulatory issues concerning the size of the facility and the
2 length of time that Florida Power would be required to make capacity
3 payments had to be resolved before a lender would likely agree to
4 finance the project. Even before Florida Power filed its Petition, lenders
5 were aware of and concerned about those issues. The letter dated June
6 23, 1994, from Ted Hollon of Panda to David Gammon of Florida Power
7 outlines concern on behalf of prospective lenders regarding the issue of
8 what price, if any, Florida Power was going to pay for power delivered
9 by the project in excess of the 74.9 MW limit in the standard offer
10 contract.

11
12 **Q. What does the concern of lenders expressed in Ted Hollon's letter**
13 **indicate to you?**

14 A. Since this issue had still not been resolved prior to the January 25,
15 1995 filing by FPC, I would have to believe that this was still a major,
16 unresolved due diligence item for any of the prospective financial
17 institutions, since these excess power sales appear to represent
18 approximately 35% of the project's total revenue stream.

19
20 **Q. Would the concern expressed by these prospective lenders be sufficient**
21 **to interfere with financing for the project?**

22 A. Definitely. Financial institutions would not close on non-recourse
23 financing of this magnitude without having satisfactory answers to these
24 questions.

1 **Q. Would other lenders be likely to have similar questions?**

2 **A. Certainly.**

3
4 **Q. You stated previously in your testimony that the lack of a secured**
5 **thermal host would have interfered with Panda-Kathleen, L.P.'s, meeting**
6 **its milestone dates. Please elaborate.**

7 **A. It is clear from the documents that Panda-Kathleen, L.P., had a problem**
8 **securing a thermal host for the project. Panda-Kathleen, L.P., first**
9 **attempted to contract with Erly Juice. When those efforts were**
10 **unsuccessful, Panda-Kathleen, L.P., apparently decided it would have a**
11 **subsidiary of Panda Energy Corporation be the thermal host for the**
12 **facility. Several problems remained, however. The thermal host facility**
13 **had yet to be designed, and financing had to be obtained, not only for**
14 **the cogeneration facility, but also for the thermal host facility. Lenders**
15 **would have to have the design in hand to review, and would also have**
16 **to look even more carefully at Panda's financial structure before**
17 **approving the lending for Panda's enhanced needs.**

18
19 **Q. You referred previously to the fact that Panda-Kathleen, L.P.,**
20 **"mothballed" the project for a period of time. What does "mothballing"**
21 **the project mean to you?**

22 **A. It means stopping all progress on the project until certain obstacles**
23 **could be surmounted.**

1 **Q. Do you often see developers "mothball" their projects as Panda-**
2 **Kathleen, L.P., did?**

3 **A. Occasionally, but usually the project is "shelved" because of economic**
4 **reasons and these projects typically never get completed in the original**
5 **configuration. For instance, if fuel costs or availability became an issue,**
6 **a developer may shelve a project until they could resolve the**
7 **outstanding fuel issues. One resolution might take the form of changing**
8 **fuels or co-firing with another less expensive or readily available fuel.**
9 **This could also be done in the event that the project loses its thermal**
10 **host. This seemed to be the case with Panda-Kathleen, L.P., and its**
11 **negotiations with Eryl Juice.**

12
13 **Q. What does the fact that the project was mothballed for a period of time**
14 **indicate to you in terms of Panda-Kathleen, L.P., meeting its milestone**
15 **dates?**

16 **A. While one cannot directly relate Panda-Kathleen, L.P.'s, mothballing of**
17 **the project to its failure to meet the construction start date, the**
18 **mothballing is an additional symptom of a troubled project.**

19
20 **Q. In addition to the issues already discussed, did you see any evidence**
21 **that Panda-Kathleen, L.P., would not likely be able to obtain financing**
22 **for its project?**

23 **A. Yes.**

24
25 **Q. Please describe those issues.**

1 A. The evidence that I saw that would indicate that Panda-Kathleen, L.P.,
2 would not be likely to obtain financing for the Panda-Kathleen project is
3 as follows:

- 4 ● Panda-Kathleen, L.P.'s, initial 1994 financing plan was to fund the
5 project with rated, senior taxable debt via the public or private
6 (144a) markets with a term of 25 + years through the firm of Smith
7 Barney. This term, especially for non-investment grade, taxable
8 debt, seems quite long. (The 144a debt market which is comprised
9 primarily of institutional debt investors has been very active in the
10 private placement of rated, corporate debt issues. It wasn't until
11 early 1993 that independent power projects began to test the
12 viability of this market for project financing. Even then, many
13 investors did not think that independent power projects belonged
14 in the 144a marketplace because of the complexity of issues
15 involved with these types of project financing.) Also, by the latter
16 part of 1994, all discussion of Smith Barney and this financing had
17 disappeared which would lead anyone to believe that there was no
18 market for this type of issue with the interest rate and amortization
19 schedule required by the Panda-Kathleen project.
- 20 ● I reviewed several draft Indication of Interest letters from Bank of
21 Tokyo (BOT) over a period of several months beginning in October
22 1994 and continuing into 1995. The actual scope of the BOT
23 financing structure changed from (i) an approximate 18 month
24 construction loan with a 13-15 year permanent loan; into, (ii) a
25 construction loan with a 2 year bridge loan. These documents

1 comprise a series of draft terms sheets that continue discussions
2 into early 1995 with no firm commitment letter from BOT.

- 3 ● In the latter half of 1994, after Smith Barney was unable to market
4 a long-term debt issue with a 25 + year term for the project, Merrill
5 Lynch was hired to arrange a Medium Term Note (MTN) issue with
6 a term of 25-30 years. This seems a bit puzzling since a MTN issue
7 would typically have a term of only 3-7 years and require the issuer
8 to have an investment grade rating.
- 9 ● In August of 1994, Panda Energy Corporation took it upon itself,
10 without the assistance of any of its many financial advisors, to
11 issue an Investment Memorandum in order to place \$15 million in
12 limited partnership interests in the Panda-Kathleen project. This
13 effort seems to have come up empty since there is no further
14 discussion on the topic except for reference to Calpine as a
15 potential equity investor.
- 16 ● In a letter dated January 23, 1995, Calpine dropped out as a
17 potential equity investor citing, among other things, numerous
18 concerns such as the capital cost of the project, the operating costs
19 of the project, issues revolving around the distilled water plant, and
20 the overall inadequate economics of the project.

21 Any of these factors alone could cause any financial institution to pass
22 on this transaction until such issues were resolved.

1 **Q. Are you familiar with the original configuration for the facility proposed**
2 **by Panda-Kathleen, L.P., at the time Panda-Kathleen, L.P., submitted its**
3 **standard offer?**

4 **A. Yes. The various documents indicated that Panda-Kathleen, L.P.,**
5 **considered several different equipment configurations in order to**
6 **generate a net capacity delivered of not more than 75MW.**

7
8 **Q. Have you analyzed those original configurations from a financial**
9 **perspective?**

10 **A. Yes. I reviewed a truncated spreadsheet analysis dated December 23,**
11 **1993 for the 75MW Panda-Kathleen project.**

12
13 **Q. Was the project as originally configured a viable project?**

14 **A. No. The project proforma analysis had significant negative cashflows**
15 **for the first four years (1997-2000) and coincidentally had debt service**
16 **coverage ratios of less than 1.0x during each of those four years. This**
17 **analysis showed that the project would not be able to make all of its**
18 **scheduled debt payments during each of those four years.**

19
20 **Q. Have you analyzed the internal financial structure of Panda Energy**
21 **Corporation?**

22 **A. Yes.**

1 **Q. Did you find any problems with the internal financial condition of Panda**
2 **Energy Corporation which would make it unlikely that Panda-Kathleen,**
3 **L.P., would be able to obtain the necessary financing for the project?**

4 **A. Yes. Panda Energy Corporation continually lost money over the period**
5 **1991-1994 recording a significant cumulative net income loss, and it**
6 **posted a sizeable negative net worth position by December 31, 1994.**
7 **This also indicates that Panda Energy Corporation has accumulated**
8 **substantial losses during its operating years prior to 1991. So, the fact**
9 **that Panda Energy Corporation had continually lost money could possibly**
10 **limit the arena for potential project equity partners since Panda Energy**
11 **Corporation would probably continue to be in dire need of operating**
12 **capital at the corporate level.**

13
14 **Q. In your opinion, was the Panda-Kathleen project a viable candidate for**
15 **financing on January 24, 1995?**

16 **A. No. The project had gone through so many changes since the**
17 **"mothballing", including several different financial advisors, that it**
18 **appears that the Panda-Kathleen management team was grasping at**
19 **straws during the last quarter of 1994 in order to come up with some**
20 **structure that was bankable. This concludes with Merrill Lynch**
21 **proposing a medium term note financing on January 19, 1995, with a**
22 **30 year term and interest only for 7 years, a highly unorthodox proposal**
23 **which indicated the desperate straits of Panda-Kathleen, L.P. in**
24 **obtaining financing.**

1 **Q. Does this conclude your testimony?**

2 **A. Yes.**

FPSC DOCKET NO. 950110-EI
EXHIBIT NO. _____ (BAM-1)
CONSISTING OF ONE PAGE

BRIAN A. MORRISON

EXPERIENCE:

- 1993 - Present** **Morrison & Kibbey Ltd.**
Managing Director
Leasing and project finance specialists with industry focuses in power generation, environmental, natural resources, forest products, pulp and paper and food processing.
- 1986 - 1993** **Hicks Morrison & Company Inc.**
Managing Director
Leasing and project finance specialists with industry focuses in power generation, environmental, natural resources, forest products, pulp and paper and food processing.
- 1985 - 1986** **Amvest Capital Corporation**
Senior Vice President
Leasing, project finance and real estate finance.
- 1982 - 1985** **Dean Witter Reynolds, Inc.**
First Vice President
Investment banking with a focus on private placements of equity and debt.
- 1979 - 1982** **Shearson/American Express Inc.**
Assistant Vice President
Investment banking/Corporate finance.
- 1976 - 1978** **Citibank, N.A.**
International banking/Institutional investment.

EDUCATION:

- 1977 - 1979** **Harvard Business School**
MBA - Finance
- 1971 - 1975** **Georgetown University**
BS - Mathematics