DeAnn T. Walker
Chairman

Arthur C. D'Andrea
Commissioner

Shelly Botkin
Commissioner

John Paul Urban
Executive Director

Greg Abbott
Governor

2019 JUN 10 AM 10:00

PUBLIC UTILITY COMMISSION FILING CLERK

Public Utility Commission of Texas

TO: Central Records

FROM: Mark Hovenkamp
Commission Advising

RE: Correspondence related to P.U.C. Docket No. 49308 – *Application of AEP Texas Inc. for a Financing Order to Securitize System Restoration Costs*

DATE: June 10, 2019

Chairman Walker and Commissioners D'Andrea and Botkin received the attached correspondence pertaining to the above-styled docket.

Please note that a member or employee of a state agency assigned to render a decision in a contested case may not directly or indirectly communicate in connection with an issue of fact or law with any state agency, person, party, or representative of those entities, except on notice and opportunity for each party to participate. See Administrative Procedures Act, Texas Government Code § 2001.061.

Commission Advising is filing the correspondence. Parties will not be served copies of the attached document, but can access it through the PUC Interchange at http://interchange.puc.texas.gov/.

cc: All Parties (without attachment)

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June 5, 2019

The Honorable DeAnn Walker
Chairman, Public Utility Commission of Texas
1701 N. Congress Avenue
PO Box 13326
Austin, TX 78711-3326

RE: Docket 49308 Proposed Servicing Fee

Dear Chair Walker:

This letter addresses evidentiary issues concerning AEP's proposed servicing fee it seeks for system restoration bonds in Docket #49308. Saber Partners LLC is a leading provider of expert financial advisory services to public utility commissions regarding securitizations. It is Saber Partner's intent that the Commission is presented with as much public information as possible prior to making final decisions concerning AEP's application for a financing order in this docket. Saber Partners has formally withdrawn its response to the Public Utility Commission's solicitation for a financial advisor and seeks no role in this transaction. Nonetheless, Saber Partner's mission is to ensure lowest cost outcomes for customers in the context of securitization transactions generally. Saber Partners has been a national leader in this regard for almost two decades. Sixty-five investor-owned utility securitization transactions have occurred in the United States in the last twenty-two years and there have been significant developments in the public record since 2012 that provide the foundation of trends and national standards. It is unreasonable to expect staff of any Commission to have ready and independent access to such information.

It is in the spirit of providing facts and circumstances that lend themselves to the Public Utility Commission's public interest charge and legislative mandate concerning achieving the lowest transition charges under market conditions at the time of pricing, that Saber Partners conveys the following public information to you for your perusal and consideration prior to your final decision in Docket #49308. We hope this letter provides helpful information to evaluate AEP's requested servicing fee in the context of the national standards regarding such fees in securitization transactions across the country, and that it assists in identifying crucial omissions in evidence that the Commission may want elucidated.

AEP's Proposal to Double the Servicing Fee for the System Restoration Bond Transaction Is Not Justified by the Evidence Presented in the Case and Is Contrary to the Industry Standard – It Unduly Burdens Customers

The primary basis for the Transition Bond servicing fee is an "arm's length" market-based fee to establish a legal, bankruptcy-remote relationship between the special purpose entity as issuer and the sponsoring utility as servicer for rating agency purposes. This is a well-established principle of all utility fee securitizations.

AEP has proposed 10 basis points (0.10%) of the initial principal amount per annum as its "servicing fee," or an additional $229,000 from customers per year ($2.29 million total over a 10-year amortization). This amount of servicing fee is neither justified by the evidence AEP presented in the case, nor is it consistent with the industry standard for servicing fees in other electric utility securitizations nation-wide.

AEP's 10 basis point proposal is a 100% increase from its servicing fee charged in prior transactions and is not the market or "industry standard" for securitization transactions of any size, small or large. Every transaction Saber has directly been involved – from $21 million (2009) to $1.85 billion (2005) – the fee negotiated and accepted by the utility was the industry standard of approximately 5 basis points (0.05%) per annum of the initial principal amount of the bond issue. Moreover, we required a credit back to customers if the utility's actual incremental costs were *less* than the industry standard servicing fee.

AEP accepted this market-based standard servicing fee on all three of its previous Texas Transition Bond transactions. Moreover, AEP's last securitization for a sister subsidiary, Appalachian Power, in West Virginia in 2013, also was at the industry standard of 0.05%. The size of the transaction was $380.3 million and was completed in November 2013.

However, AEP's Randall W. Hamlett in his direct testimony proposed a doubling of its servicing fee. He gave the following justification:

> *"The rationale for increasing the servicing fee from 5 basis points to 10 basis points is that while the size of the bond issuance is smaller than past securitizations reviewed by the Commission, the scope of activities required by the servicing entity is generally unrelated to the size of the amount financed by the system restoration bonds; rather, it represents the administrative costs of the servicer performing its servicing functions described above. Looking at prior Texas securitizations, and excluding the outliers (primarily the stranded cost securitizations over $1 billion), servicing fees approved by the Commission have generally fallen in the $250,000 to $400,000 range, which is slightly higher than the amount proposed in this transaction."*[1]

Mr. Hamlett's testimony is an assertion, and AEP gave no evidence to support that AEP's incremental servicing costs on this transaction would exceed the industry standard cap. It is also incomplete information as to the legal rationale for the servicing fee amount. Moreover, AEP's servicing activities *are inextricably tied to what they already do now in their normal course of business of charging, billing and collecting on the same customer bill and transferring funds to the bond trustee.*

Indeed, it would seem that AEP's incremental costs likely would be largest for the *first* securitization transaction for a particular servicer, with smaller (not larger) *incremental* costs for subsequent securitization transactions which generally would use the same systems and personnel already in place and performing similar functions. If there is evidence of additional incremental costs for this follow-on securitization transaction, AEP should present it rather than just assert it.

AEP (or its predecessor, Central Power & Light) has been a servicer of $797.3 million of Texas Transition Bonds issued in 2002, $1,739.7 million issued in 2006, and $800.0 million issued in 2012. AEP should be able to show clearly and easily how much it actually did incur as incremental costs on each of its three previous Texas Transition Bond offerings to perform the servicing function so as to justify their current

[1] Hamlett, Direct Testimony at page 26 lines 16-23 and page 27 lines 1-2

request. They chose not to present any evidence from their records of actual costs from those transactions. So, there is nothing in the record to justify any increase above the 5 basis point market standard fee.

One should note that the alternative third party servicer fee remained at the industry standard of 0.60% regardless of transaction size, and the administration, trustee and other ongoing fees remained the same for each of AEP's 3 previous transactions. If AEP's assertion that "the scope of activities required by the servicing entity is generally unrelated to the size of the amount financed by the system restoration bonds," how is it that this fee in most all other utility securitizations remains at the industry standard of 0.60% regardless of the size of the transaction? The answer is straightforward. The fees are consistent with legal and rating agency requirements which are the primary reasons for establishing servicing fees in securitization transactions.

Post 2012 Precedents on the Appropriate Amount of Servicing Fee as Percent of Initial Principal Amount Support Lowering AEP's Request to 0.005%

This servicing fee issue concerning 0.05% per annum or more has arisen in other recent (post 2012) utility securitization transactions in other states where Saber was not involved as well. Those cases also support Saber's view that the AEP servicing fee in this case should be reduced by $115,000 per year to 0.05% of the initial principal amount with no harm to AEP a saving for customers of $1.15 million over the life of the bonds.

While some transactions have been higher without scrutiny, when the issue was examined the 5 basis point standard has been confirmed independently and repeatedly from the public record in other states as noted below.

At a hearing **December 6, 2017** before the State of New Hampshire Public Utilities Commission on a proposed stranded cost securitization of $650 million, one of AEP's servicing fee witness in this case, Goldman Sachs's Katrina Niehaus, also appeared with the Assistant Treasurer of the sponsoring utility, Eversource/Public Service of New Hampshire (PSNH), Emilie O'Neil. They were questioned about the justification for the utility's servicing fee of 0.05%.

> "*Q And how is that [servicing fee] collected and calculated, do you know?*
>
> *A (O'Neil) Yes. So, the market notion is an annual servicing fee would be 0.05 percent of the principal amount of the bonds issued. And that would be considered an ongoing cost. ...*
>
> ***Q Is that calculation determined through reference to an industry standard or is it through an estimate of costs that the Company has done internally?***
>
> *A (O'Neil)* ***It's an industry standard****, and the cost needs to be such that there is sort of -- we have to be looked at almost like as a hands-off relationship, because there has to be, between the SPE and -- it has to be arms length between the SPE and PSNH in order for it to be bankruptcy remote.* ***So, the 0.05 is an industry standard****. The amount would be significantly higher if we were not currently*

> *billing other charges or remitting other charges." **(Emphasis added. Ms. Niehaus made no corrections or amplifications to Mr. O'Neil's testimony.)*** [2]

Attached is the listing of recent utility securitization servicing fees that Eversource (and AEP's) witness Katrina Niehaus submitted to the Public Service Commission of New Hampshire in 2017 to support the 0.05% "industry standard" request of the utility.

Moreover, at the **December 6, 2013** meeting of the Michigan Public Service Commission approving a financing order for $378 million Consumers Energy securitization (Case No. U-17473) who also proposed a 10 basis point fee also a 100% increase from a prior transaction, the Commission rejected the proposal and stated in the financing order

> *"The Staff also recommends that servicing fees be reduced by $3.2 million over the life of the bonds, arguing that a fee of 0.05% is reasonable compensation for Consumers. 2 Tr 424. <u>The Staff notes that the utility provides no support for its request for 0.10% other than the fact that it has been used in two other recent transactions.</u>"* [3]

The Michigan Commission set the servicing fee at 0.05%.

There are many other recent precedents that contradict AEP's assertion and more than doubling of the amount collected from customers each year to $239,000 from $115,000 is necessary.

- In 2014, the same year of the Consumers $378 million transaction above where the Commission rejected a 0.10% fee, Entergy in Louisiana completed a $243 million securitization (just $4 million larger than the AEP proposed securitization) with a servicing fee of 0.06%.
- In 2013, the **AEP subsidiary, Appalachian Power** in West Virginia, had a servicing fee of only 0.05% on a transaction of $380.3 million.
- In 2008, a $180 million Cleco Katrina/Rita Hurricane Recovery Funding LLC securitization was done for 0.05% servicing fee.

Bottom Line: AEP' Proposal is Inconsistent with PURA's "Lowest Transition Charge" Mandate Under Market Conditions at the Time of Pricing to the PUCT and Should Be Adjusted

While there have been cases of higher servicing fees achieved by utilities, the servicing fee is not dependent on issue size but is approximately 0.05% of the initial principal amount.

We also note that AEP's Hamlett also stated in direct testimony "It is important to note that the servicing fee revenues will reduce AEP Texas' revenue requirement in future base rate cases. As a result, customers will not be impacted by any variance of actual servicing costs paid to AEP Texas from the servicing fee included in the transition charges."[4]

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[2] https://www.puc.nh.gov/Regulatory/Docketbk/2018/18-177/TRANSCRIPTS-OFFICIAL%20EXHIBITS-CLERKS%20REPORT/18-177_2019-01-18_TRANSCRIPT_HEARING_12-18-18.PDF

[3] https://w2.lara.state.mi.us/ADMS/Mpsc/ViewCommissionOrderDocument/10729

[4] This provision was first proposed by Saber Partners to the Texas Commission and adopted as policy in the 2001 Reliant/CNP transaction and adhered to on all subsequent Transition Bond transactions.

While a portion (or possibly even all) of the increase may reduce revenue requirements in the future, this is not sufficient justification for increasing charges today on AEP customers simply to potentially pay them back later if they have a rate case. This makes it at best an interest free borrowing from customers.

AEP's proposal certainly is not consistent with establishing the lowest transition charges "at the time of pricing," present value analysis and other standards.

Recommended Action: Approve Joint Stipulation but Lower AEP's Fee to the Industry Standard of 0.05%

The Joint Stipulation states that the financing order agreed to make the following Finding of Fact #23

> *"It is also appropriate to impose additional limits to ensure that the servicing fees incurred when AEP Texas serves as servicer* ***do not exceed 0.10% of the initial principal balance*** *of the system restoration bond..."*

Ordering paragraph 17 states

> *"AEP Texas may recover its actual ongoing qualified costs through its system restoration charges,* ***subject to the caps*** *on the servicing fees and administrative fees (which are applicable as long as AEP Texas serves as servicer or administrator, as applicable) set forth in Finding of Fact No. 23"*

Since the fee is described in the Joint Stipulation as a not to exceed cap, the Commission can lower the actual amount allowed to be charged and recovered from customers to the industry standard 0.05% and still be consistent with the Joint Stipulation. This prevents AEP from billing the additional $115,000 from customers even if it asserts it will pay it back at the next rate case.

Please call with any questions.

Sincerely,

Joseph S. Fichera
Chief Executive Officer

Attachment: Public Service of New Hampshire d/b/a Eversource Energy Docket No. DE 17-096 Exhibit 13 RR 1-013

cc: Honorable Shelly Botkin
Honorable Arthur D'Andrea
Darryl Tietjen

Dean Criddle
Paul Sutherland
Hyman Schoenblum
Brian A. Maher

EXHIBIT

13

DE 17-096

Public Service of New Hampshire d/b/a Eversource Energy
Docket No. DE 17-096

Date Request Received: 12/06/2017 **Date of Response: 12/11/2017**
Request No. RR 1-013 **Page 1 of 1**
Request from: **New Hampshire Public Utilities Commission Staff**

Witness: **Emilie G. O'Neil, Katrina T. Niehaus**

Request:
Please provide a table listing the servicing fee structure for recent utility securitized financings.

Response:
Please refer to Attachment RR 1-013 for a table listing the servicing fee structure for recent utility securitization financings.

State	Entity	Closing Date	Approx. Size ($mm)	Initial Servicing Fee (% of initial principal)
New York	Long Island Power Authority	2017	$369	0.05%
New York	Long Island Power Authority	2016	$469	0.05%
Florida	Duke Energy Florida	2016	$1,294	0.05%
New York	Long Island Power Authority	2016	$637	0.05%
New York	Long Island Power Authority	2015	$1,002	0.05%
Louisiana	Entergy New Orleans	2015	$99	0.15%
Hawaii	Department of Business, Economic Development, and Tourism	2014	$150	0.01%
Louisiana	Entergy Louisiana (EGSL)	2014	$71	0.21%
Louisiana	Entergy Louisiana (ELL)	2014	$244	0.06%
Michigan	Consumers Energy	2014	$378	0.05%
New York	Long Island Power Authority	2013	$2,022	0.05%
West Virginia	AEP West Virginia	2013	$380	0.05%
Ohio	AEP Ohio	2013	$267	0.10%
Ohio	FirstEnergy	2013	$445	0.10%
Texas	AEP Texas Central	2012	$800	0.05%
Texas	CenterPoint Energy	2012	$1,695	0.05%
Louisiana	Entergy Louisiana	2011	$207	0.07%
Arkansas	Entergy Arkansas	2010	$124	0.12%
Louisiana	Entergy Louisiana (ELL)	2010	$469	0.03%
Louisiana	Entergy Gulf States Louisiana (EGSL)	2010	$244	0.06%
West Virginia	Potomac Edison Company	2009	$22	0.05%
West Virginia	Monongahela Power Company	2009	$64	0.05%
Texas	CenterPoint Energy	2009	$665	0.05%
Texas	Entergy Texas	2009	$546	0.05%
Louisiana	Entergy Louisiana (EGSL)	2008	$278	0.06%
Louisiana	Entergy Louisiana (ELL)	2008	$688	0.03%
Louisiana	Cleco Power	2008	$181	0.05%
Texas	CenterPoint Energy	2008	$488	0.05%
Maryland	Baltimore Gas & Electric	2007	$623	0.05%
Texas	Entergy Gulf States	2007	$330	0.12%
Florida	Florida Power and Light	2007	$652	0.05%
West Virginia	Monongahela	2007	$344	0.05%
West Virginia	Potomac Edison	2007	$115	0.05%
Texas	AEP Texas Central	2006	$1,740	0.05%
New Jersey	Jersey Central Power & Light	2006	$182	0.13%
Texas	CenterPoint Houston	2005	$1,851	0.05%
California	Pacific Gas & Electric	2005	$844	0.09%
Pennsylvania	West Penn Power	2005	$115	0.25%
New Jersey	Public Service Electric & Gas	2005	$103	0.05%
Massachusetts	Nstar (Boston Edison)	2005	$675	0.05%
California	Pacific Gas & Electric	2005	$1,888	0.09%
New Jersey	Rockland Electric	2004	$46	0.13%
Connecticut	State of Connecticut (CL&P/UIC)	2004	$205	0.07%
Texas	TXU Electric Delivery	2004	$790	0.05%
New Jersey	Atlantic City Electric	2003	$152	0.10%
Texas	Oncor Electric Delivery	2003	$500	0.05%
New Jersey	Atlantic City Electric	2002	$440	0.10%
New Jersey	Jersey Central Power and Light	2002	$320	0.13%
Texas	Central Power and Light	2002	$797	0.05%
New Hampshire	Public Service of New Hampshire	2002	$50	0.25%*
Michigan	Consumers Energy	2001	$469	0.25%*
Texas	Reliant Energy	2001	$749	0.05%
Massachusetts	Western Massachusetts	2001	$155	0.05%
New Hampshire	Public Service of New Hampshire	2001	$525	0.25%*
Connecticut	Connecticut Light & Power	2001	$1,438	0.05%
Michigan	Detroit Edison	2001	$1,750	0.05%
Pennsylvania	PECO Energy	2001	$805	0.25%*
New Jersey	PSE&G	2001	$2,525	0.05%
Pennsylvania	PECO Energy	2000	$1,000	0.25%*
Pennsylvania	West Penn Power	1999	$600	0.21%
Pennsylvania	Pennsylvania Power & Light	1999	$2,420	0.05%
Massachusetts	Boston Edison	1999	$725	0.05%
California	Sierra Pacific Power	1999	$24	0.25%*
Pennsylvania	PECO Energy	1999	$4,000	0.25%*
Illinois	Illinois Power	1998	$864	0.25%
Illinois	Commonwealth Edison	1998	$3,400	0.09%
Montana	Montana Power	1998	$63	1.59%
California	San Diego Gas & Electric	1997	$658	0.25%*
California	Southern California Edison	1997	$2,463	0.25%*
California	Pacific Gas & Electric	1997	$2,901	0.25%*
Washington	Puget Sound Energy	1997	$35	0.004%
Washington	Puget Sound Energy	1995	$202	0.001%

* Outstanding Principal Balance

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