



# Utility Securitization: A Brief History

## With New Uses to Lower Ratepayer Costs

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# Saber Financial Advisor Securitization Assignments



Wisconsin



West Virginia



Florida



Texas



New Jersey



Vermont

## Why does Securitization matter?

- **Public interest solution to slowing the rise in energy rates**
  - Benefits consumers and utilities
- **Mitigates long-term rate impact of investment decisions and government mandated costs**
  - Least cost alternative in global capital markets.
- **Creates economic value in capital markets from Commission's powerful regulatory authority**

## Different Names; Same Technology

### Also known as....

- Rate Reduction Bonds
- Stranded Cost Bonds
- Utility Fee Bonds
- Energy Recovery Bonds
- Environmental Trust Bonds
- Storm Recovery Bonds

# What is Securitization?

It is **not**...

- ***Not* a bond by the Utility**
  - Non-recourse to utility, its shareholders and creditors, completely independent corporate bond
- ***Not* a Municipal Bond**
  - Not a charge against the state's taxing or budget authority
- ***Not* an Asset Backed Security**
  - No pool of receivables, financial assets or other complexities

## What is Securitization?

It is:

- Direct borrowing on rate base – “ratepayer-backed” bond
- Guaranteed by State’s regulatory authority over rates – an R.O. (regulatory obligation) not G.O. (general obligation)
- AAA rated, top quality
- Lowest cost way to raise investment funds in debt capital markets today

## What Makes a Successful Securitization

- **Specific state statutory authorization (Generally) which includes a “State Pledge” of non-impairment (Always)**
- **Irrevocable financing order which includes an automatic adjustment mechanism (true-up/true-down)**
- **Active Commission oversight of, and involvement in, financing process**

## Debt Structure

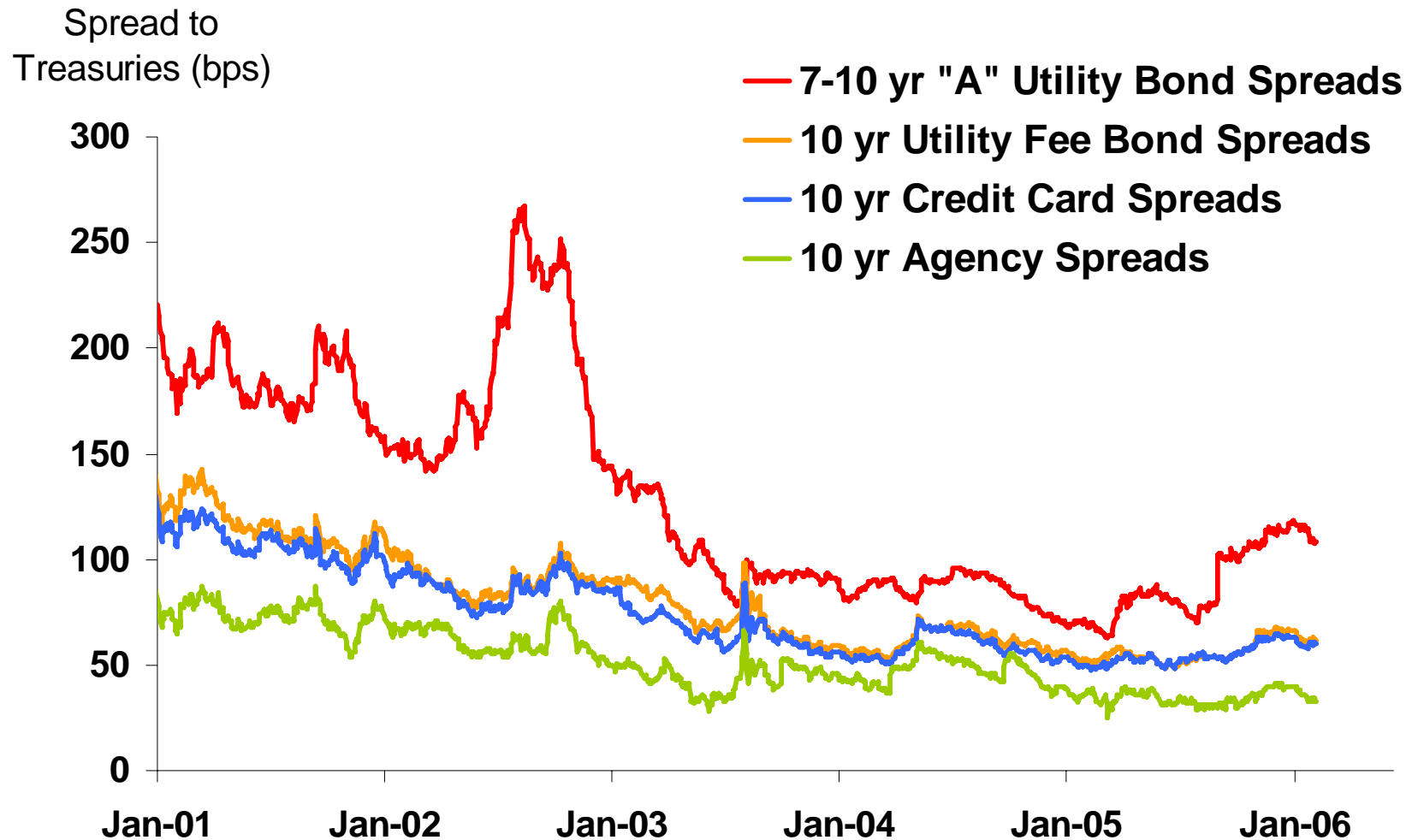
- Issued by a special purpose entity, owned by utility and responsible to the Commission – “bankruptcy remote”
- Secured by and payable from a dedicated component of the retail rate
  - Broadly based
  - Non-bypassable
  - Not more than 20% of the total bundled rate

## Any Credit Risk Effectively Eliminated

**“The broad-based nature of the true-up mechanism and the State Pledge will serve to effectively eliminate for all practical purposes and circumstances any credit risk associated with the Bonds.”**

**Source: SEC Prospectus: TXU Electric Delivery**

## Lower/Less Volatile Rates than Utility bonds



# With Large Benefits to Ratepayers: e.g., \$1 billion 10-Year Average Life Financing

**SAVINGS  
vs. Other  
Utility  
Financing  
Options**



**Total Nominal Savings from Securitization, \$ millions**

Based on Citigroup utility bonds spreads versus securitization spread 2001-2006

## Differing uses in States...expanding over time

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# Expanding Use of Securitization



# Expanding Use of Securitization



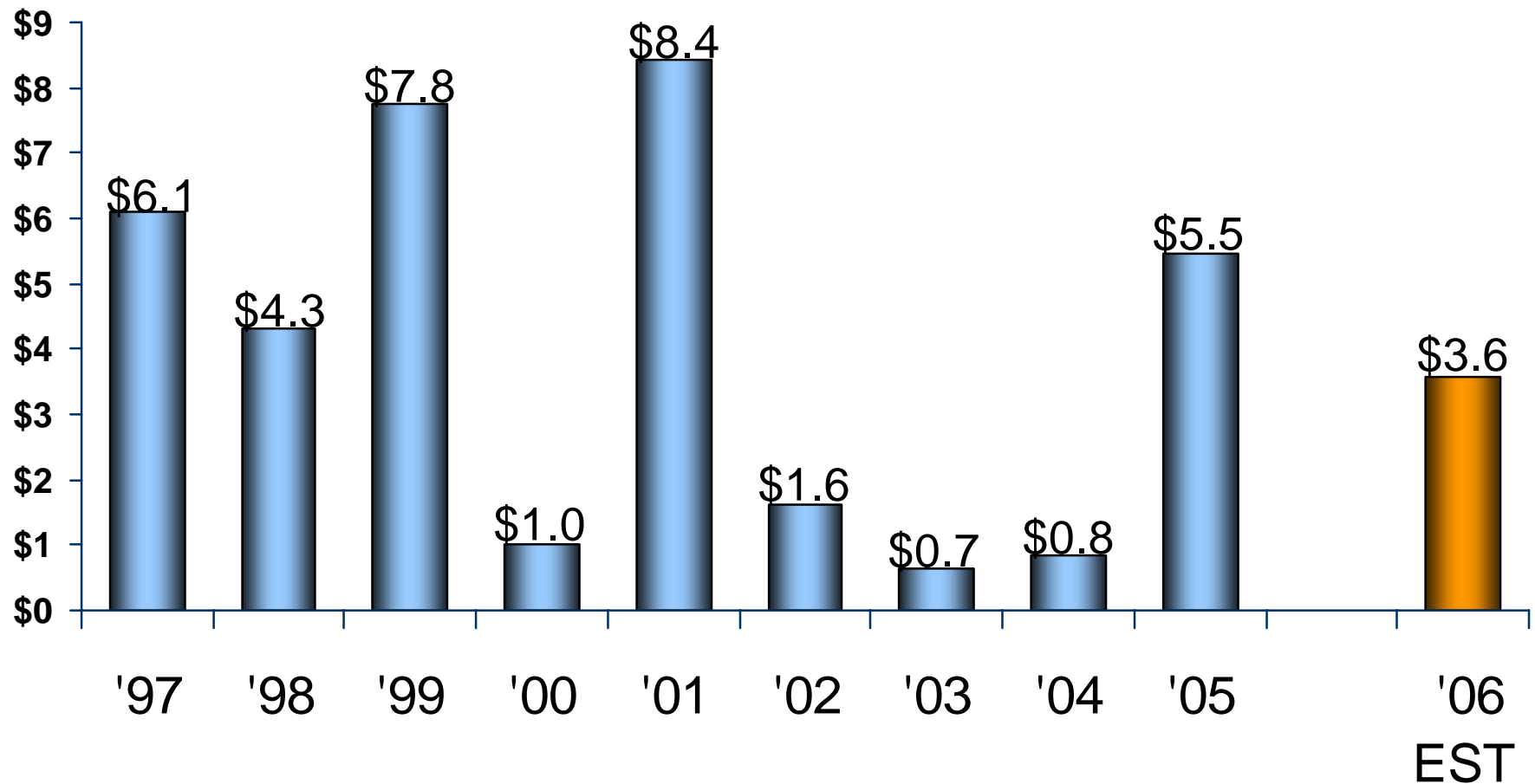
# Expanding Use of Securitization





# \$33.5 Billion Issued; \$3.6 billion Expected '06

(\$ billions)



Sources: Bloomberg, Transition Bond prospectuses, and other SEC filings.

Proprietary

## 1994 - 1997

- **Introduced by Puget Power**
  - Demand side management
- **Followed by several issuances from California**
  - Finance 10% rate reduction facilitating deregulation
  - Consumer groups oppose

Date	Issue	State	Size (\$mm)	Purpose
Jun-95	Puget Power, Series 1995-1	Washington	202.3	Demand Side Management
1997	Puget Power, Series 1997	Washington	35.2	Demand Side Management
Nov-97	PG&E, Ser. 1997-1	California	2,901.0	Rate Reduction
Dec-97	SCE, Ser. 1997-1	California	2,463.0	Rate Reduction
Dec-97	SDG&E, Ser. 1997-1	California	658.0	Rate Reduction
<b>Total</b>			\$ 6,259.5	

**Source: SEC Documents, Fitch.**

## 1998 - 2000

- Financing method quickly embraced for stranded costs by utilities
- Securitization becomes synonymous with deregulation and stranded costs

Date	Issue	State	Size (\$mm)	Purpose
Dec-98	Montana Power	Montana	62.7	Stranded Costs
Dec-98	ComEd, Ser. 1998	Illinois	3,400.0	Stranded Costs
Dec-98	Illinois Power, Ser. 1998-1	Illinois	864.0	Stranded Costs
Mar-99	PECO, Ser. 1999-A	Pennsylvania	4,000.0	Stranded Costs
Apr-99	Sierra Pacific	California	24.0	Stranded Costs
Jul-99	Boston Edison	Massachusetts	725.0	Stranded Costs
Jul-99	PP&L, Ser. 1999-1	Pennsylvania	2,420.0	Stranded Costs
Nov-99	West Penn Power, Ser. 1999-A	Pennsylvania	600.0	Stranded Costs
Apr-00	PECO, Ser. 2000-A	Pennsylvania	1,000.0	Stranded Costs
		<b>Total</b>	\$ 13,095.7	

Source: SEC Documents.

## 2001

- Energy Crisis/Enron – PG&E goes bankrupt – Securitization bonds perform without a hitch... no downgrade or even watchlist
- Texas issues securitization order but requires active and involved oversight of financing process to “ensure lowest cost of funds”

Date	Issue	State	Size (\$mm)	Purpose
Jan-01	PSE&G, Ser. 2001-1	New Jersey	2,525.0	Stranded Costs
Feb-01	PECO, Ser. 2001-A	Pennsylvania	805.5	Stranded Costs
Mar-01	Detroit Edison, Ser. 2001-1	Michigan	1,750.0	Stranded Costs
Mar-01	CL&P, Ser. 2001-1	Connecticut	1,438.4	Stranded Costs
Apr-01	PSNH, Ser. 2001-1	New Hampshire	525.0	Stranded Costs
May-01	WMECO, Ser. 2001-1	Massachusetts	155.0	Stranded Costs
Oct-01	CenterPoint Energy, Ser. 2001-1	Texas	748.9	Stranded Costs
Oct-01	Consumers Funding, Ser. 2001-1	Michigan	468.6	Stranded Costs
		<b>Total</b>	\$ 8,416.3	

Source: SEC Documents.

## 2002 - 2003

- Vermont passes cost mitigation statute for power purchase buy-downs
- PG&E bankruptcy settlement - consumer groups now PROPOSE \$3 billion securitization to refinance new regulatory asset carried at WACC

Date	Issue	State	Size (\$mm)	Purpose
Jan-02	PSNH, Ser. 2002-1	New Hampshire	50.0	Stranded Costs
Jan-02	CPL, Ser. 2002-1	Texas	797.3	Stranded Costs
Jun-02	JCP&L 2002-1	New Jersey	320.0	Stranded Costs
Dec-02	Atlantic City Electric 2002-1	New Jersey	440.0	Stranded Costs
Aug-03	Oncor Electric 2003-1	Texas	500.0	Stranded Costs
Dec-03	Atlantic City Electric 2003-1	New Jersey	152.0	Stranded Costs
<b>Total</b>			\$ 2,259.3	

Source: SEC Documents.

## 2004 - 2005

- Financing method expands to uses other than “stranded” investments/costs
- New Jersey issues securitization for deferred balances

Date	Issue	State	Size (\$mm)	Purpose
May-04	Oncor/TXU Electric 2004-1	Texas	789.8	Stranded Costs
Jul-04	Rockland Electric	New Jersey	46.3	Deferred Balances
Feb-05	Pacific Gas and Electric	California	1,887.9	Refinance Regulatory Asset
Feb-05	Mass. Special Purpose RRB Trust	Massachusetts	674.5	PPC Contract Buydown
Sep-05	Public Service Electric & Gas	New Jersey	102.7	Deferred Balances
Sep-05	West Penn Power, Ser. 2005-A	Pennsylvania	115.0	Stranded Costs
Nov-05	Pacific Gas and Electric	California	844.5	Refinance Regulatory Asset
Dec-05	CenterPoint Energy	Texas	1,851.0	Stranded Costs
		<b>Total</b>	\$ 10,675.7	
		<b>Total All Deals</b>	\$ 36,342.5	

Source: SEC Documents.

## 2006 Estimate

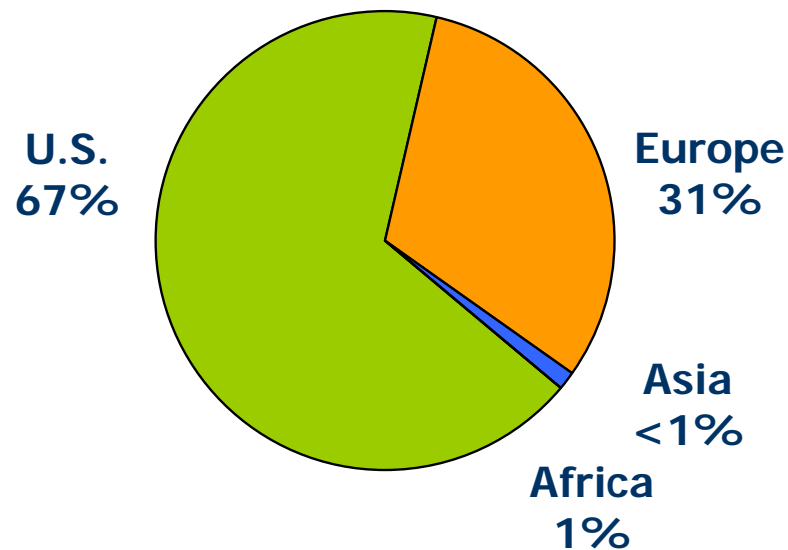
- Wisconsin and West Virginia apply method to environmental facilities
- Florida to use technology for storm recovery financing/reserves
- Idaho legislature authorizes securitization for any utility purpose up to 40% of balance sheet

Date	Issue	State	Size (\$mm)	Purpose
Pending	Wisconsin Electric Power	Wisconsin	450.0	Environmental Control
Pending	Allegheny Power	West Virginia	381.0	Environmental Control
Pending	JCP&L	New Jersey	300.0	Deferred Balances
Pending	AEP	Texas	1,300.0	Stranded Costs
Pending	Florida Power & Light	Florida	1,050.0	Storm Recovery
Pending	Gulf Power	Florida	150.0	Storm Recovery
<b>Total</b>			<b>\$ 3,631.0</b>	

**Source: SEC Documents, Proposal Requests.**

## Bonds begin to Attract International Investors

In December 2005:  
Texas Transition Bonds - 33% sold internationally...



TX: \$1.85 Billion CNP  
Series A



## But Ratepayer Savings are not Automatic

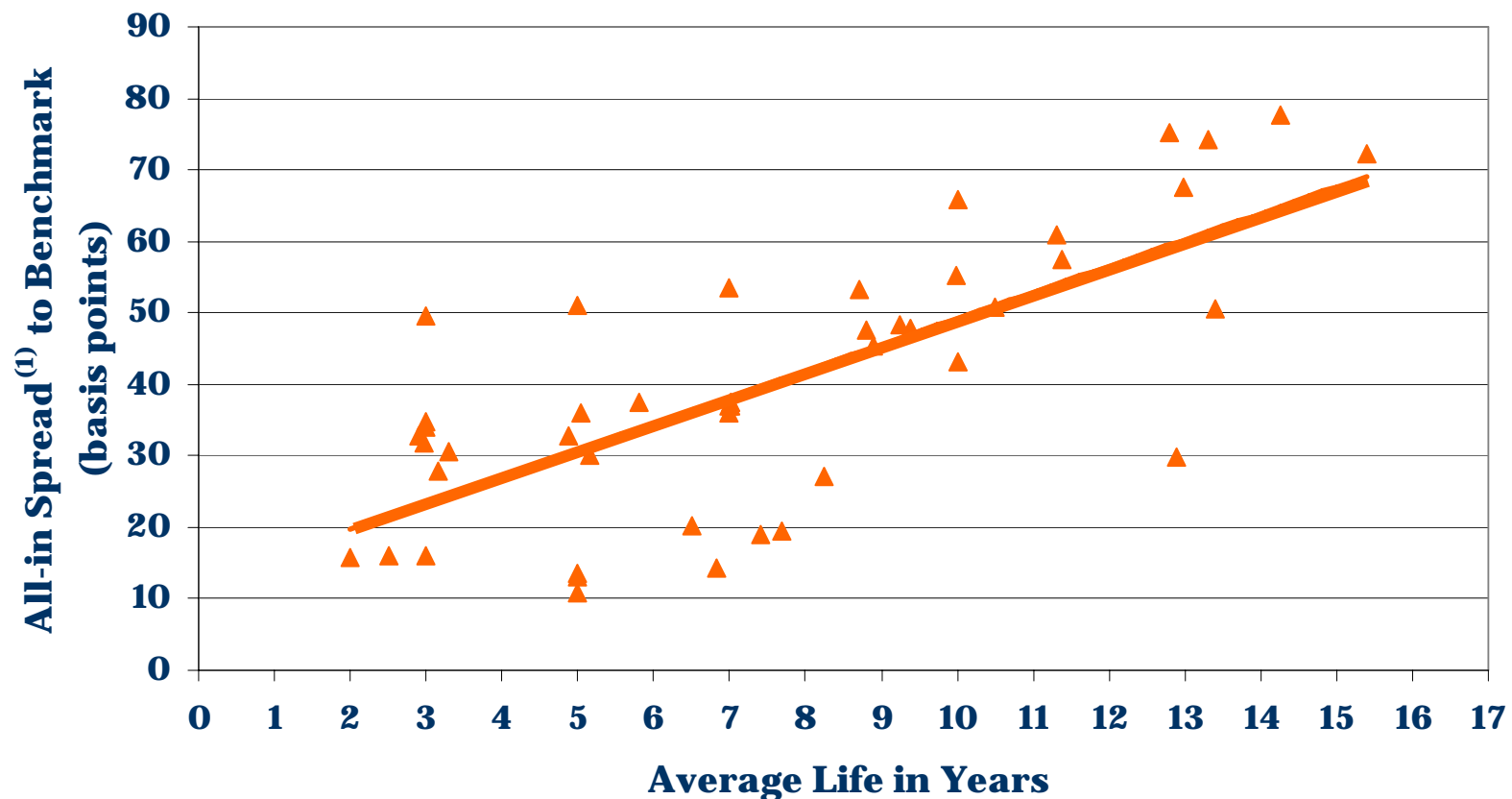
- **Irrevocable Order? No post-financing review or adjustments**
  - Closer consideration of prudence, eligibility for securitization
- **Up-front transaction costs, interest rate: every dollar a ratepayer dollar**
  - More involved Commission and Staff and cooperation with utility throughout financing process
- **High Transaction Costs?**
  - Commission with state-wide, ratepayer perspective and leverage
  - Programmatic, state-wide approach keeps costs low versus application by application

## But Ratepayer Savings are not Automatic

- **Lowest Possible Bond Rate, Fees and Other Costs?**
  - Wall Street always looking for a bargain - doesn't want to pay full value if it can
  - Requires cooperation between Commission and Utility. Activist Commission/Staff/Utility with Wall Street in all negotiations with financial service providers, counsel, investors and others
  - Active vs. Passive makes substantial difference in ratepayer costs

# Difference Active PUC Makes in Pricing

Securitization Pricings  
Non-Activist PUC Deals Since 2001

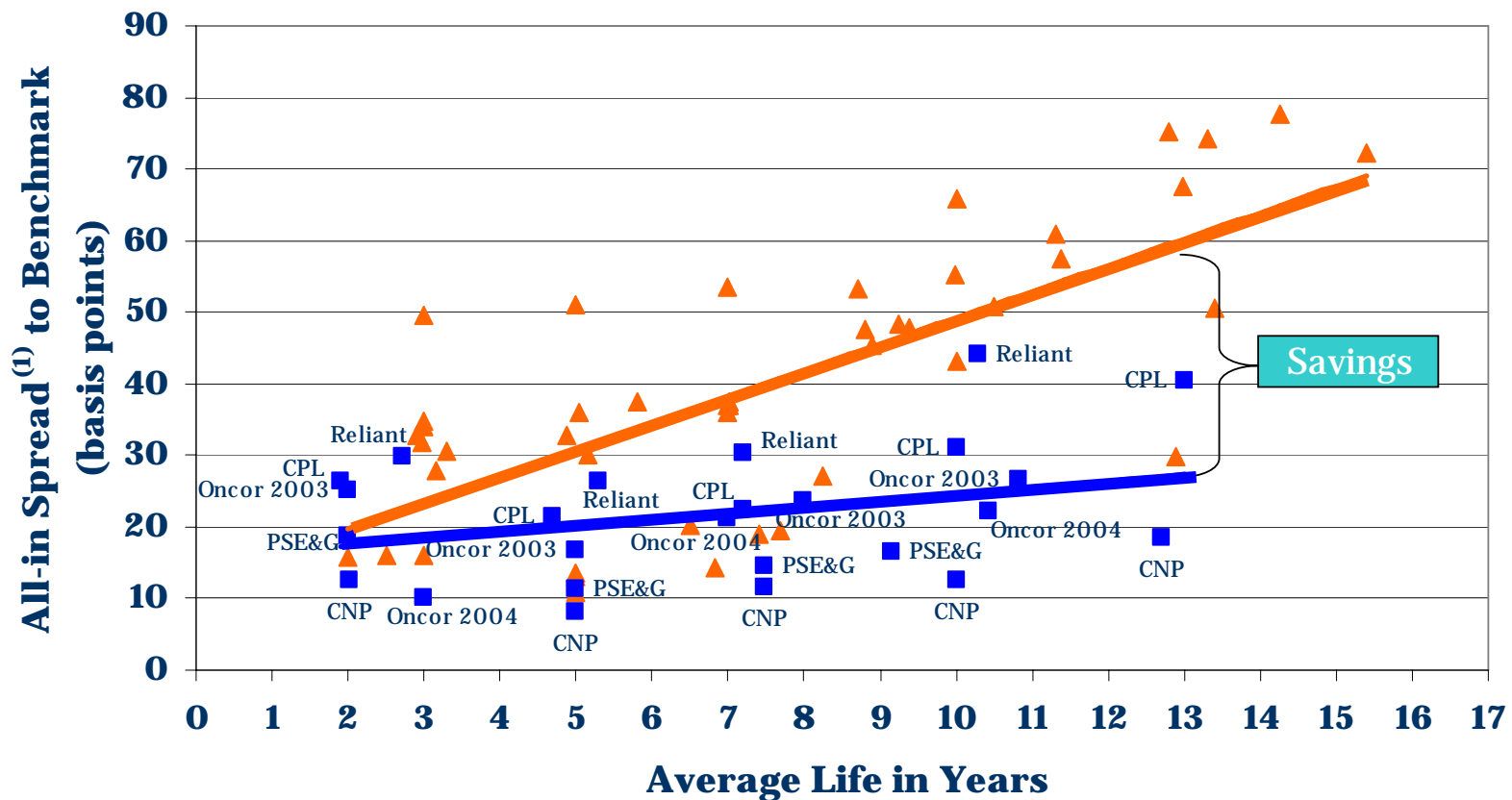


Source: SEC Prospectus, Bloomberg. (1) All-in spread includes credit spread, underwriting and structuring fees, if any.

# Difference Active PUC Makes in Pricing

Passive █  
 Activist PUC with FA █

## Ratepayer Savings from Pricing Activist PUC Deals vs. All Others Since 2001



Source: SEC Prospectus, Bloomberg. (1) All-in spread includes credit spread, underwriting and structuring fees, if any.

## Going Forward: Policy Questions/Steps for a “New” Financial Tool

- Step One:  
**Where can securitization be used? (utility infrastructure, government mandated costs) Commissions can be proactive.**
- Step Two:  
**How can the transaction costs be minimized? Programmatic approaches, closer cooperation between Commission and utility.**
- Step Three:  
**How can the benefits to ratepayers be maximized and extended? Achieve lowest financing costs and potential positive balance sheet effect resulting in lower WACC for the utility**



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