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# Coal Plant Closure Bonds Gain Steam With Shift In Power Mix

By **Keith Goldberg**

Law360 (March 13, 2019, 7:24 PM EDT) -- A clean energy bill passed by New Mexico state legislators Tuesday allows utilities to issue ratepayer-backed bonds in order to close coal-fired power plants, and experts say the idea is gaining favor as a way for states to accelerate the transition from coal to cleaner electricity sources without soaking ratepayers in the process.

Under the bill sent to New Mexico Gov. Michelle Lujan Grisham's desk, Public Service Co. of New Mexico, the state's main utility, would be able to issue bonds to cover the costs of shuttering a coal-fired plant it co-owns. The bonds would be paid off by non-bypassable charges to PNM customers over a period no longer than 25 years.

One state north, Colorado lawmakers are moving along with a similar securitization bill to encourage the early retirement of the state's coal plants. Meanwhile, securitization bills have been recently introduced in states including South Carolina and Missouri, though they don't explicitly target coal plants.

Still, experts say the securitization path becomes more viable as coal-fired power grows more uneconomical and more states enact aggressive climate change and clean energy regulations.

“It makes sense, to the extent that there's going to be some big charge on utility customers in connection with abandoning or replacing coal-fired facilities pursuant to the regulatory mechanisms the utility deals with,” said Baker Botts LLP partner Tim Taylor, who represented utilities in the development of securitization laws in Texas and Louisiana. “It's the lowest cost to the customer and that's why these statutes have been put in place.”

Environmental groups eager to see coal-fired power rapidly replaced by renewables are also on the securitization bandwagon. The Sierra Club's Colorado chapter supports that state's bill, while Dave Rogers, the North Carolina representative for the group's Beyond Coal campaign in North Carolina, said he'd like to see that state's lawmakers explore a similar effort to deal with coal plants owned by Duke Energy Corp.

“The ratepayers would start to save money right away,” Rogers said. “It gives the utility an opportunity to invest in cleaner sources of energy and maintain their rate base if they recycle that capital into new investments.”

State-backed utility securitization isn't a new concept. There are already 21 states that have enacted utility securitization laws, according to Saber Partners LLC, a New York-based financial advisory firm that specializes in utility securitization work. Experts say they've generally been enacted for specific utility purposes, such as recovering the costs of stranded assets, storm recovery and installation of plant pollution controls.

But in 2013, Michigan authorized utility Consumers Energy to use securitization to cover the remaining value of several coal-fired and gas-fired generation units slated for early retirement. Two years later, Florida allowed Duke to issue $1.3 billion in bonds to cover the premature closure of its damaged Crystal River nuclear plant.

"I think you'll see more of it," Saber CEO and senior managing director Joseph Fichera said. "There's room to bring more of this product to market. Investors are looking for high-quality investments with duration."

It's hard to find many higher-quality, long-term investments than a utility bond backed by state law, experts say. Not only are the charges to ratepayers set in stone, but state regulators generally aren't allowed to interfere with the utility's rights to collect the charges and can adjust the charges to ensure the bond is fully paid off on time.

"It's a mechanism whereby the state regulator has the ability to take a lot of the credit risk out of the deal such that you get Triple-A-rated debt, which means it has a lower interest rate than if the utility was financing it off its balance sheet," said Akin Gump Strauss Hauer & Feld LLP partner Lucas Torres, who's worked on utility securitizations.

Which ultimately means lower costs for consumers compared to a utility financing a closure itself and rolling all of those costs into its rates, experts say.

Still, there are potential downsides to securitization. If a state securitization law gives utilities a complete free pass from regulators, they could be tempted to overvalue already uneconomic plants they're looking to close, knowing that ratepayers will have to pick up the charges regardless, experts say.

"There's a pretty strong incentive to gold-plate the exiting [power plant] stock, to pump up the value, so when the securitization for that plant comes, you get the most value," said Karl Rabago, a former Texas utility regulator who's now the executive director of Pace Law School's Energy and Climate Center.

There's also the question of what the utilities do with the money raised from the bonds. For clean energy advocates, a utility simply investing that cash into more fossil fuel generation, such as new gas-fired power plants, defeats the purpose of the securitization and leaves ratepayers facing a future bill for retiring those facilities.

"If it isn't done properly, it's a windfall for the utility and ratepayers are just exposed with the regulator sidelined," Fichera said.

Practical limitations also exist. Issuing bonds to fund plant closures only works when the utility itself owns the facilities, which limits the possibilities to states that haven't fully deregulated their power generation markets and still have vertically integrated utilities, experts say.

Then there's the matter of getting the utilities to buy in. As long as a plant is still economic, experts say a utility will be reluctant to securitize its closure, especially since the returns on those bonds will be less than those for keeping the plant as part of the utility's rate base, even if it ultimately closes or replaces the plant.

While Duke decided securitization was the best route for closing Crystal River in Florida, company spokesman Randy Wheeless told Law360 that Duke isn't considering making a securitization proposal to state legislators for its North Carolina coal plants.

It's a delicate balancing act for state lawmakers that decide to go down the securitization path in order to ensure ratepayers, utilities and potential bond investors get a fair shake, experts say. Tough questions include what assurances utilities should get for reinvesting in renewables or energy efficiency, as well as how to compensate communities and workers affected by plant closings.

"It's a bit of a political dance for legislators," Torres said. "Each region, each company, each plant probably has its own separate facts and situation that may or may not be supported by the political environment."

New Mexico's securitization plan calls for any retired coal plants to be replaced by more environmentally friendly electricity sources, as well as energy storage, and is tucked within a broad clean energy bill that, among other things, would require the state to generate all of its electricity from zero-carbon sources by 2045.

Meanwhile, Colorado's securitization bill would require a portion of the funds raised to be invested in communities affected by coal plant closures.

Rabago said coal's dwindling fortunes means states have more leverage to cut the most favorable deal they can to serve climate and ratepayer goals. Coal will make up just 25 percent of U.S. electricity generation this year and 23 percent in 2020, down from 39 percent in 2013, according to the U.S. Energy Information Administration. Meanwhile, 54 coal-fired units with a combined 16 gigawatts of generation capacity are slated for retirement by February 2021, according to data collected by the Federal Energy Regulatory Commission.

“The reason we're able to have this conversation is because everyone sees the writing on the wall,” Rabago said.

Experts say the best way to view utility securitization is as a tool for states to advance the conversation about how to shift from coal to cleaner electricity sources. It's a tool that is part of an overall decarbonization plan and one that states must use wisely, because every dollar raised is a ratepayer dollar, Fichera said.

"Securitization is like a breakfast of ham and eggs, where the chicken is involved but the pig is committed,” Fichera said. “The utility is involved but the ratepayers are really committed.”

--Editing by Kelly Duncan and Orlando Lorenzo.

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