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NOV 17 2015

BOARD OF PUBLIC UTILITIES
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STEFANIE A. BRAND
Director

November 17, 2015

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Via Hand Delivery

Irene Kim Asbury, Secretary
New Jersey Board of Public Utilities
44 South Clinton Avenue, 9th Floor
Trenton, New Jersey 08625-0350

**RE: In the Matter of the Petition of Atlantic City Electric Company
for Authority to Issue Up to \$300 Million of Long-Term Debt
Securities Pursuant to N.J.S.A. 48:3-9 (2016 – 2017)
BPU Docket No. EF15091078**

Dear Secretary Asbury:

Please accept for filing an original and ten copies of these comments filed on behalf of the Division of Rate Counsel ("Rate Counsel") regarding the above-referenced matter. Enclosed is one additional copy. Please date stamp the copy as "filed" and return it to the courier. Thank you for your consideration and attention to this matter.

*Case Mgmt
List Copied*

Background

On September 16, 2015, Atlantic City Electric Company (“ACE” or the “Company”) filed a Petition with the Board of Public Utilities (“BPU” or the “Board”) requesting authority to issue new long-term debt in the amount of \$300 million through December 31, 2017. The proposed long-term debt to be issued will have terms ranging from one to 40 years, depending on market conditions. The proposed new long-term debt could take many possible forms including First Mortgage Bonds (“FMBs”), senior secured notes, unsecured notes, tax-exempt debt or even bank loans. *Petition, paragraphs 6, 11 and 12.* The new long-term debt could be issued through public issuances or private placement, through underwriters or placement agents, as appropriate. *Petition, paragraph 8.*

The Petition includes a Market Yield Spread Table (Exhibit C) which identifies the maximum allowable coupon interest rate on the new long-term debt (relative to yields on U.S. Treasury debt of the same tenor) that would be permitted under the Board’s approval order. In the event current or anticipated market conditions change and the debt cannot be issued within the parameters of the yield spread table, the Company would request approval of an updated yield spread table from the Board before undertaking the issuance. *Petition, paragraph 10.*

On December 18, 2013, the Board granted the Company authority to issue up to \$300 million in new long-term debt through December 31, 2015. *I/M/O the Petition of Atlantic City Electric Company for Authority to Issue up to \$300 Million of Long-Term Debt Securities Pursuant to N.J.S.A. 48:3-9, BPU Docket No. EF13090843, December 18, 2013.* The Company issued \$150 million of long-term debt in 2014 (and none in 2015 to date) pursuant to this authority. *Response to RCR-3, Attachment 1.*

The requested \$300 million in new long-term debt is to be used to provide funds during

2016 and 2017 for the refunding of a maturing debt issue which will total \$2 million. The remaining \$298 million shall be used primarily to reduce short-term debt balances and fund the Company's construction program. As of September 2015, the Company's balance of short-term debt was relatively large, totaling \$225 million. *Response to RCR-10*. The net increase in the Company's long-term debt balance through 2017 would be about \$298 million if the entire authority is utilized. *Petition, paragraph 5*. The Company reports that its planned construction spending will total about \$645 million during 2016 and 2017 and \$910 million during 2015 – 2017. *Petition Exhibit A and Response to RCR-11*.

Notably, the Company's Petition includes a number of reservations and acknowledgments of Company obligations. *Petition, paragraphs 16 – 19*. For example, paragraph 18 states that Board approval of the Petition does not limit the Board's authority with respect to ratemaking, accounting or other regulatory functions in any future proceedings, nor does it limit the rights of Rate Counsel or Board Staff with respect to rate setting matters in the Company's next base rate case. Paragraph 19 states that Board approval of this Petition does not provide pre-approval of any costs relating to this transaction. Paragraph 25 states that the debt proceeds are to be used only for the explicit purposes identified in the Petition and not to fund corporate affiliates or affiliate transactions. In addition, ACE commits that none of the debt proceeds approved by this order shall be used to provide funding for the pending merger between parent PHI and Exelon Corporation. *Response to RCR-5*. The Company further acknowledges its obligation to achieve the lowest reasonable cost of capital and utilize a prudent mix of capital to fund its operations. *Petition, paragraphs 26 and 27*. Rate Counsel concurs with these reservations of rights and Company prudence obligations. ACE states that all of the approval conditions and reservations set forth in the BPU's last order approving long-

term debt issuances in Docket No. EF13090843 remain appropriate for the instant petition.

Response to RCR-8.

Discussion

A. ACE's Financing Status

In addition to the Petition, data responses to requests issued by Board Staff and Rate Counsel provide information on ACE's financial status, credit quality and recent experience with debt issues. ACE is presently rated by all three major credit rating agencies, Standard & Poor's ("S&P"), Moody's Investor Service ("Moody's") and FitchRatings. All three of the agencies assign ACE a corporate credit rating of medium to high triple B, and a designation as "Stable". The Company's secured senior debt is rated as low single A. *Response to BPU-3.* Moreover, all three agencies indicate that ACE is viewed as having very favorable business risk attributes (e.g., "excellent", according to S&P), with New Jersey regulation and the most recent base rate case orders viewed as being credit supportive. The Company participates in the parent company (PEPCO Holdings) \$1.5 billion credit facility, with ACE's sublimit being \$350 million, which extends to 2018. This serves as the backstop and support for the Company's commercial paper program. *Response to RCR-14.* The Company's total capital was \$1.791 billion at June 30, 2015 and on a pro-forma basis becomes \$2.089 billion with the proposed debt issues net of the scheduled redemption. *Response to BPU-1.* The response indicates that the Company's current capital structure (excluding short-term debt) has a common equity ratio of about 49 percent. The Company states that its target includes a capital structure with an equity ratio of 48 to 50 percent. *Response to BPU-1 and BPU-8.* This is consistent with the approved capital structure in the last two rate cases.

B. Rate Counsel Assessment of the Petition

The Company has identified in its Petition a need to issue \$300 million of new long-term debt during the next two years, which is a net increase in debt outstanding of about \$298 million due to \$2 million of maturing debt during the period. *Response to BPU-1*. The Petition states that this amount of net new debt is needed (along with other funding sources) to finance its capital expansion which will total about \$645 million during this time period and to reduce its short-term debt balances which temporarily finance construction.

Based on our review of the projected capital spending, scheduled debt maturities and financing needs of the Company, Rate Counsel does not object to the request for authority to issue \$300 million of new long-term debt through 2017. The specific type and terms of long-term debt to be issued and methods of issuance should be selected in a manner designed to minimize the costs to customers over the long term. In particular, the Company should take advantage of opportunities to finance with low-cost, tax-exempt debt, if and when such opportunities arise. While the Petition requests authority for tax-exempt financing, the response to RCR-4 indicates that the Company has no plans at this time to undertake such financing. In addition, the Company should investigate opportunities and be granted authority to redeem outstanding long-term debt prior to maturity if it is determined to be economic for the Company's ratepayers to do so. The Company's response to RCR-15 indicates that at this time no cost-effective refinancing opportunities have been identified but that this is an issue that is periodically reviewed by management.

The Petition seeks authority to issue new debt as either secured or unsecured, but it provides no basis for using the unsecured form. In fact, the Company acknowledges that the

secured debt would (all else equal) be less costly with an expected interest rate savings on the order of 30 basis points (i.e., 0.3 percent) under normal market conditions. *Response to RCR-9.* Consequently, Rate Counsel urges ACE to issue the authorized long-term debt in the form of secured debt rather than unsecured debt assuming doing so is practicable and would provide material savings.

Rate Counsel Conclusions

At this time, Rate Counsel does not oppose the requested authority to issue \$300 million in new debt to fund projected capital spending and the 2016 scheduled debt maturity, which along with retained equity will help to achieve a balanced capital structure. This should be undertaken using the conventional financing methods outlined in Paragraphs 6 and 9 of the Petition, but preferably using secured (as opposed to unsecured) long-term debt, as financial market conditions permit. In addition, while not discussed in the Petition, the Company should be authorized to undertake further debt issuances for purposes of cost-effective refinancing of outstanding debt if market conditions permit savings. (No such candidates for refinancing have been identified at this time by the Company even though the Company has a large amount of high cost and substantially above market long-term debt outstanding.) Despite expectations that the Federal Reserve will gradually increase short-term interest rates over the near term, conditions remain quite favorable for the issuance of long-term debt, given ACE's favorable credit profile.

Rate Counsel agrees with the various reservations, limitations, and acknowledgments of the Company's prudence obligations set forth in paragraphs 16-19 and 25-27 of the Petition, and these should be reflected in any Board Order of approval. In addition, Rate Counsel

accepts ACE's representation that none of the long-term debt proceeds will be used to fund the pending PHI/Exelon Corporation merger.

Rate Counsel recommends that the Order issued by the Board in this proceeding should retain the following conditions and customer protections that were reflected in the Board's Order in ACE's last financing case in Docket No. EF13090843. As noted above, ACE has stated that it accepts all of these approval conditions. *Response to RCR-8.*

1. This Order shall not be construed as directly or indirectly fixing, for any purpose whatsoever, any value of the tangible or intangible assets now owned or hereafter owned by Petitioner.
2. This Order shall not be construed as certification that the Debt Securities herein authorized will be represented by tangible or intangible assets of commensurate value or investment cost.
3. Except as previously set forth herein, this Order shall neither affect nor in any way limit the exercise of the authority of this Board or of the State in any future Petition or in any future proceeding with respect to rates, franchises, services, financing (including method of sale of securities), accounting, capitalization, or any other matters affecting Petitioner. Rate Counsel, Board Staff and any other parties reserve the right to examine the transactions authorized by this Order and their impact on rates in the Company's next base rate case.
4. This Order shall not constitute pre-approval or presumed approval of any costs associated with the Debt Securities. All such costs shall be subject to review for reasonableness in Petitioner's next base rate case.
5. This Order shall not affect or in any way limit the manner in which the Petitioner registers its securities with the SEC.

6. Petitioner shall provide Rate Counsel and the Board with a copy of its SEC registration statement for these debt issues, upon request.
7. Petitioner shall furnish the Board with copies of all executed indentures.
8. Whether the Debt Securities are sold publicly or in private placements directly to prospective purchasers, Petitioner shall not issue Debt Securities at coupon rates in excess of those that would result from the Market Yield Spread Table set forth in this Order. In the event that market conditions change, Petitioner may request Board approval to issue Debt Securities at coupon rates in excess of those that would result from the Market Yield Spread Table. Any such request shall be accompanied by Petitioner's statement of the basis or the rationale therefore. If the Board approves such request, ACE may issue Debt Securities at the revised rates.
9. The Debt Securities authorized herein shall not be redeemed prior to maturity without further Board approval unless to achieve cost savings or more efficient capital structure. Petitioner shall maintain the records and documentation necessary to demonstrate the prudence of any such redemptions.
10. The Debt Securities authorized in this docket shall be only for the purposes identified in the Petition. The Debt Securities shall not be used to fund any affiliate transactions, including the pending PHI/Exelon Corporation merger.
11. Petitioner shall undertake long-term debt financings in a manner that achieves the lowest reasonable cost of capital for its customers.
12. Petitioner is obligated to use a prudent mix of capital to finance its utility operations and investments.

13. The authority granted in this Order shall become null and void and of no effect with respect to any portion thereof which has not been exercised by December 31, 2017.

Notwithstanding our recommendations, Rate Counsel reserves all rights to take appropriate positions in current and future Board proceedings that involve the Petitioner. These provisions, if approved by the Board, will satisfy Rate Counsel's concerns that the customers of ACE will not be harmed by the granting of the debt issuance authority. It will also ensure that Board authority is limited to the transactions discussed herein and does not constitute approval of any specific assets or rate base valuations, nor does it authorize any specific ratemaking treatment or establish precedent with regard to approval of future financing petitions.

Respectfully submitted,

STEFANIE A. BRAND
DIRECTOR, DIVISION OF RATE COUNSEL

By:



Diane Schulze
Assistant Deputy Rate Counsel

DS/lg

C: Service List (via electronic and USPS regular mail)

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Authority To Issue Up To \$300
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Securities
Pursuant To N.J.S.A. 48:3-9 (2016 -
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BPU Docket No. ER15091078**

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