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BOARD OF PUBLIC UTILITIES
TRENTON, NJ

State of New Jersey

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October 23, 2019

Via Hand Delivery

Aida Camacho, 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
Public Service Electric and Gas Company
Pursuant to N.J.S.A. 48:3-7 and 48:3-9 for Authority,
from January 1, 2020 through December 31, 2021,
to Sell and/or Encumber Property and Purchase,
Issue and Sell Debt
BPU Docket No. EM19070774**

Dear Secretary Camacho:

Please accept for filing an original and ten (10) copies of comments of the Division of Rate Counsel's ("Rate Counsel") to Public Service Electric and Gas Company's ("PSE&G" or the "Company") petition filed with the Board of Public Utilities ("BPU" or the "Board") dated June 27, 2019 requesting authority to issue new long-term debt in the amount of \$3.2 billion from January 1, 2020 through December 31, 2021. Enclosed is one additional copy. Please date stamp the copy as "filed" and return it to our courier. Thank you for your consideration and attention in this matter.

CMS
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BACKGROUND

On June 27, 2019, the Company filed a Petition with the Board requesting authority to issue new long-term debt in the amount of \$3.2 billion from January 1, 2020 through December 31, 2021. The proposed long-term debt to be issued will have tenors ranging from one to 40 years and may be secured or unsecured, depending on market conditions.

On October 20, 2017, the Board granted the Company authority to issue up to \$2.5 billion in new long-term debt through December 31, 2019 plus additional long-term debt as needed for economic refinancings. (BPU Docket No. EF17050550) As of the date of the filing of the current Petition, \$2.1 billion of the new debt had been issued under this authority in the form of secured Medium-Term Notes (“MTNs”), with a total remaining authority of \$400 million remaining through the end of this year. *Petition, paragraph 4*. However, in response to Rate Counsel RCR-5, the Company stated that in August 2019 it had issued an additional \$400 million of MTNs thereby exhausting its total debt issuance authority under the October 2017 Board Order. Thus, the Company may not issue any further long-term debt during the remainder of this year.

The requested \$3.2 billion in new long-term debt is to be used to provide funds for “the financing of Petitioner’s physical plant and facilities, construction and/or other general corporate purposes” *Petition, paragraph 5* and, in addition, to redeem \$693.4 million in long-term debt that will become due at various times in 2020 and 2021. *Id. and Staff OE-1*. Hence, the net increase in the Company’s long-term debt balance through the end of 2021 if the entire authority is utilized would be about \$2,507 million. *Staff OE-2*. This is a very large net increase relative to the Company’s current long-term debt balance of about \$10 billion, as

shown in paragraph 3 of the Petition. The Company also requests authority to issue new long-term debt to redeem its outstanding debt if doing so can provide net savings, or if needed to efficiently manage its capital structure. *Petition, paragraphs 6 and 7.* New long-term debt issued to finance such discretionary redemptions (if any) would be in addition to the \$3.2 billion of new long-term debt issuance authority requested in the Petition. *RCR-10.*

The Petition seeks authority for the issuance of a very wide range of possible long-term debt securities and to use different methods of issuance. This would include Mortgage Bonds, debentures, medium-term notes, promissory notes “and/or other debt instruments or evidences of indebtedness, secured or unsecured”. *Petition, paragraph 5.* The Company also seeks the flexibility to take advantage of tax-exempt (or otherwise low-cost) financing available from state, local or federal agencies through the issue of new long-term debt to those agencies. *Petition, paragraph 11.*

The Petition further seeks Board authority for transactions or debt instruments that are unconventional or much less common than the type of debt the Company typically has issued in the past. The Company requests authority to issue long-term debt in market or negotiated transactions including “domestic and/or non-U.S. public sales, private placements, loans, swaps, puts, calls, multi-mode programs, secured receivables financings and other asset-backed debt transactions”. *Petition, paragraph 9.* The asset-backed transactions, which are further identified in Paragraph 18 of the Petition, could involve the creation of special purpose entities (“SPEs”) that would be subsidiaries of the Company. Under this potential arrangement, the SPE would be the owner of the asset and provide the Company with debt issuance proceeds. The Petition identifies no specific proposals to actually undertake these

unconventional financings, including asset-backed securities using SPEs, only a commitment to file the related documents with the Board at a later date and obtain a Board Order before the Company undertakes any such a transaction. *Petition, paragraph 18*. In response to Staff OE-23, the Company further explains that it has no plans to utilize asset-backed debt securities, and would not do so without first submitting a formal filing with the Board that would provide an opportunity for Board Staff and Rate Counsel to fully review any such proposal prior to obtaining Board authority and proceeding. The Company also acknowledges that it has not previously used such instruments or arrangements for debt issuance other than many years ago for stranded cost recovery. *RCR-6*.

DISCUSSION

A. PSE&G's Financing Status

In addition to the Petition, data responses to requests issued by Board Staff and Rate Counsel provide information on PSE&G's financial status and recent experience with debt issues. The major credit rating agencies rate the Company's secured long-term debt medium single A to low double A, indicating that the Company is considered to be financially strong and "stable" and with a very favorable business risk profile. Standard & Poor's ("S&P") assigns PSE&G a corporate rating of BBB+ due to its status as a subsidiary of Public Service Enterprise Group ("PSEG") whereas Moody's assigns it an issuer rating of A2. *Staff OE-16 Attachment*. The Company has a \$600 million credit agreement that extends essentially to March 2023, which serves as the backstop and support for the Company's commercial paper program. *Staff OE-17*. Exhibit 3 of the Petition indicates the Company's total capital was

\$20.184 billion at year-end 2018 and is projected to increase to \$27.019 billion year-end 2021, in accordance with its very large capital spending plan for gas, electric distribution, renewable resources and transmission utility operations. The Company projects total capital spending in 2020 and 2021 to total \$6.855 billion. *Petition, Exhibit 4.* In the Company's last base rate case, the ratemaking capital structure was set at 54 percent common equity and 46 percent long-term debt. The Company indicates that its current actual capital structure (at June 30, 2019) is nearly identical in equity percentage as compared to its last rate case with the equity ratio at 54.1 percent. *Staff OE-5.* Moreover, Exhibit 3 of the Petition shows a target capital structure through 2021 with a projected equity ratio of 54.2 percent. The Company asserts that this target or planning 54 percent equity ratio is needed in order to maintain its very strong credit ratings (i.e., medium single A to low double A for secured debt) and thereby a low cost of debt. *RCR-17.*

B. Assessment of the Petition

The Company has identified in its Petition a need to issue \$3.2 billion of new long-term debt during the next two years, which is a net increase in long-term debt outstanding of about \$2.5 billion due to \$693 million of maturing debt during the period. *Staff OE-2.* The Petition states that this amount of new debt is needed (along with other funding sources) to finance its capital expansion and to maintain its target capital structure and current credit ratings. This is supported by Exhibit 4, which is the projected "Sources and Applications of Funds" for 2020-2021. For this two-year time period, capital spending budget will be \$6.855 billion, which divided among transmission projects (about \$2 billion), renewable/EMP (about

\$1 billion), gas distribution projects (about \$2.1 billion) and electric distribution projects (\$1.8 billion). *RCR-21*. The Company provided its cash and financing needs over the 2021-2022 period in response to *RCR-20*. The response reports total capital requirements for those two years of \$6.855 billion for capital spend plus \$693 for funding maturing debt, or a total of \$7.548 billion. The Company projects for those two years that it will generate net cash flow from operations of \$4.348 billion. *Petition Exhibit 4*. Thus, the sum of the net cash flow from operations and the requested \$3.2 billion of debt issuance authority totals to an identical \$7.548 billion ($\$4.348 \text{ billion} + \$3.2 \text{ billion} = \$7.548 \text{ billion}$). Thus, assuming the accuracy of the Company's projection of its 2020 – 2021 net cash flow, it has demonstrated that the full \$3.2 billion of debt issuance authority is needed (and is adequate) to fully fund budgeted capital spending and maturing debt. Of course, this finding is based on the assumption that the Company's projection of its net cash flow of about \$4.3 billion is realistic, and the Petition does not provide much detail. However, to the extent that actual net cash flow differs from the projection (or alternatively, actual capital spend differs from the budgeted amount), the Company can manage any such positive or negative discrepancy through dividend payments to the parent, equity contributions from the parent and short-term debt borrowings. It should be noted that during the past five years, the Company has not made any dividend payments to its parent, and it has received equity contributions from the parent totaling \$575 million. *RCR-15*.

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 \$3.2 billion of new long-term debt through 2021. This requested amount is adequately

supported by the information supplied in the Petition and data responses. 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 time. Potentially, this could include the use of low-cost, tax-exempt debt, if feasible and if doing so can provide cost savings. We note that at this time, the Company does not anticipate tax-exempt debt being advantageous (see response to RCR-16), but market conditions could change. In addition, the Company should be granted authority to redeem outstanding long-term debt prior to maturity if it is determined to be economic to do so (i.e., would provide net savings for ratepayers). The response to RCR-11 indicates that at this time no cost-effective refinancing opportunities have been identified due to “make whole” provisions with its existing debt. However, that could change with market conditions, which is why such authority has been requested by the Company in the Petition. Consequently, the Company should periodically monitor opportunities to obtain net savings for customers through economic refinancing.

While Rate Counsel does not oppose the Company’s request for issuance authority for \$3.2 billion of long-term debt based on conventional debt instruments (i.e., MTNs, Mortgage Bonds, debenture bonds, tax-exempt financing through governmental agencies and promissory notes, as identified in Paragraph 5), the Petition also requests authority to utilize unconventional (or less commonly used) financings listed in Paragraph 9. This includes such items as interest rate swaps, calls and puts, sales of receivables, multi-mode programs and asset-backed securities using SPEs that would be subsidiaries of the Company, as described in paragraph 18 of the Petition. The Company has acknowledged that it does not anticipate using these instruments during 2021 and 2022, has not used them in the past (with a couple of

exceptions) and has only included them in the scope of the Petition for “completeness” in the event such instruments or features are justified by highly unusual market or other conditions.

In response to Staff OE-15, the Company acknowledges that it generally does “not utilize puts or calls in its debt issuances.” The Company expresses concern that the use of puts can create “liquidity risk” since it would allow bondholders to force PSE&G to redeem the bonds “when it may be challenging to access the markets.” Similarly, the Company in this same response questions the benefits of including call features in debt issuances since doing so could be costly. Despite the Company’s own cost and risk concerns about the use of puts and calls, and its acknowledged reluctance to employ such instruments, it is requesting such authority in its Petition. The Company indicates that it is including the possibility of using such instruments in its Petition as a matter of completeness in order to encompass all possible scenarios. *RCR-12(a)*. However, the Company has not employed such financial instruments or debt features during the past ten years (with the limited exception of the repurchase and remarketing option associated with tax-exempt debt). *RCR-12(b)*.

Similarly, the Company includes in its Petition asset-backed debt (through the potential use of SPEs) as part of the range of the financing strategies it may decide to use. The Company’s response to RCR-6(a) and (b) clearly states that at this time, it has no specific plans to utilize asset-backed debt and only included such in the Petition for completeness, i.e., “to present a comprehensive outline of all reasonably possible long-term debt financing scenarios”. *RCR-6(a)*. Moreover, the response to RCR-6(c) states that this form of financing has not been used by PSE&G in the past decade.

The Company's response to Staff OE-23 goes on to clarify that it would not actually seek to employ asset-backed debt without first obtaining a "further BPU Order" permitting it to do so. The Company in that response states that it understands the concerns of Board Staff and Rate Counsel and that the "process of obtaining such further Order should provide ample opportunity to resolve any additional questions or concerns." *Id.*

Rate Counsel finds the explanation and clarification of position in the Company's response to RCR-6 and Staff OE-23 to be helpful in resolving our concern regarding the potential use of asset-backed debt. In this Petition, the Company is not seeking authority or Board pre-approval for the issuance of asset-backed debt, but instead is informing the Board that this is a possible financing authority that, depending upon circumstances, it may choose to employ. However, it would not do so without first making a filing with the Board and receiving a Board Order that allows it to proceed. In such circumstances, Rate Counsel would be provided an "ample" opportunity to respond to such petition. Given this clarification, Rate Counsel does not object to the Company's identification of asset-backed debt as a possible financing scenario, subject to submitting a formal filing and formal Board approval during 2020-2021.

At this time, conditions in financial markets remain very favorable for the issuance of conventional secured MTNs, which has been the Company's past practice in recent years. The Company estimates that the current credit spread for MTNs, relative to Treasury securities, is 80 basis points for a ten-year MTNs and 100 basis points for 30-year MTNs. *RCR-7*. These currently estimated yield spreads are dramatically lower than the yield spreads requested in the Petition at paragraph 10 of 220 basis points for ten-year MTNs and 310 basis points for 30

year MTNs. Given current market conditions, with 30-year Treasury yields at about 2.0 to 2.5 percent, this suggests that the Company should be able to issue new 30-year MTNs at cost rates of about 3.5 percent or less. As the Company has noted, it is difficult to project with confidence what utility debt markets will be over the next two years.

RATE COUNSEL RECOMMENDATIONS

At this time, Rate Counsel does not oppose the requested authority to issue \$3.2 billion in new debt to help fund capital spending and scheduled debt maturities and to meet the Company's capital structure targets. Absent highly unusual market conditions, this should be undertaken using the conventional financing methods outlined in Paragraph 5 of the Petition, primarily secured (and preferably 10 to 30 year) MTNs, and caution should be exercised in the use of any less or unconventional methods listed in Paragraph 9 of the Petition. In addition, the Company should be authorized to undertake further debt issuances for purposes of cost-effective refinancing of outstanding high cost debt if market conditions permit net savings for customers. (No such candidates for refinancing have been identified by the Company at this time due to make whole provisions of the outstanding debt.)

Rate Counsel agrees with the Company that it should not proceed with an asset-backed debt program or SPE without first filing a petition and receiving Board authorization. This should only be in a docketed proceeding in which Board Staff and Rate Counsel have a full opportunity to investigate the request.

As a final matter, Rate Counsel notes that the Company appears to be targeting a relatively high equity ratio for capital structure purposes as compared to those approved for

New Jersey's other electric utilities. In response to RCR-17, the Company argues that this is needed in order to maintain credit metrics (per Moody's), and therefore its very favorable medium single A/ low double A secured debt rating. While achieving and protecting credit ratings is a valid corporate objective, Rate Counsel observes that this would come at the expense of potentially increasing the ratemaking cost of capital as compared with using a somewhat lower equity ratio. Rate Counsel's concurrence with the requested debt issuance authority in this Petition should not be construed as our endorsement of this relatively expensive capital structure target.

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 PSE&G's last long-term debt financing case in Docket No. EF17050550. The Company has stated that it has no objection to any of the conditions, information requirements and reservations of rights provided in the Board Order in that docket. *RCR-4*. These conditions, requirements and reservations are as follows:

1. Subject to provision ten (10) below, Petitioner may issue the New Long-Term Debt and refinance its Outstanding Long-Term Debt Securities without further Order of this Board, provided that such issuance is in compliance with this Order.
2. Petitioner shall issue the New Long-Term Debt solely for the purposes stated in the Petition and authorized in this Order, including as further clarified in provision fifteen (15) below.
3. Petitioner shall not issue MTNs at coupon rates in excess of the MTN Maximum Spread Table set forth in Paragraph 10 of its Petition. In the event that market conditions change, Petitioner may file with this Board an updated MTN Maximum

Spread Table for Board approval, accompanied by Petitioner's statement of the basis or rationale for the requested changes.

4. Petitioner shall telephonically notify the Chief Economist prior to its issuance of New Long-Term Debt, and shall furnish the following for informational purposes only: (a) principal amount or amounts of the New Long-Term Debt proposed to be issued and sold; (b) anticipated maturity ranges; (c) actual current yields of U.S. Treasury Securities; (d) range of estimated coupon spreads over U.S. Treasury Securities; (e) data, as available, with respect to recent sales of comparable debt issuances of other utilities; (f) the identity of any Government Authority to whom Petitioner issues New Long-Term debt as described in the petition, (g) the identity of any SPE; (h) anticipated material terms of the New Long-Term Debt, including redemption provisions; (i) any related pledges, transfers or sales of assets; (j) a summary description of the contemplated transaction and (k) other information relevant to assess the reasonableness of the expected sale of the New Long-Term Debt.
5. As promptly as practicable, after the issuance and sale of any New Long-Term Debt, Petitioner will provide the Chief Economist with the information Petitioner relied on in making its decision to sell, such as market data with respect to utilities with similar credit ratings that have issued comparable debt.
6. As promptly as practicable following the issuance of New Long-Term Debt, Petitioner shall file with this Board a statement describing the Transaction concluded, including: (a) the names of the agents, dealers, underwriters, purchasers, managers, institution and/or Government Authority with respect to any Government Financing; (b) principal amount, maturity date, interest rate (and the interest rate spread over comparable U.S. Treasury Securities), redemption provisions, security interest, and other material terms, including the pledge, transfer or sale of assets, and commissions; and (c) the use of proceeds.

7. Petitioner shall furnish this Board, as promptly as practicable following the issuance of New Long-Term Debt, a copy of the following: (a) all material agreements between the Petitioner and any Government Authority; (b) any agent/dealer/underwriter/purchaser/manager agreement; (c) each Indenture and/or Supplemental Indenture; (d) any UCC financing statement, security agreement and/or pledge; (e) all documents as executed and filed with other regulatory agencies relating to the New Long-Term Debt, and (f) all material agreements related to the Transaction.
8. With regard to refinancing to achieve cost savings or more efficient capital structure, Petitioner will, as promptly as practicable following the financing, provide to the Chief Economist a statement of the rationale for the Transaction and, if applicable, detailed analysis of the savings realized from each such financing.
9. The New Long-Term Debt 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 redemption.
10. New Asset-Backed Debt shall not be issued except pursuant to further Order of this Board.
11. This Order shall not be construed as a certification that the securities authorized to be offered for sale will be represented by tangible or intangible assets of commensurate value or investment costs.
12. This Order shall not affect nor in any way limit the exercise of the authority of this Board, or of this State, in any future petition or in any proceeding with respect to

rates, franchises, services, financing, capitalization, depreciation or any other matters affecting the Petitioner.

13. 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 to be owned by Petitioner.
14. Petitioner shall undertake long-term debt financings in a manner that achieves the lowest reasonable cost of capital for customers. This shall include an obligation by Petitioner to review from time to time opportunities for economic refinancing of outstanding long-term debt.
15. The proceeds of the long-term debt issuance shall be used only for the purposes identified in the Petition and not to fund Petitioner's unregulated operations or affiliates.
16. The Board's approval of the authority requested by the petition does not constitute pre-approval of any cost recovery from customers or set ratemaking. Petitioner's regulated capital structure and capital costs are subject to review in Petitioner's next base rate case or other appropriate proceeding.
17. Petitioner is obligated to use a prudent mix of capital to finance its utility operations and investments.
18. The authority granted in this Order shall become null and void and of no effect with respect to any portion thereof which is not exercised by December 31, 2021.

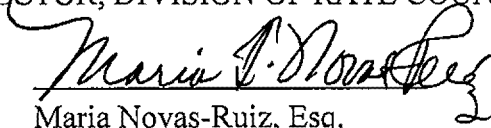
Notwithstanding our recommendations in these Comments, Rate Counsel reserves all rights to take appropriate positions in current and future Board proceedings that involve the

Petitioner. These provisions, if approved by the Board, will satisfy Rate Counsel's concerns in this docket at this time that the customers of PSE&G will not be harmed by the granting of the requested 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:


Maria Novas-Ruiz, Esq.
Asst. Deputy Rate Counsel

MNR/dl

C: Service List (via electronic mail and U.S. Regular Mail)

**In the Matter of the Petition of Public
Service Electric and Gas Company to
Sell and Encumber Property and
Purchase, Issue and Sell Debt**

BPU Docket No. EM19070774

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