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BEFORE THE PUBLIC UTILITIES COMMISSION

OF THE STATE OF CALIFORNIA

Application of Southern California Edison Company (U338E) for Authority to Securitize Certain Costs and Expenses Pursuant to Public Utilities Code Section 850 et seq.	Application 20-07-008

WILD TREE FOUNDATION
OPENING BRIEF

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In accordance with the provisions of Rule 13.11 of the Rules of Practice and Procedure of the California Public Utilities Commission ("Commission"), Wild Tree Foundation ("Wild Tree") respectfully files this opening brief opposing the Application of Southern California Edison Company ("SCE") for Authority to Securitize Certain Costs and Expenses Pursuant to Public Utilities Code Section 850 et seq. ("Application").

INTRODUCTION

The Commission should not ride roughshod over statutory and constitutional mandates intended to protect ratepayers in a rush to approve a financing order to meet a statutory deadline. It should deny SCE's application as incomplete as it lacks the basic information necessary to demonstrate compliance with Public Utilities Code sections 850 et seq. It should also deny the application because the paltry information that SCE has provided regarding the proposed

recovery bond demonstrates that its proposal is not, in fact, just and reasonable, is not in the public interest, and will not minimize ratepayer costs, as required by the Code. Following the denial of this application, the Commission should open a proceeding to establish a methodology for addressing the slew of securitization applications soon to be coming down the pipeline.

The Commission must make a number of findings that require development of a record and must engage in a detailed review of the bond terms to ensure that the issuance of bonds "would reduce, to the maximum extent possible, the rates . . . that consumers would pay as compared to the use of traditional utility financing mechanisms."[1] Once the bonds are sold the Commission gives up all further review of the recovery bond charge and cannot alter SCE's other rates for any reasons related to the financing order. Getting it right at the outset, therefore, is critical. Because the financing order will be irrevocable, it is necessary to ensure from the outset that clear standards and effective measures are in place to safeguard the interests of ratepayers.

A decision approving SCE's proposed recovery bond based upon the current proceeding schedule would result in a decision not in compliance with the law. The Commission statutory mandate to act within a stated time period does not serve to negate the application of constitutional due process or requirements of other statutes or regulations. If, within the time allotted by statute for a Commission decision it cannot ascertain whether the applicant has satisfied the statute's requirements, the Commission is obligated to reject the application

In this case, the Commission is tasked, for the first time, with interpreting and applying new law that will create far-ranging precedent effecting many billions of dollars of future securitized recovery bonds that will cost ratepayers $100's of millions. This decision will set precedent for at least $5 billion of securitizations under AB 1054 as well as additional unknown

[1] Pub. Util. Code, § 850.1, subd. (a)(1)(A)(ii)(III).

amounts for "the recovery of verified incremental undercollection amounts for calendar year 2020" pursuant to AB 913, should the governor sign the bill. The decision reached in this case will also likely lay the foundation for future decisions in PG&E's application for $7.5 billion bond to cover the costs of the death and destruction it wreaked when it starts multiple fires in 2017.[2] Regarding that case, President Batjer has stated that "My main interest…is to ensure we have sufficient information in the record" and "I expect it will be necessary to dig deeply into PG&E's proposed structure in order to fully understand the potential risks and benefits to the ratepayers."[3] Yet here, in this extraordinarily rushed process, whereby there is less than two months between the scoping memo and a decision, the Commission will not even begin to scratch the surface, much less dig deeply, into SCE's proposed structure.

The application should be denied as incomplete as it lacks basic information necessary for the Commission to make the determinations required by section 850 et seq. SCE has not determined what the material terms and conditions of the recovery bonds are and has not conducted requisite scenario analyses to determine what terms will minimize ratepayer costs. Such analyses would demonstrate, for example, that a longer maturity than SCE has proposed would save ratepayers approximately $30 million.[4]

Instead, SCE would have the Commission issue an irrevocable financing order based upon its plan to let the underwriters determine the material terms of the bonds after the Commission has approved the financing order. SCE's plan to rely upon "the advice of the underwriters" to meet the statutory "objective of reducing, to the maximum extent possible, the

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[2] Wild Tree notes that PG&E is not eligible for securitization pursuant to under SB 901 and D.19-06-027 yet is still pursing securitization.
[3] A.20-04-023, Prehearing Conference Transcript (June 18, 2020) at p. 7:9-14.
[4] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at pp. 13:12 – 14:4.

total cost of borrowing"[5] is unacceptable. Underwriters, by design have no fiduciary duty to ratepayers or the Commission and, in fact have adverse interests to the ratepayers.

If the Commission does not outright deny the application and instead moves ahead with approving a financing order in this proceeding, it must retain oversight over the structure, marketing, and pricing of the bond to ensure maximum ratepayer savings in accordance with AB 1054 rigorous standards. This can be accomplished in this proceeding by the approval of a financing order that establishes a pre-issuance review process utilizing a financing team comprised of the utility, the Commission and its staff, and independent experts.

The Commission need look no further than its own precedent in approving utility securitizations for justification for the establishment of a financing team and pre-issuance review process. In the Commission's most recent decision on an application for a securitized bond, the Commission relied upon a financing team in the same manner as suggested here.[6] Earlier this year, the Commission also established a financing team to review PG&E's interest rate hedges.[7] Given that the Commission has never reviewed an application for securitization under the standard of ratepayer cost minimization, best practices from other state utility commissions that have approved securitized recovery bonds similar to that at issue also provide valuable models. Best practices demonstrate that a pre-issuance review financing team process is the only option the Commission has, given the confines of sections 850 et seq., to meet the statutory mandate that ratepayer costs be minimized.

SCE would also have the Commission engage in a rulemaking in this proceeding. SCE elected to take the unusual step in applying for just a portion of the costs it intends to securitize

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[5] See Exhibit SCE-03, Transaction Overview (B. Pang) at p. 26.
[6] D.04-11-015.
[7] D.20-03-008.

and requesting that the Commission establish an advice letter process for future costs it would like to securitize. By seeking a decision approving such a process, SCE is requesting that the Commission engage in a rulemaking. The Commission should not undertake a rulemaking brought about in this fashion and should not attempt to engage in a rulemaking that could establish precedent regarding approval of billions in bonds absent any process or record. An advice letter process is entirely insufficient to meet the requirements of sections 850 et seq. and Commissions approval of such a scheme would set very poor precedent and should be denied.

ARGUMENT

I. RECOVERY COSTS MAY OR MAY NOT BE JUST AND REASONABLE

Scoping Question 1. Have the recovery costs sought to be reimbursed been found to be just and reasonable, in compliance with Public Utilities Code § 850.1(a)(1)(A)(i)?

Wild Tree was not a party to the proceeding or settlement upon which SCE claims the recovery costs were deemed just and reasonable and so does not take a position here whether SCE has met the requirements of Public Utilities Code section 850.1, subdivision (a)(1)(A)(i).

II. THE PROPOSED RECOVERY BONDS ARE NOT JUST AND REASONABLE, ARE NOT CONSISTENT WITH THE PUBLIC INTEREST, AND HAVE NOT BEEN DEMONSTRATED TO MINIMIZE RATEPAYER COSTS AND THE APPLICATION SHOULD, THEREFORE, BE DENIED

Scoping Question 2. Are the proposed Recovery Bonds just and reasonable, in compliance with Public Utilities Code §850.1(a)(1)(A)(ii)(I)?
Scoping Question 3. Are the proposed Recovery Bonds consistent with the public interest, in compliance with Public Utilities Code § 850.1(a)(1)(A)(ii)(II)?
Scoping Question 4. Would the proposed Recovery Bonds reduce consumer rates to the maximum extent possible compared to traditional utility financing mechanisms, in compliance with Public Utilities Code § 850.1(a)(1)(A)(ii)(III)?

A. SCE Has Not Provided Basic Evidence Needed to Demonstrate that the Proposed Recovery Bonds are just and reasonable, are consistent with the public interest, or will maximize ratepayer savings

The Code requires that the "issuance of the recovery bonds, including all material terms and conditions of the recovery bonds, including, without limitation, interest rates, rating, amortization redemption, and maturity, and the imposition and collection of fixed recovery charges as set forth in an application satisfy all of the following conditions:" be just and reasonable, be in the public interest, and maximize ratepayer savings.[8]

SCE has not determined what the material terms and conditions of the recovery bonds will be including interest rates, rating, amortization redemption, and maturity, and the imposition and collection of fixed recovery charges. SCE has not and cannot, therefore, demonstrate that the proposed recovery bond is just and reasonable, in the public intertest, or will maximize ratepayer savings. Instead, SCE would have the Commission approve its Application and issue a proposed financing order based upon its plan to let the underwriters determine the material terms of the bonds after approval of the irrevocable financing order with no Commission oversight. SCE says that it will update the Commission after the financing order is issued.

The plain language of the statute requires that the Commission be able to make a determination of the reasonableness of the material terms of the recovery bond and if the terms will create maximum present value savings for ratepayers. In this case, approval based upon SCE's proposed recovery bond would be done in the shadows, with the Commission not even knowing what the material terms will be until after it has made it decision, much less having conducted a thorough review of the terms and their impacts on ratepayers.

[8] Pub. Util. Code, § 850.1.

Wild Tree's expert, Steven Heller, a structuring agent for utility securitization transactions, has demonstrated that SCE has not provided the Commission the basic data or modeling it needs upon which it can base a decision on. The structuring agent should prepare analyses of timing of a transaction under different market conditions and different bond structures and requirements of the issuer and commission to help the Commission make an informed decision regarding the securitization bond application.[9] Such modeling for a utility recovery bond securitization to compare costs to the ratepayer in alternate scenarios should include the following inputs:

- Long-term demand forecast by customer class to the expected final term of the financing
- Historical collection curve by customer class
- Targeted proceeds - how much money is to be raised including all recoverable expenses
- Allocation of financing cost by customer class
- Targeted term (maturity) of financing
- Targeted Settlement Date of initial offering
- U.S. Treasury yield curve and assumed pricing credit spreads for average lives of tranches of two years and up
- Historical demand variance - actual six month vs forecast six month[10]

To determine the greatest savings to ratepayers on a present value basis, this data should be used to set up an initial model that provides the required amount of financing that is paid back over the desired term using a charge per class determined by the model so that when applied to the demand forecast and collected at the pace of the collection curves for each class, allocates the cost of the financing across classes as required by the allocation provided.[11] Scenarios are then modeled based upon alternative inputs for targeted proceeds, cost allocation, and terms to

[9] Supplemental Testimony of Steven Heller on Behalf of Wild Tree at pp. 3:1 – 5:14.
[10] Supplemental Testimony of Steven Heller on Behalf of Wild Tree at pp. 4:13 – 5:3.
[11] Supplemental Testimony of Steven Heller on Behalf of Wild Tree at p. 5:4-14

determine the structure with the lowest all-in cost of funds. Over the course of the pre-pricing period of a bond offering, many deal structures will be analyzed repeatedly as benchmark U.S treasuries and credit spreads move around.[12] In this case, SCE has neither conducted such analysis nor provided the basic data needed for such a model.[13] In supplemental testimony it filed, last week, outside of this proceeding's schedule, SCE modeled only one timing scenario - a $337 million transaction today versus a $1.5 billion transaction two years from now. As discussed further below, that model and analysis is flawed and incomplete in many respects, most notably, the fact that SCE failed to calculate ratepayers costs on a present value basis, as required by section 850 et seq.

B. The SCE Analysis That Was Completed Does Not Prove That SCE Has Designed A Bond That Meets Any Of The Statutory Requirements

The modeling in SCE's Supplemental Testimony comparing two scenarios of a $337 million transaction today versus a $1.5 billion transaction two years from now with only two bond structures is fundamentally flawed in many respects.[14] First, contrary to the express provisions of AB 1054, SCE's analysis was not initially conducted to determine present value ratepayer savings to the maximum extent possible. SCE concluded that its phased execution strategy structure "would save customers approximately $23-53 million on a *nominal basis* over TURN's single, delayed securitization approach."[15] But, the required standard of the relevant statute is that the bond "would reduce, to the maximum extent possible, the rates on a present

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[12] *Ibid.*
[13] Supplemental Testimony of Steven Heller on Behalf of Wild Tree at p. 7:15-19.
[14] Supplemental Testimony of Steven Heller on Behalf of Wild Tree at p. 5:15-14.
[15] SCE Supplemental Testimony (September 14, 2020) at p. 1 (emphasis added).

value basis that consumers within the electrical corporation's service territory would pay as compared to the use of traditional utility financing mechanisms."[16] Only in response to intervenor discovery requests did SCE rerun this analysis on a present value basis. It concluded that its phased execution strategy would save ratepayers $12.4 - $28.3 million over a single, future transaction.[17] SCE has refused to disclose the interest rates publicly used for this analysis claiming it is confidential, third party propriety information. But, SCE has otherwise stated that the phased execution strategy is necessary because "major interest rate forecasts are showing that rates will be higher" by 2023.[18] SCE's principal rationale for its phased execution strategy is that interest rates are at historical lows, are likely to climb and that, therefore, it is "prudent to begin securitizing eligible costs as soon as possible in order to lock in the historically low interest rates to minimize costs for customers."[19] SCE's strategy of dividing up issuances over multiple periods may reduce "the impact of market volatility over time," as SCE claims,[20] but if SCE is worried about *climbing* interest rates, this benefit is offset by the risk that when additional amounts are financed, interest rates will have already climbed/ increased.[21] SCE wants the Commission to make a decision based on a prediction of higher interest rates and not on sound financial analysis. If SCE's phased execution analysis is conducted with a constant interest rate, then the phased execution strategy would cost ratepayers more than a single issuance.

Additionally, SCE's concerns about climbing interest rates still ignore the larger problem - it has not done an industry standard sensitivity analysis of its assumptions to determine whether

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[16] Pub. Util. Code, § 850.1, subd. (a)(1)(A)(ii)(III).
[17] TURN-SCE-003-Q1
[18] A.20-07-009, SCE Supplemental Testimony (September 14, 2020) at p. 1.
[19] A.20-07-009, SCE Supplemental Testimony (September 14, 2020) at p. 3 (emphasis added).
[20] *Ibid.*
[21] Supplemental Testimony of Steven Heller on Behalf of Wild Tree at p. 6:7 - 7:9.

other bond structures, such as longer scheduled maturities, even at higher interest rates would "would reduce, to the maximum extent possible, the rates on a present value basis."[22] Had SCE done so, it might have concluded that, even if it should not wait until 2023 to issue bonds for the full $1.575 billion of AB 1054 CapEx, it could match the size of issuances with the maximum amounts it could prudently spend at the earliest possible dates – even at the risk of somewhat higher interest rates between now and the last of its issuances. Finally, as discussed further below, SCE ignores the fact that the supposed savings from its phased execution strategy, even if proven correct, may well be outweighed by the increased costs to ratepayer if the recovery bond is are marketed solely as an asset-backed security or too short a maturity is used.

SCE also makes the wild claim that the mandated requirements of the statute must be "balanced" against the demands of underwriters and investors.[23] While acknowledging "that generally the longer the maturity of the bonds, the higher the present value savings to customers," SCE argues that "the bond maturity must be balanced with other important considerations."[24] Those considerations, SCE maintains, are "to ensure that the bond maturities chosen would result in the tightest spread possible and not result in a spread premium, inefficient pricing or lack of investor demand, SCE took into account a number of variables including investor maturity preference, size of potential investor base at each maturity, perceived investor liquidity, investor. risk appetite and historic and relative pricing comps at different tenors."[25]

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[22] Cal. Pub. Util. Code, 850.1.
[23] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at Attachment A:WTF-SCE DR #1 Q014a.
[24] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at Attachment A:WTF-SCE DR #1 Q014b.
[25] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at Attachment A:WTF-SCE DR #1 Q014a.

This argument suffers from three fatal defects. First, this rationale was not part of its case. Second, SCE never explains *how* it allegedly balanced these factors. Finally, these concerns are not relevant to compliance with AB1054, which directs that the applicant must "reduce rates to the maximum extent possible." SCE's "explanation" for ignoring present value considerations underscores why the Commission must get independent expert advice to examine the claims of SCE's underwriters as they "balance" their needs versus the ratepayers.

C. SCE's Reliance Upon its Advisor and Underwriters to Demonstrate Compliance with section 850 et seq. is Unreasonable

1. SCE Does Not Have An Interest In Striking The Best Deal For Ratepayers But Does Have An Interest In Finalizing Recovery Bonds As Quickly As Possible

SCE's proposal to rely entirely on "the advice of the underwriters" to meet cost minimization requirement is insufficient because this "advice" would come following the Commission's approval of the financing order and because there is an inherent conflict of interest between underwrites and ratepayers. Substantial amounts of consumer dollars will be "left on the table" in interest costs, fees and more without proactive oversight by someone with a direct duty to the real obligor in this transaction, the ratepayer.[26] Underwriters serve their own interests, not the interests of the issuers or the ratepayers who will have to pay. The critical distinction between the proposed recovery bonds and traditional debt instruments is the absence of the usual incentives for the utility to keep the borrowing costs down. Under SCE's proposed plan, for example, it will receive the same amount of money from the issuance of Recovery Bonds regardless of the level of interest rates or issuance costs, high or low. Further disincentivizing the utility, once the Commission approves the issuance, it gives up all further

[26] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at p 5:14-18.

review, insulating the utility from future scrutiny or disallowance of the costs even if they are later found to have been unnecessarily high.

SCE has not structured, marketed or sold a similar utility securitization bond in 23 years[27] and has never done so for a bond that meets the requirements that ratepayer present value savings be maximized. SCE's inexperience in this area is demonstrated by the unreasonable decision it has made in regards to selection of and reliance upon a structuring advisor and underwriters. In this case, SCE does not have an interest in striking the best deal for ratepayers. In contrast, in traditional financing, a utility has an incentive to issue bonds at the lowest possible interest rate because a lower cost of debt reduces the utility's financial risk and, other things being equal, can result in lower interest rates, higher earnings and ultimately the possibility of a higher stock price.[28] SCE acknowledges that they have a financial incentive to keep the interest of their traditional bonds as low as possible. Specifically, SCE admits that between cost of capital proceedings its earnings increase as the interest rate and underwriting fees of traditional utility debt securities decrease.[29] But in a Recovery Bond securitization like that at issue, the utility's ordinary incentives are not present because the entire risk falls on the ratepayer and the state. The interest paid on securitization bonds is collected directly from ratepayers by SCE for the SPE. In the case of under collection, the securitization bond holders can require ratepayers to make up the shortfall through the true-up mechanism; the utility company's earnings, dividends and therefore its stock price will not be affected.

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[27] See SCE, *Prospectus* (December 8, 1997), available at: https://www.sec.gov/Archives/edgar/data/1041856/0000898430-97-005206.txt.
[28] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at pp. 5:19 – 6:17.
[29] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at Attachment A: SCE-WTF DR#1 Q004.

Because the utility has no financial risk for the Recovery Bonds, the utility does not have the incentive to strike the best deal in the marketplace in negotiations with underwriters and investors.[30] SCE's principal financial objective in this transaction is to get the money from the bonds as quickly as possible. As Michael L. Noel, the former CFO of SCE has explained in regards to a similar application for securitization of a recovery bond, "[The utility's] highest priority in this transaction likely will be to get the issuance done quickly, with cost taking a lower priority."[31]

SCE would not have the Commission retain any oversight over bond terms other than to make a "yes/no" determination on the bond offering within four business days of the pricing of the bonds with only "updates" on what it has decided. As described above, SCE has not provided the basic information the Commission requires to make the many necessary determinations under sections 850 et seq. This extraordinarily rushed proceeding - whereby intervenors had one week to prepare testimony following the scoping memo and were not permitted any rebuttal testimony; evidentiary hearings have been denied despite glaringly obvious disputed issues of material facts; and a truncated comment period on a proposed decision is planned – is entirely insufficient to develop a record even if SCE had put the basic data on the record. Obviously, no record can be developed during the four days after pricing and the Commission will not, therefore, have the evidence upon which to make an informed decision regarding bond terms. The Commission cannot ensure that the statutory mandate to minimize ratepayer costs will be met unless, as proposed by SCE, the Commission essentially delegates its

[30] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at pp. 5:19 – 6:17.
[31] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at Attachment A: Florida Public Service Commission, Docket No. 060038-EI, *Direct Testimony of Michael L. Noel on Florida Power & Light Company's Proposed storm-recovery bond* (March 31, 2006) at p. 7:7-8.

decision making power to SCE's underwriters. If the Commission does not think the SCE bond offering fulfills California statutory requirements it has only two options: stop the entire transaction after it has been structured, marketed and priced or approve a transaction that does not fulfill the statutory requirements. This is a classic "Hobson's Choice" - the illusion of a choice with two bad outcomes.

A similar four day review period scheme has been proposed to this Commissions before and turned it down in favor of financing team review. In I.02-07-015, "PG&E propose[d] to submit its interest rate hedges as advice letters, subject to an extremely expedited and truncated review and approval process."[32] The Commission declined to modify the existing "financial decision-making structure" whereby "The Commission has vested authority to negotiate and place securities in the hands of its Financing Team. For the purpose of approving the interest rate hedges authorized by this decision, the Commission's Financing Team shall be the General Counsel and the Director of the Energy Division."[33] The proposed four day review period was most emphatically deemed unreasonable: "PG&E proposed a "death-march" schedule where it would file an advice letter leaving the Energy Division only four business days to review it. PG&E wanted its filing "deemed approved" if not rejected within those four days. Four days is simply inadequate for a thorough review and precludes meaningful review by other interested parties."[34]

Ensuring that the bond is structured correctly, at the outset, is therefore, critical. Once the bonds are sold the Commission gives up all further review of the Recovery Bonds charge and cannot alter SCE's other rates for any reasons related to the financing order. This situation

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[32] D.03-09-020 at p. 10.
[33] D.03-09-020 at p. 11.
[34] *Ibid.*

"represents an extraordinary relinquishment of future regulatory authority and a shifting of all economic burdens in connection with [these] Recovery Bonds from [the utility] to its customers."[35] Thus, because the financing order will be irrevocable it is necessary "to ensure from the outset that clear standards and effective measures are in place to safeguard the interests of consumers."[36] Instead of proposing a plan wherein the interest of ratepayers are safeguarded, SCE would have the wolf guarding the hen house, relying on the underwrites to ensure cost minimization for ratepayers.

2. SCE's Plan to Rely Entirely on Underwriters to Ensure Maximum Ratepayer Present Value Savings is Unreasonable Because Underwriters Represent Interests Adverse to the Ratepayers

Underwriters have an inherent conflict of interest in determining the cost of the bonds. SCE's proposal to rely entirely on "the advice of the underwriters" to meet cost minimization requirement is unreasonable because of the conflict of interest between underwrites and consumers. The interests of underwriters are fundamentally adverse to the interests of ratepayers; underwriters are motivated to negotiate for relatively high rates of interest so that their sales forces will be able to sell the bonds with the least effort, satisfying the desires of their investor clients for high interest rates.[37] Higher interest rates results in higher bond costs to be born by ratepayers.

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[35] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at Attachment A: Florida Public Service Commission, *Florida Power and Light,* FPSC Order No. PSC-06-0464-FOF-EI at p. 6.
[36] *Ibid.*
[37] See Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at Attachment A: Florida Public Service Commission, Docket No. 060038-EI, *Direct Testimony of Michael L. Noel on Florida Power & Light Company's Proposed storm-recovery bond* (March 31, 2006) at p. 7:7-8.

As discussed further below, in the last securitization bond approved by the Commission, the Commission utilized a Financing Team to make critical determination on the material terms of the bond, rather than leaving it up to an underwriter.[38] The overwhelming choice of state utility commissions since 2005 is for proactive oversight and involvement in structuring, marketing and pricing of ratepayer -backed bonds to protect consumer interests, instead of blind reliance on the post-financing order actions of underwriters.[39] This is because even underwriters with a track record of integrity and transparency must be expected to act in their own economic interests.

The underwriter's economic interest is in obtaining the *highest* yield for the bonds and in structuring a transaction for the quickest and easiest sale in the market at the lowest possible risk to their capital.[40] Indeed, they would prefer never to have to actually "underwrite" any portion of the bonds but instead sell all the bonds at the yield that is attractive to their customers not the utility's ratepayers. The higher the interest rate, the easier it is for the underwriters to resell the bonds, earn their full fee and move on to the next deal. Therefore, it is in the underwriters' economic interest to get a higher cost to make the sale easier to their customers, the ultimate investors.[41] Investors also want as high an interest rate as possible. And often investors – who are the main customers of the underwriter – are willing to write big checks and buy the bonds with as high a yield as possible from the underwriter. They use their large orders to drive the pricing to their desired levels. Underwriters are often happy to accommodate this because they

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[38] D.04-11-015.
[39] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at Attachment A: Chart of all investor owned-utility securitization financing orders from 2005 to present.
[40] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at pp. 8:1 – 11:22.
[41] *Ibid.*

need those same large investors to buy other deals from them and trade securities. Underwriter's motivation to act with speed[42] would thus be beneficial to SCE's efforts to have the bond process move as quickly as possible, but detrimental to ratepayers and adverse to the statutory requirement that ratepayer costs be minimized.

The underwriter's conflict of interest is well known. Under Dodd-Frank, an underwriter cannot lawfully be both the advisor to a state or local government on the structure, marketing and pricing of government bonds and also serve as the underwriter of those bonds.[43] While underwriters of private bonds are not subject to this prohibition, the inherent conflict is the same. Indeed, underwriters make clear in all written engagement agreements that they have no fiduciary duty to act in the best interests of those responsible for paying back the bonds. For example, a recent SCE underwriting agreement included the following acknowledgments: "The Company. . . shall be responsible for making its own independent investigation and appraisal of the transactions contemplated hereby, and the Underwriters shall have no responsibility or liability to the Company with respect thereto. Any review by the Underwriters of the Company, the transactions contemplated hereby or other matters relating to such transactions will be performed solely for the benefit of the Underwriters and shall not be on behalf of the Company."[44] SCE, in fact, admits that these acknowledgements are the "market standard and will appear in the underwriting agreements with the selected underwriters."[45]

SCE has made no demonstration that its plan to rely upon underwriters to ensure cost minimization is reasonable and the evidence weighs heavily against this scheme as unreasonable

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[42] See Supplemental Testimony of Steven Heller on Behalf of Wild Tree at p. 9:16-20.
[43] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at pp. 8:1 – 11:22.
[44] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at Attachment A: WTF-SCE DR#1 Q007a.
[45] *Ibid.*

and unworkable. SCE's response to the question, "how will SCE or the Commission determine that the information provided by the underwriters at the time of pricing meet the legislative standards reducing rate to the maximum extent possible and terms of the financing order?" is as follows:

> The underwriters will be made aware of the statutory standard imposed by Public Utilities Code § 850.1(a)(1)(A)(ii)(III) that SCE is bound to meet. They will hold each other accountable to help SCE meet the standard by virtue of the inherent competitive nature of the process to become part of the underwriting group. Further, SCE will require the underwriters to document what steps they have taken to obtain the optimal pricing of the recovery bonds. SCE will also require the structuring agent to document the same. SCE will make these documents available to the Commission.[46]

SCE is effectively saying – we will tell the underwriter what the standard is, make them write some things down, and then after all is said and done we will tell the Commission what the underwriters wrote down. Of course, at this point, the Commission will have no oversight over the irrevocable financing order and will be faced only with a Hobson's choice of "take it or leave it" in regards to the bonds as designed by the underwriters. SCE's plan ignores the fact that the underwriter is under no obligation to SCE, ratepayers, or the Commission; per SCE's agreement with the underwriter, SCE "shall be responsible for making its own independent investigation and appraisal of the transactions contemplated hereby, and the Underwriters shall have no responsibility or liability to the Company with respect thereto."[47]

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[46] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at Attachment A: WTF-SCE DR#1 Q007b.
[47] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at Attachment A: WTF-SCE DR#1 Q007a.

D. SCE's Use Of An Advisor That May Later Also Act As An Underwriter For The Same Transaction Is Not Reasonable

The fact that underwriters hold no fiduciary duty to ratepayers or state utility commissions has led commissions to conclude that the advice they receive should not be from financial advisors who also underwrite the utility's debt and equity with conflicting loyalties, but from those solely with a duty of loyalty and care to the commission and its ratepayers.[48] But in this case, SCE has apparently already selected Barclays to be both an advisor and underwriter in this case thus compounding the problem it has created by unreasonably relying upon underwriters in the first place. SCE states, "Barclays, as structuring advisor, will also assist in the preparation of expert testimony on proposed securitization and the analysis of the cost savings and cash flow modeling. As part of the group of underwriters to be chosen, Barclays will offer advice on marketing and pricing of the recovery bonds as one of a team of underwriters and it is in this capacity that the acknowledgement applies."[49]

As discussed above, SCE's plan to ensure cost minimization relies upon the underwriters holding "each other accountable to help SCE meet the [section 850.1(a)(1)(A)(ii)(III)] standard by virtue of the inherent competitive nature of the process to become part of the underwriting group."[50] Its not entirely clear what SCE means by this but, read any way, it makes no sense. How does the supposed competitive nature of the selection process in any way mean that underwriters will then hold each other accountable? Further, SCE has apparently already

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[48] See, e.g., Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at p. 10:11-15.
[49] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at Attachment A: WTF-SCE DR#1 Q007a.
[50] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at Attachment A: WTF-SCE DR#1 Q007a.

conducted a process to select Barclays as an underwriter and it was very much lacking in competition. Wild Tree's expert, Steven Heller, a structuring advisor with actual substantial experience working on utility recovery bond securitizations, unlike Barclays, did not receive a request for proposal ("RFP") from SCE to serve as structing advisor in this case.[51] The selection process for a structuring advisors and underwriter was combined with SCE requesting quotes for both services in the same RFP.[52] The RFP requests proposals to "clarify advisory v. underwriting fee structure" and asks "what portion of the advisory fee is creditable against the transaction underwriting?"[53] SCE / Barclays witness Chang stated "SCE reviewed proposals for the roles of structuring advisor and as a potential underwriter… Barclays is not precluded from being selected as an underwriter on the securitization."[54] SCE solicited advisors and underwriters in the same request for proposal and scored them on a combined score.[55] Clearly, SCE has contemplated having a joint advisory / underwriter despite the clear conflicts of interest that party has with ratepayers.

Furthermore, by design there is no impetus for the obligor in a ratepayer backed bond to create a competitive process.[56] The obligor needs to create a competitive process among underwriters and investors to achieve the greatest leverage in negotiations and therefore the lowest possible cost. But the nominal obligor in the securitization – the SPE owned by the utility

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[51] Supplemental Testimony of Steven Heller on Behalf of Wild Tree at p. 3:14-18.
[52] PAO-SCE-001-LMW Q003.
[53] *Ibid.*
[54] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at Attachment A: WTF-SCE DR#1 Q006a.
[55] *Ibid.*
[56] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at pp. 8:1 – 11:22.

– has the unfettered ability to pass all costs directly onto consumers. The real obligor – the ratepayer – doesn't get a say in that process under the SCE proposal.

SCE's approach as described by Barclays' witnesses fails to consider the importance of keeping the advisor separate from the underwriter even though Barclays has previously recognized the importance of this separation. Barclays undertook an analysis in 2005 that showed the Texas "best practice" deals with an independent financial advisor to the Texas commission produced lower costs to ratepayers than all other deals.[57] Barclay is either ignorant of its own study or intentionally responded to discovery requests in such a way so as to not produce the report. In response to a Wild Tree data request, Mr. Chang states that "Barclays has not produced any research reports specifically for investors on utility securitizations."[58]

E. Barclays has demonstrated its inexperience in utility recovery bond securitizations by making recommendation on the Bond Structure and Marketing that will not serve to minimize ratepayer costs

1. Marketing The Bonds As Asset Backed Securities Will Likely Increase The Cost To Ratepayers In Violation of Sections 850 et seq.

SCE / Barclays proposed structuring and marketing strategy could result in higher interest rates than necessary, thus increasing ratepayer costs in violation of section 850 et seq.
In particular, Barclays would structure the bond as an "asset-backed securities" within the meaning of SEC Regulation AB. Wild Tree's financial experts recommend that the recovery

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[57] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at Attachment A: Barclays, *Rate Reduction Bond and Credit Card ABS Spread Comparison* (May 2005).
[58] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at Attachment A: WTF-SCE DR#1 Q005e.

bond should not be characterized an "asset-backed security" within the meaning of SEC Regulation AB but instead marketed as a corporate bond.[59]

ABS are riskier than utility securitized bonds for many reasons and underwriters and investors demand higher credit spreads to benchmarks securities to be compensated for these risks.[60] An ABS is collateralized by a pool of assets, such as car loans, mortgages and credit card debt. The owner of an ABS faces credit risk because the principal amount of the asset pool is reduced when assets defaults.

In stark contrast, SCE's securitized utility bonds will be backed by "Recovery Property", which is the right to receive payments from a nonbypassable electric rate component. The owner of SCE's securitized bonds will not face the credit risk that owners of ABS must bear because a true-up mechanism will increase the Fixed Recovery Charge on SCE's customers' bills to make up for deficiencies caused by those who do not pay their bill. There is nothing like this in any asset backed security on the market.[61]

As a lower risk investment, there are a number of benefits to marketing a recovery bond as a corporate bonds.[62] An asset-backed securities cannot be added to the Bloomberg/Barclays U.S. Corporate Bond Index. Such listing can provide for a lower interest rate. Especially for tranches of SCE's proposed Recovery Bonds that have scheduled final maturity dates longer than 15 years, corporate bond structuring can help justify marketing and pricing them using U.S.

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[59] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at pp. 21:8 – 24:18; Supplemental Testimony of Steven Heller on Behalf of Wild Tree at pp. 11:1 – 13:22.
[60] *Ibid.*
[61] *Ibid.*
[62] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at pp. 21:8 – 24:18

Treasury notes and bonds as the benchmark securities. Charters of many mutual funds limit the portion of their portfolio that may be invested in asset-backed securities.[63]

SCE's own witness admits that "there are no other forms of ABS that have cash flows generated by property created by statute" and that "use a similar true-up mechanism as a form of credit enhancement."[64] Mr. Chang concedes that "utility securitization debt could be perceived as being more creditworthy compared to other forms of 'AAA'-rated ABS debt."[65] In so acknowledging he makes the case why SCE's recovery bonds should not be marketed as ABS – as less creditworthy, more risky investment than corporate bonds, interest rates will be higher and ratepayers savings will not be maximized.

2. Maturity

Barclays has recommended an 18 year maturity and SCE/Barclays have provided no evidence that this maturity would maximize present value savings to ratepayers as required. On the contrary, issuing securitized recovery bonds with different maturities than proposed by SCE could both promote inter-generational ratepayer equity and maximize present value ratepayer savings. Wild Tree's expert Aaron Rothschild estimates that ratepayers would receive an incremental present value savings of approximately $30 million or more if SCE's recovery bond is issued with a maturity of 30 years instead of 18 years.[66] With a longer maturity, the present

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[63] *Ibid.*
[64] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at Attachment A: SCE-WTF DR#1 Q005.
[65] *Ibid.*
[66] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at pp. 13:12 – 14:4.

value savings to consumers for the entire planned issuance of over $1.5 billion would be substantial.

The securitization structures presented by SCE's witnesses do not demonstrate that its proposal will reduce, to the maximize extent possible, the rates consumers will pay on a present value basis. As explained above, the structuring agent should prepare scenario analyses with different maturities to compare costs to the ratepayer in present value to help the Commission make an informed decision regarding the securitization bond application.[67] SCE has not conducted such modeling yet has unreasonably relied upon Barclays' recommendation of an 18 year maturity.

SCE witness Pang presented what was referred to as four structures and stated that they examined both shorter and longer maturities but, in essence, only two structures were examined.[68] One structure had a weighted average life of about 6 years and the other three structures had a weighted average life of about 10 years. The longest final scheduled maturity data Barclays examined was 18 years.[69] It appears that because Barclays insists on characterizing the bonds as asset backed securities of which there are few with maturities longer than 5-10 years, Barclays only altered the "classes" to have different weighted average lives but still the same maturity.[70]

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[67] Supplemental Testimony of Steven Heller on Behalf of Wild Tree at pp. 3:1 – 5:14.
[68] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at p. 12:1-13.
[69] See TURN – SCE Q003; PAO-SCE-001-LMW Q002 – Attachment 2, Structure 2, 3 and 4. The furthest maturity date provided was 11/15/2038.
[70] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at p. 12:1-13.

F. The Proposed Recovery Bond Will Not Maximize Ratepayer Present Value Saving As Mandated by Section 850 et seq.

SCE has not demonstrated that the bond "would reduce, to the maximum extent possible, the rates on a present value basis that consumers within the electrical corporation's service territory would pay as compared to the use of traditional utility financing mechanisms, which shall be calculated using the electrical corporation's corporate debt and equity in the ratio approved by the commission at the time of the financing order."[71] On the other hand, as explained above, the terms SCE has proposed (e.g. maturity, characterization as ABS, reliance on underwriters to minimize costs) clearly will fail to minimize costs.

SCE has not even attempt to demonstrate that it will meet the statutory mandate that the costs to ratepayers be minimized. Instead, it would have the Commission approve a financing order that would address costs to ratepayers solely through the underwriters, despite the fact that underwriters interests are adverse to ratepayers interests.

If the Commission does not outright deny the application as incomplete and failing to meet any of the mandates of 850 et seq. and instead moves ahead with approving a financing order in this proceeding, it must retain oversight over the structure and marketing of the bond to ensure that ratepayers costs are minimized. This can be accomplished in this proceeding by the approval of a financing order that establishes a pre-issuance review process utilizing a financing team comprised of the utility, the Commission and its staff, and independent experts. This is the only way that SCE can demonstrate in this proceeding that its bond will reduce, to the maximum extent possible, the rates on a present value basis.

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[71] Pub. Util. Code, § 850.1, subd.(a)(1)(A)(ii)(III).

III. IF THE COMMISSION DOES NOT DENY THE APPLICATION, IT SHOULD APPROVE A FINANCING ORDER ONLY IF THE FINANCING ORDER ESTABLISHES A PRE-ISSUANCE REVIEW PROCESS WHEREBY A FINANCING TEAM WILL MAKE DETERMINATIONS ON ALL FINANCING MATTERS RELATED TO STRUCTURE, MARKETING AND PRICING OF THE BONDS

Scoping Question 6. What are the required contents of a financing order?
Scoping Question 7. What continued reporting compliance is required?

If the Commission issues a financing order in this proceeding, it must establish continuing Commission oversight over the material terms of the recovery bond. There is no other way that SCE can demonstrate that the requirements of sections 850 et seq. can be met in this proceeding. This can be accomplished by including language in the financing order that sets-up a financing team composed of the utility, Commission and its staff, and any necessary outside financial and legal experts that will provide approvals of the material terms of the bond in a pre-issuance review process to create a bond with material terms that can meet the statutory requirements, in particular, minimization of ratepayer cost.

Critically, Commission precedent and nationwide best practices utilize a financing team pre-issuance review process for utility securitized bonds. While AB 1054 refers to these instruments as Recovery Bonds, they are also often called Ratepayer-Backed Bonds, or RBBs. The critical distinction between the proposed recovery bonds and traditional debt instruments is the absence of the usual incentives for the utility to keep the borrowing costs down. Under SCE's proposed plan, for example, it will receive the same amount of money from the issuance of Recovery Bonds regardless of the level of interest rates or issuance costs, high or low. Further disincentivizing the utility, once the Commission approves the issuance, it gives up all further review, insulating the utility from future scrutiny or disallowance of the costs even if they are later found to have been unnecessarily high.

Because the Commission loses later oversight of these bonds, it has essentially one shot to ensure that consumers are paying the lowest possible cost to the debt holders, consistent with AB 1054. And it only has one shot at the complex documentation, representations, warranties and indemnities offered by SCE. It is, therefore, critical then that the Commission focus on the best practices in its history as well as those developed by other state commissions that have been called upon to regulate financing arrangements under statutes similar to AB 1054.

A. Commission Precedent For The Use Of A Financing Team Pre-Issuance Review Process

The Commission has not issued many utility securitized bonds in the past; the last Commissions securitized bond decisions was in 2004 under a different statutory scheme. Public utility securitizations are relatively infrequent; there have been only 16 such transactions nationwide over the past 10 years, SCE has not structured, marketed or sold a securitization bond in 23 years,[72] and the Commission has not issued a financing order for a bond in about 16 years.[73] However, of the 16 transactions in the past 10 years, the vast majority - 14 transactions or 87.5% - have had active commission oversight, utilizing a financing team supported by independent financial advisors, with a pre-issuance review process for approving both final upfront - and most importantly to ratepayers - ongoing costs primarily, the interest rates and credit spreads on the bonds.[74] The Commission is about to face an onslaught of applications for securitized bonds under new law and this proceeding, thus, takes on outsized importance as precedent for the applications for billions of dollars of bonds the Commission will soon be ruling

[72] See SCE, Prospectus (12-08-1997), available at https://www.sec.gov/Archives/edgar/data/1041856/0000898430-97-005206.txt.
[73] A.04-07-032.
[74] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at p. 14:18 - 15:5.

on. Commission precedent provides the blueprint for this and future securitized bond applications.

The last time that the Commission issued a financing order for a securitized bond, it utilized a financing team, advised by an outside expert, in the securitization of costs related to PG&E's first bankruptcy.[75] The Commission established the financing team in D.04-11-015 through the following language in the financing order:

> Prior to the issuance of each series of Energy Recovery Bonds, the Bonds and the associated Bond transaction shall be reviewed and approved by the Commission's Financing Team consisting of the Commission's General Counsel, the Director of the Energy Division, other Commission staff, outside bond counsel, and any other outside experts that the Financing Team deems necessary. The other outside expertise may include, for example, an independent financial advisor to assist the Financing Team in overseeing and reviewing the issuance of each series of Bonds. The Financing Team's approval of each series of Bonds shall be evidenced by a letter from the Financing Team to PG&E. Any costs incurred by the Financing Team in connection with its review and approval of each series of Bonds shall be treated as a Bond issuance cost."[76]

The financing order permitted the bond issuance only following the issuance of "a certificate that states the Commission's Financing Team has reviewed and approved each series of Energy Recovery Bonds in accordance with this Financing Order.[77]

D.04-11-015 was based upon a less stringent standard than that at issue here – maximization of present value ratepayers savings was not required. The 2004 version of Public Utilities Commission section 848.1, subdivision (a) that states that the Commission may issue a financing order for recovery bonds if doing so "would reduce the rates on a present value basis that consumers within the recovery corporation's service territory would pay if the financing order were not adopted."[78]

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[75] A.04-07-032.
[76] D.04-11-015 at Financing Order, ordering paragraph 33.
[77] D.04-11-015 at Financing Order, ordering paragraph 73.
[78] D.04-11-015.

AB 1054's higher ratepayer protection bar makes it is even more important now that the Commission follow its own best practices and best practices developed by other state utility commission since it last considered a securitization application. That is, the Commission should establish a financing team supported by independent experts and a pre-issuance review process. The legislative standard applicable to this securitization and others to come is much clearer and more favorable to consumers than that applied in 2004. The AB 1054 standard that present value savings to customers must "reduce rates to the maximum extent possible . . . for present value saving" is the toughest standard ever applied by this or any other state utility commission.

While SCE acknowledges that the Commission employed an independent bond team in PG&E's last securitization, it says only that such protection isn't necessary because states now have experience with securitizations.[79] SCE argues that, "Given that Commissions across the country have gained experience using this type of financing and given that PG&E was in bankruptcy, potentially necessitating additional oversight, this level of oversight may not be needed here."[80]

But it was the experience of prior securitizations that led other state commissions to *use*, not eschew the financing team approach. And, the Commission has very recently issued a decision requiring this level of oversight.

In the Commission's March 2020 *Decision Authorizing Pacific Gas And Electric Company (Pg&E) To Enter Into Interest Rate Hedges In Connection With PG&E's Exit From Bankruptcy*, the Commission established a financing team review process. In that case, PG&E

[79] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at Attachment A: WTF-SCE DR#1 Q002b.
[80] *Ibid.*

proposed a process in "which PG&E will work collaboratively with a proposed Finance Team, which will consist of such representatives as the Commission may designate, including the Commission's General Counsel and Director of the Energy Division."[81]

The Commission found:

> Although certain parties question the Finance Team proposal, we find such a team staffed by the Commission's General Counsel and the Director of the Energy Division or their designated representatives appropriate. (The Finance Team may also include outside consultants and advisors retained by the Commission.) The Finance Team's role will ensure sufficient oversight of the process so that any exercise of PG&E's requested hedging authority does not prejudge I.19-09-016 or the Bankruptcy Court process. Further, this is identical to the process the Commission adopted in D.03-09-020 to avoid delay in the negotiation process, but also to ensure oversight. While several parties protest the Finance Team proposal, no party offers a different solution. The proposed regulatory process addresses the practical realties associated with evaluating, and potentially executing interest rate hedges in a short timeframe while also not proposing that PG&E exercise unilateral authority to execute interest rate hedges.
>
> We deny PG&E's request for the Finance Team approval to be deemed a determination of reasonableness. The Commission finds Finance Team review will promote the expediency and confidentiality sought by PG&E. However, this process limits stakeholder engagement. As discussed below in the Ratemaking Treatment section, a later reasonableness determination for hedging costs will permit stakeholder engagement. We believe this strikes a good balance given the parties' concerns.
>
> In granting PG&E the authorization to enter into hedging transactions, this authority is conditioned upon PG&E receiving approval to execute specific transactions from the Finance Team (as well as any required approvals of the Bankruptcy Court) and does not constitute any determination that the associated costs are reasonable or recoverable in rates. The relief granted in this Application in no way limits the Commission's authority to review PG&E's Plan in I.19-09-016. We further authorize confidential treatment of documents and information shared between PG&E and the Commission Finance Team.[82]

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[81] D.20-03-008 at p. 12.
[82] D 20-03-008 at pp. 13-14.

B. Proposed Financing Order Terms Based upon Commission Precedent and Best Practices

Wild Tree's experts have reviewed legislation authorizing securitizations and materials from all state commission proceedings that involved similar utility applications for orders authorizing the use of ratepayer-backed bonds similar to recovery bonds from 1997 to present; the language of and approval process for financing orders for securitization transactions in California and other states for investor-owned electric utilities; various securitization transactions' implementation agreements; Issuance Advice Letters ("IALs") submitted by the utility to their regulator after the recovery bond transaction; and the dockets of proceedings before this Commission including public testimony submitted by experts on the topic of securitization before this Commission.[83] Relevant financing orders, testimony, implementation agreements, and IALs can be found in Attachment A to the Direct Testimony of Aaron Rothschild on Behalf of Wild Tree. Based upon this expert review of precedent and best practices, Wild Tree recommend the that financing order include the following general principles. These recommendations are discussed further below and specific language is proposed in Appendix A:

1. Establish pre-issuance review process whereby all financing matters related to structure, marketing and pricing of the bonds including the selection of underwriters will be determined.
2. Creation of a Commission "financing team" that will include the utility and their advisors, the Commission and staff, and advisors with assistance from outside expert as joint decision makers.
    - The financing team will meet, discuss and decide on all financing matters related to structure, marketing and pricing of the bonds including the selection of underwriters.

[83] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at Attachment A.

- The financing team will negotiate with the underwriters. Underwriters are not, therefore, members of the financing team.

3. Commission retention of an experienced, independent financial advisor with a sole duty of loyalty and care to the Commission and ratepayers so that staff can meaningfully and actively participate in the financing process.
   - The advisor must not be an underwriter or participate in the sales or trading of SCE securities.
   - The advisor will be paid from bond proceeds as a financing cost the same as to utility advisors and underwriters.
4. Require SCE, the lead underwriter, and the Commission's financial advisor to provide written unqualified certifications in the issuance advice letter ("IAL") to the Commission within one business day after pricing that the structure marketing and pricing of the bonds reduce rates to the maximum extent possible by the SCE and book running underwriter.
5. Require the Commission's independent advisor to submit within 2 business days after pricing and after review SCE's certification and IAL, its own certification to the Commission verifying the certifications made by SCE or documenting and explaining any disagreements. If the Commission determines that all required certifications have been delivered and that the transaction complies with the financing order and other applicable law, the transaction would proceed without any further Commission action.
6. The Commission may issue a stop order within 4 business days of pricing. If it does nothing, the transaction can proceed to closing.

C. Best Practices from State Utility Commission's Decisions on Securitized Bonds Call for a Financing Team Pre-Issuance Review Process

The key best practices for recovery bond securitizations are exemplified by financing orders issued by the Florida Public Services Commission's in 2006 and 2015 whereby the Florida Commission utilized a financing team, termed a "bond team," that advised the commission on structuring the financing order, participated in the negotiation process with potential underwriters, and participated in the negotiation and drafting of agreements related to the securitization with fully accountable certifications required to be submitted in a rigorous issuance advice letter process.[84]

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[84] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at p. 15:6 – 16:10.

The Florida commission concluded that to "achieve a lowest cost to the consumer" and the "greatest customer protections" the commission should be "actively and integrally involved in the bond issuance [process]" and should secure the advice of experts who are independent of the underwriters and are able to evaluate proposals and structure the safeguards that will "ensure that the processes are competitive."[85] The bond team concept utilized in Florida included active involvement in the bond issuance by the Commission and its staff, the Commission's independent financial advisor and outside legal counsel as joint decision makers with the utility.

Other states have utilized similar bond or financing teams and pre-issuance review processes. For example, the Texas Commission included a similar provision as Florida establishing a bond team in 2001, 2002, 2004 and 2005 financing ordersand the New Jersey Board of Public Utilities utilized a negotiating team as part of the process to authorize securitized bonds related to stranded cost recovery in 2005. [86]

The recommended financing order principles address the issue of the inherent conflict in having the utility rely on the same entity to advise it on the transaction and to serve as underwriter and the inadequate incentive of the utility, given its insulation from risk, to drive the hardest bargain with the underwriter and maximize present value savings to customers. This is illustrated by the experience of the West Virginia commission in 2009. Underwriters in West Virginia advised the local utility seeking securitization authorization from the state's utility commission that, in the aftermath of the 2008 financial crisis it should enter into securitized bonds with a weighted average life of ten years. But acting on the advice and recommendation of

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[85] *Ibid.* Since 2005, the public service commissions in multiple states – Florida, New Jersey, Texas, West Virginia, Ohio, Maryland and Louisiana -- have issued securitization financing orders with similar provisions ensuring expert, independent oversight of the process.
[86] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at p. 15:6 – 16:10.

its own independent experts, the state commission approved, as part of a joint stipulation, a 19-year bond. That bond sold for the lowest credit spreads ever for a securitized utility bond of that duration and it maximized net present value savings to West Virginia consumers where the ten-year bonds recommended by the underwriter would not have. [87]

SCE and the special purpose entity (SPE) will enter into a servicing agreement under which the sponsoring utility will bill, collect and remit the securitized charge to a bond trustee for the account of the SPE. Like any other contracts for services, that servicing agreement will have provisions concerning performance, care, liabilities, and indemnities. Pursuant to best practices, the utility should indemnify ratepayers for any negligent acts. All these could affect ratepayers during the life of the securitized utility bonds. Yet, the servicing agreement is essentially between affiliated parties with all the liabilities associated with the agreements falling to ratepayers under the securitized charge and the true-up mechanism.

The financing order should not allow SCE to receive an economic windfall as a result of the time lag in assessing and collecting the charges, the SPE could have collected in excess of the bonds after the bonds have been paid off. This consumer protection can be achieved by crediting ratepayers after the last bonds are repaid. Regulatory oversight should be preserved concerning the servicing agreement and other transaction documents for the life of the securitized utility bonds. Ever-changing corporate structures need scrutiny by the Commission because capital markets are likely to change over the life of the bond. Other state utility commissions have retained this authority consistent with similar securitization statutes.

There will be a number of agreements that need to be developed associated with underwriting the bonds - legal, advisory, administrative. The primary agreement is the servicing

[87] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at pp. 19:12 – 20:7.

agreement. Without the use of a financing team, SCE could also receive a windfall from the annual servicing fee it will be permitted to collect. SCE proposes a Finding of Fact that "SCE should be authorized to charge an annual servicing fee of 0.05 percent of the initial Bond principal amount, plus out-of-pocket expenses (e.g., legal, accounting fees), which is a level estimated to cover the servicer's incremental costs and expenses in servicing the Recovery Bonds." Despite discovery requests seeking this very information, SCE has yet to provide the commission the basis for this estimate. On the contrary, there is no evidence on the record that SCE will not incur any incremental ongoing costs for the activities associated with the annual fee it proposed to collect - billing and collecting, remitting funds to the SPE, and developing charges The cost for these activities "are tightly bound with operations already performed by [the utility] in the normal course of business."[88] The best practice in this regard is to include a true up provision requiring the utility to treat any excess amounts recovered from servicing fees above its actual costs by crediting other customer rates i.e. not the recovery bond charge but other customer rates charged to the consumer.[89]

IV. THE COMMISSION SHOULD OPEN A RULEMAKING PROCEEDING TO DETERMINE THE APPROPRIATE METHODOLOGY FOR THE HANDLING OF SECURITIZATION BOND APPLICATIONS

Scoping Question 8. What are the appropriate procedures to establish for future such SCE financing order applications, in compliance with Public Utilities Code § 850.1(a)(1)(B)?

This decision will set precedent for many billions of dollars of securitizations under 850 et seq. that will cost ratepayers many 100's of millions of dollars. This includes, not just the $5 billion of securitization permitted under AB 1054, but potentially also the $7.5 billion PG&E has applied for in A.20-04-023 to securitize costs associated with the death and destruction PG&E

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[88] Direct Testimony of Aaron Rothschild on Behalf of Wild Tree at pp. 20:8 – 21:6

[89] *Ibid.*

caused by starting multiple fires in 2017, as well as "the recovery of verified incremental undercollection amounts for calendar year 2020" pursuant to AB 913, should the governor sign the bill.

Given the importance of the manner in which the Commission implements 850 et seq., the 120 day deadline for a ruling on a financing order application, and the fact that financing orders are irrevocable, the Commission should open a rulemaking to develop a methodology for securitization applications. Under no circumstances, however should the Commission engage in a rulemaking in this proceeding to establish an advice letter process, as SCE has proposed, for approval of any bonds. Such a process is woefully inadequate to make determinations of whether rate increases to cover bond costs are just and reasonable, within the public interest, and minimize ratepayer costs.

CONCLUSION

For the reasons stated herein and in Wild Tree's testimony, the application should be denied as incomplete and not meeting the requirements of sections 850 et seq. that it demonstrate that the recovery bond and all of its material terms are just and reasonable, in the public interest, and minimize ratepayer costs. If the Commission does not deny the application, it should approve a financing order only if the financing order establishes a financing team pre-issuance review process informed by Commission precedent and best practices.

(signature page follows)

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