153 FERC ¶ 61,263
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Norman C. Bay, Chairman;
Cheryl A. LaFleur, Tony Clark,
and Colette D. Honorable.

Jersey Central Power & Light Company	Docket Nos. ES15-40-000
Pennsylvania Electric Company	ES15-43-000
Metropolitan Edison Company	ES15-44-000

ORDER AUTHORIZING ISSUANCE OF SECURITIES

(Issued December 1, 2015)

1. On July 31, 2015, as amended on October 9, 2015, FirstEnergy Service Co. (FirstEnergy) filed an application pursuant to section 204 of the Federal Power Act (FPA)[1] on behalf of Jersey Central Power & Light Co. (JCP&L), Pennsylvania Electric Co. (Penelec), and Metropolitan Edison Co. (Met-Ed) (collectively, Applicants) requesting Commission authorization to issue short-term debt securities described below.[2] We will grant the authorizations, as discussed below.

I. Background

2. Applicants are public utilities that provide service to electric customers in portions of New Jersey, Pennsylvania, West Virginia, and Maryland. Applicants state that PJM Interconnection, L.L.C. (PJM) retains functional control of their transmission facilities, and operates those facilities pursuant to PJM's Open Access Transmission Tariff.

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[1] 16 U.S.C. § 824c (2012).

[2] *See* Application Under Section 204 of the Federal Power Act for Authorization to Issue Securities, Docket Nos. ES15-40-000, ES15-43-000, and ES15-44-000 (filed July 31, 2015) (Application). Amendments to the Application Under Section 204 of the Federal Power Act for Authorization to Issue Securities, Docket Nos. ES15-40-000, ES15-43-000, and ES15-44-000 (filed October 9, 2015) (Amended Applications).

3. Previously, in Docket No. ES14-9-000, Applicants were authorized to issue short-term debt which consisted of borrowings from either commercial banks, or other financial institutions, in aggregate principal amounts not to exceed the following: (1) $850 million for JCP&L; (2) $300 million for Penelec; and (3) $500 million for Met-Ed.[3] According to Applicants, the authority requested in the Application "will replace and supersede the authority granted by this Commission in Docket No. ES14-9-000 (December 18, 2013)."[4]

II. Application and Amended Applications

4. Applicants seek authorization to issue short-term debt securities, having a maturity of not more than one year, in aggregate principal amounts not to exceed the following at any one time: (1) $500 million for JCP&L; (2) $300 million for Penelec; and (3) $500 million for Met-Ed (Short-Term Debt Limits). The short-term debt securities will consist of Applicants' borrowing of funds from external sources, including borrowings from commercial banks, other financial institutions, or affiliates outside of the Utility Pool of FirstEnergy Corp.[5]

5. Applicants propose to issue short-term indebtedness through the utility pool of FirstEnergy Corp. (Utility Money Pool),[6] provided that aggregate short-term borrowings do not exceed the applicable Short-Term Debt Limits.[7] Applicants state that the interest rate for the short-term debt securities will not exceed the highest of the following:

> the highest of (i) the rate of interest per annum (rounded upwards by no more than 5 basis points) for the one-week, one-month, two-month, three-month, and six-month London Interbank Offered Rate (LIBOR) for

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[3] *See First Energy Serv. Co.*, 145 FERC ¶ 62,203 (2013).

[4] Application at 4.

[5] *Id.* at 2, 8.

[6] Commission-regulated entities are required to file their cash management agreements with the Commission. The information provided is used to aid the Commission in monitoring cash management programs. The rule is not in the nature of a regulation governing participation in cash management programs. Therefore, this order does not address a request for authorization to participate in a cash management program. *See Regulation of Cash Management Practices,* Order No. 634-A, FERC Stats. & Regs. ¶ 31,152 (2003) (Order No. 634-A).

[7] Application at 9.

> deposits in U.S. Dollars two business days before the date of issuance obtained through a nationally recognized service or publication such as the Money Rates Table in *The Wall Street Journal,* plus (ii) an applicable margin of up to 250 basis points; or
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> the Base Rate, plus up to 150 basis points; the "Base Rate" shall be the rate per annum equal to the highest of (i) the rate of interest published by *The Wall Street Journal* from time to time, as the "prime rate," (ii) the sum of up to 50 basis points plus the Federal Funds Rate in effect from time to time, and (iii) the rate of interest per annum (rounded upwards by no more than 5 basis points) for the one-month LIBOR rate for deposits in U.S. Dollars) on the date of issuance obtained through a nationally recognized service or publication such as the Money Rates Table in *The Wall Street Journal,* plus 100 basis points.[8]

6. Applicants state that the short-term debt securities for which it seeks authorization will be used to meet Applicants' working capital needs, to fund Applicants' day-to-day operations including funding loans to the Utility Money Pool, to reimburse obligations under letters of credit which may be issued on Applicants' behalf at some future date, and for other general corporate purposes of Applicants as permitted in its articles or certificate of incorporation.[9]

7. Applicants request authorization to issue short-term debt securities to be effective for the two-year period beginning December 19, 2015 through December 19, 2017. Applicants state that the short-term debt securities issued pursuant to the authorization requested in the Application will be subject to the four restrictions on such securities specified in *Westar Energy, Inc.*[10]

III. Notice of Filing, Interventions, and Protests

8. Notice of the Application was published in the *Federal Register*, 80 Fed. Reg. 47,483 (2015), with interventions and protests due on or before August 21, 2015. None were filed.

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[8] *Id.* at 10.

[9] *Id.* at 14.

[10] *Id.* at 1 (citing *Westar Energy, Inc.*, 102 FERC ¶ 61,186, at PP 20-21, *clarified*, 104 FERC ¶ 61,083, at PP 15-26 (2003)).

9. Notice of the Amended Applications was published in the *Federal Register*, 80 Fed. Reg. 63,758 (2015), with interventions and protests due on or before October 30, 2015. None were filed.

IV. **Discussion**

10. FPA section 204(a) provides that requests for authorization to issue securities or to assume any obligation or liability as guarantor, indorser, surety, or otherwise in respect of any security of another person shall be granted if the Commission finds that the issuance or assumption: (1) is for some lawful object, within the corporate purposes of the applicant and compatible with the public interest, which is necessary or appropriate for or consistent with the proper performance by the application of service as a public utility and which will not impair its ability to perform that service; and (2) is reasonably necessary or appropriate for such purposes.[11]

11. The Commission has explained that, in reviewing filings under FPA section 204, "the Commission evaluates a utility's financial viability based on a review of the financial statements submitted in the application and the utility's interest coverage ratio. An interest coverage ratio is a measure of the utility's ability to meet future debt and interest payments."[12] The interest coverage ratio is the sum of income before interest and income taxes divided by total interest expense.[13] The Commission generally requires that FPA section 204 applicants demonstrate, on a *pro forma* basis in accordance with its regulations, that net income will equal or exceed twice total interest expense. This is a screen test used primarily to provide the Commission with comfort that the financing authorized will not impair an applicant's ability to perform public utility service.[14] Nevertheless, the Commission has stated that whether or not an applicant meets this interest coverage screen does not by itself determine whether the Commission will

[11] 16 U.S.C. § 824c(a) (2012).

[12] *Westar Energy, Inc.*, 102 FERC ¶ 61,186, at P 15, *order on reh'g*, 104 FERC ¶ 61,018 (2003) (*Westar*).

[13] *Id.* at n.15.

[14] *Mont. Alberta Tie Ltd.*, 128 FERC ¶ 61,217, at P 16 (2009) (citing *Startrans IO, L.L.C.*, 122 FERC ¶ 61,253, at P 18 (2008) (*Startrans*)). The Commission has also described the interest coverage ratio as measure of a utility's ability to meet future debt and interest payments. *Westar*, 102 FERC ¶ 61,186 at P 15.

authorize or deny the application,[15] and the Commission has approved section 204 applications that have not met this threshold.[16]

12. In the Amended Applications, Applicants filed revised versions of Exhibits C, D, and E *pro forma* financial statements as of March 31, 2015. Exhibit E of the Amended Applications shows that Applicants have the following *pro forma* interest ratios: (1) 1.61 for JCP&L; (2) 1.35 for Penelec; (3) and 1.58 for Met-Ed. All ratios are below the Commission's 2.0 times interest coverage test.[17]

A. JCP&L

13. Applicants state that JCP&L's interest ratio falls below the Commission's benchmark of 2.0 as a result of several factors. First, JCP&L made a non-cash pension mark-to-mark adjustment of $198 million ($113 million nets of amounts capitalized) for the 2014 fiscal year to reflect the change in the fair value of plan assets and net actuarial gains and losses. Second, two March 25, 2015, decisions by the New Jersey Board of Public Utilities (BPU), combined, result in an overall reduction in JCP&L's annual revenues of approximately $34 million and annual storm amortization expense (non-cash) of $55 million, effective April 1, 2015.[18]

14. According to Applicants, JCP&L is wholly capable of meeting all of its financial and utility obligations for several reasons. First, Applicants state that JCP&L retains an investment grade credit rating on its long-term debt—"BBB-" by Standard & Poor's Rating Services and "Baa2" by Moody's Investors Service. Applicants explain that in direct response to the BPU on March 26, 2015, effective April 1, 2015, Moody's Investors Service affirmed JCP&L's senior unsecured rating and changed the company's rating outlook to stable from negative, citing the resolution of JCP&L's long-standing base rate case and storm recovery cases. In addition, Applicants note that Moody's Investors Service noted that a future downgrade for JCP&L was "quite unlikely." Applicants state that, as recently as August 18, 2015, JCP&L accessed capital markets, issuing $250 million in long-term debt at a coupon rate of 4.30 percent. Applicants note that BPU, in its order approving the recovery of storm costs, recognized the importance of JCP&L maintaining its investment grade credit ratings, stating:

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[15] *Startrans*, 122 FERC ¶ 61,253 at n.7.

[16] *See, e.g.*, *NorthWestern Corp*., 151 FERC ¶ 61,120 (2015); *ITC Great Plains, LLC*, 147 FERC ¶ 61,005 (2014); *Westar*, 102 FERC ¶ 61,186.

[17] *See* Amended Applications, Exhibit E.

[18] *See* Application at 11; JCP&L Amended Application at 2.

> The Company's credit ratings are BBB- from Standard & Poor's, and Baa2 from Moody's, the two major credit rating agencies. If Standard & Poor's downgrades the Company's debt, JCP&L's bonds would be rated as speculative, while a downgrade by Moody's would leave the bonds one notch above. Having a major New Jersey utility with bonds rated below investment grade sends a negative message to the investment community, which could in turn be counter-productive from a ratepayer standpoint. Given the capital-intensive nature of the utility business, customers rates would likely increase over time as a result of a downgrade-associated increase in the company's borrowing costs.[19]

15. Second, Applicants state that JCP&L has access to substantial liquidity, i.e., up to $600 million from its affiliates through a Utility Money Pool to fulfill its utility operations and financial obligations. In addition, Applicants state that JCP&L has obtained substantial liquidity from non-affiliates, in that it may, under its own name, borrow up to $600 million at any one time through March, 2019 under a fully committed revolving credit facility comprised of a syndicate of 29 banks. Applicants note that such revolving credit facility contains a financial covenant requiring JCP&L to maintain a debt-to-total-capitalization ratio of no more than 65 percent in order to borrow under that facility. Applicants state that this financial covenant measures the financial leverage of JCP&L and is intended to limit the risk to the bank syndicate of a default. Applicants state that JCP&L satisfies its financial covenant requirement, with debt-to-capitalization ratios of 48 percent in 2014, and approximately 49 percent in 2013, and expects to continue doing so going forward. In addition, the bank syndicate regularly monitors JCP&L's financial status, as JCP&L is required to provide audited financial statements annually together with unaudited financial statements on a quarterly basis, each accompanied by an officer's certificate certifying continued compliance with the financial covenant. Applicants note that JCP&L's continued participation in the syndicated revolving credit facility and its recent successful long-term debt issuance demonstrate the financial community's confidence in the company's ability to meet its financial obligations.[20]

16. Third, Applicants state that JCP&L's parent company, FirstEnergy, commits to ensuring that JCP&L continues to satisfy its utility and financial obligations. Applicants explain that FirstEnergy will make an equity contribution of $250 million to JCP&L on or before May 1, 2016 to support its retirement of $300 million in JCP&L senior notes, which are maturing on May 1, 2016. Applicants state that the retirement of these senior notes eliminates a $16.9 million annual interest expense obligation for JCP&L.

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[19] JCP&L Amended Application at 3-4 n.10.

[20] *Id.* at 4.

Applicants note that this expected annual interest expense savings, when offset against the potential $20 million in additional interest expense resulting from the issuance of the short-term debt securities as requested in this Application ($500 million at an assumed 4.00 percent coupon rate) would result in a net annual increase of interest expense of approximately $3 million.[21]

17. Fourth, Applicants state that JCP&L currently has, and will continue to have, sufficient liquidity to satisfy their incremental interest expense obligation. Applicants state that JCP&L historically has reported strong cash flows from operations, and expects to continue to have strong cash flows going forward. Applicants state that its rate base remains strong and JCP&L continues to grow its asset base, reporting growth in its utility plant over the past four years. Applicants note that, looking at Exhibit E, if JCP&L were to exclude the impact of the non-cash pension adjustment to net income and include the expected annual interest savings associated with the retirement of senior notes, it would have a *pro forma* interest coverage ratio of 2.68.[22]

18. Applicants state that the proposed issuance of short-term debt securities is reasonably required, necessary, appropriate and consistent with JCP&L's investment grade credit ratings and the proper performance by JCP&L of service as a public utility, including working capital, funding day-to-day operations, satisfying current maturities of existing obligations, and for other general corporate purposes. Applicants state that an example of the reasonableness, necessity, and appropriateness of JCP&L's request was their ability to issue short-term debt critical to the extensive repair and restoration efforts in 2012 and 2013 necessitated by the unexpected severe damage caused by Hurricane Sandy for which JCP&L ultimately spent in excess of $600 million to fully restore utility operations. Therefore, Applicants submit that the Commission should find that the proposed issuance of short-term debt securities will not impair JCP&L's ability to meet its utility and financial obligations.[23]

B. <u>Penelec & Met-Ed</u>

19. In addition, Applicants submit that Penelec and Met-Ed are wholly capable of meeting all of their financial and utility obligations for several reasons. First, Applicants explain that the Pennsylvania Public Utility Commission on April 9, 2015, effective May 3, 2015 approved a $90.8 million and $89.3 million increase in annual distribution rate revenue of Penelec and Met-Ed, respectively. Applicants state that because the rate

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[21] *Id.* at 5.

[22] *Id.*

[23] *Id.* at 5-6.

increase became effective May 3, 2015, the financial benefit of the rate increase is not reflected in their *pro forma* financial statements for the period ending March 31, 2015. However, factoring in such additional revenue in the *pro forma* financials would result in interest coverage ratios in excess of the 2.0 times threshold. Applicants claim that Penelec and Met-Ed began collecting under the new rate on May 19, 2015. Penelec and Met-Ed historically have reported strong cash flows from operations, and expect to continue to have strong cash flows going forward. Applicants state that the additional revenue resulting from the distribution rate increase, as well as Penelec and Met-Ed's continued strong operations, will help to ensure that they are able to meet their utility and financial obligations.[24]

20. Second, Applicants state that Penelec and Met-Ed retain investment grade credit ratings with Standard & Poor's Rating Service, and Moody's Investors Service on its long-term debt, indicating that it can access capital markets at attractive prices.[25]

21. Third, Applicants further state that Penelec and Met-Ed have access to substantial liquidity, i.e., up to $300 million for Penelec and $500 for Met-Ed from its affiliates through the Utility Money Pool to fulfill its utility operations and financial obligations. Applicants also submit that Penelec and Met-Ed have obtained substantial liquidity from non-affiliates, in that each may, under its own name, borrow up to $300 million at any one time through March 2019 under a fully committed revolving credit facility comprised of a syndicate of 29 banks. Applicant states that this revolving credit facility contains a financial covenant requiring Penelec and Met-Ed to maintain a debt-to-total-capitalization ratio of no more than 65 percent in order to borrow under that facility. Applicants state that this financial covenant measures the financial leverage of Penelec and Met-Ed and is intended to limit the risk to the facility of a default. Applicants state that Penelec and Met-Ed satisfy this financial covenant requirement, with debt-to-capitalizations ratios of 52 percent for Penelec and 53 percent for Met-Ed in 2014, and approximately 53 percent for Penelec and 52 percent for Met-Ed in 2013; Applicants expect to continue doing so going forward. In addition, Applicants state that the facility regularly monitors the financial status of Penelec and Met-Ed, through annual audited annual financial statements along with quarterly unaudited financial statements, each accompanied by an officer's certificate certifying continued compliance with the financial covenant. Applicants state that the continued participation of Penelec and Met-Ed in the facility demonstrates the financial community's confidence in the companies' ability to meet their financial obligations.[26]

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[24] Penelec and Met-Ed Amended Applications at 3.

[25] *Id.*

[26] *Id.*

22. Applicants state the issuance of short-term debt securities is reasonable, required, necessary, appropriate, and consistent with the proper performance by Penelec and Met-Ed of service as a public utility, which includes working capital, funding to day-to-day operations, satisfying current maturities of existing obligations and for other general corporate purposes. Therefore, Applicants request that the Commission find that the proposed issuance of short-term debt securities will not impair the ability of Penelec and Met-Ed to meet their utility and financial obligations.[27]

C. Determination

23. As noted above, in section 204 filings, the Commission typically utilizes an interest coverage ratio calculation in its evaluation of a public utility's financial viability, and generally requires an applicant filing under FPA section 204 to demonstrate, on a *pro forma* basis, that net income will equal or exceed twice total interest expense.[28] In this case, Applicants' *pro forma* interest coverage ratio is below 2.0. The factors identified by Applicants, however, provide the Commission with an alternative basis upon which the Commission may conclude that the proposed issuances of short-term debt securities will not impair Applicants' ability both to service the proposed securities and to continue to provide service as a public utility.

24. Applicants explain that JCP&L can meet all of its financial and utility obligations based on the following: (1) JCP&L's parent company will make an equity contribution of $250 million on or before May 1, 2016 to support its retirement of $300 million in senior notes which will eliminate a $16.9 million annual interest expense obligation for JCP&L, resulting in a net annual increase of interest expense of approximately $3 million; (2) JCP&L's parent company commits to ensuring that JCP&L continues to satisfy its utility and financial obligations; (3) access to liquidity from its affiliates through the Utility Money Pool; (4) borrowings under a revolving credit facility comprised of a syndicate of 29 banks; and (5) its rate base remains strong and it continues to grow its asset base, reporting growth in utility plant over the past four years.[29]

25. Additionally, Applicants explain that Penelec and Met-Ed have the ability to service their debt based on the following: (1) a distribution rate increase; (2) access to

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[27] *Id.* at 3-4.

[28] *See, e.g., Startrans,* 122 FERC ¶ 61,253 at P 18.

[29] *See, e.g.*, *Commonwealth Edison Co.*, 145 FERC ¶ 61,214 (2013), at P 18 (noting parent company's commitment to indemnify and hold Commonwealth Edison Co. harmless from charges to equity for the interest charges and penalties resulting from tax losses).

liquidity from their affiliates through the Utility Money Pool; and (3) borrowing under a revolving credit facility comprised of 29 banks.

26. We find, based on the facts set forth in the Application and Amended Applications, that Applicants have demonstrated that the proposed issuance of debt securities described in the Application: (1) are for a lawful object, within Applicants' corporate purposes, compatible with the public interest, and necessary, appropriate for, or consistent with Applicants' proper performance as a public utility, and will not impair Applicants' ability to perform that service; and (2) are reasonably necessary or appropriate for such purposes.

27. Accordingly, based upon the terms and conditions and for purposes specified in the Application, Applicants are authorized to issue the short-term debt securities in the following amounts: (1) $500 million for JCP&L; (2) $300 million for Penelec; and (3) $500 million for Met-Ed. The short-term debt securities will consist of borrowings from commercial banks, other financial institutions, and affiliates.

28. The interest rate for the short-term debt will not exceed the highest of the following:

> the highest of (i) the rate of interest per annum (rounded upwards by no more than 5 basis) for the one-week, one-month, two-month, three-month, and six-month LIBOR for deposits in U.S. Dollars two business days before the date of issuance obtained through a nationally recognized service or publication such as the Money Rates Table in *The Wall Street Journal*, plus (ii) an applicable margin of up to 250 basis points; or
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> the Base Rate, plus up to 150 basis points; the "Base Rate" shall be the rate per annum equal to the highest of (i) the rate of interest published by *The Wall Street Journal* from time to time, as the "prime rate," (ii) the sum of up to 50 basis points plus the Federal Funds Rate in effect from time to time, and (iii) the rate of interest per annum (rounded upwards by no more than 5 basis points) for the one-month LIBOR rate for deposits in U.S. Dollars) on the date of issuance obtained through a nationally recognized service or publication such as the Money Rates Table in *The Wall Street Journal*, plus 100 basis points.

29. In *Westar*, the Commission announced four restrictions on all future public utility issuances of secured and unsecured debt.[30] First, public utilities seeking authorization to issue debt backed by a utility asset must use the proceeds of the debt for utility purposes.

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[30] *Westar*, 102 FERC ¶ 61,186 at PP 20-21.

Second, if any utility assets that secure debt issuances are divested or "spun off," the debt must follow the asset and also be divested or spun off. Third, if any of the proceeds from unsecured debt are used for non-utility purposes, the debt must follow the non-utility assets. Specifically, if the non-utility assets are divested or spun off, then a proportionate share of the debt must follow the divested or spun off non-utility asset. Finally, if utility assets financed by unsecured debt are divested or spun off to another entity, then a proportionate share of the debt must also be divested or spun off. We will condition our authorization on Applicants abiding by these restrictions.

<u>The Commission orders</u>:

(A) Applicants are hereby authorized to issue short-term debt securities provided that the aggregate principal amounts outstanding will not exceed the following amounts at any one time: (1) $500 million for JCP&L; (2) $300 million for Penelec; and (3) $500 million for Met-Ed, at the interest rates stated in the body of this order.

(B) The authorizations for short-term debt securities are effective December 19, 2015, through December 19, 2017.

(C) The authorizations granted in this order are subject to the restrictions specified in the body of this order and the restrictions on secured debt as outlined in *Westar*.

(D) The authorizations granted in this order are without prejudice to the authority of the Commission or any other regulatory body with respect to rates, service, accounts, valuation, estimates or determination of cost or any other matter whatsoever now pending or which may come before this Commission.

(E) Nothing in this order shall be construed to imply any guarantee or obligation on the part of the United States with respect to any security to which this order relates.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.