Wealth of Information in Post-Issuance Utility-fee Deal Disclosures

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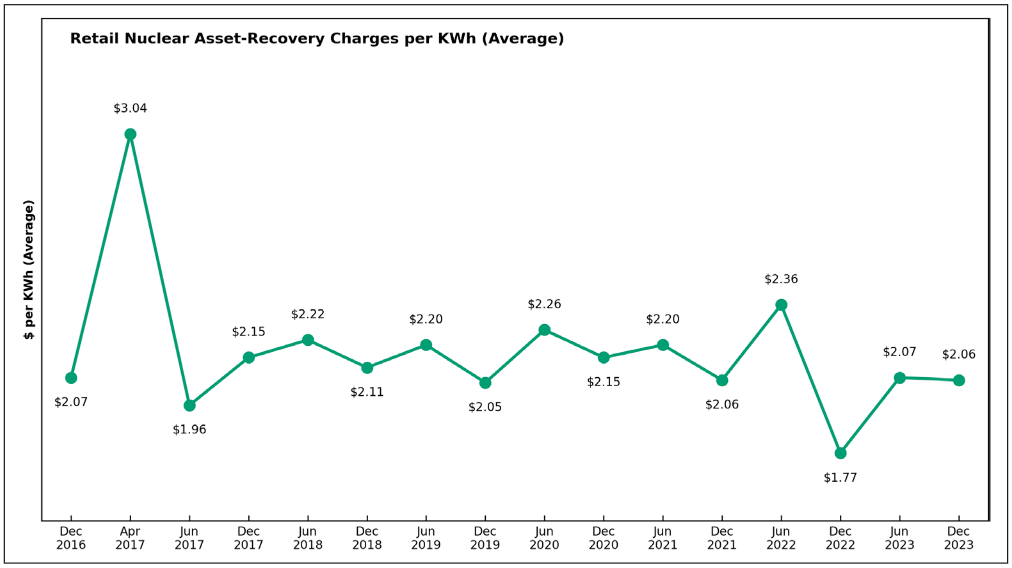
Utility-fee backed deal reporting shows how issuers implement the sector's unique true-up mechanism over the transaction's life. The reporting, which facilitates detailed deal surveillance, underscores how true-up adjustments provide what can be viewed as unlimited credit enhancement to outstanding bonds, essentially ensuring their full payment. Utility firms continuously adjust the securitized charges they impose on utility payers to make up for any under-collections in a remittance period. Over-collections will drive the charges lower.

The true up reporting also shows how firms deal with unexpected circumstances, in a way that does not disturb bond payments. For example, Duke Energy triggered an interim true up adjustment on its $1.3 billion Duke Energy Florida Project Finance LLC deal because of milder than forecasted weather, which decreased electric consumption. The utility increased its nuclear asset-recovery charge (NARC) to $3.04 per KWh from $2.07 because under-collections in a remittance period reached $20.4 million on a revenue requirement of $43.1 million (Figure 1). The NARC charges have remained relatively stable since the 2017 event, even showing a downward trend that supports ratepayer economics.

Figure 1. Duke Energy Florida Project Finance LLC Ratepayer Charges, 2016-2024



Source: Duke Energy Florida Project Finance and Academy Securities

Reporting Addresses Key Collateral Surveillance Aspects

The true up filings we reviewed are part of a comprehensive set of reporting packages that utility firms release on recovery bond deals per requirements in servicing agreements, Utility Commissions' Financing Orders, and SEC regulations. The firms may post the reporting on dedicated external websites, provide disclosures to deal trustees, or submit filings to the U.S. Securities and Exchange Commission (SEC) if required. As such, investors can review the reporting packages via a variety of platforms, including SEC's EDGAR database.

Beyond the true up adjustments, we found that the reporting packages provide a wealth of information that may be of interest to bondholders. The disclosures address several aspects we suggested investors examine as they analyze recovery bonds collateral:[1]

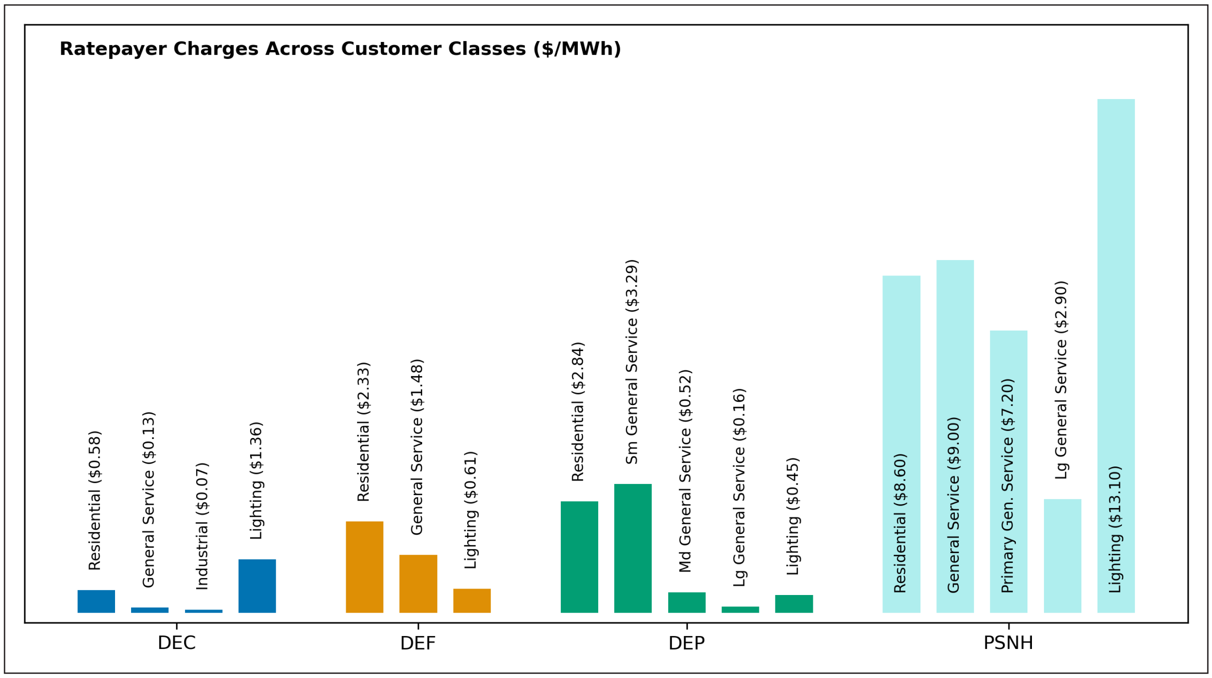
- **Collection variance and utility charge volatility.** True up calculations reveal the difference between deal revenue requirements and collections over time. The revenue requirement is comprised of bond principal and interest payments, and various deal expenses, including servicing costs. Deal collections include not only the utility charges but also revenues from capital reserve accounts, or previous over-collections. Anecdotally, we see under collections ranging from 1.46% to 7.76% on a few utility-fee deals we reviewed. The under- or over-collections lead to true up adjustments that servicers implement on an upcoming remittance period.

- **Charge adjustment frequency.** We find that deals vary in the scheduled frequency of true-up adjustments, as well as in the number of interim adjustments issuers/servicers triggered. For example, PSNH Funding LLC 3 makes annual adjustments. The deal has not seen interim adjustments since its issuance in May 2018. In turn, deals such as Duke Energy Carolinas NC Storm Funding and Duke Energy Progress NC Storm Funding make semi-annual adjustments. Both deals saw several interim true-up adjustments since their November 2021 issuance. In turn, servicers sometimes may also trigger "non-standard" true-up adjustments. For example, Entergy Texas triggers such adjustments when the forecasted billing units for one or more of the transition charge customer classes for an upcoming period decreases by more than 10% compared to the billing units (known as the threshold billing units), as deal filings note.

1 "Recovery Bonds: Diversifying Exposure Moves Beyond Disasters," Securitized Products Special Topics, Academy Securities, February 7, 2024

- **Charges vary by rate class.** The reports we reviewed show that the fee payer charges can vary across different customer types. In fact, rather than one uniform charge that deal issuance documents or rating agencies presales sometimes allude to, we see a wide range of charges. For example, in PSNH the initial charges range from $3.71/MWh on large-usage non-residential customers to $14.3/MWh on outdoor lighting usage. True-up implementations over the deal's life appear to adjust the specific charges of each customer class. Issuers/servicers may make those adjustments based on the composition of their customer base. True-up forms show the revenue requirements for each class based on their size. This may be particularly relevant for charges on residential customers. While there is limited concern over customers' motivation to make timely payments on their utility bills, onerous fees can drive performance issues, and potentially lead to political backlash, as we noted in a previous report. We see that the residential class charges sometimes fall in the middle of the charges range, but on some deals can represent the highest charge across classes (Figure 2).

Figure 2. Ratepayer Charges Across Customer Classes, $/MWh



Note: DEF - Duke Energy Florida Project Finance; DEP - Duke Energy Progress NC Storm Funding LLC; DEC - Duke Energy Carolinas NC Storm Funding LLC; PSNH - PSNH Funding LLC 3

Source: Deal Documents and Academy Securities

Academy Securitized Products Research Recent Reports

Securitized Products Special Topics:

Data Centers: Performance Wrinkles to Test Operators' Role

Recovery Bonds: Diversifying Exposure Moves Beyond Disasters

Investor Non-QM: Pockets of Value as Underwriting Tightens

Multifamily Prepays: Becoming Less Common, as Property Sales Drop

Device Payment ABS: Expect Stable Performance as Collateral Evolves

CRE CLO Mods: Rising Volume Not Immediately Telegraphing Distress

Aircraft ABS: Waterfalls Playing Catch-Up as Fundamentals Recover

Data Centers: Teakeaways from 2023-Vintage Deals

Litigation ABS: Tailwinds in Place for an Uncorrelated Segment

Agency Floaters: Adjusting Interest Rate Cap Escrows

Equipment ABS: Pick Your Spots Amid Diverging Collateral Trends

Commercial Solar ABS: Emergent Segment to Alleviate Headline Risks

Multifamily CRT: Limited Credit Risk on Synthetic Exposures

OC Triggers: Subtle Thresholds Come to the Fore As Collateral Stress Builds Up

Cell Towers: Lender-Friendly Features Dovetail with Secular Tailwinds

Timeshare ABS: Exposure to Favorable Hospitality Segments

Self Storage: Aspects to Watch as Performance Decelerates

Transitional Multifamily: Collateral Migration Away from CRE CLO Offers Different Deal Profile

Recovery Bonds: No Need to Closely Watch the Fed or the Economy Here

Affordable Mortgages: Fee Elimination Spotlights Convexity Profile

Investor Non-QM: Rental Exposure with Some Structural Twists

Data Centers: A Strong Segment Juggles ABS and CMBS

Small Balance Multifamily: Value Ahead of Slow Prepays

Future Funding: Potential Key Performance Driver as CRE CLO Pipeline Builds Up

Multifamily Prepays: Property Sales Trigger Paydowns

Manufactured Housing: Resilient Segment Amid Potential Multifamily Softness

Tender Offers: Expect More to Come, Though Not on a Predictable Schedule

NYC Multifamily: Rent Increases to Support Cashflows Amid Regulatory Restrictions

Housing at a Crossroads: Single-family and Multifamily Exposures

Senior Housing: Focus on Segment Selection Amid Pandemic Impact

Disaster Performance: Pandemic Forbearance Resolutions Bode Well for Future Stresses

Russian Sanctions Impact: Lease Terminations and Forced Property Sales

CMBS Credit Focus:

Loan Assumptions: Watch Waterfalls as New Borrowers Redevelop

Holdbacks: RENT in the Limelight, as Other Cases Brewing

Blanket NRAs: Shutting Down Advances Upends Credit IO Trades

Credit 2024: Workout Nuances Come to the Fore

Recovering the Non-Recoverable: Liquidation Nuance Bolsters Paydowns

Special Servicer Replacements: 1740 Broadway Crystalizes Implications

Crossgates Liquidation: Holdbacks Complicate Severity Projections

WODRA: Bond Cashflows Under Stress in Post-Mod Advance Recovery

Securitized Mezz: Workout Dynamics in Public Display

Dark Triggers: Nuances in Focus as Tenant Departures and Subleasing Pick Up

Upping Appraisals: Recovering Valuations Reverse Shortfalls

Non-Recoverable Advances: Unveiling a Rationale for a Key Decision

Excess Cash Allocations: Probing Advances on Positive Cashflowing Loans

Release Prices: Cherry Picking Across Office Portfolios, Sometimes at a Discount

Mezz Loan Sales: A Potential Headache for CMBS Workouts

Equity Pledges: Hotel Bossert Spotlights Dual Collateralized Loans

The Road to Conversion: Consider Office Ground Leases and ARD Loans

Credit 2023: Advancing and Workout Approaches to Play a Central Role

Hotel Receiverships: Palmer House Hilton Spotlights Stabilization Efforts

Office Modifications: 285 Madison May Offer a Blueprint for More to Come

Triple-A Shortfalls: Destiny Spotlights Delayed ASERs Impact

Inflation-Resistant Leases: Rent Steps Offer Some Revenue Protection, though Not Much

Industrial Delinquencies: Don’t Happen Often, but Watch Closely When They Do

Hotel Reserves: Key Performance Driver after Pandemic-Driven Depletion

Government Tenants: Short Termination Notices and Specialized Properties

Mall Foreclosures: What to Track as Servicers May Shift Away from Modifications

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