

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF HAWAII

In the Matter of the Application of)
)
HAWAIIAN ELECTRIC COMPANY, INC.,)
MAUI ELECTRIC COMPANY, LIMITED, and)
HAWAII ELECTRIC LIGHT COMPANY, INC.)
)
For the Approval of a Refinancing)
through the Sale of Cumulative)
Quarterly Income Preferred)
Securities and Related Junior)
Subordinated Deferrable Interest)
Debentures, Including Guarantees.)
_____)

DOCKET NO. 03-0409

DECISION AND ORDER NO. 20803

Filed Feb. 13, 2004
At 1:30 o'clock P .M.

Karen Higashi
Chief Clerk of the Commission

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Commission, State of Hawaii.

K. Higashi

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DECISION AND ORDER

I.

General Background

A.

HECO, MECO, HELCO

HAWAIIAN ELECTRIC COMPANY, INC. ("HECO") is the provider of electric utility service on the island of Oahu. It is a wholly-owned subsidiary of Hawaiian Electric Industries, Inc.

MAUI ELECTRIC COMPANY, LIMITED ("MECO") provides electric utility service in the County of Maui, comprising the islands of Lanai, Maui, and Molokai. HAWAII ELECTRIC LIGHT COMPANY, INC. ("HELCO") is the provider of electric utility service on the island of Hawaii. MECO and HELCO are wholly-owned subsidiaries of HECO.

B.

Applicants' Request

HECO, MECO, and HELCO (collectively, "Applicants") request the commission's approval to participate in up to two (2) sales of Cumulative Quarterly Income Preferred Securities ("QUIPS") in the aggregate total liquidation preference of up to \$100 million, and the related issuance of their Junior Subordinated Deferrable Interest Debentures ("QUIDS"), in a corresponding aggregate total principal amount of up to \$100 million.¹ Applicants make their joint request pursuant to Hawaii Revised Statutes ("HRS") § 269-17 and Hawaii Administrative Rules ("HAR") chapter 6-61, subchapter 9.

Applicants served copies of their joint application upon the Department of Commerce and Consumer Affairs, Division of Consumer Advocacy ("Consumer Advocate"). On January 16, 2004, Applicants responded to the Consumer Advocate's information requests. The Consumer Advocate does not object to commission approval of the application.²

C.

QUIPS and QUIDS

Applicants explain that QUIPS are hybrid securities that combine features of debt and equity securities. QUIPS have

¹Joint application, filed on December 8, 2003.

²Consumer Advocate's position statement, filed on February 4, 2004.

a lower after-tax cost than preferred stock because the periodic interest payments on the respective QUIDS are deductible from taxable income, as are interest payments on traditional long-term debt. However, QUIPS and QUIDS are similar to equity securities "in that they are deeply subordinated, have a long maturity and have a feature permitting deferral of distribution and interest payments for a significant period of time."

II.

Prior Dockets

The commission previously approved Applicants' QUIPS method of financing in Dockets No. 96-0344 and No. 98-0338.

A.

Docket No. 96-0344

On February 26, 1997, the commission approved Applicants' issuance of the \$50 million liquidation preference of QUIPS and corresponding \$50 million principal amount of QUIDS at a distribution/interest rate of 8.05 per cent (the "1997 QUIPS financing," Docket No. 96-0344).³ On March 27, 1997, Applicants completed the 1997 QUIPS financing.

³See Amended Decision and Order No. 15356, filed on February 26, 1997, in Docket No. 96-0344.

B.

Docket No. 98-0338

On December 7, 1998, the commission approved Applicants' issuance of the \$50 million liquidation preference of QUIPS and corresponding \$50 million of QUIDS at a distribution/interest rate of 7.3 per cent (the "1998 QUIPS financing," Docket No. 98-0338).⁴ On December 15, 1998, Applicants completed the 1998 QUIPS financing.

III.

QUIPS and QUIDS/Refinancing

A.

Sales of QUIPS and Issuance of QUIDS

Applicants request the commission's approval to participate in up to two (2) sales of QUIPS in the aggregate total liquidation preference of up to \$100 million, and the related issuance of their respective QUIDS, in a corresponding aggregate total principal amount of up to \$100 million. The purpose of the sales is to refinance the 1997 QUIPS financing and the 1998 QUIPS financing. Specifically, Applicants propose to participate "in either one series of \$100 million or in up to two series of \$50 million each, depending on whether the distribution/interest rate prevailing at the time of the sale or sales will result in adequate savings to warrant the sale or sales."

⁴See Amended Decision and Order No. 16728, filed on December 7, 1998, in Docket No. 98-0338.

Applicants will use the proceeds from the sale or sales to redeem in whole, either or both: (1) the 8.05 per cent 1997 QUIPS financing; and (2) the 7.3 per cent 1998 QUIPS financing. Applicants intend to achieve cost savings by replacing the existing QUIPS and related QUIDS "with less expensive QUIPS and related QUIDS, as rates are currently at relatively low levels."

Applicants represent that "[t]he terms and other features of the replacement QUIPS and related QUIDS are expected to be substantially the same as the QUIPS and related QUIDS issued in 1997 and 1998[,] " except for:

1. The pricing terms, such as the interest/distribution rate, which will be determined by market conditions at the time of the sale or sales; and
2. The provisions relating to the optional distribution of the underlying debt securities, which will be modified to permit Applicants greater flexibility.

Applicants request expedited action. The commission's approval, Applicants state, "will allow [them] the flexibility to pursue refinancings of one or both of the 1997 QUIPS and 1998 QUIPS, in a single or separate offerings, if sufficient savings are anticipated."

B.

Refinancing Structure

The structure of the QUIPS refinancing is described at pages 12 - 15 and Exhibit A of the joint application.

In general, the refinancing will involve the creation of: (1) HECO Capital Trust III for the initial sale; and (2) if a second sale is undertaken, HECO Capital Trust IV (collectively, the "Trusts").⁵ Both Trusts, Delaware statutory trusts, will sell: (1) up to \$3,092,800 in aggregate liquidation preference of common securities ("common securities") to HECO; and (2) up to \$100 million in aggregate liquidation preference of QUIPS to the public through up to two (2) registered, underwritten public offerings.

The combined total proceeds from the sale of common securities and QUIPS will be loaned by the applicable Trust to Applicants in exchange for their respective QUIDS to be issued by Applicants in the corresponding aggregate principal amount of: (1) up to \$63,092,800 for HECO;⁶ and (2) up to \$20 million each for MECO and HELCO. HECO will: (1) unconditionally guarantee the QUIDS obligations of MECO and HELCO (the "subsidiary guarantees"); and (2) guarantee the QUIPS obligations of each applicable Trust to the extent such Trust has sufficient funds for the payment thereof (the "Trust guarantee").

⁵HECO Capital Trust III is already formed, effective November 20, 2003.

⁶This amount includes up to \$3,092,800 of HECO's QUIDS issued to the Trusts in order to borrow from the Trusts the amount HECO invests in the Trusts to purchase the common securities.

C.

Major Features

Applicants note that the equity credit which rating agencies give to QUIPS results from two (2) of the major features of the QUIPS and QUIDS: (1) their deep subordination; and (2) the right to defer interest payments on the QUIDS and distributions on the QUIPS for up to five (5) years. These and other features of the QUIPS and QUIDS are described at pages 16 - 21 of the joint application.⁷

D.

Parameters

Applicants request that the commission authorize HECO, HELCO, and MECO to participate in the QUIPS refinancing and to issue its respective QUIDS, in either one (1) or two (2) series, so long as the QUIPS issued by the applicable Trusts and the

⁷The other features include: (1) Applicants' flexibility in selecting the maturity of the QUIDS and QUIPS; (2) voting rights of QUIPS holders; (3) redemption terms; and (4) the flexibility to exchange the QUIPS into QUIDS.

Pages 21 - 23 of the joint application describe the accounting and ratemaking treatment of the QUIPS and QUIDS. Pages 23 - 25 identify the documents used to undertake the refinancing. These documents include "several trust, underwriting, expense and other agreements, indentures, instruments, and guarantees, a registration statement and final prospectus, a [New York Stock Exchange] listing application (and related registration statement) and other documents[.]"

QUIDS issued by Applicants have terms within the following parameters:

1. The QUIPS will have an aggregate liquidation preference of up to \$100 million based on 4,000,000 QUIPS at a liquidation preference of \$25 per QUIP.

2. The aggregate principal amount of the QUIDS will be: (A) up to \$63,092,800 for HECO (including up to \$3,092,800 principal amount of QUIDS to be purchased with the proceeds from the sale to HECO of common securities); and (B) up to \$20 million each for MECO and HELCO.

3. The aggregate purchase price for HECO to purchase the Trusts' common securities will not exceed \$3,092,800.

4. The interest and distribution rates will be fixed at rates not to exceed: (A) 7.5 per cent for the 1997 refinancing; (B) 6.75 per cent for the 1998 refinancing; and (C) 6.75 per cent for a combined 1997 and 1998 refinancing.

5. HECO, HELCO, and MECO will each have the right, on one (1) or more occasions, to defer interest and distributions for up to twenty (20) consecutive quarters, but not past maturity, with deferred interest and distributions continuing to accumulate during the deferral period, compounded quarterly at the interest or distribution rate.

6. A maximum maturity of "[n]ot later than 49 years, including extensions."

7. The liquidation preference of the QUIPS will be one hundred (100) per cent of the principal amount of the QUIDS.

8. The securities will be senior to all preferred and common stock of each Applicant, now existing or hereafter created, except *pari passu* ("on the same level as") with the 1997 QUIDS, the 1998 QUIDS, trade credit, other hybrid securities issued by HECO Capital Trust IV, if applicable, and other securities expressly declared to be *pari passu*.

9. The underwriting commission will be up to 3.5 per cent of the aggregate liquidation preference of the QUIPS sold in the offering.

10. A no-call period not to exceed five (5) years, subject to the right to redeem at any time without premium upon the occurrence of a special event.

11. Upon dissolution of the Trust or Trusts, at HECO's election, provided that the commission's approval of the issuance of the HECO substituted QUIDS shall first have been obtained: (A) the MECO QUIDS and HELCO QUIDS will be transferred to HECO by the Trust in exchange for an equivalent amount of HECO QUIDS; (B) the QUIPS will be exchanged for an equivalent amount of HECO QUIDS; and (C) the common securities and an equivalent amount of QUIDS, together with the QUIPS and HECO's subsidiary guarantee, will be canceled.

12. The QUIDS and QUIPS covenants will not be materially more restrictive than the covenants provided in connection with the 1997 QUIPS financing and 1998 QUIPS financing or in Applicants' other outstanding securities, including covenants not to pay dividends on common stock or preferred stock, and not to make payments on debt securities or guarantees

that rank *pari passu* or junior to the underlying QUIDS, during any deferral period or under other specified circumstances.

E.

Estimated Savings

At the fixed interest rates of 7.5 and 6.75 per cent respectively, the estimated savings for the year 2004 is \$400,000. The estimated total savings over thirty (30) years, the assumed life of the new QUIPS and QUIDS, is \$12.4 million.

F.

Estimated Costs

Exhibit B of the joint application breaks down the estimated consolidated issuance costs of the proposed refinancing. The estimated costs range from \$2,055,000 (one (1) sale, \$50 million) to \$3,655,000 (one (1) sale, \$100 million).

G.

Reporting

Applicants will report to the commission "the result of the proposed refinancings as soon as practicable after they are concluded." They will "also provide information on the actual expenses incurred in the [re]financings."

IV.

Consumer Advocate's Position

In response to the Consumer Advocate's inquiry, Applicants anticipate that the proposed refinancing will not negatively affect their credit ratings. Instead, the proposed refinancing "should have more of a positive effect on their credit, if any at all, since it would decrease the cost of [Applicants'] fixed obligations and extend the life of the hybrid securities which would tend to allow for more equity consideration." Moreover, Applicants state that the proposed refinancing "will be reflected in each [of their] respective embedded cost of hybrid securities and preferred stock in future rate case proceedings."

The Consumer Advocate finds that the proposed refinancing is very similar to Applicants' requests in Dockets No. 96-0344 and No. 98-0338, will result in lower interest rates and cost savings, and "should ultimately decrease each Applicant's cost of capital."

V.

Commission's Review

HRS § 269-17 provides that, with the commission's prior approval, a public utility may issue evidences of indebtedness for the acquisition of property or for the construction, completion, extension, or improvement of or addition to its facilities or service, or for the discharge of its obligations. In approving an application to issue indebtedness under

HRS § 269-17, the commission must find that the proposed purpose for the issuances will not have an adverse effect on the public utility's operations.⁸

The commission previously approved the 1997 QUIPS financing and 1998 QUIPS financing in Dockets No. 96-0344 and No. 98-0338, respectively. The present docket involves the refinancing of the QUIDS at lower interest rates. Applicants represent that "[n]one of the proposed purposes will have a material adverse effect on any of Applicants' public utility operations."

The commission approves Applicants' request for authorization to participate in the refinancing, as set forth in Section VII below.⁹

VI.

HAR § 6-61-101(b)

HAR § 6-61-101(b) mandates that Applicants submit certain exhibits with their joint application. Applicants request a waiver of paragraphs (1), (5), (6), and (7), subsection (b). Applicants state that "[t]he proposed QUIDS and related QUIPS would simply be a replacement of existing QUIDS and QUIPS with other less expensive QUIDS and QUIPS." Thus, "it does not

⁸Amended Decision and Order No. 16728, filed on December 7, 1998, at 11, in Docket No. 98-0338; and Amended Decision and Order No. 15356, filed on February 26, 1997, at 11, in Docket No. 96-0344.

⁹Section VII of the decision and order corresponds with Applicants' requested Prayer for Relief described at pages 31 - 33 of the joint application.

appear that the information with respect to which this waiver is requested would be necessary" in the commission's review of the joint application.

The commission finds good cause to waive the requirements of HAR § 6-61-101(b)(1), (5), (6), and (7), to the extent applicable.

VII.

THE COMMISSION ORDERS:

1. HECO's formation of HECO Capital Trust III is approved, and HECO is authorized to establish HECO Capital Trust IV. HECO's purchase of up to \$3,092,800 of the Trusts' common securities is approved.

2. The Trusts are authorized to issue and sell QUIPS having an aggregate liquidation preference of up to \$100 million, through one (1) or two (2) registered, underwritten public offerings, within the parameters described in the joint application (and also described in Section III.D, above).

3. HECO, HELCO, and MECO, in their discretion, are each authorized to issue and sell its QUIDS to the Trusts in the respective aggregate principal amounts of up to \$63,092,800, \$20,000,000, and \$20,000,000. The Trusts are authorized to purchase the QUIDS of each of the companies within the parameters described in the joint application (see also Section III.D, above), in exchange for the proceeds from the offering of the QUIPS; and in HECO's case, in exchange for the proceeds from the sale to HECO of the Trusts' common securities, such QUIDS to

correspond in the aggregate principal amount, interest rate, maturity, redemption, and other material provisions to the comparable terms of the related QUIPS and Trusts' common securities.

4. HECO is authorized to provide its subsidiary guarantees and its Trust guarantee, as described in the joint application.

5. HECO, HELCO, and MECO are each authorized to execute and deliver all documents, letters, agreements, certificates, and instruments that are necessary or desirable to conclude the refinancing described in the joint application.

6. Applicants are authorized to use the proceeds of the refinancing for the purposes set forth in the joint application.

7. HECO shall file an application with the commission for approval of the issuance of HECO substituted QUIDS in the event HECO opts to proceed with an exchange.

8. Applicants shall report to the commission the results of the refinancing as soon as practicable after it is concluded. Applicants shall also provide information on the actual expenses incurred in the refinancing.

9. The filing requirements set forth in HAR § 6-61-101(b)(1), (5), (6), and (7), to the extent applicable, are waived.

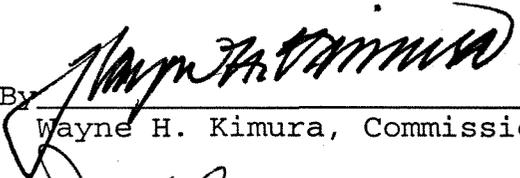
10. Applicants shall conform to all of the commission's orders set forth above. Their failure to adhere to the commission's orders shall constitute cause to void this

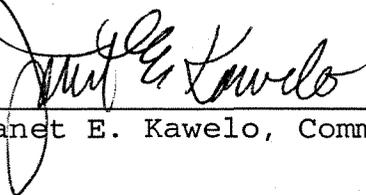
decision and order, and may result in further regulatory actions as authorized by law.

DONE at Honolulu, Hawaii this 13th day of February, 2004.

PUBLIC UTILITIES COMMISSION
OF THE STATE OF HAWAII

By 
Carlito P. Caliboso, Chairman

By 
Wayne H. Kimura, Commissioner

By 
Janet E. Kawelo, Commissioner

APPROVED AS TO FORM:


Michael Azama
Commission Counsel

03-0409.sl

CERTIFICATE OF SERVICE

I hereby certify that I have this date served a copy of the foregoing Decision and Order No. 20803 upon the following parties, by causing a copy hereof to be mailed, postage prepaid, and properly addressed to each such party.

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DIVISION OF CONSUMER ADVOCACY
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DATED: February 13, 2004