

Public Utility District No. 1 of Jefferson County, WA
Preliminary Feasibility Study
Electric System Acquisition

November 19, 2008

Overview

- Introduction
- Overview of Study
- Changes from Draft to Final report
- Break
- Next steps
 - Strategic approach
 - Discussion

Introduction

- Electric service is provided by four utilities in Jefferson County:
 - Puget Sound Energy (PSE) – 14% of area, most of population
 - Mason County PUD No. 1
 - Clallam Co. PUD
 - Grays Harbor Co. PUD
- Preliminary Feasibility Study undertaken in June 2008
- Draft study released in September 2008
 - Estimated cost to acquire PSE facilities
 - Estimated cost to establish and operate PUD electric utility
 - Compared costs of service from PUD and PSE
- Final report was issued October 24, 2008

PUDs in Washington

- Citizens have right to form PUDs in counties
- Currently 28 PUDs, mostly formed in 1930's
 - Serving 900,000 electric customers, 118,000 water customers
- Non-profit and community owned
 - Other community-owned utilities include municipalities and cooperatives
- Provide service at cost
- Access to federal hydroelectric power from Bonneville Power Administration
- Do not pay income taxes
- Access to tax-exempt financing

Study Approach

- Define necessary electric facilities
 - Estimate acquisition cost (conservative assumptions)
 - Estimate financing requirements
- Determine number of customer accounts
- Determine energy requirements
- Estimate power supply costs (conservative assumptions)
- Estimate costs of operation and overall revenue requirements (conservative assumptions)
- Compare estimated average rates for PUD and PSE

Components of Electric System

- Power supply
 - Purchased power
 - Owned power generation facilities
- Transmission
 - BPA network
 - Local 115-kV transmission lines
- Distribution system
 - Substations
 - Poles, wires, transformers, service drops

East Jefferson County Electric System



Acquisition of Facilities

- Specific facilities will be defined
- Purchase price to be negotiated or established by court
- Valuation based on established procedures
 - Cost basis – Original cost less depreciation
 - Market approach
 - Income approach – approximately OCLD
 - Cost per customer

Estimated Acquisition Cost

- Department of Revenue estimated taxing value of PSE properties in Jefferson County is \$30 million
- Preliminary estimate of OCLD
 - Original cost: \$58.2 million
 - OCLD: \$34.9 million
- Reproduction cost new less depreciation
 - \$70 million
- Estimated purchase price: \$47.1 million

Financing Requirements

- Initial purchase price to be financed with revenue bonds
 - Taxable
 - Tax-exempt
- Financing requirement

Initial System Acquisition	\$	47,200,000
Separation Costs		1,200,000
Startup Costs		<u>7,800,000</u>
Total Initial Costs	\$	56,200,000

Initial Financing Requirement

	Bond Issue A (Taxable Rate)	Bond Issue B (Tax-exempt Rate)
Initial Acquisition Costs	\$ 47,200,000	\$ -
Separation, Startup, Legal Costs ¹	-	\$ 8,600,000
Working Capital ²	-	5,000,000
Contingency Reserve	-	-
Subtotal	\$ 47,200,000	\$ 13,600,000
Financing Expense ³	515,000	148,000
Debt Service Reserve ⁴	3,738,000	910,000
Total Financing Requirement	\$ 51,453,000	\$ 14,658,000

- Approximately \$66 million total

Customer Accounts

- Approximately 18,200 customers in 2009
 - 84% are residential customers
 - Assumed growth of about 2% per year
 - About 18,900 customers by 2011

Energy Requirements

- Total energy requirement of about 336,500 MWh (38 average MW)
 - Represents total power supply requirement
- Peak demand of 66 MW
- Assumed load growth of 2% per year

Power Supply

- Expect PUD to become BPA customer
 - BPA markets federal hydroelectric power
 - Criteria to be met
 - PUD must own distribution system
 - Have financial ability to pay BPA
 - Be able to purchase power in wholesale amounts
- Other options are available
 - Market purchases
 - PUD owned generation, joint ownership

Power Supply Costs

- Lowest cost BPA power is about 3.2 cents per kWh – Tier 1
- BPA is reserving 250 average MW of Tier 1 power for new public power utilities
- PUD may need to purchase other power for a period of time initially
 - Tier 2 power – higher price
 - Assumed no Tier 1 power to PUD for 3 years

Estimated Cost of Power

- Estimated at about 5.4 cents per kWh for first three years
- Cost expected to drop as Tier 1 power becomes available – about 4.5 cents per kWh in 2015
- Network transmission adds about 0.4 cents per kWh

Operating Costs

- Distribution operations and maintenance
 - Retain management and staff
 - Line crews, engineers, office staff
 - Potentially contract for certain services
- Customer accounting, customer service
- Overall staffing requirement estimated to be 67 employees

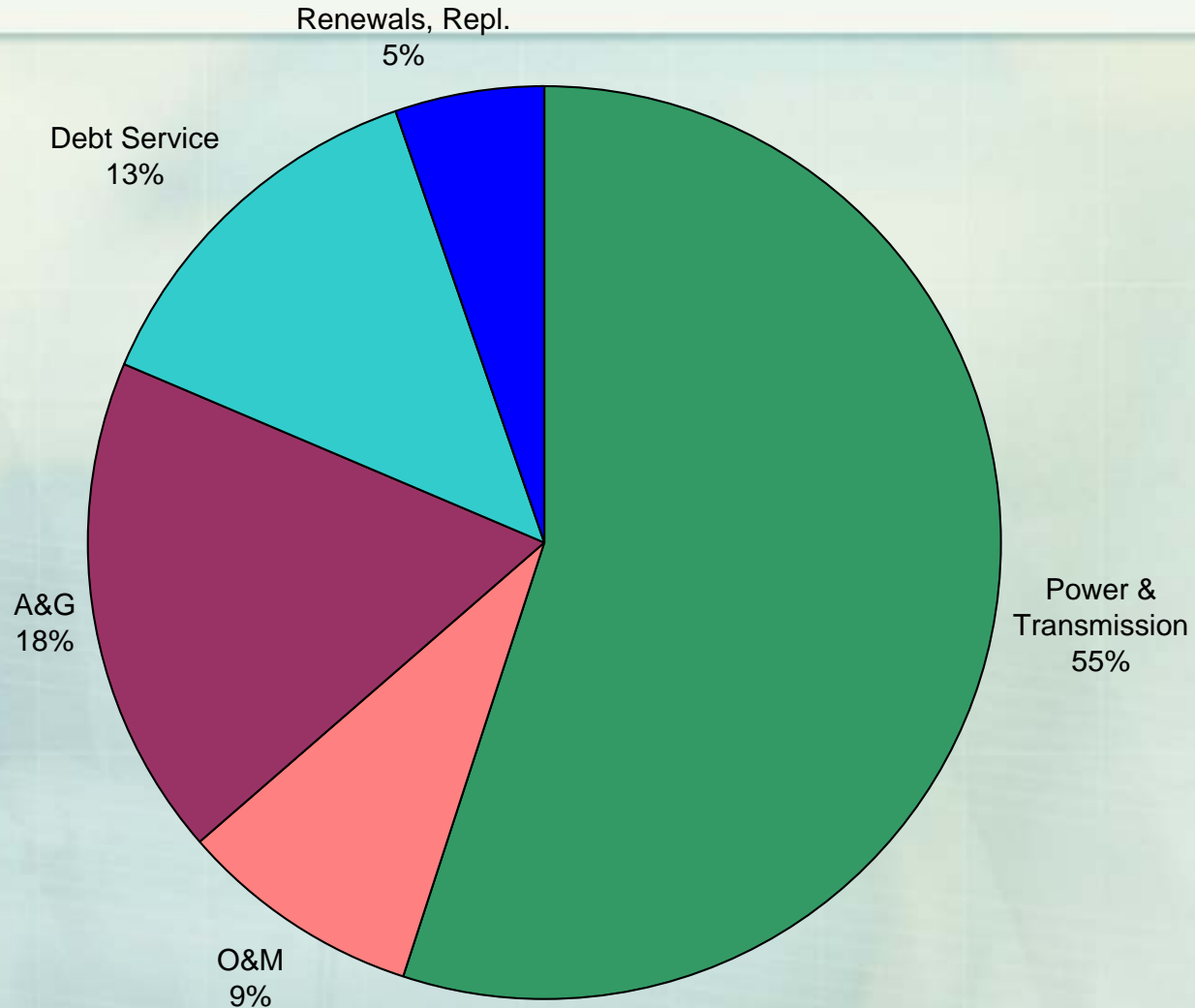
Operating Costs

- Debt service
 - 30 year repayment on initial debt
 - Estimated to be about \$4.7 million per year
- Renewals, replacements and additions
 - Estimated at about \$1.9 million per year

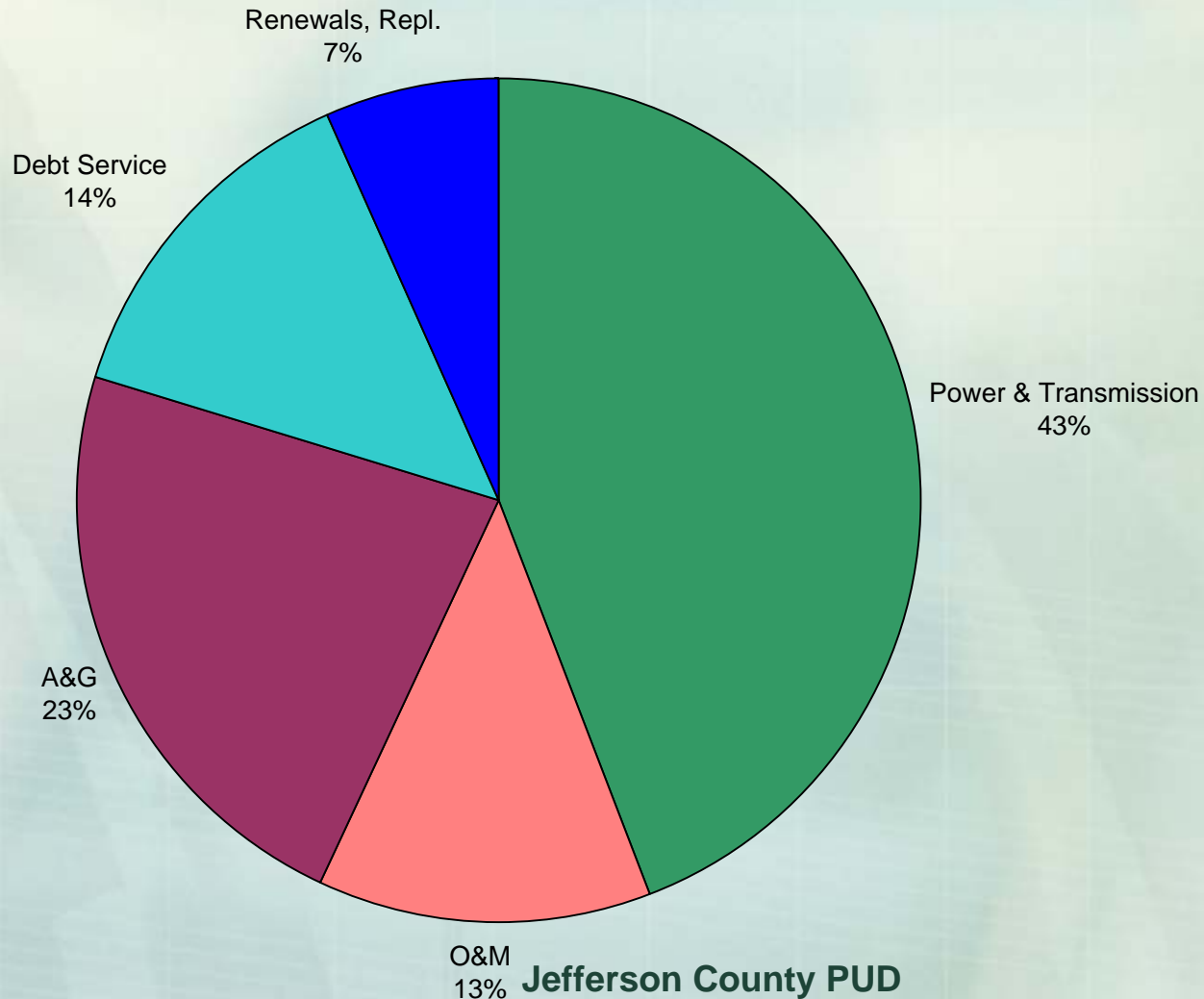
Annual Revenue Requirement

- Estimated to be about \$35 million in 2011
 - 11.1 cents per kWh
 - About 51% of total is power supply cost
- Estimated to remain relatively constant
 - Decreasing power supply costs with more Tier 1 power
 - Inflationary impacts on other costs
 - About 9.0 cents per kWh in 2020

Total Revenue Requirement 2011



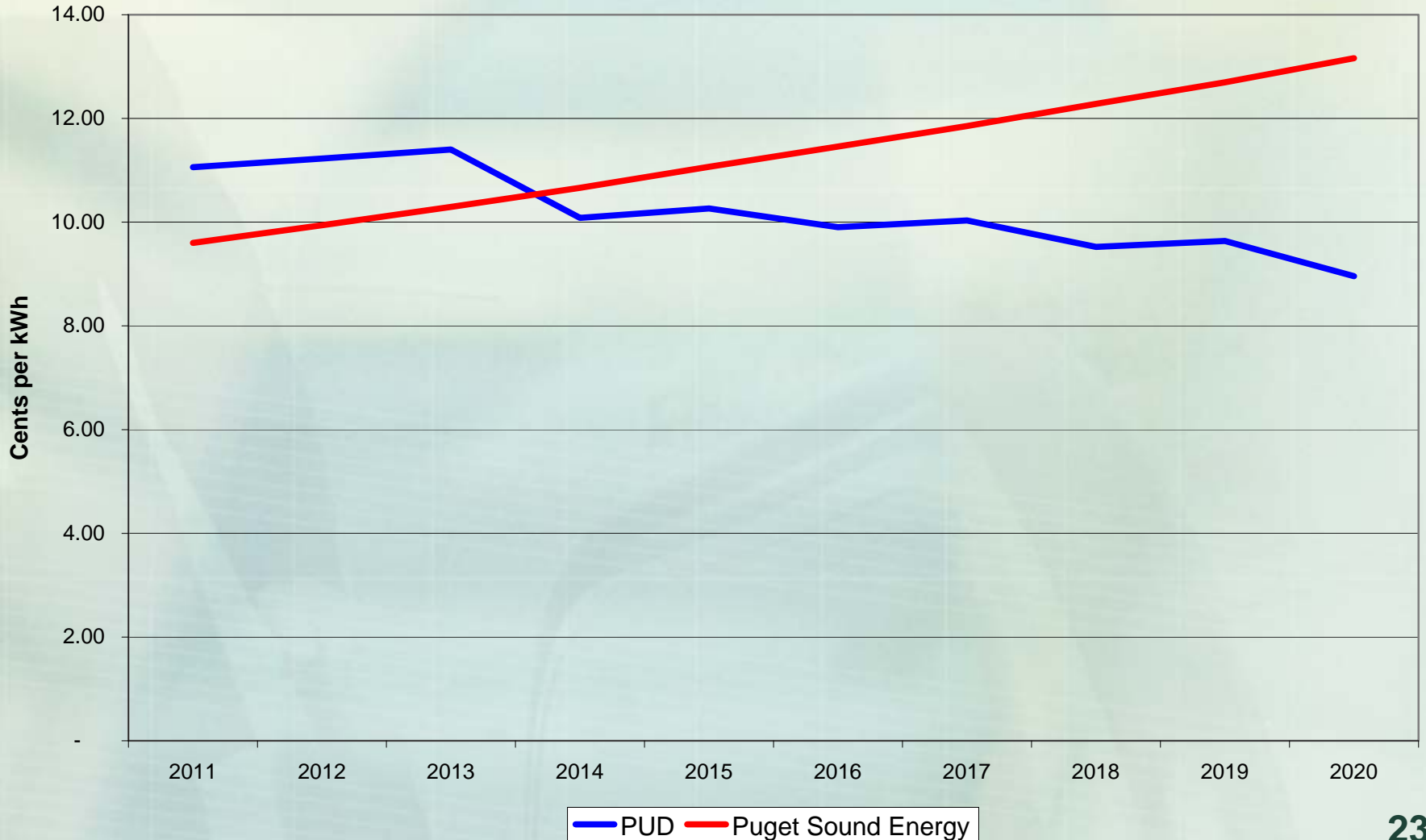
Total Revenue Requirement 2020



Comparison of Costs

- PSE rates expected to increase over time
 - Assumed to be 3.55% per year (conservative assumption)
 - New rates went into effect Nov. 1
 - Average residential charge at about 9.1 cents per kWh – includes about 1.0 cent BPA credit
- PUD rates will be based on revenue requirement (total cost of operation)

Comparison of Costs for Feasibility Study (conservative assumptions)



Comparison of Scenario Results

Case	Acquisition Price	Power Cost	Interest Rates	Present Value of Net Savings with PUD over first 10 Years
1 (Base)	Transmission and distribution at OCLD+35%	PF and Base Market price	6% taxable, 4.5% tax-exempt	\$22,535,000
2	Transmission and distribution at OCLD	PF and Base Market price	6% taxable, 4.5% tax-exempt	\$29,069,000
3	Transmission and distribution at OCLD+35%	PF	6% taxable, 4.5% tax-exempt	\$62,261,000
4	Transmission and distribution at OCLD+35%	PF and Base Market price	8.0% taxable, 6.0% tax-exempt	\$7,766,000
5	Transmission and distribution at OCLD+35%	PF and Base Market price + \$10/MWh	6% taxable, 4.5% tax-exempt	\$16,352,000
6	Transmission, distribution at 2.0 times net book value	PF and Base Market price	6% taxable, 4.5% tax-exempt	\$9,542,000

Time for a Break

Today's topics

- Strategic Approach
- Brainstorming session (four approaches):
 - (a) Stop the clock,
 - (b) expedited formation,
 - (c) wait and see formation,
 - (d) some combination of the above
- Next Steps?

Strategic Approach

- Thinking several moves ahead
- Identifying long term goals and current status (lower cost power, local control/accountability, economic development, reliability, etc.)
- Puget Sound Energy is not going to go away and its activities will impact what the PUD does and the PUD's schedule (watch out for interference lawsuits)
- Keeping Options open
- Keeping promises to voters and community

Strategic Approach (Continued)

- Maintaining community support and public opinion
 - PUD out-reach commission meetings
 - Citizen Advisory Committee
 - Meetings with government sponsors/stakeholders
 - Periodic surveys
 - Other
- Managing cost and expenditures
 - Creating a template for others that may follow

Brainstorming session

(four approaches)

- (a) Stop the clock,
- (b) expedited formation,
- (c) wait and see formation,
- (d) some combination]

(a) Stop the clock

Something to “stop the clock” on the ten-year time to provide electric services and help the local economy through such activities

- Research potential grant funding for alternate energy, renewable energy or energy conservation projects
 - Ask for community suggestions for small projects with special local benefits (economic, reliability, visibility, etc.)
 - Consider an outreach to Clallam Co PUD and Grays Harbor Co PUD’s for projects in western Jefferson County served by those utilities
 - Consider an outreach to Mason County PUD No. 1 for portion of eastern Jefferson County they serve.
 - Find one or two projects within east Jefferson County that provide broad or special benefits to the community.
 - Potential Projects with PT Paper or USN at Indian Island
 - Care must be taken not to create a BPA “high water mark” or its equivalent by this.

(a) Stop the clock (Continued)

- Through outreach identify projects that do not require grants that have the potential for being economic and build community consensus and support
 - Waste heat recovery
 - Small methane sources
 - Cogeneration or wood waste potential
 - Other

(b) Expedited formation

Advance the potential purchase of PSE assets through an expedited, pro-active electric utility formation approach

- Explore PSE's desire to sell
- Explore Macquarie's desire to sell part of PSE
- Open a dialogue with the WUTC to better understand their vision of PSE in Jefferson County so the PUD understands the full differences between the two likely approaches to customer service.
- Public relations/information campaign and constituency building

(b) Expedited formation (Continued)

- Explore PSE franchise agreements with Jefferson County and all cities and tribes
 - Find any expiration dates and terms
 - Discuss and potentially make competing applications, where appropriate
 - Find out about any service issues with government agency
- Also check contracts that PSE may have with federal government: USN Indian Island, Bangor Torpedo Testing Range (southern submarine cable), and BPA
- Have discussions with City of Port Townsend to avoid conflicts and have unified roles and future utility service vision.

(b) Expedited formation (Continued)

- Explore how PUD Eminent Domain/Condemnation cases involving PUD's are handled
 - Houghton Cluck background on all past condemnation cases
 - Initial offer and need for it to be close to court awarded amount to avoid certain costs
 - How are initial offers usually quantified, appraisal based on inventory, based on field collected data
 - Explore alternate ways to get critical data at low costs
 - Ask PSE for asset data
 - Sampled inventory of PSE assets
 - Request Jefferson County asset data currently held as confidential with WA Dept of Revenue
 - Request asset data and future rate/revenue data currently held as confidential with WUTC in Merger & Rate Case
 - Develop complete Jefferson County PSE asset inventory program with cost and schedule
- Likely time frame for such a case and likely level of legal fees and any “first steps” that may help refine costs and schedule.

(b) Expedited formation (Continued)

- How to position the PUD to be able to best borrow money needed for an electric utility system
 - Talk to financial advisors and accountants
 - Talk to bond counsel to learn about needed bond covenants and current bond tax issues.
 - Talk to attorney's
 - Talk to rating agencies
 - Talk to consulting engineer
 - Develop a financing plan to optimize future borrowing

(b) Expedited formation (Continued)

- Explore BPA Transmission requirements
- Explore BPA Power requirements
 - Regional Dialog Contract
 - Standards for Service
 - Power supply options prior to BPA Regional Dialog Tier 1 becoming available
- Non requirements customer joint purchase RFP
- BPA TAC or special purchases
- RCW 54 request to WUTC for limited power supply from PSE
- Talk to Macquarie about recent purchase of Grant Co PUD power block
- Talk to other potential power suppliers of interim power
- Some generation resources or Jefferson Co PUD contracts (Paper Mill? Other?)

(b) Expedited formation (Continued)

- Explore any alternate utility ownership options that might have benefits
 - BPA's Tier 1 power allocation favors smaller utilities over larger utilities (Jefferson Co PUD is estimated to be 37 aMW).
 - Utilities under 10 aMW have best situation
 - Utilities > 10 aMW but < 34 aMW are next best
 - Utilities > 34 a MW are next
 - Agreements with say Clallam Co PUD and/or Mason Co PUD No. 1 (or other PUD's?) for initial operations and cost sharing.
- Talk to IBEW to learn about how they can help and their expectations.
- Talk to State Auditor
- Talk to Dept of Revenue and local taxing districts

(b) Expedited formation (Continued)

- Hire or appoint a project manager who will work for the PUD as an employee, contract employee or consultant
 - DHA could arrange for a past PUD Manager such as Dennis Bickford or Tom Anderson to initially help.
 - Want someone experienced in electric PUD laws and operations
 - Want someone who doesn't have a potential conflict of interest, (i.e. long term job security interest) in the outcome of their advice
 - Identify employee or new employee and provided any needed training
 - Recruit a new employee with the necessary skills

(b) Expedited formation (Continued)

- Pull together a complete project schedule and business plan
 - Financial feasibility
 - Organizational structure, plan and interim milestones
 - Staffing & training
 - Equipment
 - Inventory
 - Contract services
 - Other
 - Legal Plan
 - Financing Plan
 - Engineering/Asset plan
 - Power Supply Plan
 - Transmission Plan
 - Regulatory Plan
 - Public Relations Outreach Plan
 - PUD Management Plan & key decision points

(c) Wait and see formation

Advance the potential purchase of PSE option through slow or “wait and see” electric utility formation approach

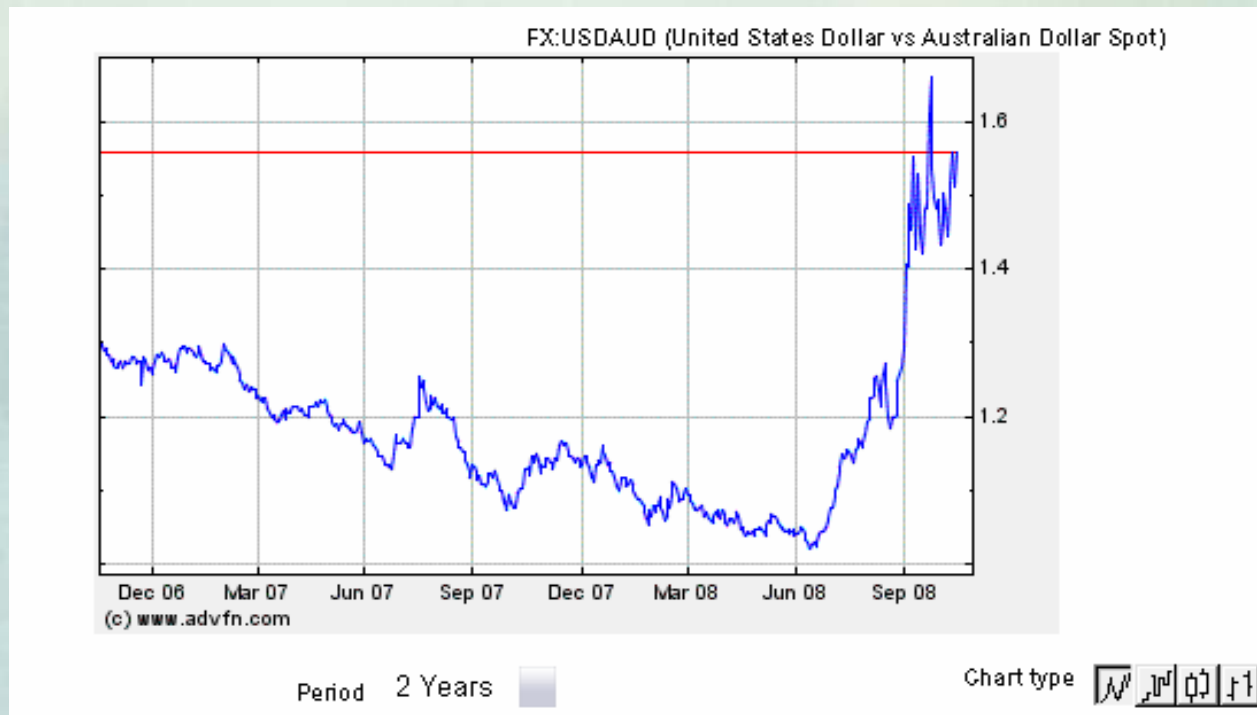
- Explore PSE’s desire to sell
- Explore Macquarie’s desire to sell
- Focus on community outreach, public support and consensus building in support of PUD electric service.
- Wait to see WUTC Merger/Sale decision

(c) Wait and see formation (Continued)

- Wait to see if Macquarie/PSE are entangled in world financial problems
 - Credit crisis (PSE/Macquarie are counting on significant amounts of borrowed funds) may impact ability to perform merger as outlined in Oct 2007 agreements.
 - Changes in currency rates between countries may have made funds originally identified for \$30/share offer no longer sufficient from Canadian pension funds and from Australian investors.
 - Will world or local recession change plans or desire of either Macquarie or PSE for their previous PSE business plan

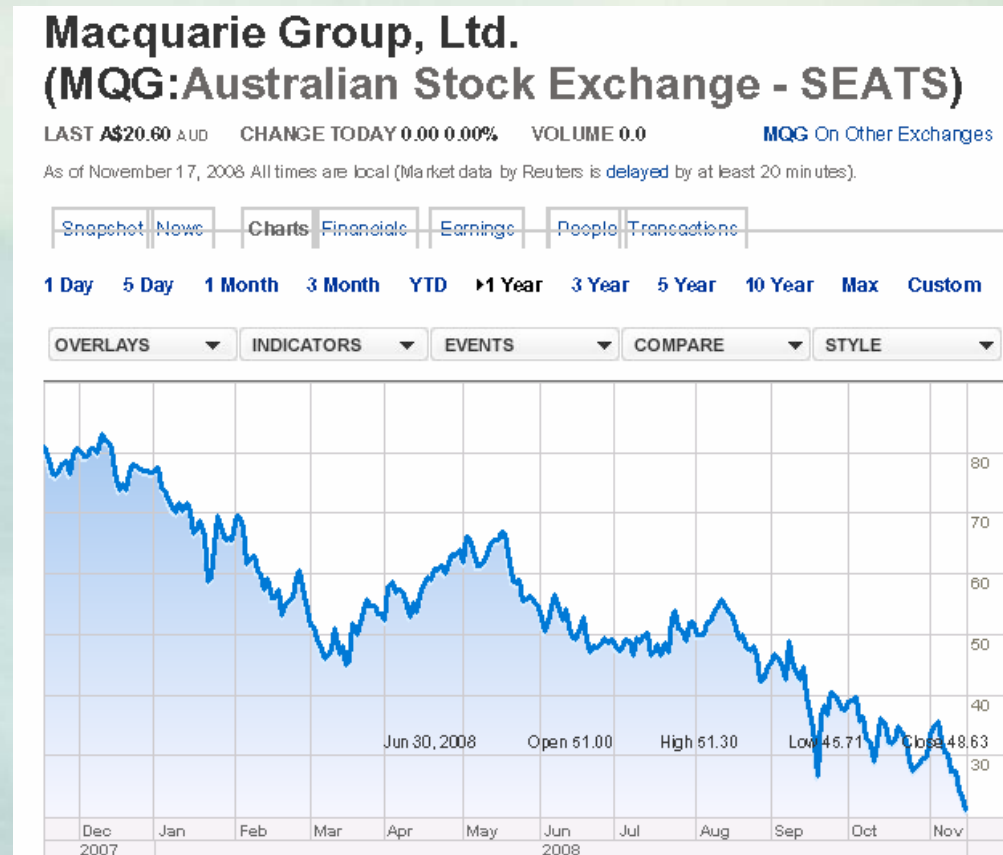
(c) Wait and see formation (Continued)

- US \$ versus Australian Dollar (\$30/share US takes a lot more Australian Dollars than it did when merger/sale announced in Oct. 2007)



(c) Wait and see formation (Continued)

- Investment in PSE is a much greater share of Australian Macquarie Stock is worth than in October 2007



(c) Wait and see formation (Continued)

- US \$ versus Canadian Dollar (\$30/share US takes a lot more Canadian Dollars than it did when merger/sale announced in Oct. 2007)



Period 2 Years

Chart type

(c) Wait and see formation (Continued)

- See if there are any US government economic stimulus proposals from new federal administration that a PUD can better take advantage of
- Wait for PSE mis-step(s) to advance
 - Reliability/outage problems
 - PSE Rate increases
 - Other negative publicity on the part of PSE
- Work methodically using many of the steps in (a) above on a comprehensive plan and be ready to adjust the schedule based on public support and changing conditions.

(d) Some combination of (a) (b), or (c)

(a) Stop the clock,

(b) expedited formation,

(c) wait and see formation,

(d) some combination of the above

Next Steps?

- Some thoughts on timing
 - BPA busy until mid December/January
 - When is the election certified?
 - When does the new PUD Commissioner take office?
 - When does the new PUD budget take effect
- A good time to organize
 - Citizen Advisory Committee
 - RFP/Selection of some Consultants, legal and other professionals
 - Commission consensus building

On behalf of D. Hittle & Associates, Inc.

- Thank you for this opportunity to share our thoughts
- Please contact us if we can provide you with further assistance