

PUBLIC UTILITY DISTRICT # 1
of Jefferson County
January 16, 2008
SPECIAL WORKSHOP MEETING
MINUTES

DRAFT

CALL TO ORDER

The Special Workshop Meeting of the Public Utility District No.1 of Jefferson County was called to order by the President of the Board of Commissioners at 11:01 a.m. at the District Office, 230 Chimacum Road, Port Hadlock, Washington. Commissioners and staff present were:

Wayne G. King, President
M. Kelly Hays, Vice-President
Dana Roberts Secretary
James Parker, District Manager
Kate Pike, Brisa Services

AGENDA

The purpose of the Special Workshop Meeting was to receive a presentation from Nancy Neraas, of the legal firm Foster Pepper, on bonding requirements for financing any acquisition of power utilities.

Additionally, the Board is to discuss PUD Board members' areas of responsibilities and division of labor.

BOND PRESENTATION

Ms. Neraas, who has worked previously with the PUD, introduced herself to new Board and public members. She has worked as a bond counsel for 24 years and currently represents many Washington PUD's, as well as Energy Northwest, and is considered very knowledgeable regarding acquiring electric power. She identified the financing alternatives available to this PUD, noting the legality of incurring debt for any lawful purpose, including acquiring facilities, equipment and land, constructing facilities, making improvements and paying for operating costs.

Noting that a key to financing is determining how debt can/will be repaid,

she identified the three types of debt, short-term or long-term, that PUD's are permitted to issue: revenue debt, general obligation debt and Local Utility District (LUD) debt, with general obligation and LUD debt being the most unlikely and impractical for this PUD to issue.

Revenue debt, payable from the utility's revenues, has no legal limit on an amount issued but is typically limited by anticipated revenues. Purchasers of revenue debt will scrutinize the anticipated revenues to insure an ability to cover debt.

In the current "examination" phase, any moneys available to the utility such as a bank loan, current tax levy and revenues, gifts, state loans or grants may be used for that phase (i.e. feasibility study). Any short-term cost incurred in a feasibility study is permitted to be rolled into long-term debt. Such a feasibility study should be to look at costs of acquisition and at a proposed, reasonable rate structure.

It is important to have revenue sufficient to pay projected operating and maintenance expenses, debt service, and an additional "cushion" coverage requirement amount, which is suggested to be at least 25 per cent, with 50 per cent more comfortable. Electrical utilities have "policies", supported by rating agencies and Wall Street, that once a system is up and running, about 50 per cent of ongoing improvements come out of revenue and 50 per cent from issued debt. Important to the PUD security is the ability to raise rates sufficient to pay debt without approval from the UTC or a vote from the electorate.

Interim, short-term, financing is possible and typical, via bank loan, line-of-credit and publicly offered notes by an investment firm. It is usually secured by a promise to issue long-term bonds. Long-term financing from the beginning is permissible for all or a portion of anticipated debt. Debt may be issued up to 40 years; however, 20 to 30 years is more typical. There is much flexibility in the structuring of debt, with even the ability to borrow interest to pay on a debt during a construction period with principal not having to be paid immediately.

Long-term debt is usually in the form of bonds.

The District currently has no bond "rating". Ms. Neraas explained the ratings and the process by which they are obtained, noting that there are

three agencies issuing ratings (ed.note: Standard & Poors, Moody's, and Fitch). She advised the Board to consider having preliminary discussions with an appropriate agency and seek advice from financial advisors and investment bankers to get a sense of the range on capital investments.

There are a considerable number of Internal Revenue Service regulations. Typically, financing can be on a tax-exempt basis, yet a provision in the IRS Code says if output facilities, which include electric distribution facilities, are acquired from an existing non-government utility, it can't be on a tax-exempt basis; however, there are potential exceptions worth exploring. If the facility had to expand to accommodate the new utility, that could be considered tax-exempt. New equipment (truck, smart meters) could be tax exempt. Section 141(d) of the Internal Revenue Code, regarding a facility constructed or used prior to 1987 states "non-governmental property means any property or interest therein which before such acquisition was used by a person other than a governmental unit in connection with an outlet facility...Use or the holding for use before Oct. 14, 1987 shall not be taken into account." This MAY be taken to mean that tax-exempt funding could be appropriate for this project. Ms. Neraas will further investigate and report back to staff.

The District may end up with a series of bonds that are tax exempt and a series that are taxable. A varying "rule of thumb" difference between tax exempt and taxable interest rates is about 1.5 per cent. Over a certain size, bank loans are not cost effective; publicly marketed bonds via an investment firm makes sense for long-term (over \$1-2 million). Most investment firms will advertise locally.. A utility may market its own bonds; however it requires much staff time and effort.

Regarding costs, another (conservative) "rule of thumb" is that approximately 1.5 per cent of a purchase price can expect to be expended for cost of issuance (rating agencies, underwriter's fee, printing, etc.) Also, it is typical to borrow to fund a "reserve" account (previously had been a reserve insurance policy) of about 10 per cent kept available to pay interest and principal if revenues run short. This account generally sits unused, then makes the last bond payment. Bond counsel, financial advisors, make individual agreements.

With regard to a feasibility study, rating agencies and potential bond purchasers will want the same answers as the District, particularly

concerning abilities to repay debt. Concerning an appraisal, while not legally mandated, it is suggested to determine a "fair market value". It need not be performed by a real estate appraiser, but by someone with appropriate experience such as an engineer. During a negotiation stage, an appraisal would be considered "executive" and not public information.

Ms. Neraas did remark that, creating a new utility, it is imperative to maintain separate accounting procedures and bookkeeping, and a careful record of any monetary transfers between utilities. In addition, she did recommend that one next step for the District would be to confer with a condemnation attorney. She will provide staff with names.

After thanking Ms. Neraas for her advice, the Board took a break at 12:17 p.m. and resumed its workshop at 12:26 p.m.

DIVISION OF COMMISSIONER RESPONSIBILITIES

The Manager presented a memorandum from the January 21, 2009 Regular Meeting concerning a division of effort for an increased amount of work and responsibility for the District.

Initially it was decided to separate meetings, duties, responsibilities into three categories:

- 1) operational, meaning all distribution systems, operating, billing, work with neighboring utilities, include inventory of facility;
- 2) power supply, dealing with power negotiations (i.e.BPA), contacts for additional and alternative power sources and with PUD's, ; and
- 3) financial and legal, to include discussions on bonds, financial advice, underwriters, condemnation and bond legal advice.

Prior to the next Regular Meeting, the Manager will list meetings, duties, etc. within the categories for discussion.

ADJOURNMENT

Note that your minute taker left prior to adjournment, so don't have the time. Was there a motion? I know you weren't to take formal ACTION, but did anything else get determined?

