

**PUBLIC UTILITY COMMISSION OF OREGON  
ADMINISTRATIVE HEARINGS DIVISION REPORT  
PUBLIC MEETING DATE: November 20, 2001**

REGULAR   X   CONSENT        EFFECTIVE DATE \_\_\_\_\_

**DATE:** November 9, 2001

**TO:** Phil Nyegaard through Marc Hellman and Bryan Conway

**FROM:** Thomas D. Morgan

**SUBJECT:** AVISTA UTILITIES: UF 4186 - Requests an order authorizing the issuance and sale of securities not to exceed \$250,000,000.

**STAFF RECOMMENDATION:**

Avista Utilities (Avista or Company) has satisfactorily demonstrated that \$114 million of the \$250 million request will be used for lawful purposes under ORS 757.415. Relevant portions of the Oregon Revised Statute follow:

**757.415 Purposes for which securities and notes may be issued; order required.**

(1) A public utility may issue stocks and bonds, notes and other evidences of indebtedness, certificates of beneficial interests in a trust and securities for the following purposes and no others, except as otherwise permitted by subsection (4) of this section:

- (a) The acquisition of property, or the construction, completion, extension or improvement of its facilities.
- (b) The improvement or maintenance of its service.
- (c) The discharge or lawful refunding of its obligations.
- (d) The reimbursement of money actually expended from income or from any other money in the treasury of the public utility not secured by or obtained from the issue of stocks or bonds, notes or other evidences of indebtedness, or securities of such public utility, for any of the purposes listed in paragraphs (a) to (c) of this subsection except the maintenance of service and replacements, in cases where the applicant has kept its accounts and vouchers for such expenditures in such manner as to enable the Public Utility Commission of Oregon to ascertain the amount of money so expended and the purposes for which such expenditures were made.

(2) Before issuing such securities a public utility, in addition to the other requirements of law, shall secure from the commission upon application an order authorizing such issue, stating:

- (a) The amount of the issue and the purposes to which the issue or the proceeds thereof are to be applied; and
- (b) In the opinion of the commission, the money, property or labor to be procured or paid for by such issue reasonably is required for the purposes specified in the order and compatible with the public interest, which is necessary or appropriate for or consistent with the proper performance by the applicant of service as a public utility, and will not impair its ability to perform that service

At this time Avista has not demonstrated that the remaining \$136 million will be used for lawful purposes. A complete analysis describing the uses of the requested debt securities has been requested from the company. Sufficient support has not been provided to date. Therefore, Staff recommends the Commission approve the Company's application, as amended by Staff, for the issuance of \$114 million in debt

securities for refinancing purposes. Upon sufficient support to indicate lawful uses of additional funds, Staff would support further approval. Any approval should be subject to the following conditions and reporting requirements:

1. Avista's authority to issue new securities should be limited to the amount of refinanced medium and long-term debt that is anticipated through 2002 and that which has been used for purposes authorized under ORS 757.415 and is authorized for the refinancing of funds expended under its Line of Credit (further described in this Memo) having been shown to be used for obligations of the Company also allowed in ORS 757.415.
2. Avista should demonstrate that the rates it achieves on the new securities are consistent with market rates or otherwise demonstrate that the rates it achieves are competitive. The demonstrations should be filed as soon as possible after each issuance and sale.
3. The Company should demonstrate that any early refunding is cost-effective.
4. The Company should file the usual Report of Securities Issued and Disposition of Net Proceeds statements as soon as possible after each sale.
5. Staff proposes that such authorization remain in effect as long as the Company maintains senior secured debt ratings of at least BBB-/Baa3 (i.e., "investment-grade") from Standard & Poor's and Moody's Investors' Service, Inc., respectively.
6. Staff further proposes that the interest rate spreads are limited as provided for in the Attached Tables, Table 1 and Table 2.
7. The Company should provide an analysis upon entering into any interest rate swap that demonstrates that such contract would likely benefit ratepayers.

For ratemaking purposes, the Commission reserves judgment on the reasonableness of the Company's capital costs, capital structure and the commissions and expenses incurred for security issuances. In its next rate proceeding, the Company will be required to show that its capital costs and structure are just and reasonable.

#### **DISCUSSION:**

On October 31, 2001, Avista filed an application for the proposed offering of up to \$250,000,000 to be used in connection with the refinancing of certain existing obligations that will become due over the next nine months as well as refinancing a portion of the outstanding balance of the Company's existing \$220 million revolving line of credit ("Revolver").

The Company has not provided specific details as to the form(s) of the issuance. The Company has indicated that the purposes would be authorized by law in forms necessary or convenient to its operations. The Company's application specified that no

specific transactions are presently pending or contemplated under the proposed authority and that the Company would only enter into transactions where the fees, interest rates and expenses charged or incurred would be competitive with market prices for similar transactions.

The Company further indicated that it may be able to reduce its borrowing costs by issuing fixed-rate or floating-rate debt and entering into one or a series of interest rate swaps ("Swap") contracts to convert fixed interest payments into favorable floating-rate payments, or vice-versa or to convert floating-rate payments tied to one index (e.g. LIBOR) into floating-rate payments tied to another index. The Company indicated that utilizing Swaps might result in savings for ratepayers.

During a conversation with Diane Thoren, Assistant Treasurer, on November 11, 2001, the Company represented that the proposed funds available under this application would, in part, be used for the refinancing of \$114 million of debt maturing over the next nine months and that a portion of the funds would also be used to pay down a portion of the existing Revolver that currently has a balance of \$155 million. During a call on October 30, 2001, the Company represented that the Revolver was used, at least in part, for "day-to-day" operations along with capital expenditures. Staff requested that the Company file an analysis that demonstrated that any refinancing of the Revolver would apply to costs incurred for lawful purposes under Oregon law. Such analysis has not been provided to date.

Of the \$250 million security issuance requested for approval in this application, \$114 million is explicitly for the refinancing of outstanding debt, duly authorized by the Commission. Staff believes that further authorization should be provided when an analysis is available from the Company that satisfactorily demonstrates that the remainder (\$136 million) will be used to refinance funds explicitly utilized for lawful purposes.

Staff believes that **after** the Company has satisfactorily demonstrated to the Commission that a portion of the Revolver was utilized for lawful purposes that the additional authority (up to \$136 million) should be granted. The additional authority should be consistent with the dollar value the Company demonstrates was utilized for lawful purposes under Oregon law.

The Company's application indicated that the fees for underwriters, banks or agents are not expected to exceed 2.5% and that the terms and specific banks, agents or underwriters would be selected at the time of issuance.

The interest rates incurred by the Company on these Securities was not specified although the Company did provide two tables that have been included as attachments

as Table 1 and Table 2. These tables provide the proposed maximum spreads for the debt instruments.

I am concerned that the indicated spreads appear to be considerably higher than those approved under recent Commission Orders. This concern is addressed in my recommended conditions. The underwriter's fees appear at the high-end of the range of recently authorized Commission orders.

The Company has provided its current rating agencies' decisions. These decisions (included in Addenda A) show that the Company's credit worthiness is weakened and the rating for senior secured debt is bordering on high-risk (i.e., non-investment-grade). The Company has represented that it is working on shoring up its credit rating and that the issuance of this long-term debt will help improve their financial footing. This will be, in part, due to the increased flexibility the company will receive by paying down its Revolver.

**PROPOSED COMMISSION MOTION:**

Avista's application, UF 4186, should be approved, as amended by Staff and subject to the conditions and reporting requirements specified in Staff's recommendations.

**Table 1. Maximum Spreads**

<u>Maturity</u>		<u>Maximum Spread Over Benchmark Treasury Yield</u> <sup>1</sup>
<u>Equal to or Greater Than</u>	<u>Less Than</u>	
9 months	2 years	+ 600 basis points <sup>2</sup>
2 years	3 years	+ 620 basis points
3 years	4 years	+ 640 basis points
4 years	6 years	+ 660 basis points
6 years	9 years	+ 675 basis points
9 years	10 years	+ 675 basis points
10 years	11 years	+ 675 basis points
11 years	15 years	+ 675 basis points
15 years	20 years	+ 675 basis points
20 years		+ 675 basis points

**Table 2. Maximum Spreads over Index**

<u>Term in Years</u>	<u>Maximum Spread over Index</u>	
	<u>LIBOR Index</u>	<u>Fed Funds Index</u>
1	+ 400 bp	+ 425 bp
2	+ 400 bp	+ 425 bp
3	+ 400 bp	+ 425 bp
4	+ 400 bp	+ 425 bp
5	+ 400 bp	+ 425 bp

<sup>1</sup> The Benchmark Treasury Yield with respect to any medium-term note maturity range means the yield to maturity of that issue of direct obligations of the United States which, out of all actively traded issues of such obligations with a remaining term to maturity within such note maturity rate, is generally considered by dealers in such obligations to be the standard for such obligations, whether federal, state or corporate, with approximately the same remaining terms to maturity. With respect to the issuance of any Securities, the Benchmark Treasury Yield shall be determined as of the time the commitment to purchase such Securities is received by the Company and the agents.

<sup>2</sup> A basis point is defined as one-one-hundredth of a percentage point, i.e., 100 basis points is 1.00 percent.