

**PUBLIC UTILITY COMMISSION OF OREGON
STAFF REPORT
PUBLIC MEETING DATE: July 15, 2003**

REGULAR **CONSENT** **EFFECTIVE DATE** _____

DATE: July 8, 2003

TO: John Savage through Marc Hellman and Bryan Conway

FROM: Thomas D. Morgan

SUBJECT: IDAHO POWER COMPANY: (Docket No. UF 4200) Application to Refund Pollution Control Bonds.

STAFF RECOMMENDATION:

The Commission should approve Idaho Power Company's (Idaho or Company) application subject to the following conditions and reporting requirements:

- 1) The Company shall file the usual Report of Securities Issued and Disposition of Net Proceeds statement as soon as possible after any issuance. Upon each issuance of Securities the Company shall file documentation with the Commission providing a specific description of the terms and conditions of each issuance of the Securities.
- 2) The Company shall demonstrate that the rate(s) it achieves on new securities is consistent with market rates or otherwise demonstrate that the rate(s) it achieves is competitive. The demonstrations should be filed as soon as possible after each issuance and sale and will include a demonstration that fees for partial issuances are reasonable.
- 3) The Company shall demonstrate that any early refunding or any call provision or required sinking fund placed on the issuance is cost-effective.
- 4) The Company shall, as of the date any hedging tools are used, conduct an economic analysis that clearly indicates the costs and/or benefits of the transaction. This demonstration shall be provided to Staff within 30 days of the consummation of the contract and will specify the future date (Exercise Date) that the Company has hedged, for purposes of the analysis.
- 5) As of the assumed Exercise Date, the Company shall provide an additional report that includes three indicative quotes consistent with the terms of the securities that were entered into by hedging alternatives. Before the Company

requests to put any of the hedging costs incurred into rates, the Company will provide this analysis and a report that clearly shows the effects of the hedges on debt costs.

- 6) The authorization shall remain in effect as long as the Company maintains debt ratings of at least BBB-/Baa3 (i.e., "investment-grade") from Standard & Poor's and Moody's Investors' Service, Inc., respectively on any debt security type it intends to market, e.g., senior secured versus unsecured.
- 7) For ratemaking purposes, the Commission will reserve judgment on the reasonableness of the Company's capital costs, capital structure and the commissions and expenses, including hedging costs, incurred for security issuances. In its next rate proceeding, the Company shall be required to show that its capital costs, including imbedded expenses, and structure are just and reasonable.
- 8) The interest rates and commissions shall be consistent with the parameters specified in the Company's application and detailed in this Memo.
- 9) If any agents or underwriters are involved in the sale of the Bonds, the names of such, the initial price to the public, any applicable commissions or discounts and the net proceeds to the Company shall be filed with the Commission. If the Debt is sold to an agent or agents as principal, the name of the agents, the price paid by the agents, any applicable commission or discount paid by the Company to the agents and the net proceeds to the Company will be filed with the Commission.

DISCUSSION:

On June 24, 2003, Idaho filed an application with the Commission, pursuant to Oregon Revised Statute (ORS) Chapter 757. It plans to refund (refinance) debt originally incurred for uses consistent with 757.415.¹

¹ Purposes allowed by law include the acquisition of utility property, the construction, extension or improvement of utility facilities, the improvement or maintenance of service, the discharge or lawful refunding of obligations that were incurred for utility purposes (such as higher cost debt or preferred stock) or the reimbursement of the Company's treasury for funds used for the foregoing purposes, all as permitted under ORS 757.415(1).

Idaho seeks authority to issue and sell up to \$49.8 million, in aggregate, of debt securities (Debt) to refund existing Pollution Control Bonds. The refunding is intended to lower the average interest rate and/or to extend the average maturities.

The Company's outstanding senior-secured debt is currently rated "A2" (Negative Outlook) by Moody's Investors Service; and "A" (Positive Outlook) by Standard & Poor's Corporation and Fitch IBCA. These ratings are reasonably within the investment-grade scale and, as a result, would result in lower interest rates and fees than other financing applications recently approved by the Commission. More details will be provided about these issues.

The Debt series may be collateralized with the Company's First Mortgage Bonds (FMBs). Upon each issuance of the Securities, the Company will file the documentation with the Commission providing the terms and conditions of each issuance of the Securities.

The Company seeks authority to enter into a "forward delivery process" that would allow it an early interest rate lock to allow the Company to take advantage of favorable interest rates. The Company may enter into interest rate swaps, or interest rate-hedging arrangements including treasury rate locks, interest rate caps and/or treasury interest rate collars.

The Company has indicated that it will place the debt on or before December 1, 2003, with an average maturity of 11 years.

Staff has some concerns about the use of hedging alternatives, in general. However, Staff feels that there is some potential value to be derived from such activities. The proposal that the Company is requesting is for a relatively short time frame (less than five months) and the underlying securities are Pollution Control Bonds, a reasonably low-cost financing source. This, coupled with the reporting requirements, help to reduce some of Staff's concerns.

Staff's concerns center on properly balancing the risks and rewards among the Company's shareholders and ratepayers. Staff includes reporting requirements to address these concerns. The Company will be expected to show the economic cost/benefit analysis that would clearly indicate the reasonableness of its decision.

Additionally, due to the current popularity of the types of hedging techniques considered by the Company, Staff will continue to evaluate how to properly align the incentives of the Company with those of its customers.

RATES AND FEES

The coupon interest rate will be less than 7.0 percent and the total "all-in" cost, including total issuance expenses, underwriting and insurance fees, will be no greater than 7.05 percent. The Company will be expected to show that expenses on a partial issuance are cost-effective.

Based on Staff's review, approval of Idaho's application with the proposed conditions will provide reasonable access to the capital markets and is therefore in the public interest.

PROPOSED COMMISSION MOTION:

Idaho's application for the authority to issue up to \$49.8 million in Debt Securities is approved with Staff's Conditions.