

City of Boulder



CITY OF BOULDER, COLORADO

DISCUSSION REGARDING POTENTIAL ELECTRIC SYSTEM ACQUISITION

December 11, 2012



The PFM Group

GENERAL TIMELINE

- December 2012 – February 2013
 - Determine feasibility of purchasing the system
 - Establish guidelines for financial and operating goals of the new system
 - Analyze financing options and costs
 - Seek general indication of credit rating

- March 2013
 - Independent review of analysis and assumptions
 - “Go” vs. “No-Go” Decision by Council

- Post March 2013 (assuming “Go” decision by Council)
 - Proceed with acquisition
 - Work toward establishing legal pledge of revenues
 - Aggregate system data and update models and projections
 - Finalize financing approach
 - Request formal credit rating
 - Bring in other financing team members (underwriter, bond/disclosure counsel, etc.)
 - City Charter amendment to provide negotiated sale

BONDING PROCESS

- Bonding process for any Electric Acquisition would not be materially different than what the City has done for the Water & Sewer System
- Enterprise fund needs to borrow money for a “project”, but can't afford to pay for that project out of available funds
 - Has a long-term revenue stream
 - Decides to issue long-term bonds to fund project with bonds to be paid from revenue stream

First and foremost though...

- City must establish clear ownership rights to the Electric System assets, authority to operate those assets and the legal authority to set rates and charges
- State Law and the legal proceedings to acquire the system and settle any disputed claims will establish the legal framework
- **Governance:** City Charter will provide the framework for the ownership, operation, management and governance of the utility

BONDING PROCESS

- Bond process can move forward once the City legally owns the system and has the rights to establish and pledge the revenue stream to investors
- Enterprise fund would put together requisite financing team and proceeds to put together required documentation
- **Bond Ordinance:** Will establish pledge to investors to operate the system according to prudent utility practice and will provide for the revenue framework to repay any debt associated with the acquisition
 - **Revenue Pledge:** establishes the necessary obligation to investors
 - **Rate Covenant:** Boulder Electric would pledge to establish rates and charges to produce revenues after the payment of O&M sufficient to pay debt service and provide a 25% cushion for investors (1.25x coverage) – *Charter Requirement*
- **Official Statement:** An offering document prepared by the Issuer that contains information about the municipality and the security pledged to meet principal and interest payments; also known as a prospectus
- **Notice of Sale:** Required for Competitive Bond Sale. A printed document announcing and soliciting bids for the bonds. It is generally an appendix to the preliminary official statement. It includes pertinent details of bidding requirements

BONDING PROCESS

- City Charter currently restricts the manner in which the bonds can be sold to a Competitive Sale Process
 - FA and City staff jointly develop plan of finance without the benefit of an underwriter's input
 - Underwriting team selected solely based on bid rate/spreads (TIC) at sale
 - Less pre-sale marketing activity
- A Negotiated Sale Process may be more appropriate for the City's potential electric bond sale
 - Identified underwriting team prior to sale date via a competitive selection process
 - Negotiated underwriting spread
 - Assistance in developing plan of finance and legal framework allows added perspective to be incorporated
 - Pro-active marketing campaign allows the City and Electric System to get out and tell its unique story to the investor base
- Negotiated Sale Process is the market standard for taxable financings and for start-up enterprises like the City's potential undertaking

CREDIT CONSIDERATIONS: OVERVIEW

- One of the largest drivers of the long term success of the Utility will be the credit rating obtained at inception
- City is "AAA" rated which provides a solid place to start the discussion regarding service territory quality
- However, in PFM's experience it is highly likely that the credit agencies will assign several areas/layers of risk to the utility and, therefore, derive a lower rating
 - Our goal is for an investment grade rating in the "BBB" to "A" category
- Similar start-up efforts have shown a credit curve:
 - Initial utility assessment is well below expected future going concern rating
 - "Start-up Period" varies but can span several years
- The Rating Process is not about absolutes. The City's Electric Enterprise will be graded on a curve as compared to other similarly situated utilities according to pre-established Rating Agency frameworks for assessment

CREDIT CONSIDERATIONS: FOCUS AREAS

- Start-up nature of the enterprise
 - Timing of hiring outside contractors and experience of those firms
 - Condition of the system and status of deferred maintenance
- Competitiveness and Rate Setting Mechanisms
 - Partially addressed by City Charter but added metrics will also be graded
 - Cost pass-throughs from Utility to customer base
 - Willingness to raise rates
- Governance
 - Establishing an oversight body that is experienced and capable
 - Formal financial, risk management and operating policies: provides functional framework for how system financial and operational risks will be addressed
 - Formal policies on transfers from the Utility to the City
- Organization / Management structure and competence
 - Includes experience of hired outside contractors

CREDIT CONSIDERATIONS: FOCUS AREAS

- Power resource management
 - Procurement plan and resulting costs
 - Stated carbon and renewables goals will be viewed critically as “before their time”
 - Engineering report on state of assets as this will impact capital improvement plans in the future
- Legal construct of bond documents
 - 1.25x stated coverage vs. target coverage a higher level?
 - Debt service reserves—stated goal from engineers report of maximum allowable
 - Reserves: initial start-up reserves and ongoing policy
- Legal Risk, if any

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CREDIT CONSIDERATIONS: FINANCIAL METRICS

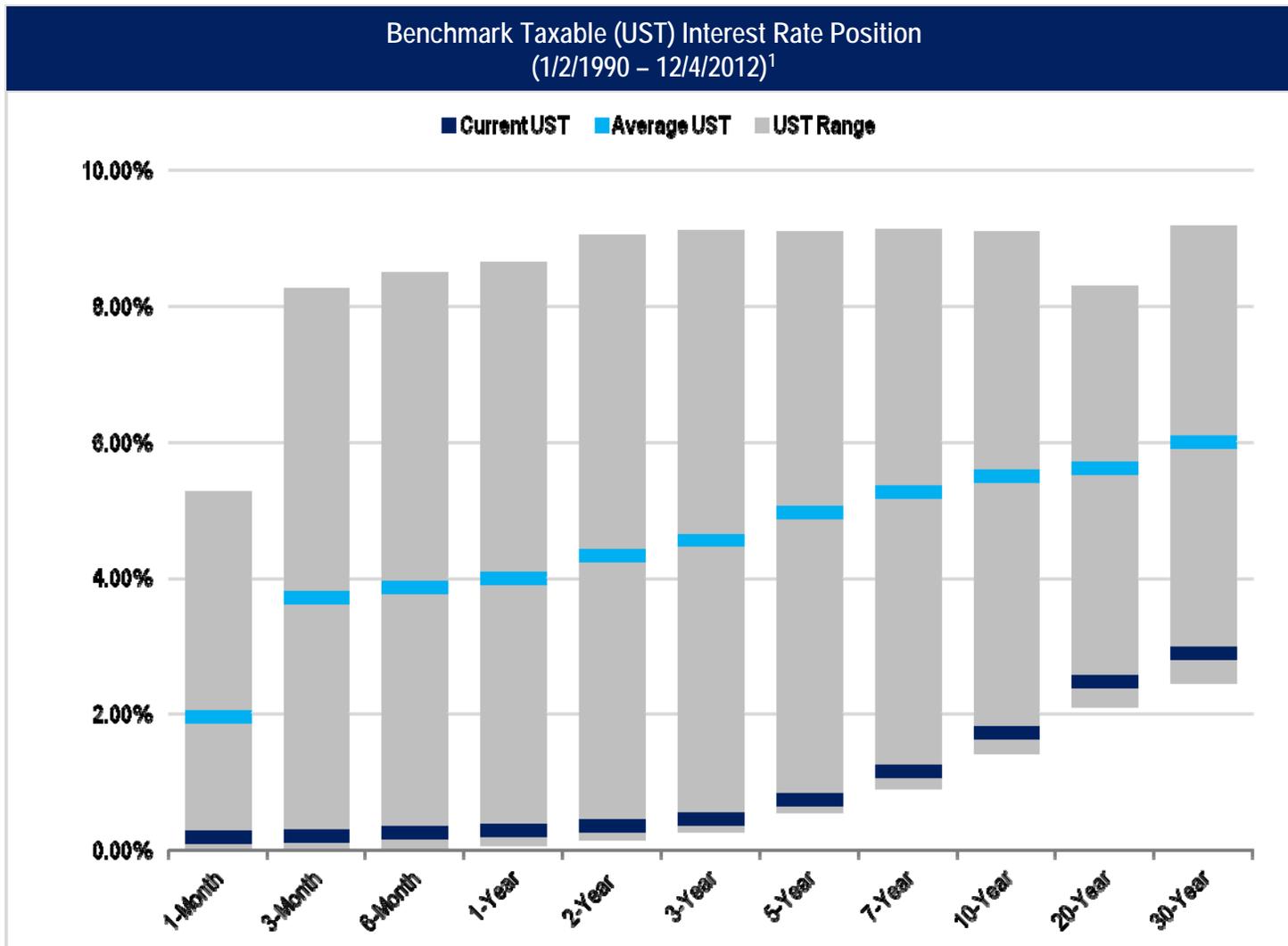
- The table below provides a sampling of both the important financial metrics evaluated by the ratings agencies and the medians for retail systems across ratings categories as measured by Fitch Ratings in their most recent U.S. Public Power Peer Study

Fitch Retail System Medians				
Metric (2011 Data)	"AA" Rated	"A" Rated	"BBB+" Rated	"BB" Rated
Debt Service Coverage (x)	2.09x	1.57x	1.42x	0.90x
Days Cash On Hand	167	84	16	(2)
Transfer Payment as % of Op. Revs	4.9%	4.5%	1.0%	0.2%
Capex / Depreciation (%)	159.7%	124.2%	165.4%	184.4%
Equity / Capitalization (%)	51.0%	38.8%	35.6%	22.8%
Debt Per Customer (\$)	\$4,542	\$7,362	\$4,145	\$9,511

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MARKET CONSIDERATIONS: INTEREST RATE POSITION

- Benchmark tax-exempt and taxable interest rates are at historic lows across the yield curve

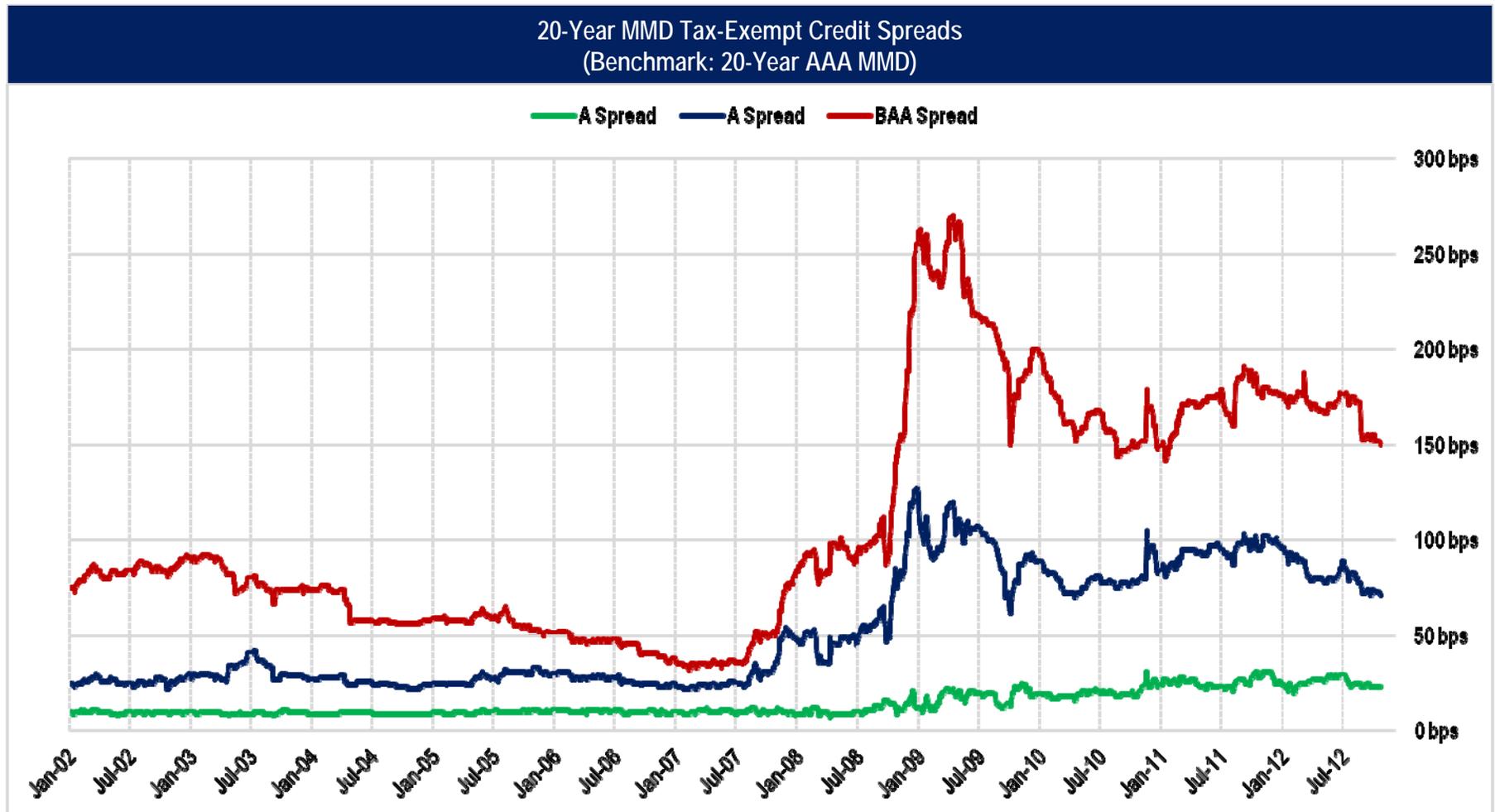


Source: Thomson Reuters, U.S. Treasury¹ Certain maturities unavailable for certain periods of time. Visit www.treasury.gov for details

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MARKET CONSIDERATIONS: CREDIT SPREADS

- Since the collapse of the bond insurance market, investors have been focused on underlying credit factors. While credit spreads have retreated substantially from the severely elevated levels seen during the financial crisis, they remain above the pre-crisis / bond insurance era levels



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MARKET CONSIDERATIONS: BORROWING RATE COMPARISON

- Current benchmark rates are low even for lower rated credits

