

FUNDING STRATEGIES & RECOMMENDATIONS

Study Session, 11/26/2007

Guiding Principles

1. We can best serve our customers by providing multiple utility services and utility infrastructure improvements
2. We should implement annual financial plans to achieve a combined (as a whole) positive “Change in Net Assets” (positive bottom line)
3. As a whole, we should manage rates to cover operating costs as measured by an acceptable operating ratio
4. A surcharge is an appropriate way to manage risk and volatility if necessary
5. Utility Services cash reserves should be available to fund the capital needs of any District utility service
6. Cost control and efficiencies should be a component of annual financial plans
7. Debt should be managed within established parameters

Team Goals

1. Develop a strategy for funding the Rate Stabilization Fund
2. Fund an Operating Reserve Fund to qualify for coverage under the new Master Bond Resolution
3. Evaluate debt management options
4. Address short-term funding requirements

Funding Strategy - Net Results

1. Effective utilization of cash reserves
2. Funding of capital programs for Rock Island, Lake Chelan and Networks
3. Reduce ~50% of Senior Non-Hydro debt
4. Improve debt coverage and reduce risk

Non-Hydro Debt Reduction Options

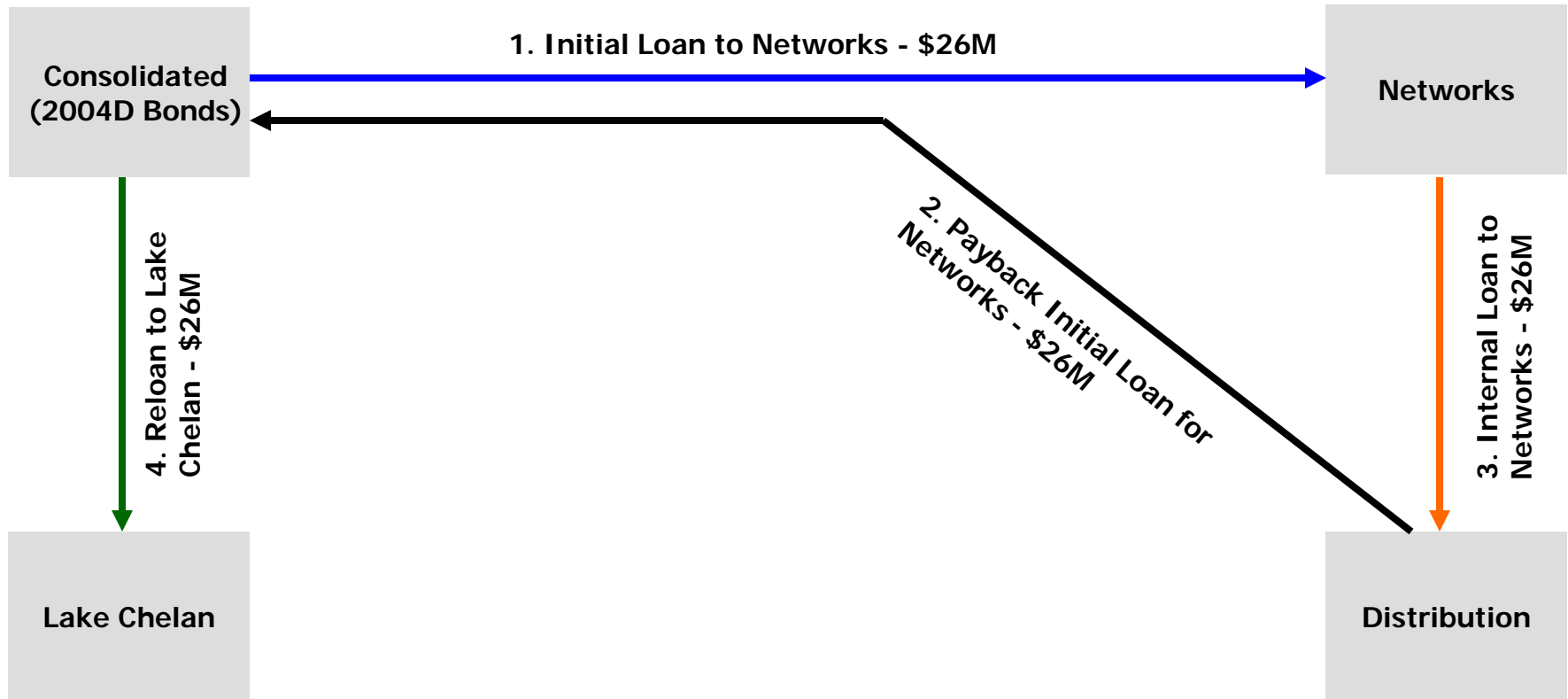
Senior Non-Hydro Coverage is challenged through 2011
in stressed wholesale years

$$\text{Senior Coverage Ratio} = \frac{\text{Net Revenues}}{\text{Debt Service}}$$

Tools or options to mitigate the risk of low coverage

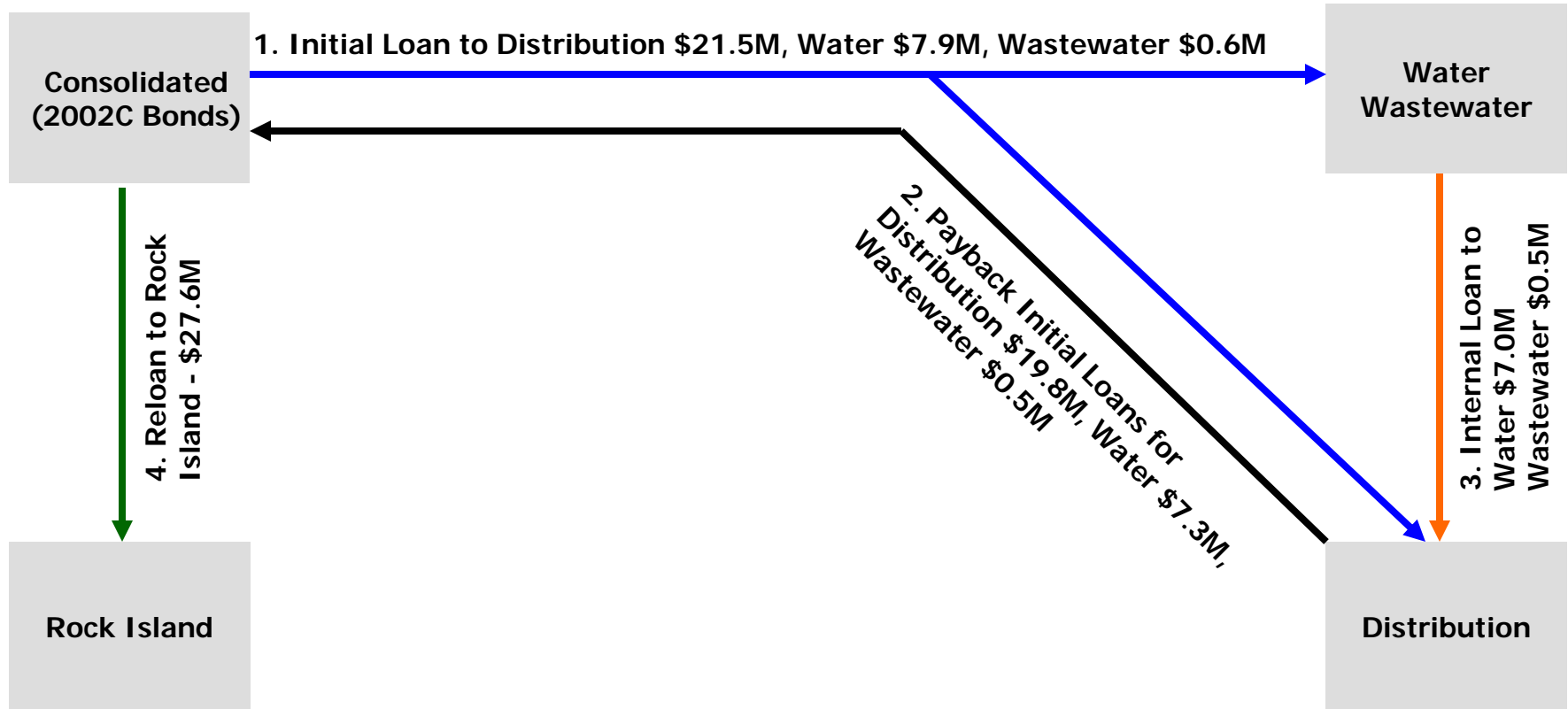
1. Cash defeasance (take the debt out)
 - \$106.2M debt + \$5.6M cost to defease = \$111.8M
2. Refinance
 - Increase to subordinate debt service costs
3. Repayment & reloaning concept

Repayment & Reloaning Concept



1. The District issued Consolidated System 2004D Bonds and loaned part of the bond proceeds to Networks.
2. The Distribution System pays back Networks 2004D loan to the Consolidated System with available cash.
3. Networks reimburses the Distribution System for this payback via an internal loan to be paid back over time.
4. The Consolidated System reloans these funds to Lake Chelan for its capital and licensing funding needs.

Repayment & Reloaning Concept



1. The District issued Consolidated System 2002C Bonds and loaned part of the bond proceeds to Distribution, Water and Wastewater.
2. The Distribution System pays back its 2002C loan the Water and Wastewater 2002C loans to the Consolidated System with available cash.
3. Water and Wastewater reimburses the Distribution System for this payback via an internal loan to be paid back over time.
4. The Consolidated System reloans these funds to Rock Island for its capital funding needs.

Repayment & Reloaning Concept

Benefits:

- Reduces Non-Hydro debt by 50%
- Bypasses defeasance or refinancing cost
- Improves coverage
- Reduces future coverage risks
- Effective and efficient use of cash reserves
- Cost effective financing for hydro projects needing funding

Rate Stabilization Fund (RSF)

- Mechanism in Master Subordinate Resolution that impacts Subordinate Cover
 - Initial 'free' deposit prior to January 1, 2008
 - Future withdrawals or deposits will impact subordinate cover

$$\text{Subordinate Cover Ratio} = \frac{\text{Net Revenues} + \text{RSF Withdrawals} - \text{RSF Deposits}}{\text{Debt Service}}$$

- Use of funds/priority
- Senior cover challenged to 2011
- RSF – Additional tool for future cover challenge
- Propose deposit of \$50.0M into the Rate Stabilization Fund

Operating Reserve Fund (ORF)

- New “available funds” definition under Consolidated System Master Resolution
 - Revenue Funds do not count as available funds
 - Approximately \$210M in Distribution Revenue Fund at year end
- Propose transfer of all but \$10.0M for working capital needs out of Distribution’s Revenue Fund into the Operating Reserve Fund
- Funds in the Operating Reserve Fund would still be available for any District purpose
- Periodic transfers between Revenue and Operating Reserves to adequately maintain both funds

Networks 2008 funding needs

- Remaining 2007 funding needs
 - \$8.1M authorized under prior resolution #06-13029
- Authorization needed to fund \$23.8M of 2008 costs
 - Capital \$13.0M
 - Debt service \$10.8M
- Funding amount cannot exceed 2008 budget
- Propose loaning Networks the remaining 2007 funding needs and also the 2008 budgeted amount for total loans of \$31.9M

Total Required Funding through 2008	\$ 31,926,000
Less: 2007 authorized funding Reso #06-13029	<u>\$ (8,120,000)</u>
Requested authorization to fund for 2008 budget	\$ 23,806,000

Net Cash Impact of Finance Plan

	Revenue Fund	Operating Reserve	Rate Stabilization Fund	Consolidated Loan Repay Fund	Rock Island Constr	Lake Chelan Constr	Networks Constr
Est Bal at 12/31 before transfers	210,000,000	-	-	-	-	-	(8,120,000)
<i>Resolution #06-13029</i>							
Fund NW for Remaining 2007	(8,120,000)						8,120,000
<i>Resolution #1</i>							
2002C Payback DS Loan (P)	(19,766,544)			19,766,544			
Payback WS Loan (P)	(7,325,849)			7,325,849			
Payback WW Loan (P)	(537,607)			537,607			
Reloan to RI				(27,630,000)	27,630,000		
2004D Payback NW Loan (P)	(26,000,000)			26,000,000			
Reloan to LC				(26,000,000)		26,000,000	
<i>Resolution #2</i>							
Fund the Rate Stabilization Fund	(50,000,000)		50,000,000				
Fund the Operating Reserve Fund	(64,444,000)	64,444,000					
<i>Resolution #3</i>							
Fund NW for 2008	(23,806,000)						23,806,000
	10,000,000	64,444,000	50,000,000	-	27,630,000	26,000,000	23,806,000

Balance in the Distribution System → 124,444,000

Resolutions Goals

First Resolution

- Reduce the Senior Non-hydro debt coverage requirement by repaying \$53.6M of Non-Hydro Consolidated System loans
- Authorize internal replacement loans to Water, Wastewater and Networks from Distribution for a total of \$33.9M
- Fund Rock Island \$27.6M capital requirements & Lake Chelan \$26.0M capital and licensing requirements

■ Second Resolution

- Initial deposit to the Rate Stabilization Fund \$50.0M
- Transfer all but \$10.0M from Distribution's Revenue Fund into Distribution's Operating Reserve Fund

■ Third Resolution

- Loan Networks up to \$23.8 million for 2008 capital and debt service requirements

Questions?

ADDITIONAL INFORMATION

Senior Non-Hydro Debt Defeasance Analysis

Series	Par to Defeasance	Final Maturity	Call Date	Tax Status	Advance Refundable?	Cost to Cash Defeasance (2)	Increased Debt Service if Refunded (5)		System
1998C	\$ 565,000	07/01/18	07/01/08	Non-AMT	Yes	\$ 578,359	\$250/year add'l debt service		WS
2001C	123,523	07/01/32	07/01/11	AMT	No	136,720	\$300k/year add'l interest + est. \$15k add'l par	(3)	IS
2002C	27,630,000	07/01/33	07/01/12	Non-AMT	Yes	29,559,099	\$89k/year add'l debt service		DS, WS, WW
2003A	451,389	07/01/32	07/01/13	AMT	No	512,778	\$400k/year add'l interest + est. \$75k add'l par	(3)	IS
2004B	15,679,161	07/01/34	07/01/12	Non-AMT	Partially	16,952,511	\$49k/year add'l debt service	(4)	DS, WS, IS
2004C	15,000,000	07/01/24	Any time (1)	Taxable	(taxable)	15,805,147	\$145k/year add'l int + est. \$1.1MM add'l par	(3)	NW
2004D	26,000,000	07/01/24	35 Days	Taxable	(taxable)	26,000,000	\$15k/year add'l int + est. COI \$425k	(3)	NW
2004E	20,120,000	07/01/20	07/01/12	Non-AMT	No	21,564,135	\$149k/year add'l int + est. \$1.8MM add'l par	(3)	DS, NW, IS
2005A	680,000	07/01/39	07/01/15	AMT	No	744,666	\$5k/year add'l int + est. \$80k add'l par	(3)	IS
	<u>\$ 106,249,073</u>					<u>\$ 111,853,415</u>			

(1) Make-whole call

(2) Assuming January 1, 2008 defeasance; excluding accrued interest

(3) Assumes taxable refunding

(4) Assumes entirely tax-exempt refunding, which is subject to further review by tax counsel

(5) Assumes 1.5% issuance costs and bond insurance at 17 basis points