

Exploring Consolidation

The Chugach-ML&P Study Process

**Elizabeth Vazquez, Board Chair
Chugach Electric Association**

**Alaska Railbelt Electrical Grid Authority
Technical Conference
November 26, 2007**

Why Study the Possibilities?

- **Close Geographical Proximity**
- **Small Size of Each Utility**
 - Chugach Electric 64,400 members
 - Municipal Light & Power 30,000 customers
- **Both Have Aged and Inefficient Natural Gas Generation Facilities**
- **Increases in Fuel Cost**

Objective of Phase I Study

Determine Benefit, if Any, to Electric Customers from a Reorganization, Merger, Consolidation, Joint Operation of Chugach Electric and Municipal Light & Power

Key Principles of Phase I Study

- 1. Ensure greatest benefit for existing ratepayers of the two utilities.**
- 2. Eliminate duplication of services.**
- 3. Increase efficiency of services.**
- 4. Create rate stability for current and future ratepayers.**
- 5. Maximize asset value for owners of both companies.**

The Participants

Chugach Electric

- Board of Directors
- Management

MOA

- Mayor & Administration
- ML&P Management

Advisory Panel

Each side has unique responsibilities

Each desiring an open, transparent process

The Participants

Advisory Panel

- **Chugach BOD Chair Elizabeth Vazquez, co-chair**
- **Mayor Mark Begich, co-chair**
- **Robert Ballow – CPA and investor**
- **Mike Barry – Former chair of AIDEA**
- **Chris Birch – Anchorage Assemblyman**
- **Steve Pratt – ML&P Advisory Commissioner**
- **Don May – Former Alaska Public Utility Commissioner**

Phase I Study Schedule

June 2007	July	August	September
Agreement Signed	Advisory Panel Formed Consultant Selected	Data Gathering Report Preparation	
October	November	December	January 2008
Data Gathering Report Preparation	Draft Phase I Report Released Review & Analysis Public Comment		

Where Are We Now?

- **Report Released November 5, 2007**
- **MOA & CEA's Comments held until November 29**
 - **Management & Consultants to Review and Analyze Report**
 - **Chugach Submits Extensive Questions to Navigant, Consultant. To date, MOA and ML&P Have no Questions**
 - **Consultant Provides Answers on November 22, 24 & 25**
 - **Chugach Staff and Consultants Presently Reviewing Answers- Possible Additional Questions**
- **Public Comment November 29**

The Phase I Report

- **Intended to be a High-Level Screening Study**
- **Identifies Alternatives for Possible Further Study**
- **7 Scenarios Considered**
 - **Joint Ownership of New Generation**
 - **Joint Operations**
 - **Acquisitions**

The Phase I Report Results

- **Savings Through Joint Ownership of New Generation**
- **Potential Savings Through Joint Operations**
- **Potential Savings Through Change in Utility Ownership – but Uncertain Due to Tax and Legal Issues**

NOTE: Cost of capital differences between tax exempt government (Authority, Municipal) & taxable (Coop and IOU) forms were the primary considerations evaluated in this study.

Some Assumptions of Consultant

- **Ability to Issue Tax Exempt Financing for Certain Case Models:**
 - Case 1- ML&P Acquires Chugach
 - Case 4- Governmental Entity Acquires Both
 - Case 5 - New G&T (Govt. Entity) acquires all of the Generation & Transmission Assets of Both
- **No Ability to Issue Tax Exempt Financing For Other Case Models**

Additional Assumptions of Consultant

- **Focus on Cost of Capital Differences**
 - Between taxable and non-taxable debt issued to finance transaction

Difference of 1.5 basis points between taxable and non-taxable debt

- 5% interest for non-taxable debt
- 6.5% interest for taxable debt

Additional Assumptions by Consultant

Acquisition Price =

**Outstanding Debt + Defeasance Premium
+ Capital Credits/Retained Earnings**

**This Should not be Considered a Market Value,
Only a basis for Screening Comparison of
the Alternatives**

Phase I Report Findings Table

CASE	Savings* (\$millions)	% Savings
1 – ML&P Acquires CEA co-op	\$168	6.3%
2 – CEA co-op Acquires ML&P	(\$45)	(1.7%)
3 – IOU Acquires both	(\$243)	(9.1%)
4 – Gov't Authority buys both	\$218	8.2%
5 – New Gov't G&T	\$30	1.1%
6 – Joint Contracted Operations	\$97	3.6%
7 – Jointly Owned Power Plant	\$86	3.2%

* Net Present Value of retail rate savings 2009-2020

Summary of Anticipated Issues

- **Tax Questions**

- Tax-exempt Financing
- Tax Consequences to CEA (membership and co-op)

- **Legal Issues**

- Statutory Restrictions
- Voting Requirements
- Debt Restrictions

- **Regulatory Requirements & Policy**

Anticipated Issues

Tax Questions

Issuance of Tax-exempt Bonds to Finance Acquisitions – Critical for Case 1, 4 & 5

- **Case 1 – ML&P Acquiring CEA**
- **Case 4 – Governmental Entity Acquires Both**
- **Case 5 – New G&T (Governmental Entity) Acquires all of the Generation & Transmission Assets of Both**

Totally Dependent on Tax- Exempt Financing- “each assumes the ability to issue tax-exempt debt for the acquisition” page 61 of Report

Anticipated Issues

Tax Questions

– Taxable consequences to CEA:

- The Cooperative – presently exempt from paying federal income tax. Income from non-electric sources cannot exceed 15% of income. CEA could lose tax exemption for the year of sale or acquisition. Income would be taxed at 35%.**
- Members – would need to pay tax on their distribution share.**

Anticipated Issues Regulatory

- **Example**
- **Case 4 – Governmental Entity Acquires Both ML&P & Chugach**

- Involves creating an entity that is 100% debt financed
- No equity ownership
- Unusual for regulated utilities in Alaska

“If this option were to be pursued, extensive consultation with the RCA would likely be necessary to demonstrate the ability to maintain financially secure performance without equity.” Page 63 of Report.

Anticipated Issues- Legal Issues

Statutory Limitations on Merger Activity

- **Chugach – is only permitted to merge with other cooperatives. AS 10.25.240**
- **ML&P is not a cooperative**
- **Thus, Chugach and ML&P cannot merge with present state statutory restriction unless successor corporate form is changed.**

Anticipated Issues - Legal

- **Statutory Limitations on Selling, Leasing, or Disposing of Utility Assets**
 - **ML&P – MOA’s charter requires 60% of voters to approve (Section 16.02).**
 - *BUT: Only 50% is required to amend the charter.*
 - **Chugach – Bylaws require 2/3 approval of a minimum 50% members voting (Article IX Section I).**
 - *BUT: There has never been more than 30% voter participation in any previous CEA election.*

Anticipated Issues - Legal

– Debt Restrictions

- **ML&P – If Assets are Acquired or Transferred, Tax-exempt Debt Must be Defeased & Notice Provided to IRS**
- **Chugach may have limitations on their bonds**

Actual Recommendation of Phase I Draft Report

**Evaluate whether tax-exempt financing
can be used for case 1 and 4.**

If this is not possible,

Focus on the combination Cases of 6 & 7

- Joint Contracted Operations**
- Jointly Owned Power Plant**

Case 6 Analysis

Joint Contracted Operations

- **No sale of assets or utility.**
- **Each utility places large portion of their employees into a separate operating entity to manage, operate and maintain many functions.**
- **Functions such as distribution, customer service, G&T operation, maintenance, etc.**

Case 7 Analysis

Single Jointly-Owned Power Plant

- **Both utilities would retain all their assets, including generation, transmission and distribution.**
- **Jointly own a 260 MW gas-fired combined cycle generating plant, each owning 50% of the plant.**
- **Each Utility brings their own financing and their own fuel for their pro rata share of electricity produced by plant.**

Next steps

- **After Careful Analysis, Chugach Submitted Extensive List of Questions to Consultant**
- **Consultant Submitted Answers to Chugach on November 22, 24 and 25**
- **Analysis of Answers & Possible Additional Questions**
- **Hold Comments on Report Until November 29th**
- **Next Public Meeting November 29th**
- **Determine Next Course of Action**

Electric Industry Restructuring Coming to Anchorage?

- **YES! It's already here with the ID of several options for an ML&P-CEA reorganization or joint operations.**
- **Electric consumers worldwide have benefited from realigning assets in more economic and efficient ways.**
- **This study has identified up to 8% in savings looking only at consolidation and financing changes.**
- **The Future Task : Think beyond those two items and explore other opportunities for even greater cost savings for our consumers!**

Questions?