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MEMORANDUM

2001 SEP 12 P 2:44

AZ CORP COMMISSION
DOCUMENT CONTROL

TO: Docket Control

FROM: Steven M. Olea
Acting Director
Utilities Division

DATE: September 10, 2001

RE: STAFF REPORT FOR THE APPLICATION OF SALT RIVER PROJECT AGRICULTURAL IMPROVEMENT AND POWER DISTRICT FOR AN ORDER AUTHORIZING ITS ISSUANCE OF REVENUE BONDS AND REFUNDING REVENUE BONDS (DOCKET NO. E-02217A-01-0183)

Attached is the Staff Report for the application of Salt River Project Agricultural Improvement District for an order authorizing its issuance of revenue bonds and refunding revenue bonds. Staff recommends approval of the request without a hearing.

SMO:LAJ:jbc

Originator: Linda A. Jaress

Attachment: Original and Eleven Copies

Arizona Corporation Commission
DOCKETED

SEP 12 2001

DOCKETED BY | nac

Service List for: Salt River Project Agricultural Improvement District
Docket No. E-02217A-01-0183

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STAFF REPORT
UTILITIES DIVISION
ARIZONA CORPORATION COMMISSION

SALT RIVER PROJECT AGRICULTURAL IMPROVEMENT DISTRICT.
DOCKET NO. E-02217A-01-0183

APPLICATION
FOR AUTHORITY TO ISSUE REVENUE BONDS AND
REFUNDING REVENUE BONDS

SEPTEMBER, 2001

STAFF ACKNOWLEDGMENT

The financial analysis contained in the Staff Report for Salt River Project Agricultural Improvement District. (Docket No. E-02217A-01-0183) was prepared by Linda A. Jaress.

Linda A. Jaress

Linda A. Jaress
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Asher Emerson prepared the Engineering analysis.

Asher Emerson

Asher Emerson
Utilities Engineer

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SCHEDULES

Introduction

On March 1, 2001, Salt River Project Agricultural Improvement and Power District ("SRP" or "the District") filed an application with the Arizona Corporation Commission ("Commission") for an order authorizing the issuance of up to $500,000,000 in revenue bonds and up to $550,000,000 in refunding bonds. On June 11, 2001, SRP filed Amendment No. 1 to the application requesting approval of up to an additional $175,000,000 in revenue bonds to refund commercial paper and up to an additional $200,000,000 of refunding bonds.

SRP is both a political subdivision of the State of Arizona and an agricultural improvement district. It supplies electricity in areas in the Arizona Counties of Maricopa, Pinal and Gila. At the end of SRP's fiscal year ending April 30, 2001, it served 746,368 customers.

SRP has three affiliated companies. One wholly owned subsidiary, New West Energy Corporation ("New West"), received a Certificate of Convenience and Necessity to provide competitive retail electric service in Arizona in Commission Decision No. 61944, dated September 17, 1999. The District acts as a guarantor of New West's contractual obligations. New West markets SRP's surplus energy and provides other retail energy services. Papago Park Center, Inc., another wholly owned subsidiary of SRP, is engaged in land development. It develops and manages approximately 320 acres of land owned by SRP adjacent to its headquarters in Tempe. The third affiliate, The Salt River Valley Water Users' Association, is the predecessor of the District and operates and maintains the irrigation system of the Salt River Project as the District's agent. The District's electric operations commonly subsidize the water operations of the Salt River Valley Water Users Association.

Jurisdiction

SRP exists as an agricultural improvement district pursuant to Arizona Revised Statutes. Exhibit 1 lists selected Arizona Revised Statutes applicable to agricultural improvement districts and to this application for financing in particular. These statutes provide SRP broad power to determine the purpose, amount, terms and types of bonds, including refunding bonds, to issue. The sentence in bold print on the first page of Exhibit 1 is the portion of the statute that gives the Corporation jurisdiction over SRP's bond issuances. The Commission does not have jurisdiction over the setting of SRP's electric rates.

Previous Commission Decisions for SRP Bond Issuances

The two most recent Commission decisions approving SRP bond issuances are Decision No. 58386, dated September 2, 1993, and Decision No. 58625, dated May 2, 1994. The first Decision authorized the issuance of $990.0 million of refunding revenue bonds and included a limitation on the percentage of SRP's capital structure that could be comprised of derivatives. The second Decision approved the issuance of $2.3 billion of refunding revenue bonds and retained the 7.0 percent limitation on derivatives.

SRP has customarily requested broad authority for its revenue bond and refunding revenue bond issuances. Other than the addition of the 7.0 percent limitation and some reporting requirements, the Commission has historically approved the authority SRP requested. The Commission has provided upper limits to the debt issuances while leaving the dates and amounts of individual series along with the terms and specific form of the bonds to SRP's discretion.

Commercial Paper

Commercial paper is a form of short-term debt consisting of unsecured promissory notes issued by a corporation. The maturity of commercial paper is typically less than 270 days, but can exceed one year.

SRP currently has outstanding commercial paper in the amount of $525.0 million; $150.0 million of Series A commercial paper and $375.0 million of Series B commercial paper. Decision No. 55209, dated September 18, 1986, and Decision No. 56381, dated March 9, 1989, approved the issuance of up to a total of $425.0 million of revenue bonds to be used to retire the Series B commercial paper. Currently there is no authority outstanding to issue bonds to retire the Series A.

SRP's amendment to the application requests authorization to issue up to $175.0 million of revenue bonds to retire SRP's Series A commercial paper. The requested amount exceeds the balance of Series A commercial paper to provide for discounts, contributions to the debt reserve fund and issuance expenses. When the revenue bonds are issued, the proceeds will be used to pay and retire the Series A commercial paper and/or other obligations incurred by SRP pursuant to the commercial paper program including, but not limited to draws on the revolving credit agreements underlying the Series A.

Revenue Bonds

The application requests authorization to issue up to $500.0 million in revenue bonds to be used to finance plant. Revenue bonds issued by an agricultural improvement district are secured by a pledge of and a lien on the revenues of its electric system. As such, they differ from mortgage bonds issued by most investor-owned utilities, which are secured by the assets of the issuing utility. Additionally, interest paid on revenue bonds issued by a district is not subject to income tax. Thus, districts are able to issue revenue bonds at coupon rates considerably lower than rates paid on taxable corporate bonds of comparable quality. Interest and amortization of bond discount and issuance expenses on SRP's various outstanding revenue bonds results in an effective, embedded interest rate of 5.88 percent. For comparison purposes, Southwest Gas Company's embedded cost of debt in its current rate case is 7.98 percent.

Revenue bonds issued by SRP often have "call" features. Call features are debt contract provisions that allow for the redemption (refund) of a bond prior to its scheduled maturity. In general, call features stipulate the date after which a bond issue may be redeemed and the call premium, which must be paid to the bondholders when the bonds are called before maturity. Any bond refunded prior to its call date is considered an "advance refunding".

Refunding Bonds and the Defeasance Process

SRP is also requesting authorization to issue up to $550.0 million in refunding bonds, the funds from which will be used to refund the $500.0 million of bonds previously discussed. SRP uses several criteria to decide when to refund and which bonds to refund. Interest rates on outstanding bonds, current market interest rates, the costs of funding an escrow, call provisions on the refunding candidates and potential debt service savings are all considered. This information is utilized in an analysis to determine the overall net present value savings for each issue considered. According to SRP, it historically has not refunded long maturity debt unless the debt service savings were 7.0 percent or greater, but it has refunded shorter maturity debt with savings as low as 3.0 percent.

The refunding process is often carried out by the use of a process called "in substance defeasance." Arizona Statutes (See Exhibit 1, A.R.S. Section 48-2471.C.) specifically allow the defeasance process. Defeasance consists of the issuance of new revenue bonds and purchasing debt securities issued by various state and local governments ("SLGs") with the proceeds. The maturities of the SLGs correspond precisely to the call dates of the revenue bonds refunded. The SLGs are placed in an escrow account to be held by a trustee whose duty it is to pay the bondholders their interest and principal when payable. Under this process, the SLGs are irrevocably placed in a trust with the sole purpose of paying off the future contractual payments relating to the debt. Thus SRP's obligation to repay the principal and interest is a contingent one permitting SRP to record a journal entry removing the "refunded" debt from its balance sheet.

The refunded bonds are in fact still held by the bondholders but removed from SRP's books. There is no impact on the holders of the debt. They are generally unaware that these transactions have been entered and do not experience any interruption in the receipt of principal and interest payments. SRP removes the debt from its balance sheet and replaces it with the new debt which has a debt service requirement with a reduced present value.

Bond Derivatives

SRP's requested authority includes a request for authorization to issue bond derivatives, also known as alternative bond products. Bond derivatives are debt instruments that provide bondholders an income stream based on the market rather than a coupon rate. For example, some bond derivatives allow investors to receive a variable rate of return which fluctuates directly with changes in market rates of interest, while others provide investors with the opportunity to earn a rate of return, which moves inversely to those same interest rate changes. Large institutional investors typically purchase bond derivatives for use in hedging their interest rate positions. Because the derivatives more precisely match the needs of certain investors, the cost to the District can be less than traditional bonds.

The District currently has outstanding two types of alternative bond products. As part of its 1993 Series C bond sale, SRP issued $36.7 million of Short Term Adjustable Rate Securities ("STARS") and $36.7 million of Short Term Rate Inverse Payment Exempt Securities ("STRIPES"). The total of the two derivative issues of $73.4 million equals slightly over 2.0

percent of SRP's total outstanding debt at the end of the most recent fiscal year. While the returns received by the holders of STARS and STRIPES vary with market interest rates, the District pays a combined fixed rate on the derivatives of 5.05 percent.

The Commission first granted the District the authority to issue derivatives in Decision No. 58386. As previously mentioned, the Decision also restricted the District from issuing derivatives in excess of 7.0 percent of its total capitalization.

Staff believes that the District should continue to have the ability to issue these alternative debt instruments in a limited amount. SRP has not indicated that it has ever missed any opportunities to reduce the cost of debt or experience debt service savings based upon the 7 percent limitation from Decision No. 58386.

Financial Health

SRP's financial statements reflect continued strong financial health. Exhibits 2 and 3 illustrate SRP's balance sheets and income statements for the past three years. On the balance sheet, it can be seen that long-term debt has declined while accumulated net revenues (equity) increased. Comprehensive net income, as shown on the income statement, has steadily increased over the past three years. Exhibit 4 illustrates SRP's strengthening capital structure showing long-term debt falling from 63.0 percent of the capital structure in 1999 to 57.3 percent in 2001.

One remarkable financial statistic found on the financial statements is SRP's cash position. At the end of the 2000-2001 fiscal year, SRP's cash, cash equivalents and temporary investments totaled close to $1.0 billion. Cash equivalents and temporary investments generally can be readily converted to cash. Exhibit 5 illustrates financial information from other Arizona electric utilities and from selected municipal utilities throughout the country. It shows that SRP's balance of cash, cash equivalents and temporary investments, far exceeds that of any of the other utilities shown. Also, were it not for an adjustment for unrealized losses on securities of $36.6 million and SRP's write-down of $85.0 million related to the Competition Transition Charge, SRP would have experienced greater net profits than all of the utilities shown on the Exhibit except for LADWP.

In December 2000, Moody's Investors Service, Municipal Credit Research, Public Power published an analysis of SRP's financial health and credit strength in particular. In discussing SRP's financial strengths, Moody's listed SRP's proactive response to competitive forces, New West Energy, SRP's exposure to competition and stranded costs, competitive rates, growth projections and diverse power sources as the primary factors contributing to its financial health.

Moody's commented that:

> "The Salt River Project's Aa2 rating and positive outlook rests on its strong financial position, competitive rates, diverse power mix, and a history of stable management....SRP has favorable financial operations with strong revenues and debt service coverage of 3.35 times in fiscal 2000....Moody's believes that SRP's

debt management strategy will allow the utility to continue to lower its power rates, improving its competitiveness."

Because SRP's financial health is so strong and its bond ratings are favorable, it expects to issue previously approved bonds in September at interest rates of approximately 5.0 percent.

Engineering Analysis

On July 31, 2001, SRP filed an "Independent Review of the Salt River Project Distribution Capital Program" prepared by R.W. Beck. Staff Engineer, Asher Emerson, reviewed and analyzed the application and the Beck report including the 2002-2007 Distribution Construction Work Plan and determined that the planned distribution plant additions for 2002 through 2007 and their costs are reasonable. Staff's Engineering Report containing this analysis is attached as Exhibit 6.

Electric Competition and the Competition Transition Charge

During the fiscal year ending April 30, 1999, the District evaluated the carrying amount of its generation operations on its books in relation to projected cash flows from their use. The final result of the analysis was that SRP determined that $850.0 million of assets were "impaired."

SRP's Board of Directors determined that $795.5 million of the $850.0 million would be recovered through a non-bypassable Competition Transition Charge ("CTC"). The CTC would be collected on a per kWh basis over the six-year period from December 31, 1998, to December 31, 2004, at different rates depending on the customer class. For example, the CTC for residential service is $0.0067 per kWh, while the CTC for large general service is $0.0116. During the fiscal years ending in 1999, 2000 and 2001, $34.5 million, $132,2 million and $145.3 million of revenue respectively, was generated by the CTC for a total recovery of $312.0 million.

Based upon projections, SRP believes that it is no longer probable that the full CTC amount will be collected. Therefore, on April 30, 2001, SRP management reduced the amount of the CTC asset resulting in a charge to depreciation and amortization of $85.0 million. Also, there are mechanisms in place for further evaluation of the CTC with respect to actual market price variances from the 2.6-cent market price per kWh used to determine the CTC.

The impact of a CTC is that it generally recovers non-cash expenses and is instrumental in a utility's accumulation of cash. It is notable that although SRP has recovered $312.0 million from its CTC, it has lost no customers to competition that have not returned.

Capital Expenditure Budget and Purpose of the Debt

For the fiscal years 2001 through 2003, SRP expects to spend approximately $1.1 billion on capital items. Distribution plant, the largest category of expenditures, will require $522.2

million of expenditures while transmission, generation, competitive services, corporate services and water operations will require, in total, $596.7 million over the same period.

The $500.0 million of new debt will be used to finance distribution plant. In the past, the allocation of SRP's debt proceeds to the various distribution, generation or transmission functions was inconsequential because the three functions were included under one rate. However, as competition nears and rate unbundling impacts the retention of customers, the allocation of new debt solely to distribution assets could affect rates to distribution customers. In the process of SRP's recent rate unbundling, SRP assigned outstanding debt to each of the three functions in roughly the same proportion as plant.

SRP has indicated that although it is financing distribution plant with the proposed debt, for accounting purposes, issuance purposes and rate setting, it will continue to spread the debt balances among the three functions proportionately. However, for income tax purposes, SRP will "attribute" the new bond proceeds solely to distribution plant. The IRS Code restricts the use of assets paid for by tax-exempt debt to "non-private use." If, for example, SRP desired to sell a substation to a non-governmental party, it is likely that any debt associated with the substation would have to be extinguished before the transfer.

Recapitalization Plan

Over the next few years, SRP plans to enact a new master bond resolution and recapitalize its debt. The 1972 master bond resolution will be modernized and bonds issued under that resolution will be eliminated. The concern that the Federal Energy Regulatory Commission ("FERC") may eventually require SRP to place its transmission assets under the control of a Regional Transmission Organization ("RTO") is one reason for the recapitalization plan. In the event the transmission assets are used for purposes other than to serve SRP's customers (within certain designated levels), the interest on the revenue bonds partially attributed to transmission would become immediately taxable to the bondholders. At that time, SRP would likely call or purchase the bonds at whatever price is necessary at that time. Depending on interest rates and the bond market, premature refunding or purchasing of outstanding bonds could be uneconomic. SRP, through its recapitalization plan, intends to take actions to refund or deface bonds attributed to the whole system, transmission included, and issue bonds attributable only to the distribution business in their place to avoid the possibility of uneconomic, forced refunds.

The result of the recapitalization process is expected to be at present value savings ranging from $20.0 to $40.0 million. The process would entail the Board of Directors passing a new master bond resolution and SRP calling, purchasing with equity or issuing refunding bonds to eliminate all bonds issued under the old resolution. SRP has indicated that if interest rates rise to a level where any part of the process becomes uneconomic, the process may be halted until such time as the issuance of bonds for refunding provides savings.

The result of the recapitalization will be to significantly increase the amount of debt attributed to distribution. SRP believes that this is a favorable time to recapitalize because competition is in a hiatus, its cash resources are strong and interest rates are extremely favorable.

SRP currently has outstanding approximately $2.0 billion of refunding authority from this Commission under which most of the recapitalization will be accomplished.

Analysis

Staff has concerns about SRP earmarking all of the proposed new debt funds to finance distribution assets only. This could cause the cash requirements of the distribution business to be disproportionately higher than the cash requirements of the more competitive sectors of SRP's business. If the result is higher rates to the distribution customers, the customers would have no alternative provider as their service would not be subject to competition. Although SRP has assured Staff it has no plans to divest generation and/or transmission, the concept is certainly within the realm of possibilities.

SRP has also assured Staff that the allocation or "attribution" of debt for income tax purposes will not be adopted for ratemaking. SRP's Unbundled Revenue Analysis for the May 2000 Price Adjustment (supplied to Staff in response to a data request) illustrates how SRP sets its unbundled rates. The Analysis indicates that target rates of return are set for each business function based primarily on SRP's weighted cost of capital for the whole company. However, the target rates of return are also adjusted according to the risk related to the function. Finally, the revenue requirement determined in the budget is spread across the functions to reach the target rates of return.

SRP's current rate setting process does not specifically allocate debt service requirements to the individual business functions. The rates of return, which are based on the cost of capital, indirectly allocate interest payments among the functions. Thus, if SRP continues to construct rates as they currently do the attribution of all of the new debt to the distribution function for tax purposes will not affect customers' rates for distribution service. SRP's Board of Directors is the ultimate decision-maker on such issues.

SRP's position in the electricity market is complicated by the outstanding revenue bonds. It could be at a significant disadvantage if it must refund or refinance debt when interest rates are not favorable. At the same time, the low interest rates on revenue bonds help keep SRP's costs below other electric service providers who must issue debt with higher-rate taxable interest. Thus, if SRP does not attribute a disproportionate amount of debt to the distribution service, it could be at a competitive disadvantage in the future.

Although SRP has assured Staff that it has no plans to divest generation or transmission, one of the reasons given to attribute the new debt to distribution is to prepare for the eventual possibility of the transfer of transmission assets into a regional transmission organization. Because the distribution assets are unlikely to be transferred, SRP's attribution of any new debt to distribution is a competitively advantageous course of action for SRP.

Conclusions

Staff believes that SRP's management has shown restraint and conservatism in its financing practices. SRP's debt ratio is falling and SRP has shown little reliance upon derivatives and other alternative bond products. However, from time to time management and financing policies of all utilities can change. Staff believes that the 7.0 percent limitation adopted by Decision Nos. 58386 and 58625 will not compromise SRP's ability to negotiate and sell financial instruments that are in the public interest, and should be retained in this decision.

Staff believes that SRP should be allowed the flexibility to refinance bonds when interest rates and other capital market factors make refunding prudent. The Commission has allowed such authority in the past and SRP's financial health and bond rating indicate that it has made prudent decisions relating to issuing and refunding bonds. The Commission's alternative would be to approve only the revenue bonds and require SRP to apply for separate approval to issue refunding bonds when they determine the time is right. The apparent risk in that scenario is that the necessary processing time at the Commission could cause SRP to miss an advantageous market window.

Recommendations

Staff recommends approval of SRP's application. Staff recommends that the Commission authorize SRP to issue revenue bonds for construction purposes in an amount not exceeding $500,000,000, refunding bonds in an amount not to exceed $550,000,000 to refund the revenue bonds, revenue bonds for purposes of retiring Series A commercial paper in an amount not exceeding $175,000,000 and refunding bonds in an amount not exceeding $200,000,000 to refund the bonds used to retire the Series A commercial paper.

Staff recommends that the Commission limit the issuance of bond derivatives and alternative bond products to 7.0 percent of SRP's capital structure.

Staff recommends that SRP file certain information related to the revenue bonds and refunding bonds authorized in this docket. SRP should file information including the date of issuance, interest rate, maturity, the amount of discount or premium and issuance expenses within two weeks after the issuance of any bonds authorized by the decision in this docket. Also, the Commission should order SRP to file within two weeks of the issuance of refunding bonds, an analysis showing the savings to be experienced from the issuance of refunding bonds authorized by the decision in this docket.

With the above conditions, Staff believes that, pursuant to the requirements of A.R.S. Section 40-302, the debt issuance is reasonably necessary and appropriate for the purposes specified in the application and that such purposes are not reasonably chargeable to operating expenses or to income. Staff recommends approval of the authorizations requested in the application without a hearing.

Exhibit 1

SELECTED ARIZONA REVISED STATUTES APPLICABLE TO AGRICULTURAL IMPROVEMENT DISTRICTS

40-301. Issuance of stocks and bonds; authorized purposes

B. A public service corporation may issue stocks and stock certificates, bonds, notes and other evidences of indebtedness payable at periods of more than twelve months after the date thereof, only when authorized by an order of the commission.
C. The commission shall not make any order or supplemental order granting any application as provided by this article unless it finds that such issue is for lawful purposes which are within the corporate powers of the applicant, are compatible with the public interest, with sound financial practices, and with the proper performance by the applicant of service as a public service corporation and will not impair its ability to perform that service.

48-2302. District as municipal corporation
An agricultural improvement district organized under the provisions of this chapter is a public, political, taxing subdivision of the state, and a municipal corporation to the extent of the powers and privileges conferred by this chapter or granted generally to municipal corporations by the constitution and statutes of the state, including immunity of its property and bonds from taxation.

48-2463. Purposes for which revenue bonds may be issued
After the organization of an agricultural improvement district, the board of directors may cause revenue bonds to be issued for any undertaking.

48-2464. Powers of district
In the exercise of the powers granted or permitted by law, the district shall have the additional power:
1. To issue its bonds to finance, in whole or in part, the costs of any undertaking.
3. To fix, levy, and collect fees, rentals or other charges for the use of or in connection with the services and facilities of the district or the undertaking, and, if any agreements with holders of bonds are made as may be provided by law, to fix, levy and collect such fees, rentals and other charges in accordance with such agreements and subject thereto.

48-2465. Revenue bonds
A. To undertake, carry out and accomplish any or all of the purposes and powers of the district authorized or permitted by law, the district may borrow money and issue its negotiable bonds therefor. No bonds may be issued unless authorized by a resolution of the board of directors adopted by an affirmative vote of a majority of its members, which shall set forth a brief description of the undertaking to be accomplished, the estimated cost thereof, and the amount, maximum rate of interest and time of payment of the bonds...
B. No bonds shall be issued pursuant to this article until the district first secures an order authorizing the issuance of such bonds in accordance with those provisions of section 40-302 pertaining to the issuance of bonds. All additional costs which are necessarily incurred by

the corporation commission in connection with securing such order shall be paid for by the district.

48-2466. Forms of bonds
A. All bonds and coupons issued under the provisions of this article are payable in lawful money of the United States and shall be payable in not exceeding fifty years from the date of the bond.
B. The bonds may be issued in one or more series, bear such date or dates, mature at such time or times not exceeding fifty years from their respective dates, be in such denomination or denominations, be in such form, carry such registration, exchangeability and interchangeability privileges, be payable in such medium of payment and at such place or places, within or without the state, be subject to such terms of redemption prior to their express maturity at such time with or without premium, be equally and ratably secured without priority, or be entitled to or subject

to such priorities on all or any portion of such revenues and receipts of the district or of the undertaking and contain such other terms, conditions and covenants as the board of directors may adopt in the authorizing resolution.
C. The bonds shall bear interest at such rate or rates and are payable at such time or times and in such manner as the board of directors may determine by resolution.

48-2470. Sale of bonds
A. Bonds shall be sold at public or private sale, as the board of directors may determine.

48-2471. Refunding bonds
A. If a district has outstanding any bonds issued pursuant to this article or article 6 of this chapter, it may issue, by resolution of the board of directors, bonds to refund such outstanding bonds. Such bonds shall be designated "refunding bonds" and shall be secured by the revenue of the district or any part thereof or all or any part of revenues pledged to the bonds which have been thereby refunded.
B. Refunding bonds may be issued in an amount up to an amount sufficient to pay:
1. The principal of the outstanding bonds or other obligations to be refunded.
2. The redemption premium, if any, on such outstanding bonds on the prior redemption thereof.
3. The interest due and payable on such outstanding bonds to the dates upon which the principal of such bonds matures or to the dates upon which the outstanding bonds are called for redemption by the district, which call dates may, subject to the resolutions authorizing said outstanding bonds, be any date prior to maturity of said outstanding bonds, including any interest theretofore accrued and unpaid.
4. Any expenses of the issuance and sale of refunding bonds, including the creation of initial debt service reserve funds and reasonable and necessary fees of financial and legal advisers.
Refunding bonds may be issued to refund more than one issue of outstanding obligations notwithstanding that such outstanding obligations may have been issued at different times and for different purposes.

C. Any monies in the sinking or reserve funds or other funds for such outstanding bonds to be refunded may be used for the purpose stated in paragraphs 1, 2, 3 and 4, of subsection B, or may be deposited in a sinking fund or reserve fund or other funds for the refunding bonds to be issued. When refunding bonds issued pursuant to this section are sold, a sufficient amount of the proceeds of the refunding bonds shall be invested and reinvested in direct obligations of the United States of America or in time deposits evidenced by certificates of deposit in the bank or trust company holding such fund, or in time deposits evidenced by certificates of deposit in one or more banks or trust companies, each of which is a member of the federal deposit insurance corporation or in such other securities or obligations as may be determined by the board which are scheduled to mature with interest so as to provide funds to pay when due, or when called for redemption, the outstanding bonds to be refunded together with the interest thereon and redemption premiums, if any, and such proceeds or obligations shall, and other funds legally available for such purpose may, be deposited in the respective principal and interest redemption funds and shall be held in trust for the payment of the refunded bonds with interest and

redemption premiums, if any, on maturity or redemption. The bank or trust company holding the proceeds of such refunding bonds in trust shall deliver monthly to the treasurer of the district which issued the refunding bonds a copy of the document evidencing each transaction relating to the trust fund.

D. When refunding bonds are issued under this chapter, the resolution authorizing them may also provide for other bonds to be issued jointly with such refunding bonds for any other purpose or purposes authorized and provided for by law. Any refunding bonds may be sold as provided in this article or may be exchanged for the bonds to be refunded thereby.

48-2473. Disposition of proceeds and other monies

All proceeds received from the sale of the bonds, all fees, rental or other charges received by the district from any undertaking financed by the bonds, and all monies received from any source in connection therewith shall be used, applied and disposed of as the board determines by its bond resolution or trust agreement.

Exhibit 2

Salt River Project Agricultural Improvement and Power District

Combined Balance Sheets
As of April 30, 2001, 2000 and 1999
($000)

	2001	2000	1999
ASSETS			
Utility Plant			
Plant in Service			
Electric	$ 5,948,320	$ 5,765,976	$ 5,509,688
Irrigation	234,392	227,423	216,371
Common	$ 391,698	$ 396,627	$ 379,862
Total Plant in Service	$ 6,574,410	$ 6,390,026	$ 6,105,921
Less Acc. Depreciation	$ (3,102,243)	$ (2,926,142)	$ (2,742,260)
	$ 3,472,167	$ 3,463,884	$ 3,363,661
Plant Held for Future Use	$ 31,134	$ 31,134	$ 32,795
Construction Work in Progress	326,215	200,805	255,505
Nuclear Fuel, Net	$ 37,044	$ 40,980	$ 40,956
Net Plant	$ 3,866,560	$ 3,736,803	$ 3,692,917
Non-Utility Property and Investments and Segregated Funds	$ 439,875	$ 661,404	$ 634,587
Cash, Cash Equivalents and Temporary Investments	$ 986,985	$ 455,792	$ 378,333
All Other Current Assets	$ 544,118	374,079	333,083
Deferred Charges and Other Assets	$ 516,410	$ 747,545	$ 899,348
TOTAL ASSETS	**$ 6,353,948**	**$ 5,975,623**	**$ 5,938,268**
CAPITALIZATION AND LIABILITIES			
Long-Term Debt	$ 3,098,273	$ 3,164,866	$ 3,235,386
Accumulated Net Revenues	$ 2,312,014	$ 2,038,893	$ 1,898,934
Current Liabilities	$ 545,383	$ 387,251	$ 404,594
Deferred Credits and Other Non-Current Liabilities	$ 398,278	$ 384,614	$ 399,354
TOTAL CAPITALIZATION AND LIABILITIES	***$ 6,353,948***	***$ 5,975,624***	***$ 5,938,268***

Source: SRP's Annual Reports

Exhibit 3

Salt River Project Agricultural Improvement and Power District

Combined Statements of Net Revenues and Comprehensive Income
For the Years Ended April 30, 2001, 2000 and 1999
($000)

	2001	2000	1999
Operating Revenues	$ 3,026,787	$ 1,797,745	$ 1,714,158
Operating Expenses			
Power Purchased	$ 914,646	$ 368,628	$ 338,624
Fuel Used in El. Generation	514,049	278,263	262,574
Other Operating Exp.	471,670	304,237	318,382
Maintenance	156,002	146,631	122,779
Depreciation and Amortization	473,334	368,016	290,500
Taxes and Tax Equivalents	$ 82,335	$ 90,931	$ 91,819
Total Operating Expenses	$ 2,612,036	$ 1,556,706	$ 1,424,678
Net Operating Revenues	$ 414,751	$ 241,039	$ 289,480
Other Income (Expenses)			
Interest Income	$ 68,147	$ 55,699	$ 47,090
Other Income (Expense) net	$ (2,662)	$ (5,652)	$ 1,629
Total Other Income, net	$ 65,485	$ 50,047	$ 48,719
Net Revenues Before Financing Costs	$ 480,236	$ 291,086	$ 338,199
Financing Costs			
Interest on Bonds Net of Capitalized Interest	$ 141,578	$ 146,070	$ 147,263
Amortization of Bond Discount and Issuance Expenses	4,951	5,449	5,253
Interest on Other Obligations	$ 24,011	$ 20,887	$ 19,463
Net Financing Costs	$ 170,540	$ 172,406	$ 171,979
Net Revenues Before Extraordinary Item	$ 309,696	$ 118,680	$ 166,220
Extraordinary Item	$ -	$ -	$ 54,701
Net Revenues	$ 309,696	$ 118,680	$ 111,519
Other Comprehensive Income			
Unrealized Gains on Securities	$ (36,575)	$ 21,279	$ 18,885
Comprehensive Income	$ 273,121	$ 139,959	$ 130,404

Source: SRP's Annual Reports

Exhibit 4

Salt River Project Agricultural Improvement and Power District

Statistics and Financial Ratios
For the Years Ended April 30, 2000, 1999 and 1998
($000)

	2001	%	2000	%	1999	%
Capital Structure						
Long-Term Debt	$ 3,098,273	57.3%	$ 3,164,866	60.8%	$ 3,235,386	63.0%
Accumulated Net Revenues	$ 2,312,014	42.7%	$ 2,038,893	39.2%	$ 1,898,934	37.0%
Total Capital	$ 5,410,287	100.0%	$ 5,203,759	100.0%	$ 5,134,320	100.0%
Debt Service Coverage Ratio	4.72		3.35		3.20	
		% Change		% Change		
Customers	746,368	2.7%	727,070	3.7%	701,196	
Total Electric Sales (million kWh)	36,323	10.7%	32,801	3.8%	31,615	

Exhibit 5

Salt River Project
Comparison with Municipal Electric Utilities
($000)

	Salt River Project	Arizona Public Service	Tucson Electric Power	City Public Service of San Antonio	Orlando Utilities Commission	LADWP	Omaha Public Pwr. District	Seattle City Light
Revenue	$3,026,787	$3,480,252	$ 1,028,368	$ 1,338,970	$ 501,131	$ 2,396,137	$ 567,734	$ 396,065
Net Income	$ 273,121	$ 306,594	$ 51,169	$ 276,003	$ 51,307	$ 402,078	$ 70,850	$ (52,028)
Long-term Debt	$3,098,273	$1,806,908	$ 1,989,914	$ 2,687,689	$ 1,388,343	$ 3,948,168	$ 708,837	$1,023,192
Equity	$2,312,014	$2,119,768	$ 295,660	$ 2,139,531	$ 598,431	$ 3,058,800	$ 1,082,768	$ 373,465
	$5,410,287	$3,926,676	$ 2,285,574	$ 4,827,220	$ 1,986,774	$ 7,006,968	$ 1,791,605	$1,396,657
Long-term Debt	57.3%	46.0%	87.1%	55.7%	69.9%	56.3%	39.6%	73.3%
Equity	42.7%	54.0%	12.9%	44.3%	30.1%	43.7%	60.4%	26.7%
	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Net Plant	$3,866,460	$4,910,835	$ 1,706,290	$ 4,089,140	$ 1,512,663	$ 4,241,600	$ 1,589,624	$1,242,167
Capital Expenditures	$ 372,962	$ 464,368	$ 98,063	$ 389,545	$ 79,859	$ 148,134	$ 117,545	$ 177,974
Cash, cash equiv. & Temp. Inv.	$ 984,985	$ 2,609	$ 88,712	$ 116,177	$ 39,097	$ 439,923	$ 14,359	$ 21,100
Customers	746,368	850,000	340,000	884,107	264,700	1,433,427	293,331	349,558

Sources: Annual Reports

Salt River Project Agricultural Improvement District, year ending April 30, 2001.
Includes water customers.

Arizona Public Service Company, year ending December 31, 2000.

Tucson Electric Power, year ending December 31, 2000.
Capital structure includes capital lease obligations.
San Antonio, year ending January 31, 2001. Includes 305,811gas customers.
Net income before transfer of $185.0 million to the City of San Antonio.

Orlando Utilities Commission, Year ending September 30, 2000. Includes 117,935 water customers.

Department of Water and Power of the City of Los Angeles, year ending June 30, 2000.
Provides water service but all amounts are energy only.

OPPD, Year Ending December 31, 2000.

Seattle City Light, year ending December 31, 2000.

Exhibit 6

M E M O R A N D U M

TO: Linda Jaress, Executive Consultant III

FROM: Asher Emerson
Utilities Engineer

DATE: August 29, 2001

RE: SALT RIVER PROJECT FINANCING E-02217A-01-0183

Staff Engineering ("Engineering"") reviewed the above referenced application, which was submitted by the Salt River Project Agricultural Improvement and Power District ("SRP"). SRP seeks approval for issuance of $675,000,000 in revenue bonds and $750,000,000 in refunding revenue bonds. These revenue bonds are to be used in financing SRP's distribution construction work plan for fiscal year 2002 through fiscal year 2007.

Utility Overview

SRP provides electric power to approximately 750,000 customers in its 2,900 square mile service territory in central Arizona. SRP's distribution system consists of more than 140 substation sites and 28,800 miles of distribution lines.

Assessment of Distribution Plan

Engineering has reviewed SRP's 2002-2007 Distribution Construction Work Plan ("Plan"). In order to evaluate the Plan, Engineering centered on the following three questions.

- Is the level of projected customer growth reasonable?
- Are the projected distribution capital expenditures necessary and reasonable?
- Are the reliability targets reasonable and are the reliability targets being met?

Customer Growth

Since 1996, SRP has added approximately 124,000 new customer connections. SRP's customer accounts has increased approximately 20 percent since 1996, or at a 3.7 percent, average annual growth rate. The 2.9 percent average annual customer growth projection in SRP's plan appears reasonable as the Arizona Department of Economic Security projects a 3.0 percent average annual population growth in the Phoenix-Mesa area for the same time period.

Projected Distribution Capital Expenditures

A primary driver of SRP's distribution capital expenditures is customer growth. The New Business portion is 39 percent of the plan. SRP projects the expenditures per new customer added to average $2,815 per customer compared to $2,247 per customer average for the last 10 years. The Distribution Line portion of the budget is 21 percent of the plan. SRP projects distribution line expenditures to decrease by 3.4 percent per year, from $233 in 2002 to $196 in 2007. Underground cable replacements is 18 percent of the plan. Underground cable replacements are a significant portion of the plan because 50 percent of SRP's underground cable is direct buried and is reaching the end of its service life. The remaining 22 percent of plan expenditures is for Substations, other distribution facilities and Municipal Aesthetics. Engineering finds that the projected distribution capital expenditure are reasonable and appropriate.

Reliability Targets

SRP uses three measures of reliability that are industry standards and widely tracked by electric utilities across the United States. These measures are:

- CAIDI (customer average interruption duration index) is a measure of the average duration of interruptions per year and is measured in minutes.
- SAIFI (system average interruption frequency index) is a measure of the average number of interruptions per customer per year.
- SAIDI (system average interruption duration index) is a measure of the average number of customer outage minutes per year and is the product of CAIDI and SAIFI.

SRP
Reliability Index Comparison
1991 - 2000

	CAIDI	SAIFI	SAIDI
SRP Average	49	1.5	75
SRP Target	45	1.5	67.5
Industry Median	106	1.22	88

Engineering believes SRP uses reasonable reliability targets and has generally met its reliability targets over the last decade. A major storm and a cascading extra high voltage outage throughout the interconnected western U.S. grid, both in August of 1996, impacted the average for the ten-year period.

Conclusion

SRP is seeking financing approval to construct facilities that will (1) be used for new member line extensions, and (2) improve system reliability through the replacement of deteriorated underground cable. Engineering believes the planned distribution plant additions and their costs for 2002 through 2007 are reasonable given the growth being experienced by the utility and the information provided in its Distribution Construction Work Plan.