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OPEN MEETING ITEM OPEN MEETING

MEMORANDUM

RECEIVED

TO: THE COMMISSION

2006 MAR -6 P 12: 52

FROM: Utilities Division

AZ CORP COMMISSION  
DOCUMENT CONTROL

DATE: March 6, 2006

RE: TUCSON ELECTRIC POWER COMPANY FOR A FINANCING ORDER  
AUTHORIZING VARIOUS FINANCING TRANSACTIONS (DOCKET NO.  
E-01933A-05-0654)

Please find attached the Staff Report and Recommended Opinion and Order for the above referenced matter. Staff recommends approval with conditions.

Ernest G. Johnson  
Director  
Utilities Division

EGJ:DTZ:lhmlLF

ORIGINATOR: Daniel T. Zivan

**STAFF REPORT  
UTILITIES DIVISION  
ARIZONA CORPORATION COMMISSION**

**TUCSON ELECTRIC POWER COMPANY**

**DOCKET NO. E-01933A-05-0654**

**APPLICATION FOR FINANCING**

**MARCH 6, 2006**

## STAFF ACKNOWLEDGMENT

The Staff Report for Tucson Electric Power Company, Docket No. E-01933A-05-0654 was the responsibility of the Staff members listed below: Daniel Zivan was responsible for the review and financial analysis of the Company's application. Kim Battista was responsible for reviewing the Commission's records on the Company and determining compliance with Commission policies and rules.



DANIEL ZIVAN  
PUBLIC UTILITIES ANALYST III



KIM BATTISTA  
CHIEF – COMPLIANCE AND ADMINISTRATION

**EXECUTIVE SUMMARY  
TUCSON ELECTRIC POWER COMPANY  
DOCKET NO. E-01933A-05-0654**

Tucson Electric Power Company ("TEP" or "Company") filed an application with the Arizona Corporation Commission ("Commission") on September 16, 2005 requesting authorization to amend its Springerville Common Facilities Leases ("Common Facilities Leases") and its Irvington Unit 4 Lease ("Irvington").

TEP is a Class "A" Arizona C-corporation that serves approximately 375,000 customers and is located in and around Tucson, Arizona.

TEP proposes to refinance its Common Facilities Leases and its Irvington Lease in order to avoid a "special event of loss" on the Common Facilities Leases which would result in a loss of at least \$59 million and to obtain more favorable financing for both leases.

The pro forma times interest earned ratio ("TIER"), debt service coverage ratio ("DSC") and cash coverage ratio ("CCR") resulting from the proposed refinancing of the leases are 1.56, 1.71 and 2.32, respectively.

Staff concludes that the lease refinancing for the purposes stated in the application is lawful and within TEP's corporate powers, compatible with the public interest, consistent with sound financial practice and will not impair its ability to provide services.

Staff recommends approval of the request for authorization to cause the Common Facilities Leases and Irvington Lease to be refinanced.

TABLE OF CONTENTS

	<u>PAGE</u>
INTRODUCTION .....	1
NOTICE .....	1
BACKGROUND.....	1
PURPOSE OF FINANCING.....	1
<i>COMMON FACILITIES LEASE</i> .....	1
<i>IRVINGTON LEASE</i> .....	2
DESCRIPTION OF PROPOSED FINANCING .....	2
FINANCIAL ANALYSIS .....	2
COMPLIANCE .....	3
STAFF CONCLUSIONS AND RECOMMENDATIONS .....	4

SCHEDULES

SELECTED FINANCIAL DATA.....	Schedule DTZ -1
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ATTACHMENTS

COMPLIANCE REPORT.....	ATTACHMENT 1
PUBLIC NOTICE .....	ATTACHMENT 2

## **Introduction**

Tucson Electric Power Company ("TEP" or "Company") filed an application with the Arizona Corporation Commission ("Commission") on September 16, 2005 requesting authorization to amend its Springerville Common Facilities Leases ("Common Facilities Leases") and its Irvington Unit 4 Lease ("Irvington").

## **Notice**

Notice of a financing application was published in *The Arizona Daily Star* and in *The Daily Territorial* on November 23, 2005. *The Arizona Daily Star* and *The Daily Territorial* are newspapers of general circulation in Pima County, Arizona. The affidavits of publication are attached along with a copy of the Notices.

## **Background**

TEP is a wholly owned subsidiary of UniSource Energy Corporation. TEP, a class "A" C-corporation located in Tucson, Arizona, provides generation, transmission and distribution services to approximately 375,000 customers in Cochise and Pima counties. TEP's current rates were approved in Decision No. 59594, dated March 29, 1996.

## **Purpose of Financing**

### *Common Facilities Lease*

In January of 1991 TEP instituted a payment moratorium which resulted in the Company withholding payments to various lenders and lessors. As a result, TEP restructured the Common Facilities Leases and Irvington Lease. TEP is required to cause the secured notes underlying the Common Facilities Leases "...to be refinanced or refunded prior to June 30, 2006, in order to avoid a "special event of loss." If a special event of loss were to occur, the Common Facilities Leases would be terminated and TEP would be required to repurchase the Common Facilities (as defined herein) for an amount equal to the higher of stipulated loss value of \$127 million or the fair market value of those Common Facilities."<sup>1</sup> The principle balance due on the Common Facilities Leases on June 30, 2006 will be approximately \$68 million. If a special event of loss were to occur, TEP would be forced to repurchase the facilities for an amount of at least \$127 million despite only owing a balance of \$68 million resulting in an additional cost of at least \$59 million. In addition to avoiding additional cost, TEP anticipates that it can obtain an interest rate on the Common Facilities Leases approximately 2.5 percent below the existing interest rate by refinancing.

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<sup>1</sup> Page 1, Line 24 of TEP's application

### *Irvington Lease*

TEP proposes to cause the Irvington Lease to be refinanced. There is no requirement for TEP to refinance the Irvington Lease at this time; however the Company states that it may be able to lower the cost of debt service by taking advantage of existing market conditions resulting in a lower interest rate. The applicable interest rate on the Irvington Lease is 8 percent, which represents 7.25 percent plus a .75 percent annual fee for bond insurance. TEP anticipates that it will be able to obtain an interest rate that is approximately 2.0 percent lower than the current interest rate on the Irvington Lease.

### **Description of Proposed Financing**

TEP proposes to cause the Common Facilities Leases to be refinanced by issuing lease obligation bonds to investors, obtaining financing through one or more financial intermediaries or by amending and extending the existing lease. TEP anticipates that it will obtain financing at an interest rate equal to the current London Interbank Offered Rate ("LIBOR"), which was 4.79 as of January 9, 2006, plus 100 to 150 basis points with a five year term.<sup>2</sup> An interest rate of LIBOR plus 150 basis points would represent an interest rate reduction of 2.5 percent.

TEP proposes to cause the Irvington Lease to be refinanced through the sale of lease obligation bonds to investors or by obtaining financing from one or more financial intermediaries. TEP anticipates that it will obtain financing similar, if not identical, to that of the Common Facilities Lease which would be at an interest rate of LIBOR plus 100 to 150 basis points with a five year term.<sup>3</sup> An interest rate of LIBOR plus 150 basis points would represent an interest rate reduction of 2.0 percent.

### **Financial Analysis**

Schedule DTZ-1 presents historical financial information for the year ended December 31, 2004 in column A. Column B presents pro forma financial information with the effects of the proposed refinancing of the Common Facilities Leases at an interest rate reduction of 2.50 percent and the Irvington Lease at an interest rate reduction of 2.00 percent. Schedule DTZ-1 presents TEP's interest expense for 2004 in the amount of \$157.0 million (column A), and TEP's interest expense with the effects of the proposed financing in the amount of \$154.6 million (column B). The effects of the proposed refinancing would result in TEP reducing interest expense in the amount of approximately \$2.4 million.

Schedule DTZ-1, column A shows the times interest earned ratio ("TIER"), debt service coverage ratio ("DSC") and cash coverage ratio ("CCR") for the year ended December 31, 2004. TEP had a 1.54 TIER, a 1.69 DSC and a 2.28 CCR. Schedule DTZ-1, column B shows that the

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<sup>2</sup> Response to data request DTZ 2.2

<sup>3</sup> Response to data request DTZ 2.2

pro forma effects of the proposed refinancing are to increase TIER to 1.56, DSC to 1.71 and CCR to 2.32.

TIER represents the number of times earnings cover interest expense on long-term debt. A TIER greater than 1.0 means that operating income is greater than interest expense. A TIER less than 1.0 is not sustainable in the long term but does not mean that debt obligations cannot be met in the short term.

DSC represents the number of times internally generated cash will cover required principal and interest payments on long-term debt. A DSC greater than 1.0 indicates that operating cash flow is sufficient to cover debt obligations. A DSC less than 1.0 means that debt service obligations cannot be met by cash generated from operations and that another source of funds is needed to avoid default.

CCR represents the number of times internally generated cash covers required interest payments on long-term debt. A CCR greater than 1.0 means that operating cash flow is greater than interest expense. A CCR of 2.32 indicates that TEP would be able to meet the loan covenant that requires maintaining a CCR greater than 2.25.

### **Compliance**

The Compliance Report is attached and states that TEP had four compliance items that required discussion. The four items are listed and discussed below. Staff has determined that none of the items listed below represent legitimate compliance delinquencies.

1. In Decision No. 58379 TEP was required to "File monthly reports with the Commission which account for the funds collected by the temporary fuel surcharge, and will include the amount of the under-collected balance." The Company asserts that the requirement for the compliance item expired in December 2003. Staff has determined that the Company has complied with this requirement and that this item is no longer delinquent.
2. In Decision No. 60221 TEP was required to "...file with Staff, subject to a confidentiality agreement, reports on January 1 and July 1 of each year, including the projects in which it is considering investing so that Staff can act more quickly if expedited actions are required." The Company asserts that this requirement has been superseded by A.A.C. R14-2-805. Staff has recommended, and the Company has concurred, that TEP should file a request for an indefinite waiver for this portion of Decision No. 60221.
3. In Decision No. 59224 TEP was required to "...provide reports to the Commission and access to all affiliate books and records, as outlined in Paragraph 17 of its Application for Limited Waiver." The Company states that it has sold its partial ownership in its Coors Power Plant, therefore, absolving it of this requirement. Staff

recommends that this item be eliminated from TEP's compliance report as the Company has sold the related facilities.

4. According to Decision No. 59224 "TEP and the Nations Energy Subsidiary will report all sales of power to the Staff annually under the terms of a confidentiality agreement. The Nations Subsidiary will provide access to all information needed to verify the accuracy of the reported information." The Company states that Nations Energy has ceased to participate in the sale of power, therefore, absolving it of this requirement. Staff recommends that this item be eliminated from TEP's compliance report as the Company has sold the related facilities.

### **Staff Conclusions and Recommendations**

Staff concludes that the proposed refinancings of the Springerville Common Facilities Leases and the Irvington Unit 4 Lease are lawful and within the corporate powers of the applicant, would be compatible with the public interest, consistent with sound financial practices and not impair TEP's ability to provide service.

Staff concludes that TEP has complied with the requirements set forth in Decision No. 58379.

Staff recommends that TEP file a request for an indefinite waiver as it pertains to the Compliance matter set forth in Decision No. 60221.

Staff recommends that the Compliance items related to Decision No. 59224 and discussed herein be eliminated from the Compliance report.

Staff recommends approval of the request for authorization to cause the Common Facilities Leases and the Irvington lease to be refinanced or amended in the manner discussed herein.

Staff further recommends approval of TEP's request to enter into amendments and agreements necessary to refinance the lease debt underlying the Common Facilities Leases and the Irvington lease in the manner described herein.

Staff further recommends that copies of all notes and other evidences of indebtedness be provided to the Commission within 60 days of execution.

**FINANCIAL ANALYSIS**

	[A] 12/31/2004	[B] Pro Forma Change
1 Operating Income	\$ 206,684,000	\$ 206,684,000
2 Depreciation & Amort.	117,109,000	117,109,000
3 Income Tax Expense	34,815,000	34,815,000
4		
5 Interest Expense	157,012,000	154,555,900
6 Repayment of Principal	55,336,000	55,336,000
7		
8		
9 <b>TIER</b>		
10 [1+3] ÷ [5]	1.54	1.56
11 <b>DSC</b>		
12 [1+2+3] ÷ [5+6]	1.69	1.71
13 <b>CCR</b>		
14 [1+2+3] ÷ [5]	2.28	2.32
15		

[A] 2004 actual financial information

[B] Column [A] adjusted to reflect the proposed refinancing of notes underlying capital leases resulting in a 2.50% interest rate reduction on the Common Facilities Lease and a 2.00% interest rate reduction on the Irvington Lease

MEMORANDUM

TO: Dan Zivan  
Utilities Division  
Arizona Corporation Commission

FROM: Brian K. Bozzo   
Compliance Manager  
Utilities Division

DATE: March 2, 2006

RE: TUCSON ELECTRIC POWER - DOCKET NO. E-01933A-05-0654

Mr. Zivan-

To summarize TEP compliance, only four pending items have remained that required discussion. They are shown below:

## Tucson Electric Power Company (E-01933A)

	Docket	Decision	Compliance Item	Current Recommendation
1)	93-0006	58379	Temporary Fuel Surcharge	Complied.
2)	97-0096	60221	Bi-Annual Project Investment Report.	Waiver.
3)	95-0332	59224	Quarterly Affiliate Reports	Eliminate
4)	95-0332	59224	Sales of Power Reports (Nations Sub.)	Eliminate

Based on discussions yesterday between Ms. Barbara Keene and Mr. Dave Couture of Tucson Electric Power Company ("TEP") and myself, Staff has determined that none of the above items represent legitimate compliance delinquencies. Staff has determined that the Company has complied with item number 1. It is therefore no longer considered a delinquency. Regarding item number 2, Staff should recommend that the Company file a request for an indefinite waiver of that compliance item. The Company has agreed to do so. Regarding item numbers 3 and 4, Staff should recommend that the Commission eliminate those compliance items as they represent outdated or moot reporting requirements. Detail for each of the four items is provided below. *With the exception of item number 1 below which was determined to be in compliance, the following information may be included in your Staff report.*

Staff Review of TEP Compliance Items.

- 1) Temporary Fuel Surcharge - Decision No. 58379 states that the temporary fuel surcharge should be in place until the fuel cost bank balance reached zero. TEP filed paperwork with Staff indicating that the bank balance reached zero on January 25, 1994. This item has been complied with and is not a delinquency.

- 2) Bi-Annual Project Investment Report – Decision No. 60221 orders TEP to provide a bi-annual report on the projects in which it was considering investing. In discussion with Staff, the Company noted that such investment has not been done at the TEP level since the creation of the holding company (UniSource Energy Corporation) in 1997. The Company indicated it was highly unlikely that TEP would do this kind of investing while the holding company exists. Based on this, Staff recommends the Company file an application for an indefinite waiver of this requirement as the appropriate method of addressing this compliance item. The Company has agreed to do so.
- 3) Quarterly Affiliate Reports - Decision No. 59224 approved a limited waiver of Affiliated Interest rules allowing a TEP subsidiary to acquire a partial ownership in some Colorado based generating facilities. In approving this waiver, the decision imposed a requirement that the Company file regular affiliate reports (finding of fact 8e). According to the Company, however, the ownership interest in those facilities was sold in 1998 and there has been nothing to report on since that time. The Company further stated that with the generating facilities sold, the waiver granted in Decision 59224 to acquire those facilities is no longer necessary. Staff agrees that if the facilities were sold and the waiver is no longer necessary, then the related compliance items are not relevant. Based on the above, Staff recommends that this compliance requirement be eliminated by the Commission.
- 4) Sales of Power Report – In approving Decision No. 59224, the Commission also ordered TEP and the subsidiary acquiring the Colorado facilities to file an annual report on all sales of power (finding of fact 8p). In discussions, the Company stated that since the facilities were sold in 1998 there is no longer any relevance to this reporting requirement. As in item number 3 above, Staff agrees that if the facilities were sold and the waiver is no longer necessary, then the related compliance items are not relevant. Based on the above, Staff recommends that this compliance requirement be eliminated by the Commission.

Staff recommends that the Company file an application for an indefinite waiver of the Bi-Annual Project Investment Report compliance requirement which was ordered in Decision No. 60221. Staff notes that the Company has agreed to do so.

Staff further recommends that the Commission eliminate both the Quarterly Affiliate compliance requirement and the Sales of Power compliance requirement which were ordered in Decision No. 59224.

Given these recommendations and subsequent commission approval, the compliance database indicates that TEP would then be in compliance.

**Tucson Electric Power Company**

One South Church, Suite 200  
Tucson, Arizona 85701  
Telephone 520 884-3752  
Facsimile 520 884-3601

February 10, 2006

Mr. Ernest Johnson  
Director, Utilities Division  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, AZ 85007

Re: Reporting Matters

Dear Mr. Johnson:

As you may know Tucson Electric Power Company ("TEP") is working with your Staff to resolve discrepancies between our records and those of the Arizona Corporation Commission Utilities Division's Compliance Section. TEP's Regulatory Services Coordinator, Jessica Bryne has discussed the discrepancies with Brian Bozzo and Carmela Leon of the Compliance Section. Mr. Bozzo and Ms. Leon have been very helpful and cooperative in this effort.

Currently, there are four remaining items. The first is a monthly report regarding a TEP temporary fuel surcharge from Decision No. 58379 that began September 1, 1993 and ended December 2003. The second item is a report on the projects TEP is considering investing in, found in Decision No. 60221 in 1997. This report has been superseded by A.A.C. R14-2-805. The final two items concern Nations Energy (a UniSource subsidiary) and a partial ownership in the Coors Power Plant, which was sold in 1998 as reported in TEP's 1998 annual 10k report (see Decision No. 59224 from 1995). We can no longer file these reports because Nations has ceased to participate in the sale of power.

TEP is working with Mr. Bozzo and Ms. Leon to determine how best to remove these items from the compliance filings list.

If you have any questions, please do not hesitate to contact me.

Sincerely,



Dave Couture  
Director, Regulatory Services

Cc: Brian Bozzo, ACC  
Carmela Leon, ACC  
Raymond Heyman, TEP

STAR PUBLISHING COMPANY

Tucson, Arizona

STATE OF ARIZONA)  
COUNTY OF PIMA)

Janice Anderson, being first duly sworn deposes and says: that she is the Legal Advertising Representative of the STAR PUBLISHING COMPANY, a corporation organized and existing under the laws of the State of Arizona, and that the said STAR PUBLISHING COMPANY prints and publishes The Arizona Daily Star, a daily newspaper printed and published in the City of Tucson, Pima County, State of Arizona, and having a general circulation in said City, County, State and elsewhere, and that the attached

*Legal Notice*

was printed and published correctly in the entire issue of the said The Arizona Daily Star on each of the following dates, to-wit:

*Janice Anderson*

Subscribed and sworn to before me this 23 day  
of 2004

*Valerie S. Gonzales*

Notary Public



VALERIE S. GONZALES  
Notary Public - Arizona  
Pima County  
Expires 09/30/06

My commission expires \_\_\_\_\_

TNI AD NO. 4316679

**PUBLIC NOTICE OF AN  
APPLICATION BY  
TUCSON ELECTRIC POWER  
COMPANY FOR A FINANCING  
ORDER AUTHORIZING VARIOUS  
FINANCING TRANSACTIONS**

On September 16, 2005, Tucson Electric Power Company ("Applicant") filed an Application with the Arizona Corporation Commission ("Commission") for an order authorizing amendments in connection with the refinancing of approximately \$68 million of Springerville Common Facilities lease debt and \$45 million of Irvington Unit lease debt prior to June 30, 2006. The Application is available for inspection during regular business hours at the offices of the Commission in Phoenix at 1200 West Washington Street, Phoenix, Arizona, and at the office of the Company, Tucson Electric Power Company, One South Church, Tucson, Arizona 85701.

Intervention in the proceeding on this matter shall be permitted to any person entitled by law to intervene and having a direct and substantial interest in the matter. The granting of motions to intervene shall be governed by A.A.C. R. 14-3-105. Persons desiring to intervene must file a Motion to Intervene with the Commission which must be served upon Applicant and its counsel and to all parties of record, and which, at a minimum, shall contain the following information:

1. The name, address and telephone number of the proposed intervenor and of any person upon whom service of documents is to be made if different than the intervenor.
2. A short statement of the proposed intervenor's interest in the proceeding (e.g. a customer of the Applicant, a shareholder of the Applicant, etc.).
3. A statement certifying that a copy of the Motion to Intervene has been mailed to Applicant, its counsel and all parties of record.

The granting of intervention, among other things, entitles a party to present sworn evidence at hearings and to cross-examine other witnesses. However, failure to intervene will not preclude any person from appearing at the hearing and making a statement on such person's own behalf.

The Commission does not discriminate on the basis of disability in admission to its public meetings. Persons with a disability may request a reasonable accommodation such as a sign language interpreter, as well as request this document in an alternative format by contacting Linda Hogan, ADA Coordinator, voice phone number 602-542-3990, e-mail lhogan@azcc.gov. Requests should be made as early as possible to allow time to arrange the accommodation.

Published November 23, 2005  
The Arizona Daily Star and Tucson Citizen

**AFFIDAVIT OF PUBLICATION**

STATE OF ARIZONA )  
                          ) ss.  
COUNTY OF PIMA )

**Audrey Smith**, being first duly sworn, deposes and says that (s)he is the **Legal Advertising Manager of THE DAILY TERRITORIAL**, a daily newspaper printed and published in the County of Pima, State of Arizona, and of general circulation in the City of Tucson, County of Pima, State of Arizona and elsewhere, and the hereto attached:

**PUBLIC NOTICE OF AN APPLICATION  
BY TUCSON ELECTRIC POWER COMPANY FOR A  
FINANCING ORDER AUTHORIZING FINANCING  
TRANSACTIONS**

was printed and published correctly in the regular and entire issue of said **THE DAILY TERRITORIAL** for 1 issues; that was first made on the 23rd day of November 2005 and the last publication thereof was made on the 23rd day of November 2005 ; that said publication was made on each of the following dates, to-wit:

11/23/05

at the Request of:     Tucson Electric Power

by *Audrey Smith*, Legal Advertising Manager  
Subscribed and sworn to before me this 23rd day of November 2005 .



**JAMIE C. MACIAS**  
Notary Public - Arizona  
Pima County  
Expires 02/04/08

*Jamie C. Macias*  
Notary Public in and for the County of Pima, State of Arizona

My commission expires: 2-4-08

# **PUBLIC NOTICE OF AN APPLICATION BY TUCSON ELECTRIC POWER COMPANY FOR A FINANCING ORDER AUTHORIZING VARIOUS FINANCING TRANSACTIONS**

On September 16, 2005, Tucson Electric Power Company ("Applicant") filed an Application with the Arizona Corporation Commission ("Commission") for an order authorizing amendments in connection with the refinancing of approximately \$68 million of Springerville Common Facilities lease debt and \$45 million of Irvington Unit 4 lease debt prior to June 30, 2006. The Application is available for inspection during regular business hours at the offices of the Commission in Phoenix, at 1200 West Washington Street, Phoenix, Arizona, and at the office of the Company, Tucson Electric Power Company, One South Church, Tucson, Arizona 85701.

Intervention in the proceeding on this matter shall be permitted to any person entitled by law to intervene and having a direct and substantial interest in the matter. The granting of motions to intervene shall be governed by A.A.C.R14-3-105. Persons desiring to intervene must file a Motion to Intervene with the Commission which must be served upon Applicant and its counsel and to all parties of record, and which, at a minimum, shall contain the following information:

1. The name, address and telephone number of the proposed intervenor and of any person upon whom service of documents is to be made if different than the intervenor.
2. A short statement of the proposed intervenor's interest in the proceeding (e.g. a customer of the Applicants, a shareholder of the Applicants, etc.).
3. A statement certifying that a copy of the Motion to Intervene has been mailed to Applicant, its counsel and all parties of record.

The granting of intervention, among other things, entitles a party to present sworn evidence at hearing and to cross-examine other witnesses. However, failure to intervene will not preclude any person from appearing at the hearing and making a statement on such person's own behalf.

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**PUBLISH: The Daily Territorial  
November 23, 2005  
pfinancing order a.s**

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**BEFORE THE ARIZONA CORPORATION COMMISSION**

- JEFF HATCH-MILLER  
Chairman
- WILLIAM A. MUNDELL  
Commissioner
- MARC SPITZER  
Commissioner
- MIKE GLEASON  
Commissioner
- KRISTIN K. MAYES  
Commissioner

IN THE MATTER OF THE APPLICATION  
 OF TUCSON ELECTRIC POWER  
 COMPANY FOR A FINANCING ORDER  
 AUTHORIZING VARIOUS FINANCING  
 TRANSACTIONS

DOCKET NO. E-01933A-05-0654  
 DECISION NO. \_\_\_\_\_  
ORDER

Open Meeting  
 March 15 and 16, 2006  
 Phoenix, Arizona

BY THE COMMISSION:

FINDINGS OF FACT

1. Tucson Electric Power Company ("TEP" or "Company") filed an application requesting a financing order authorizing various financing transactions with the Arizona Corporation Commission ("Commission") on September 16, 2005.
2. TEP is a wholly owned subsidiary of UniSource Energy Corporation, is a Class "A" Arizona C-corporation and serves approximately 375,000 customers.
3. TEP requests Commission authorization to amend its Springerville Common Facilities Leases ("Common Facilities Leases") and its Irvington Unit 4 Lease ("Irvington"). TEP proposes to refinance its Common Facilities Leases and its Irvington Lease in order to avoid a "special event of loss" on the Common Facilities Leases which would result in a loss of at least \$59 million and to obtain more favorable financing for both leases.
4. Notice of a financing application was published in *The Arizona Daily Star* and in *The Daily Territorial* on November 23, 2005.

...

1           5.       In January of 1991 TEP instituted a payment moratorium which resulted in the  
2 Company withholding payments to various lenders and lessors. As a result, TEP restructured the  
3 Common Facilities Leases and Irvington Leases. TEP is required to cause the secured notes  
4 underlying the Common Facilities Leases "...to be refinanced or refunded prior to June 30, 2006,  
5 in order to avoid a "special event of loss." If a special event of loss were to occur, the Common  
6 Facilities Leases would be terminated and TEP would be required to repurchase the Common  
7 Facilities (as defined herein) for an amount equal to the higher of stipulated loss value of \$127  
8 million or the fair market value of those Common Facilities."<sup>1</sup>

9           6.       The principal balance due on the Common Facilities Leases on June 30, 2006, will  
10 be approximately \$68 million. If a "special event of loss" were to occur, TEP would be forced to  
11 repurchase the facilities for an amount of at least \$127 million despite only owing a balance of \$68  
12 million resulting in an additional cost of at least \$59 million.

13           7.       TEP anticipates that it can obtain an interest rate on the Common Facilities Leases  
14 approximately 2.5 percent below the existing interest rate by refinancing.

15           8.       There is no requirement for TEP to refinance the Irvington Lease at this time;  
16 however the Company states that it may be able to lower the cost of debt service by taking  
17 advantage of existing market conditions resulting in a lower interest rate. TEP anticipates that it  
18 will be able to obtain an interest rate approximately 2.0 percent lower than the current interest rate  
19 on the Irvington Lease.

20           9.       TEP had a December 31, 2004 times interest earned ratio ("TIER") of 1.54, a debt  
21 service coverage ratio ("DSC") of 1.69 and a cash coverage ratio ("CCR") of 2.28. The result of  
22 the proposed lease refinancings would be a TIER of 1.56, a DSC of 1.71 and a CCR of 2.32.

23           10.      In Decision No. 60221 TEP was required to "...file with Staff, subject to a  
24 confidentiality agreement, reports on January 1 and July 1 of each year, including the projects in  
25 which it is considering investing so that Staff can act more quickly if expedited actions are  
26 required." The Company asserts that this requirement has been superseded by A.A.C. R14-2-805.

27 \_\_\_\_\_  
28 <sup>1</sup> Page 1, Line 24 of TEP's application

1 Staff has recommended, and the Company has concurred, that TEP should file a request for an  
2 indefinite waiver for this portion of Decision No. 60221.

3 11. In Decision No. 59224 TEP was required to "...provide reports to the Commission  
4 and access to all affiliate books and records, as outlined in Paragraph 17 of its Application for  
5 Limited Waiver." The Company states that it has sold its partial ownership in its Coors Power  
6 Plant, therefore, absolving it of this requirement. Staff recommends that this item be eliminated  
7 from TEP's compliance report as the Company has sold the related facilities.

8 12. According to Decision No. 59224 "TEP and the Nations Energy Subsidiary will  
9 report all sales of power to the Staff annually under the terms of a confidentiality agreement. The  
10 Nations Subsidiary will provide access to all information needed to verify the accuracy of the  
11 reported information." The Company states that Nations Energy has ceased to participate in the  
12 sale of power, therefore, absolving it of this requirement. Staff recommends that this item be  
13 eliminated from TEP's compliance report as the Company has sold the related facilities.

14 13. Staff concludes that the proposed refinancings of the Springerville Common  
15 Facilities Leases and the Irvington Unit 4 Lease are lawful and within the corporate powers of the  
16 applicant, would be compatible with the public interest, consistent with sound financial practices  
17 and not impair TEP's ability to provide service.

18 14. Staff further recommends approval of TEP's request to enter into amendments and  
19 agreements necessary to refinance the lease debt underlying the Common Facilities Leases and the  
20 Irvington Lease in the manner described herein.

21 15. Staff further recommends that copies of all notes and other evidences of  
22 indebtedness be provided to the Commission within 60 days of execution.

### 23 CONCLUSIONS OF LAW

24 1. TEP is a public service corporation within the meaning of Article 15 of the Arizona  
25 Constitution and Title 40 of the Arizona Revised Statutes.

26 2. The Commission has jurisdiction over the Company and over the subject matter of  
27 the application.

28 3. Notice of the application was provided in conformance with law.



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IT IS FUTHER ORDERED that the Company file one copy of executed loan documents with the Director of the Utilities Division within 60 days of the decision in this matter.

IT IS FURTHER ORDERED that this Decision shall become effective immediately.

**BY ORDER OF THE ARIZONA CORPORATION COMMISSION**

CHAIRMAN	COMMISSIONER	
COMMISSIONER	COMMISSIONER	COMMISSIONER

IN WITNESS WHEREOF, I BRIAN C. McNEIL, Executive Director of the Arizona Corporation Commission, have hereunto, set my hand and caused the official seal of this Commission to be affixed at the Capitol, in the City of Phoenix, this \_\_\_\_\_ day of \_\_\_\_\_, 2006.

\_\_\_\_\_  
BRIAN C. McNEIL  
Executive Director

DISSENT: \_\_\_\_\_

DISSENT: \_\_\_\_\_

EGJ:DTZ:red\LF

1 SERVICE LIST FOR: TUCSON ELECTRIC POWER COMPANY  
2 DOCKET NO. E-01933A-05-0654

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6 Mr. Raymond S. Heyman  
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9 Mr. Ernest G. Johnson  
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12 Mr. Christopher C. Kempley  
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16 Ms. Lyn Farmer  
Chief Administrative Law Judge  
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