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BEFORE THE ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission

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2 COMMISSIONERS
3 KRISTIN K. MAYES - CHAIRMAN
4 GARY PIERCE
5 PAUL NEWMAN
6 SANDRA D. KENNEDY
7 BOB STUMP

8 IN THE MATTER OF THE APPLICATION) DOCKET NO. E-04204A-09-0582
9 OF UNS ELECTRIC, INC. AND UNS GAS, INC.) DOCKET NO. G-04204A-09-0582
10 FOR A FINANCING ORDER AUTHORIZING)
11 VARIOUS FINANCING TRANSACTIONS)
12) **COMMENTS AND OBJECTION**
13) **TO STAFF REPORT**
14)

15 UNS Electric, Inc. ("UNS Electric") and UNS Gas, Inc. ("UNS Gas") (collectively "the
16 Companies"), submit their comments to the Staff Report. The Companies agree with the vast
17 majority of the findings and recommendations in the Staff Report. However, the recommendation
18 that the Companies satisfy financial ratio tests for each draw on the Companies' revolving credit
19 facility is not practical, and thus the Companies object to this condition.

20 The revolving credit facility is used for working capital and credit support of wholesale
21 energy procurement. Both of these items require quick access to available credit. The precondition
22 of satisfying financial ratio tests prior to each draw will greatly increase the length of the process,
23 thereby preventing quick access to credit. Moreover, this requirement is inconsistent with prior
24 Commission orders,¹ and unnecessary as the credit agreements that govern revolving credit facilities
25 typically include similar limitations.

26 Therefore, the Companies request that the Commission remove this precondition in its Order.
27 In addition, to take advantage of significant anticipated cost savings, the Companies request that the
Commission issue an order on or before September 30, 2010.

¹ For instance, the Commission did not require Tucson Electric Power Company ("TEP") to meet minimum financial ratios before drawing on its revolving credit facility in its current financing order, Decision No. 71788 (July 12, 2010), or TEP's previous financing order, Decision No. 69946 (October 30, 2007).

1 **I. BACKGROUND.**

2 On December 29, 2009, the Companies filed their joint Application requesting authority to:

- 3 (1) refinance their joint revolving credit facility that expires August 2011;
- 4 (2) increase the amount of the joint revolving facility by \$40 million (to \$100 million);
- 5 (3) refinance UNS Gas' long-term indebtedness maturing in 2011 (an amount of \$50
- 6 million);
- 7 (4) increase the amount of long-term indebtedness outstanding at each company by up to
- 8 \$50 million; and
- 9 (5) enter into these financings through December 31, 2014.

10 **A. Application.**

11 **1. Revolving credit facility.**

12 UNS Electric and UNS Gas seek Commission authority to enter into one or more credit

13 agreements (and to refinance such agreements), which may consist of one more revolving credit

14 facilities. The revolving credit facility is used as a source of liquidity for working capital purposes,

15 for general corporate purposes and may also be used to support UNS Electric's and UNS Gas'

16 energy procurement and hedging activities by issuing letters of credit to provide credit enhancement

17 to counterparties. The ability to promptly draw on these revolving credit facilities is important to

18 accomplishing these goals. Increasing the size of their revolving credit facilities would provide the

19 Companies with greater liquidity – including supporting their respective competitive procurement

20 and hedging activities. UNS Gas and UNS Electric requested this authority in December 2009 so

21 that they could refinance well in advance of the current facility expiring in August 2011.

22 **2. Long-term debt.**

23 The Companies also request authority for UNS Gas to refinance \$50 million in long-term

24 debt due in August 2011; and for UNS Gas and UNS Electric to each issue up to \$50 million in

25 additional long-term debt. The Companies made these requests in light of the future capital

26 expenditure requirements needed to provide service to customers. Flexibility in financing these

27 capital expenditures is important to obtaining reasonable debt costs – and lower debt costs ultimately

1 benefit customers. Further, UNS Gas seeks to refinance its \$50 million of 6.23% senior notes that
2 mature in August 2011.

3 **B. Staff Report.**

4 Staff recommended approval of the Companies' application. However, Staff recommends
5 conditioning approval on the Companies meeting certain minimum financial ratios when issuing
6 debt. Staff recommends an equity ratio test and a cash coverage ratio (CCR) test.² The minimum
7 CCR is reduced if the equity ratio exceeds 40%.

8 **II. THE FINANCIAL RATIO TESTS SHOULD NOT APPLY TO DRAWS ON THE**
9 **REVOLVING CREDIT FACILITIES.**

10 The Companies do not object to financial ratio tests where they: (1) are set at reasonable
11 levels; and (2) are not unduly burdensome or restrictive. The Companies have no objection to
12 Staff's proposed financial ratio tests for long-term debt. However, the Companies have significant
13 concerns with requiring these tests to be met each time a draw is made under the revolving credit
14 facilities or a letter of credit is issued. Specifically, this requirement is (1) not practical; (2)
15 inconsistent with prior financing orders; and (3) not necessary.

16 **A. Commission Staff's recommendation is administratively burdensome and not**
17 **practical.**

18 Commission Staff's recommendation is administratively burdensome and not practical.
19 Revolving credit facilities are designed to meet short-term liquidity and wholesale credit support
20 needs, and may be used for those purposes multiple times each year. Due to seasonal working
21 capital needs, temporary under-recovery of fuel and purchased energy costs, and fluctuations in
22 forward energy prices, the Companies typically use these facilities on a frequent basis. If adopted,
23 Commission Staff's recommendation would require UNS Gas and UNS Electric to go through a
24 lengthy process each and every time either company seeks to borrow from the revolving credit
25 facility or issue a letter of credit.

26
27 ² See Staff Report, Recommendation #8, at 7.

1 Imposing financial ratio tests on the revolving credit facilities would be administratively
2 burdensome and could adversely impact the Companies' ability to make timely drawings on the
3 revolving credit facilities to meet working capital requirements. In typical issuances of long-term
4 debt and upon the execution and delivery of credit agreements, both issuers and lenders take steps to
5 confirm that the borrowers have the regulatory authority necessary to incur the debt and perform
6 their obligations in respect of the debt. These steps include review by the lenders and their counsel
7 of the relevant regulatory orders and the receipt of representations and warranties from the utilities
8 acting as borrowers and the delivery of opinions of counsel to the effect that the utilities have the
9 regulatory authority necessary to incur the debt and perform their obligations. The conditions
10 proposed by Staff would result in the Companies and their lenders being unable to determine, when
11 the revolving credit facilities are initially entered into, whether the borrowings to occur in the future
12 are authorized. Instead, this determination would need to be made upon each borrowing under the
13 facilities and each issuance of a letter of credit. And for each determination, the Companies may
14 need to provide new representations, certifications and opinions of counsel. The Companies are not
15 aware of any other utility subject to such limitations. They do not know whether lenders have the
16 administrative processes in place to accommodate these additional on-going determinations or
17 whether these conditions could adversely impact their ability to obtain revolving credit facilities on
18 favorable terms. Even if the procedures can be worked out with lenders, it is reasonable to assume
19 that they will be cumbersome and could impede the ability to draw upon the revolving credit
20 facilities in a timely manner.

21 The Companies also believe that, rather than constituting a sound financial practice and
22 enhancing the Companies' financial condition, requiring the equity test and CCR to be satisfied for
23 each borrowing upon the revolving credit facilities and each issuance of a letter of credit could be
24 perceived by the financial community as jeopardizing the Companies' liquidity and as adversely
25 affecting their financial condition. Providers of wholesale energy and other trade creditors may view
26 having committed revolving credit facilities as necessary in order to be satisfied that the companies
27 have sufficient liquidity and are financially sound. The Companies believe that investors, lenders

1 and other members of the financial community concur in this view. If the Companies' ability to
2 utilize the revolving credit facilities were conditioned upon meeting the tests upon each borrowing
3 and letter of credit issuance, the facilities may not be considered as being available to satisfy
4 liquidity needs. Rather than enhancing the Companies' financial condition, the conditions may
5 adversely impact their financial condition.

6 **B. Commission Staff's recommendation to apply financial ratio tests to revolving**
7 **credit draws is inconsistent with prior Commission orders.**

8 Staff's recommendation to apply financial ratio tests to revolving credit draws is inconsistent
9 with prior Commission financing orders. The Companies are unaware of the Commission requiring
10 any other gas or electric utility to subject any and all revolving credit borrowings and letter of credit
11 issuances to financial ratio tests. For instance, the Commission did not require Tucson Electric
12 Power Company ("TEP") to meet minimum financial ratios before drawing on its revolving credit
13 facility in its current financing order, Decision No. 71788 (July 12, 2010), or TEP's previous
14 financing order, Decision No. 69946 (October 30, 2007). In both those cases, the financial ratio tests
15 applied only to long-term debt.³ Likewise, the Companies are not required to meet minimum
16 financial ratios for revolving credit draws under their current financing order, Decision No. 69395
17 (March 22, 2007), or their original financing order, Decision No. 66028 (July 3, 2003). Again, the
18 financial ratio requirements only applied to long-term debt.⁴ Notably, the Recommended Opinion
19 and Order (ROO) for the Companies' current financing order did propose applying financial ratio
20 requirements to draws on the revolving credit facilities.⁵ The Companies filed exceptions,⁶ and the
21 Hearing Division submitted a proposed amendment to limit the financial ratio requirements to long-

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24 ³ Decision No. 69946 (October 30, 2007) at page 14, lines 1-9; Decision No. 71788 (July 12, 2010)
at page 19, lines 6-10.

25 ⁴ Decision No. 69395 (March 22, 2007) at page 8, lines 9-13; Decision No. 66028 (July 3, 2003) at
26 pages 19-21 (approving financing plan in Settlement Agreement); *See also* Settlement Agreement
filed April 1, 2003 in Dockets Nos. E-01032C-00-0751 et al, at pages 10-12 and Appendix A at page
2.

27 ⁵ ROO filed on February 23, 2007 in Docket Nos. E-04204A-06-0493 et al at page 8, lines 10-12.

⁶ See Exceptions filed March 5, 2007 in Docket Nos. E-04204A-06-0493 at pages 2-3.

1 term debt only.⁷ The Commission adopted this amendment and limited the financial ratio
2 requirements to apply to long-term debt only.⁸ Thus, the Commission considered, and specifically
3 rejected the concept of applying financial ratio requirements to draws on the revolving credit
4 agreement.

5 **C. Commission Staff's recommended financial ratio test is not necessary.**

6 Commission Staff's recommended financial ratio test is not necessary. The credit
7 agreements that govern the revolving credit facilities typically include limitations on the use of those
8 facilities. UNS Gas and UNS Electric will likely be subject to financial covenants, measured on a
9 quarterly basis, which will ensure that borrowings from those facilities will not result in either
10 company being over-leveraged. Moreover, drawings on the facilities will typically be repaid in the
11 short-term. Although it is a common practice for letters of credit to be required in connection with
12 energy procurement and hedging activities, such letters of credit have never been actually drawn
13 upon in the Companies' experience.

14 **D. Companies' recommendation.**

15 Requiring financial ratio tests for draws on the revolving credit facilities is not practical,
16 contrary to Commission precedent, and not necessary. Thus, the Companies recommend that the
17 Commission simply delete "(2) and" from the first clause of Staff Recommendation No. 8 (Staff
18 Report, page 7), and not including the language of footnote 9 of the Staff Report (page 5) in the
19 Commission's order.

20 **III. IN THE ALTERNATIVE, THE AGGREGATE AMOUNT OF NEW DEBT**
21 **AUTHORIZED FOR EACH COMPANY COULD BE REDUCED, RATHER THAN**
22 **IMPOSING A BURDENSOME TEST FOR EACH DRAW ON THE CREDIT**
23 **FACILITIES.**

24 In the alternative, the Companies would be willing to agree to (1) limiting the amount that
25 either company could draw upon the proposed credit facilities to \$70 million; and (2) reducing the

26 ⁷ Hearing Division Proposed Amendment No. 1, filed March 12, 2007 in Docket Nos. E-04204A-06-
27 0493

⁸ Decision No. 69395 (March 22, 2007) at page 8, lines 9-13.

1 amount of additional long-term indebtedness that UNS Electric and UNS Gas would each be
2 authorized to issue (other than refinancing) from the proposed \$50 million to only \$30 million.
3 Therefore, the total amount of authorized indebtedness for each company would be \$50 million less
4 under this alternative proposal. This should alleviate any concern that UNS Gas or UNS Electric
5 would incur too much total debt as a result of any revolving credit facilities authorized. See Exhibit
6 A.

7 **IV. THE COMPANIES REQUEST THAT THE COMMISSION ISSUE AN ORDER ON**
8 **OR BEFORE SEPTEMBER 30, 2010.**

9 Finally, the Companies note that TEP and UniSource Energy Corporation are currently
10 preparing to refinance their credit facilities during the fourth quarter of 2010. Like UNS Gas and
11 UNS Electric, TEP and UniSource Energy have credit facilities that expire in August 2011. The
12 Companies request a Commission decision by the end of September so that they may take advantage
13 of substantial economies of scale that are expected to result from a joint refinancing effort as
14 opposed to a stand-alone refinancing. To participate in the refinancing effort, however, the
15 Companies must have prior authorization from the Commission. The Companies note that they
16 applied for the authorizations sought in this Application over seven months ago.

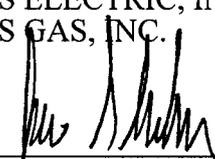
17 **V. CONCLUSION.**

18 UNS Electric and UNS Gas support the vast majority of Commission Staff's
19 recommendations made in its report. As explained above, the additional recommendation of the
20 financial ratio test prior to each draw is not practical, unduly burdensome, and not necessary.
21 Moreover, it would frustrate the Companies' ability to access credit quickly, and is contrary to prior
22 Commission financing orders. Thus, the Companies believe that the Commission should issue an
23 order that does not impose a requirement for financial ratio tests to be satisfied for each draw under
24 the credit facilities or each letter of credit. In the alternative, and instead of including such financial
25 ratio tests for draws and letters of credit, the Companies are willing to agree to: (1) limiting the
26 amount available to either UNS Gas or UNS Electric, individually, to no more than \$70 million from
27 any new credit facilities; and (2) limiting the amount of additional long-term indebtedness for each

1 company (other than refinancings) to only \$30 million instead of the proposed \$50 million. Finally,
2 the Company requests that an order be issued on or before September 30, 2010, in order to take
3 advantage of substantial cost savings in refinancing credit facilities at the same time as TEP and
4 UniSource. The Companies maintain that their joint application is in the public interest, and
5 consistent with sound financial practices and their duties as public service corporations.

6 RESPECTFULLY SUBMITTED this 9th day of August 2010.

7
8 UNS ELECTRIC, INC.
UNS GAS, INC.

9
10 By 

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20
21 Original and 15 copies of the foregoing
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1 Copy of the foregoing hand-delivered/mailed
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By Mary Appolito

EXHIBIT

"A"

Exhibit A

As an alternative, and instead of including financial ratio tests for draws and letters of credit to their revolving credit facility, the Companies propose the following recommendations to replace Staff recommendations #2, #4 and #8:

2. Authorize UNS Electric and UNS Gas to enter into one or more credit agreements, and to enter into agreements to refinance any such credit or reimbursement agreements, which may consist of one or more revolving credit facilities so long as, after giving effect to the entry of such a facility, *the amount of credit available under such facilities to each company, individually, does not exceed \$70 million*, and to specify that this newly granted authority is a replacement for the authority granted in Decision No. 69395 to amend or refinance the revolving credit facility and to affirm that all existing agreements and obligations incurred under lawful authorizations shall remain valid;
4. Authorize UNS Electric and UNS Gas to each issue up to **\$30** million in additional long-term indebtedness;
8. The Commission condition the authorities set forth in (4) above, other than in the case of refinancing long-term indebtedness, upon the borrowing entity having equity equal to at least 33 percent of its total capital and a cash coverage ratio of at least 1.75 when equity is between 33 and 40 percent of total capital, or a CCR of 1.25 if equity is 40 percent or higher of total capital;

[Emphasis added to highlight the changes from Staff's recommendations. The only change to the Companies' alternative recommendation #8 is to remove reference to recommendation #2.]