



TO: SCPPA Board of Directors

FROM: Bill D. Carnahan

SUBJECT: Meeting of the SCPPA Finance Committee

DATE: February 5, 2008

A meeting of the Finance Committee was held on February 4, 2008, at the SCPPA office in Pasadena.

Committee members in attendance were: Chairman Bill Carnahan (*SCPPA*); Ed Zacherl (*Anaheim*), Mark Mazak (via teleconference for agenda item 5) (*consultant for Anaheim*); Bob Liu (*Burbank*); Jeannette Olko (*Colton*); Ned Bassin (*Glendale*); Mario Ignacio (*LADWP*); and Shari Thomas (*Pasadena*).

Others present were: Peter Huynh (*LADWP*); Stephen Cole (*Fulbright & Jaworski*); Will Frymann and Dan Hartman (*Public Financial Management*); Therese Savery (*LADWP/SCPPA*); and Craig Koehler and Richard Helgeson (*SCPPA*).

1. Investment Reports

The Committee reviewed the Investment Reports for December 2007, and the quarter ended December 31, 2007, and agreed to forward the reports to the Board for receipt and filing.

2. SCPPA Unaudited Financial Statements

The Committee reviewed the unaudited Quarterly Financial Statements for the period ended December 31, 2007, and agreed to forward to the Board for review and filing.

3. Project Budget Comparison Reports

The Committee reviewed the Budget Comparison Reports for the period ended December 31, 2007, for all projects. The following reflects the net Authority Cost for each of the budgets:

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| • Hoover Upgrading Project | Approximately \$15K (2.56%) over budget |
| • Magnolia Power Project | Approximately \$359K (1.42%) under budget |
| • Mead-Adelanto Transmission Project | Approximately \$129K (1.23%) over budget |
| • Mead-Phoenix Transmission Project | Approximately \$678K (16.14%) under budget |
| • Natural Gas Project - Barnett | Approximately \$975K (13.15%) over budget |
| • Natural Gas Project - Pinedale | Approximately \$7.2M (53.29%) under budget |
| • Ormat Geothermal Project | Approximately \$211K (9.72%) under budget |
| • Palo Verde Power Project | Approximately \$3.79M (8.78%) under budget |
| • San Juan Unit 3 Power Project | Approximately \$5.70M (11.90%) under budget |
| • Southern Transmission System Project | Approximately \$3.43M (7.46%) under budget. |

4. Variable Rate Performance Update

PFM provided an update on variable rate bond performance, and the VRDO and Auction Rate markets. Since the end of 2007, the municipal bond insurers have been under constant reevaluation by the rating agencies that resulted in a number of negative rating actions in the last week. SCPPA currently has ten outstanding variable rate or auction rate bond issues spread across several projects; seven of the ten issues are VRDOs and three of the ten are ARS. Considerations for each outstanding VRDO/ARS series should depend on a number of variables including the insurer, the liquidity of the credit provider, and the type of hedge in place for the series. As a result of the varying participation that each SCPPA member has in the SCPPA projects, each member has a different exposure profile.

Since 1991, SCPPA has issued a number of VRDO/ARS series that have generally performed well and have traded very much in line with one another. The reset rates on SCPPA's VRDOs are important on the unhedged variable rate/auction series and also the synthetic fixed rate series. If the swap receipts do not match the rates paid on the bonds, the projected savings from the synthetic fixed rate transactions would be different. Intense market changes in December caused dislocation in the ARS resets, and further market issues in January have caused spreading problems for the VRDOs as well. While the Mead-Adelanto /Mead-Phoenix Series 2004 ARS are the most acute problem, SCPPA may also need to address other insured VRDO and ARS programs, whose performance has suffered amidst the subprime mortgage crisis. This includes (in order of importance) the Southern Transmission 2003 ARS (MBIA insured) \$50M, the Palo Verde Series 1996 B and C VRDOs (Ambac insured) \$147M, and the Magnolia Series 2007-1 (MBIA insured) \$223M.

5. Mead-Adelanto/Mead-Phoenix Refinancing Considerations

PFM discussed the options in connection with refinancing the Mead-Adelanto/Mead-Phoenix ARS to VRDOs. The subprime mortgage crisis has caused significant credit concerns that have had impacts on Ambac and on SCPPA's Mead-Adelanto/Mead-Phoenix ARS programs. Ambac bond and swap insurance policies were paid for and effective in 2004. Ambac also provided surety policies for the Debt Service Reserve Accounts. In the current market, Ambac insured ARS are trading at a significant premium to LOC-backed VRDOs. The Mead-Adelanto/Mead-Phoenix ARS currently are at 3.42%, while BMA is at 2.15%, and 65% of LIBOR is 2.04%. Line of credit providers are not willing to enter into a liquidity agreement where Ambac is the insurer, and current VRDO buyers are asking for a significant premium on Ambac-insured VRDOs in the current market.

Since Mead-Adelanto/Mead-Phoenix ARS are not multi-modal, a current refunding is the best option given the current market and other ancillary considerations. In addition, a long-term credit enhancement plus liquidity (LOC) is SCPPA's most palatable current option for dealing with the likely protracted ARS problem. To this extent, PFM solicited, on a negotiated basis, LOC bids of 32-38 bps for three years from five LOC providers. PFM is recommending a VRDO structure with a LOC, which calls for issuing a current refunding in April 2008 backed by a LOC with a three-year term. A VRDO structure with a LOC would be expected to preserve more than 80% of the estimated savings from the 2004 refunding transaction. This would include additional cost of issuance of between \$600K to \$800K, which the participants have elected to fund from their Project Stabilization Accounts or other sources.

The Finance Committee Mead-Adelanto/Mead-Phoenix participants are recommending the following actions for Board approval:

Authorize moving forward with the current refunding of the Mead-Adelanto /Mead-Phoenix Series 2004 ARS and authorize various parties, including the Working Group, to commence work on the refunding,

including any necessary amendments to the surviving documents and agreements; selection of the Bank of Nova Scotia with a bid at 32.5 bps for a three-year term as the LOC provider, subject to the understanding that the legal documents will need Board approval; and selection of UBS as underwriter for the 2008 current refunding bonds, subject to fees and other conditions acceptable by the Finance Committee.

6. Gas Reserves Takeout Financing

PFM provided a summary of pricing for the Gas Reserves Takeout Financing. On January 24th, SCPPA priced \$141.06 million of taxable bonds for Anaheim, Burbank and Colton in connection with the Gas Reserves Project. The financing will be used to pay off the expiring bridge loan from Merrill Lynch, and provide for approximately five years of capital needs for drilling through a fixed rate bond transaction.

The pricing was successfully completed in spite of one of the most challenging markets in recent history. SCPPA achieved a number of noteworthy successes. On the date of the pricing, taxable levels were below 95% of historical rate levels from the past 15 years. The transaction had a TIC of 5.58% (Anaheim 5.48%, Burbank 5.67%, Colton 5.89%), and well below long-term taxable averages. Procurement of bond insurance with FSA saved SCPPA an estimated \$600K present value and \$1.4M gross. In addition, FSA provided SCPPA surety bonds which saved SCPPA \$1M in negative arbitrage on the required debt service reserve accounts.

7. Gas Prepayment Project No. 2 Update

The Committee received an update on the Gas Prepayment Project No. 2. Project No. 2 continues to progress and will need to be approved by the LA City Council and the SCPPA Board. However, economic conditions for all gas prepay deals have become more challenging.

8. Investment Banking Team Review

The Committee reviewed the schedule for the Investment Banking Team. SCPPA and PFM will begin a draft RFP, and prepare a target schedule and potential mailing list for the next meeting.

9. Update on Sale of Vernon Assets

Richard Helgeson provided the Committee with an update on the proposed sale and of Vernon's asset relating to Mead-Adelanto and Mead-Phoenix (which were not financed through SCPPA).

10. Unsolicited Proposals

PFM provided a summary of the unsolicited proposals received. There were four unsolicited proposals received: Bear Stearns submitted updates for amending the Constant Maturity Swap on the Mead Projects and cancellation swap financing opportunity for the Southern Transmission and Palo Verde Projects; Citi submitted a proposal to fix out the ARS to VRDOs for the 2003 Series A Southern Transmission Bonds; and UBS submitted a proposal to fix out other VRDOs. The Committee decided not to take any action on the unsolicited proposals at this time.

**THE NEXT REGULARLY SCHEDULED FINANCE COMMITTEE MEETING
WILL BE HELD MONDAY, MARCH 3, 2008, AT 10:30 A.M.
AT THE SCPPA OFFICE**