STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
DIVISION OF PUBLIC UTILITIES AND CARRIERS
89 JEFFERSON BOULEVARD
WARWICK, RHODE ISLAND 02888

IN RE:	Narragansett Bay Commission	:	
	Application For Authority to Incur Debt	:	Docket No. D-08-43

REPORT AND ORDER

On June 17, 2008, the Narragansett Bay Commission ("NBC"), One Service Road, Providence, Rhode Island, filed an application with the Rhode Island Division of Public Utilities and Carriers ("Division") seeking approval for the refunding of $65,765,000 in outstanding debt from the NBC's 2004 Series A Revenue Bonds. The application was filed in accordance with the requirements contained in Section 39-3-15 of the Rhode Island General Laws.

In response to the application filing, the Division conducted a duly noticed public hearing on July 9, 2008. The hearing was conducted in the Division's hearing room, located at 89 Jefferson Boulevard in Warwick. The following counsel entered appearances:

For the NBC:	Joseph A. Keough, Jr., Esq.
For the Division's Advocacy Section:	Leo J. Wold, Esq. Special Assistant Attorney General

The NBC proffered pre-filed direct testimony from three witnesses in support of its application. The witnesses were identified as Ms. Karen L. Giebink, the NBC's Director of Administration and Finance; Ms. Karen S.D.

Grande, Esq., the NBC's Bond Counsel; and Ms. Maureen Gurghigian, Senior Vice President, First Southwest Company.

Ms. Giebink testified that the NBC is requesting Division approval for the refunding of NBC's 2004 Series A Revenue Bonds because the refunding will allow NBC to replace the bond insurance and Standby Bond Purchase Agreement (SBPA) with a stand-alone direct-pay (LOC) Letter of Credit. Ms. Giebink related that based upon municipal market conditions, it is anticipated that the new liquidity provision will improve the weekly pricing of the NBC's 2004 Series A Bonds, which have been pricing as Variable Rate Demand Bonds (VRDB), and will result in significantly lower interest rates.[1] Ms. Giebink testified that it is anticipated that once the VRDBs are backed by a LOC, the weekly remarketing rate will be the same or close to the market or Securities Industry and Financial Markets Association (SIFMA) index. She observed that since January 9, 2008, under the current liquidity structure, the remarketing of the VRDBs has ranged from 28 to 367 basis points higher than the index and 126 basis points higher on average over this period. Ms. Giebink stated that on an annual basis, "this translates into additional interest payments of more than $825,000."[2]

Ms. Giebink next testified that other than the instant petition for approval from the Division, the NBC has met all of the other requirements needed to complete the proposed transaction. She related that on April 16, 2008 the NBC's Board of Commissioners passed a resolution authorizing the

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[1] NBC Exhibit 1, Giebink Testimony, p. 2.
[2] Id.

transaction. Ms. Giebink added that the NBC's Bond Counsel is finalizing the Supplemental Indenture and that a draft has been submitted as part of the NBC's filing. She also testified that the NBC is working with its Financial Advisor, the Underwriter, the Bank and the Trustee to prepare the appropriate legal documents. Ms. Giebink also related that the NBC must complete a credit review with Standard and Poor's and plan on receiving the credit rating on or about July 9, 2008, pricing the bonds on or about July 16, 2008 and closing the transaction on July 17, 2008. Ms. Giebink testified that the NBC's current long-term credit rating with Standard and Poor's is A+.[3]

Ms. Giebink related that the NBC's current rates generate sufficient revenue to meet the debt service payments associated with the instant loan.[4] In support of this contention, Ms. Giebink offered the following observation:

> Issuers similar to NBC whose issues are enhanced by a LOC issued by a highly rated bank have been pricing at or below the SIFMA index. Since the beginning of the year, the 10-year SIFMA average is 2.60%, the annual LOC fee ranges from 42 basis points to 54 basis points and annual remarketing fees range from 10 to 12 basis points. The all-inclusive rate at the 10-year SIFMA average is approximately 3.23%. For coverage purposes we added 50 basis points to the average for our projections resulting in an all-inclusive rate of approximately 3.73%. When the projected closing costs are added, the AIC or all-inclusive cost is 3.846%. This is lower than the all-inclusive rate of 3.88%...included in the cost of service from Docket 3797 and NBC's pending Docket 3905. Accordingly, NBC's current rates generate sufficient revenue to meet the principal and interest payments associated

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[3] <u>Id.</u>, pp. 2-3 and Transcript.
[4] <u>Id.</u>, p. 3; and Transcript.

with this loan and meet the debt coverage requirements.[5]

In her final comments, Ms. Giebink testified that in order to close the transaction on July 17, 2008 Division approval is needed on or before July 10, 2008. She noted that MBIA is the insurer on the 2004 Series A Bonds and was recently downgraded from AAA to AA by Standard and Poor's. She stated that last week the NBC's VRDB priced nearly 100 basis points higher, most likely as a result of the downgrade. In closing, Ms. Giebink opined that "in order to preclude further exposure to the market volatility surrounding the bond insurers, it is in the ratepayers best interest to execute this transaction as quickly as practicable."[6]

In her introductory remarks, Karen S. D. Grande, Esq. related that she has served as bond counsel to the NBC for many years, and has assisted the NBC with the issuance of several user fee anticipation notes, revenue notes, loans from the Rhode Island Clean Water Finance Agency ("RICWFA") and revenue bonds including NBC's 2004 Series A revenue bonds.[7]

Ms. Grande indicated that the purpose of her testimony is to provide the Division with the Draft Supplemental Indenture that provides the legal framework for the refunding and the replacement of a structure with insurance and a Standby Bond Purchase Agreement (SBPA) with a stand alone Letter of Credit (LOC) as well as the Authorizing Resolution.

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[5] Id., p. 3.
[6] Id., p. 3; and Transcript.
[7] NBC Exhibit 1, Grande Testimony, p. 2.

Ms. Grande attributed the need for the Authorizing Resolution to current market conditions, which she related are negatively affecting the NBC's Variable Rate Demand Bonds. Ms. Grande explained that she drafted the Authorizing Resolution[8] "in order to put the NBC in a position whereby it could respond quickly to protect its financial interests..."[9] She related that the Authorizing Resolution authorizes: "...substitution of the existing bond insurer with another bond insurer or other credit facility such as a letter of credit" the "...conversion of the 2004 Series A Bonds to and from variable rate interest modes, or permanently to a fixed rate mode" and the "...sale of refunding bonds to an underwriter for resale to investors."[10]

Ms. Grande further testified that because each bond issue requires a supplemental indenture, she has prepared a "Tenth Supplemental Indenture" for the NBC to facilitate the proposed bond refunding. She related that the Draft Tenth Supplemental Indenture[11] "outlines the various terms and responsibilities with respect to this Issue."[12] She explained that the document is based upon the First Supplemental Indenture while taking into consideration the new form of liquidity and other supplemental indentures. Ms. Grande also noted that the drafts that she has prepared may require "certain modifications" after they are reviewed by "legal counsel for the bank, the Trustee and the Underwriter."[13]

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[8] Attached to her pre-filed testimony as "Exhibit KSG-1".
[9] NBC Exhibit 1, Grande Testimony, p. 2.
[10] Id.
[11] Attached to her pre-filed testimony as "Exhibit KSG-2".
[12] NBC Exhibit 1, Grande Testimony, p. 3.
[13] Id.

As in previous related dockets, Ms. Maureen E. Gurghigian began her testimony by stating that First Southwest Company serves as financial advisor to many bond issuers such as schools, cities, airports, hospitals, sports complexes, water and wastewater authorities and districts and toll roads. She related that the firm currently serves more than 2000 municipalities and agencies, including more than 400 in New England. She also noted that in 2007, First Southwest Company was involved in the issuance of more than $46 billion in securities on behalf of its clients, including $32.8 billion as financial advisor.[14]

Ms. Gurghigian related that she has served as financial advisor to the NBC for the past 19 years. She stated that in her capacity as the NBC's financial advisor she has assisted the NBC with a number of long-term borrowings from the RICWFA, several short-term borrowings, the $70 million Variable Rate Demand Bonds issued in April 2004, the $45 million Open Market Revenue Bond Issue in August 2005 and a $42.5 million issue in February 2007. She related that her services have included the facilitation of the credit rating process, loan structuring and other functions.[15]

Ms. Gurghigian provided supporting information regarding the proposed $65,765,000 refunding request and specifically addressed the structure and remarketing of the VRDBs, and why the current market conditions make the proposed refunding advantageous to ratepayers.[16]

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[14] Id., Gurghigian Testimony, pp. 1-2.
[15] Id., p. 2.
[16] Id., pp. 3-5.

Ms. Gurghigian explained that the NBC's VRDBs are remarketed weekly and are placed primarily with major institutional investors. She related that unlike Auction Rate Securities in weekly mode, VRDB has a 'put' option which requires the Issuer (NBC) to purchase the securities in the event that an investor no longer wishes to keep the investment and the VRDB cannot be placed with an alternative investor. She testified that there are two traditional approaches to accommodating this 'put' option. First, the Bonds can be insured in combination with a Standby Bond Purchase Agreement (SBPA), which is typically a very highly rated financial institution. Ms. Gurghigian noted that this is the approach that was taken by the NBC. She indicated that under this approach, the 2004 Series A Bond issue is insured by MBIA and the NBC executed a SBPA with Dexia Credit Locale (Dexia). The second approach, according to the witness, is the use of a stand alone direct-pay Letter of Credit (LOC) from a major financial institution, which does not require bond insurance. Ms. Gurghigian related that in order to address market volatility and improve the relative remarketing of its VRDB, the NBC wishes to refund the 2004 Series A Bonds in order to replace the insurer and SBPA with a stand-alone LOC.[17]

Ms. Gurghigian next discussed current market conditions and why she believes the proposed refunding is advantageous to NBC's ratepayers. She observed that there have been numerous news reports regarding the impacts of the fall-out in the U.S. sub-prime mortgage market. She related that the crisis

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[17] Id., 3.

became a global financial issue during 2007 and into 2008, as banks, individual and institutional investors, and financial guarantors recorded significant financial losses associated with the 'securitized' bonds that were comprised of mortgage-backed securities. Ms. Gurghigian testified that the effects have now rippled through to the municipal market. She explained that historically, bond insurers ('monoline' insurers) provided insurance guarantees for issuers of relatively risk-free municipal debt. However, during the past few years these monoline insurers began guaranteeing securities backed by sub-prime mortgages. Ms. Gurghigian related that because these investments have suffered significant losses, bond insurers' have lost capital and, as a result, have seen their credit rating adversely impacted.

Ms. Gurghigian explained that as institutional investors are concerned about reducing their exposure to monoline insurers, the NBC's VRDB began pricing higher than SIFMA in January 2008. In contrast, Ms. Gurghigian testified that VRDB issues backed by a stand-alone LOC have "not been negatively impacted by the sub-prime mortgage market." Ms. Gurghigian related that it is for this reason the NBC wishes to refund the 2004 Series A Bonds in order to replace the insurer and SBPA with a stand-alone LOC. Ms. Gurghigian also noted that Citizens Bank has approved the LOC and NBC signed a Commitment Agreement on May 15, 2008.

To complete the refunding, Ms. Gurghigian noted that once the appropriate documents have been drafted by Counsel for the Bank and Bond Counsel for the NBC, they will be forwarded to Standard and Poor's to begin the credit review process. Ms. Gurghigian related that the NBC hopes to mail the Official Statement the week of July 14, 2008 but this is contingent upon approval by the Division by July 9 or 10, 2008. Ms. Gurghigian stated that the issue is scheduled to close on July 17, 2008.[18]

The Division's Advocacy Section did not present any witnesses in this docket. Alternatively, however, the Advocacy Section proffered a memorandum from Mr. Thomas S. Catlin, a consulting economist who specializes in public utility regulation. In the memorandum, Mr. Catlin indicates that he had reviewed the filing and agrees that the NBC has a sufficient debt service allowance in rates to meet the anticipated debt service on this new bond issue.[19] After a brief cross-examination of the NBC's witnesses, the Advocacy Section stated for the record that it was satisfied from the evidence presented, that the NBC had met the requisite burden of proof set forth in R.I.G.L. §39-3-15, et seq. and that the proposed refunding was in the public interest.

FINDINGS

Predicated on a thorough examination of the record in this matter, the Division finds that the NBC's application seeking approval for the refunding of $65,765,000 in outstanding debt from the NBC's 2004 Series A Revenue Bonds, is reasonable and in the best interest of ratepayers.

Now, therefore, it is

(19332) ORDERED:

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[18] Id., p. 5 and Transcript.

[19] Advocacy Section Exhibit 1.

1. That the Narragansett Bay Commission's June 17, 2008 application, seeking approval for the refunding of $65,765,000 in outstanding debt from the NBC's 2004 Series A Revenue Bonds, is hereby approved as filed.
2. That the Division hereby makes this approval contingent upon the NBC's use of the debt service allowance previously approved by the Public Utilities Commission, or if subsequently required, by additional debt service allowances approved by the Public Utilities Commission.
3. That the Division hereby limits approval of the instant application to the terms and details identified in the record.

DATED AND EFFECTIVE AT WARWICK, RHODE ISLAND ON JULY 9, 2008.

John Spirito, Jr., Esq.
Hearing Officer

APPROVED:

Thomas F. Ahern
Administrator