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My name is Thomas Huestis and I am a partner of the firm Public Resources Advisory Group, Inc. Public Resources Advisor Group or PRAG, headquartered in New York City was retained by the State in 2011 as the State's financial advisor. The firm is an independent financial advisory firm, and does not engage in any form of underwriting, trading, marketing, or investing in tax-exempt securities. The firm was founded in 1985 to provide in-depth financing support to state and local governments, authorities and agencies and has continuously served governmental entities exclusively. PRAG has been consistently ranked as one of three top national financial advisory firms over each of the past 10 years, and is a leader in providing debt and credit advice to State governments. We represent neighboring states of New Hampshire, and New York, and the Commonwealth of Massachusetts as well as other AAA rated states including the State of Georgia, and the Commonwealth of Virginia. The firm employs over 30 professionals which are drawn from diverse backgrounds, including former governmental officials, advisors, rating agency credit analysts, bond lawyers and underwriters of tax-exempt debt to build a team with knowledge of the capital markets, quantitative skills and in-depth appreciation of unique challenges of state and local governments.

In terms of my background, I joined PRAG in 2002 as a partner of the firm and the resident manager of the firm's Pennsylvania office. I have been an independent financial advisor with PRAG, and PRAG's leading competitor for over 20 years. Prior to joining PRAG, I was the Deputy CFO and Treasurer of the District of Columbia during its financial crisis where I was responsible for the management of the District's financial assets, all District debt offerings, including maintaining rating agency and investor relations with the public debt markets and was responsible for developing the District of Columbia's 4- year budget & financial recovery plan. Currently I am the project manager or co-project manager for clients including states of Minnesota, Illinois, West Virginia and the State of Vermont. I have worked with Vermont on a variety projects over the last year including with the CDAAC committee preparing its 2012 Report, participated in rating agency presentations and currently preparing its upcoming General Obligation bond sale.

Today, I have been asked to provide testimony to the Committee on the possible credit effects on the State regarding the proposed State participation in financing 51-percent of VELCO, representing ownership interest in the management corporation responsible for Vermont's high-voltage bulk electric transmission assets. Our understanding is that (i) a financing of at least

\$500 million would be required to secure the 51% ownership interest in VELCO and that VELCO is anticipating needing an additional \$500 million to \$1 billion in new financing over the course of the next 20 years, (ii) the State is seeking the ownership interest as an investment – to participate in the dividend payments from VELCO net of paying debt service on the financing, (iii) any financing would have to be done on a taxable basis (the use of the bond proceeds does not qualify for tax-exempt debt) and (iv) that the range of financing options discussed to acquire the ownership interest have included guaranteed State financing in the form of State general obligation bonds to be issued, and a new authority or other “off balance sheet” vehicle created that would be authorized to issue bonds without State support. The balance of my testimony will summarize our views on these two options and discuss the possible credit risks associated with these types of transactions.

A \$500 million + State guaranteed general obligation bond financing, would double the State’s net tax supported debt. Although the debt is anticipated to be initially “covered” by the dividend payment from VELCO, the sheer size of the additional bonding amount and the fact that the State would be participating in a large financial venture that it has little direct experience with (and the associated risks that I discuss later in this testimony) would create stress on its existing excellent ratings. There is a strong possibility that the State would lose one or more of its triple-A ratings and this would increase the State’s cost to raise capital funds for many years to come.

On the other end of the spectrum, the State could create new authority with bond-issuing powers without statutory State support or legal obligation. Presumably the only revenues available to this authority to repay any bonds it sold would be the dividends from ownership interests in VELCO. Although the other entities that have bond financed their VELCO participation including Green Mountain Power, Central Vermont Public Service, Burlington Electric Authority and VELCO itself using additional security other than just dividend payments, including: mortgage assets, net revenues from power generation and distribution, general obligation pledges, we believe that a financing could be completed secured by just dividend payments, although at higher cost than the State’s general obligation credit or more secured credit.

For a number of reasons, despite the absence of any legal obligation of the State to support Authority debt, we believe it is likely that the Authority and the future debt of the Authority

would be perceived ultimately as the State's responsibility by credit analyst. First, given that the purchase of the ownership interests is being considered as an investment for the State, we believe that this would tie the State closer to the Authority debt. Second, since the stated public purpose of the acquisition is to protect access the State's transmission system from possible monopoly interference there would be a perception that State would need to maintain its majority ownership and therefore maintain or support future funding. Lastly, we believe that State ownership of VELCO itself (regardless of the issuer of the bonds) will invite analysts to attribute the credit of the Authority's debt to the State. One scenario that would be considered is if unanticipated events resulted in VELCO's inability to pay dividends sufficient to service the Authority's debt, future State officials would see the need to use its credit in some way to protect its investment and maintain the purpose of the acquisition.

I will now briefly discuss some of risks associated with a financing:

- There is a risk that rating agencies will be concerned with the State participating in a large financial venture that has private business risk that it has little direct experience with. The State may have to respond to questions regarding why it is changing its conservative approach to debt financing.
- There is a risk that the initial cost of the State's membership units significantly exceed \$500 million.
- There is a risk the State of Vermont's name is going to be associated with a very large borrowing (regardless of the proposed bond structure used) if the VELCO acquisition is a long-drawn out public process due to disagreements, litigation, condemnation, etc.
- VELCO's revenues are regulated and currently defined by FERC. There is a risk that future regulatory changes could affect transmission line pricing and thus revenues available for its dividend payments and may not be sufficient to pay debt service.
- TRANSCO is projecting to need significant ongoing capital investment. A new ownership structure of VELCO could negatively affect the amount and timeliness of equity contributions.
- Unanticipated events such as natural disasters, new regulations, technology changes, terrorist activities, etc., could increase VELCO's operating expenses and need for capital.

It is not certain that a new independent Authority would have access to capital markets to fund its participating share.

- VELCO/TRANSCO does not have sufficient net cash flow to fund its operating expenses, dividend payments, bond debt service and capital expenditures. VELCO/TRANSCO has been using a \$100 million external line of credit to fund its free cash flow deficits. The external facility is with one bank, has a short expiration date and no term-out provisions. There is a risk that if credit markets freeze again that the facility may not be available or not be available at the current terms which would put more pressure on the equity partner's dividends or increase equity partner funding requirements.
- It is unusual that a State would become an equity partner with private business corporations. Rating agencies would likely seek to know that the State fully understands the associated risks.
- Investors and the rating agencies are becoming more focused governments taking large business financing risks even when the debt is estimated to be self supporting, due to the recent financial collapse of the City of Harrisburg which guaranteed a portion of a trash to energy facility (and is now in receivership) and Jefferson County Alabama which defaulted on a \$2 billion water utility financing.
- Regardless of the method used to finance the initial capital contribution, we assume that the State itself will be seeking ownership and control of VELCO and with ownership comes responsibilities that could result in terms of resources needed to address problems as well as financial responsibilities.

Thank you for the opportunity to present my testimony, and would be happy to address any questions that you have.