

Navigating the PSC's financial oversight authority



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MEUW members seeking to adjust electric rates at the Public Service Commission (PSC) are generally focused on generating enough income to fund utility operating expenses and earn a reasonable rate of return. It is important to recognize, however, that the PSC's oversight authority extends beyond the assessment of the utility's revenue requirement to its overall financial condition.

One of the important factors considered by PSC rate analysts in assessing the relative financial health of the utility is the ratio of debt to equity. Utilities that historically finance operating, maintenance and capital expenditures by issuing debt in addition to internally available funds may be viewed as financially insecure. In such cases, rate orders may include restrictions on the ability of the utility to make new loans to other utility operations or to the municipality itself. In some cases, as evi-

denced by some recently issued Commission orders, the PSC may restrict utilities from pledging revenues for indebtedness unrelated to utility operations, or even from issuing any "securities" without first obtaining PSC approval.

The use of the term "securities" in this context may cause confusion. Municipal utilities, of course, are not in the habit of issuing stocks and bonds. But the PSC defines the term "securities" in terms of the utility system of accounts, which includes, among other things, "Bonds" (Account 221), "Advances from the Municipality" (223), "long term debt" (224) and "Notes payable" (231). In other words, a security in the eyes of the PSC can include most forms of debt. Since bonds can only be issued by municipalities in their governing capacity, however, it appears that in the PSC's eyes, a "security" may therefore include debt issued not only by the utility, but by the municipality itself.

Some general background on municipal debt: Municipalities raise money in many ways, including the sale of property, general taxation, issuing licenses

and collecting fees, fines, and dues. Municipalities also raise revenue by borrowing, as authorized by Chapters 66 and 67 of the state statutes, as well as by the Wisconsin Constitution. Borrowing options include "general obligation" (or "GO") financing, including long-term bonds and notes; short-term revenue anticipation notes; various state funding resources such as Public Lands Trust Fund loans; and revenue financing.

GO pledges are secured by an irrevocable tax levy imposed at the time of issuance, and subject to a constitutionally imposed debt limit equal to 5% of the municipality's equalized property value. Revenue pledges are secured by a pledge of specified revenues, such as water, sewer, or electric revenues. GO pledges are generally deemed less risky, meaning they garner lower interest rates; they also have lower costs of issuance.

Revenue financing is most often used to finance construction of public works or utility system projects.

With that in mind, municipal utilities seeking rate increases — particularly utilities carrying a significant amount of debt —

should be attuned to the potential impact of potential PSC restrictions on their ability to issue future debt, including non-utility-related municipal obligations. MEUW members facing such restrictions should be prepared to probe precisely whether or how the PSC intends to extend its jurisdiction to areas of municipal finance, not only because the scope of Commission jurisdiction in those areas is (at best) unclear, but also because additional layers of required regulatory approvals can cause costly delays in financing.

Conversely, given the potential interplay between the Commission's financial oversight responsibility and the area of municipal finance, municipal utilities who are considering the possibility of pursuing a rate increase should consider engaging a financial advisor before doing so, especially if it has been some time since the last rate case was filed. ●



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