

Financial Advisory Presentation to:

CPS Energy
regarding the
**Dodd-Frank Financial
Reform Bill and Other
Legislative Developments**

Presented by The PFM Group

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Overall Considerations of Dodd-Frank Bill

- The Dodd-Frank bill was a landmark, comprehensive bill affecting the financial industry, and will have significant and evolving impacts on the overall financial industry, with specific impacts to municipal utilities:
 - Major focus of the financial reform bill was to correct systemic risks of the overall financial industry that occurred in 2007-2009:
 - Substantial control granted to the Treasury and Federal Reserve to address systemic financial risk
 - Does contain significant municipal bond market items
 - Dodd-Frank became immediately effective when enacted in July 2010, but it defers a number of changes to future studies and rulemaking activities:



General Impact to CPS Energy

- While the ultimate impacts to CPS Energy are still unfolding, it is believed that that CPS Energy will be particularly impacted in the following areas:
 - Municipal Bond Market Reforms
 - Rating Agency Reforms and Practices
 - Derivatives / Swap Market Reforms
 - Financial Disclosure Related to Bond Market Transactions



Municipal Bond Market Reforms

- There were a number of major changes to the municipal securities business in the Dodd-Frank bill:
 - Creates the Office of Municipal Securities within the SEC,

 - Regulation of Municipal Financial Advisors
 - Expands definition of what is a Municipal Advisor
 - Imposes a fiduciary duty for municipal financial advisors

 - Major changes to the Municipal Securities Rulemaking Board (MSRB) which governs the municipal bond market

Changes to Municipal Financial Disclosure



- Substantial scrutiny will be focused on financial disclosure in securities offerings, and the municipal market will be a primary focus within the SEC:

- The Dodd-Frank bill requires the Comptroller of the United States to undertake two studies related to municipal financial disclosure and whether to move to a more “corporate style” disclosure system

- The municipal disclosure study must be completed by July 2012 and is required to set forth recommendations for municipal disclosure

- The report will also study the potential repeal of the Tower Amendment, which exempts municipal securities from the registration and ongoing filings with the SEC and MSRB

- The municipal market study must also include an analysis of market transparency, trade reporting, and quality of trade executions

Rating Agency Changes

- There are significant changes prescribed for rating agencies, many of which will carry over to the municipal market:
 - The Dodd-Frank Bill creates the Office of Credit Ratings within the SEC to administer SEC rules for credit ratings and to ensure that ratings are not influenced by conflicts of interest
 - As part of the changes, the Dodd-Frank bill requires the SEC to conduct studies and review the possibility of providing more rating agency independence and/or an independent professional organization to deliver bond ratings
 - Places greater standards on rating agencies and potentially creates ability for investors to bring civil suits against the rating agencies for their expert opinions
 - Generally, it is PFM's belief that rating agencies will respond to the financial reform in the following ways:
 - Being more conservative and quicker to take negative rating action
 - Providing less clarity on rating criteria and ratings
 - Being substantially more costly in fees and trying to pass on such fees to issuers

Derivatives / Swaps Market Changes

- Substantial portions of the Dodd-Frank Bill are related to the regulation and changes in the derivatives and swap markets:
 - In general, there are a number of provisions that impact the municipal derivatives and swaps market; however, certain exemptions do exist for municipal entities
 - Encourage derivatives and swaps to be traded on exchanges and/or require swaps and other derivatives to be cleared through derivative clearing organizations (except for commercial end users who will be exempted)
 - Will take place on the later of July 2011 or 60 days after publication of changes by the SEC and Commodity Future Trading Commission (CFTC)

 - While CPS Energy's hedging practices already use exchange traded products (e.g., NYMEX contracts), municipal utilities should maintain a commercial end user exemption for municipal entities that use derivatives and swaps for hedging purposes

 - Specific provisions are likely to apply to the municipal swap and derivative market



Other Recent Legislative Developments

Federal Subsidy Program Expiration Dates						
Year	Production Tax Credits	Investment Tax Credits	Grant in Lieu of ITC	Build America Bonds	Clean Renewable Energy Bonds	Qualified Energy Conservation Bonds
2010						
2011						
2012	2012: Wind	2012: Wind				
2013	2013: Others	2013: Others				

- CPS Energy has benefited from the programs and subsidies expanded by ARRA 2009
 - Some of these programs have sunset already and others are set to expire shortly
 - BABs expired, though some efforts to revive them linger
- Future focus should be on legislative efforts on certain of these programs, particularly if renewable projects remain a focus
 - The Grant in Lieu of ITC was extended to 2011 in light of ongoing challenges in the tax credit market

DOE Loan Guarantee Program Update

The Department of Energy Loan Guarantee program may be significantly limited moving forward, as capital markets improve.

- With the exception of nuclear component, appears that the Loan Guarantee program will be curtailed.
- Current Obama budget limits renewable component of the Loan Guarantee Program, but suggests increasing nuclear guarantees by \$36 billion (from current authorization of \$18.5 billion)
- Republican-led House version of provisions for DOE loan guarantee program may differ greatly, but Senate Republicans are highly supportive of nuclear.
- If the DOE nuclear program were to be expanded, would suggest availability of funding source for STP project.