

Mission Statement:

The UTC protects consumers by ensuring that utility and transportation services are fairly priced, available, reliable, and safe.



Washington Utilities and Transportation Commission

Comparison of Private & Public Utilities

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Basic Types of Utilities

- Private / For-Profit (Investor Owned)
- Public / Municipalities & Public Utility Districts
- Private / Not For Profit (Cooperatives)

Private / For-Profit Utilities (Investor Owned)



- Privately owned business corporations
- Provide many different types of utility services
 - Electricity, natural gas, water, sewer, garbage, telecommunications & garbage
- Subject to state & federal regulation

Private Utilities – cont.

- Often engage in other non-regulated business activities, such as property management & technical services
- In the business “to make a profit” for their owners (stockholders)

Public Utilities

- Owned by state or local government
- Usually provide only electric, water and sewer services
 - In some states they also provide natural gas or telecommunications
- Activities limited by state law
- Not-for-Profit (no stockholders)

Cooperatives

- Special type of private not-for-profit corporation
- Members are the people who receive utility service from the cooperative
- Usually only provide electric service
- Geographic area based on location of members
- Generally considered part of “public power” even though private ownership

Overview of Differences Between Private and Public Utilities

Legal Structure



- Private
 - Owned by investors (stockholders)
 - Able to engage in any “lawful” business activity
- Public
 - Owned by a state or local government entity
 - Functions limited to those authorized by state law

Organizational Structure



- Private
 - Ownership — Stockholders
 - Governance — Board of Directors elected by stockholders
 - Management — Executives hired by Board
- Public
 - Ownership — Government
 - Governance — Commission (usually 3-5) elected or appointed
 - Management — Manager hired by Commission

Financial Features-Capital



- Private
 - Obtains capital primarily from *equity* (stock sales) and *debt* (bank loans and bond sales)
 - Usually about 50% of each type
- Public
 - Obtains nearly all capital from sale of bonds
 - Also use some small bank loans
 - A few public utilities have the power to levy taxes but rarely use that power to raise capital

Bonds-Private Utilities



- “Corporate” bonds
 - These are essentially contracts to repay a loan at a certain time with an agreed amount of interest
 - The interest earned by investors on nearly all corporate bonds is *taxable*
 - For this reason, companies must pay a higher rate of interest to compensate for the taxes
 - Exception for some types of “environmental” bonds

Bonds-Private Utilities (cont.)



- Repayment of private utility bonds may be secured either by the general credit of the company, by a mortgage against specific assets or by a pledge of the revenues produced by a specific asset (such as a generator)

Bonds-Public Utilities

- Bonds issued by public utilities are generally referred to as “Municipal” bonds
- Municipal bonds contain the same type of basic repayment and interest obligations as Corporate bonds
- Interest earned by investors on Municipal bonds is generally *not taxable*
 - This means that the public utility can pay a lower rate of interest
 - Exception-interest on Municipal bonds that benefit private companies is taxable

Bonds-Public Utilities (cont.)



- Nearly all Municipal bonds issued by public utilities are secured by the *revenues* produced by a specific asset
 - Some public utilities may also issue “general obligation” bonds that are secured by the general credit of the utility but these are rarely used and are often limited by state law to small amounts of money

Bond Interest Rates

- Private utilities nearly always have to pay higher interest to bond buyers to compensate for income taxes
 - The difference is often 2-3% or more, depending on market conditions and the company's credit rating
 - Private utility bonds are also viewed by bond buyers as “riskier,” and the private utilities have to pay higher interest to offset that risk

Credit Ratings

- Buyers in the capital markets (stocks and bonds) rely heavily on independent companies that review the financial condition of both private and public utilities and issue each a “credit rating”
- The credit rating summarizes the overall financial strength of the utility

Credit Ratings (cont.)

- There are 3 primary companies that prepare credit ratings
 - Moody's
 - Standard & Poor's (S&P)
 - Fitch
- Each rating company has a team of analysts that regularly review the business & financial activities of all private and public utilities in the U.S.

Credit Ratings (cont.)

- Virtually all types of investors rely heavily on the credit ratings of utilities as a measure of the risk associated with buying a utilities stock or bonds
- Credit ratings have a direct and significant impact on the interest rate the utility must offer in order to attract investors
 - This applies equally to private and public utilities

Operating Funds-Rates

- Both private and public utilities rely primarily on revenue collected from their retail customers for their ordinary operating funds
 - Customer revenues are also the main source of “profits” for private utilities and “reserves” for public utilities
- Customer generated revenues are wholly dependant on the “rates” charged for utilities products and services

Rate Setting



- Private
 - Utilities submit financial data on their operating costs to a state commission
 - They are only allowed to charge rates subsequently authorized by the commission following a formal review process
- Public
 - The locally elected or appointed governing board sets its own rates and can change them at any time
 - Usually involves a simplified internal review of operating costs and a public presentation process

Rate Setting (cont.)

- Customers of both private and public utilities may challenge rates in court but it is very difficult to win such a case unless the rate setting commission has acted without any reasonable justification
 - Consequently, lawsuits over rates are infrequent

Access to Federal Power



- Important difference between private and public utilities in the Pacific Northwest and other parts of the U.S. is the availability of electric energy produced by generation systems owned by the U.S. government
- Bonneville Power Administration, Tennessee Valley Authority, Western Area Power Administration

Access to Federal Power (cont.)



- The price of power purchased from the federal system has been substantially lower than power purchased on the open market or self generated
 - While the price difference has been less in recent years, it is still significant
- Only Public utilities are “entitled” to purchase federal system power

Laws Applicable to all Utilities



- Both private and public utilities are required to comply with certain federal and state laws pertaining to their operations
 - Operating license requirements for generation facilities (FERC)
 - Permits for construction (site approvals)

Generally Applicable Laws (cont.)



- Federal Environmental Laws
 - Endangered Species
 - Clean Water
 - Clean Air
- State Environmental and Land Laws
 - Shoreline Management
 - Building permits
 - Wetland protection

Special Legal Requirements for Public Utilities



- Because public utilities are part of the state government, they are subject to several laws that don't apply to private utilities
 - SEPA (a Washington environmental review law), public contracting processes, open records and meeting requirements and public audits

Taxes



- Private
 - Income taxes (federal & state)
 - Property taxes (based on value of assets owned)
 - Utility taxes (based on value of services provided)
 - Business & Occupation taxes (based on revenues earned)
- Public
 - Privilege taxes (similar to property taxes)
 - Utility taxes

Summary & Conclusions



- In Washington State, approximately 50% of the electric energy customers are served by private utilities and 50% are served by public utilities
- For natural gas, over 99% is supplied by private utilities
 - only 3 small towns operate public gas systems

Conclusions (cont.)

- The main differences between private and public utilities are
 - Legal structure and powers
 - Governance structure
 - Taxability
 - Means of raising capital
 - How rates are set
 - Profit vs. Not-for-Profit character

Conclusions (cont.)

- From the perspective of the utility customers, the quality of the products and services provided is very similar
- The biggest difference is PRICE
 - Much of that is due to Public utilities
 - Not earning a profit
 - Not paying certain taxes
 - Having lower capital costs
 - Having access to cheaper federal power