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CHAIRMAN
JIM IRVIN
COMMISSIONER
MARC SPITZER
COMMISSIONER



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BRIAN C. McNEIL
EXECUTIVE SECRETARY

ARIZONA CORPORATION COMMISSION APR 18 P 12:30

DATE: April 18, 2001
DOCKET NOS: E-01787A-00-0820
TO ALL PARTIES:

AZ CORP COMMISSION
DOCUMENT CONTROL
Arizona Corporation Commission
DOCKETED

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Enclosed please find the recommendation of Administrative Law Judge Philip J. Dion, III. The recommendation has been filed in the form of an Order on:

NAVOPACHE ELECTRIC COOPERATIVE, INC.
(FINANCE)

Pursuant to A.A.C. R14-3-110(B), you may file exceptions to the recommendation of the Administrative Law Judge by filing an original and ten (10) copies of the exceptions with the Commission's Docket Control at the address listed below by **12:00 noon** on or before:

APRIL 27, 2001

The enclosed is NOT an order of the Commission, but a recommendation of the Administrative Law Judge to the Commissioners. Consideration of this matter has tentatively been scheduled for the Commission's Working Session and Open Meeting to be held on:

MAY 1, 2001 AND MAY 2, 2001

For more information, you may contact Docket Control at (602)542-3477 or the Hearing Division at (602)542-4250.

BRIAN C. McNEIL
EXECUTIVE SECRETARY

1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2 WILLIAM A. MUNDELL
CHAIRMAN

3 JIM IRVIN
COMMISSIONER

4 MARC SPITZER
COMMISSIONER

5
6 IN THE MATTER OF THE APPLICATION OF
NAVOPACHE ELECTRIC COOPERATIVE, INC.
7 TO OBTAIN A LINE OF CREDIT.

DOCKET NO. E-01787A-00-0820

DECISION NO. _____

8 **ORDER**

9 Open Meeting
May 1 and 2, 2001
Phoenix, Arizona

10 **BY THE COMMISSION:**

11 On October 16, 2000, Navopache Electric Cooperative, Inc. ("Navopache") filed an
12 application with the Arizona Corporation Commission ("Commission") requesting authorization to
13 obtain an unsecured line of credit totaling \$10,000,000 from the National Rural Utilities Cooperative
14 Finance Corporation ("CFC"). Navopache published notice of its application on November 28, 2000,
15 in The White Mountain Independent, a newspaper having general circulation in Apache, Greenlee,
16 Gila and Navajo Counties, Arizona and Catron County, New Mexico. On February 26, 2001, the
17 Commission's Utilities Division Staff ("Staff") filed its Staff Report in the matter, recommending
18 approval of the application without a hearing.

19 **DISCUSSION**

20 **Introduction**

21 Navopache is a non-profit rural electric distribution corporation authorized to provide electric
22 utility service to parts of Apache, Greenlee, Gila and Navajo Counties, Arizona. Navopache also
23 provides electric service to consumers in Catron County, New Mexico. Navopache has approximately
24 29,682 customers in Arizona and in New Mexico. Its current rates were approved in Decision No.
25 58041 which had an effective date of August 10, 1992. Navopache's growth rate in customer count
26 is estimated to be fifteen percent (15%) over the period of 2000 to 2003. Navopache has maintained
27 an average of 3.77 outage-hours per customer in the last five years, which is within the Rural Utility
28

1 Service guideline of five outage-hours per customer.

2 **Purpose of Financing**

3 Navopache has submitted a construction work plan for the years 2000 through 2003 to Staff.
4 The project includes the construction of a new delivery point at the Springerville Power Plant with a
5 twenty (20) mile, sixty-nine (69) kilovolt line to the Round Valley Switching Station. The project will
6 help Navopache meet expected future growth of customers, improve existing reliability, improve
7 voltage levels, dramatically reduce losses on the system and continue servicing its eastern system in
8 the event the Colorado Transformer, which serves the area, fails. The new line is expected to reduce
9 electrical losses from 855 kilowatts to 183 kilowatts, which is a seventy-eight percent (78%)
10 reduction in losses. Staff Engineering reviewed the proposed capital projects and concluded that they
11 are reasonable, proper and prudent, given the growth being experienced by the utility, and based on
12 their technical study assessments.

13 According to Navopache, it will soon have insufficient internal funds to complete the four
14 year work plan and requires immediate financing to continue providing reliable service. The line of
15 credit will be used to fund the first two years of the four-year construction plan totaling \$18,434,984.

16 **Terms of Debt**

17 Navopache proposes to obtain the line of credit from CFC to use as a "bridge loan" until it
18 obtains long-term financing from Rural Utilities Service ("RUS"). The line of credit is necessary
19 since there is a delay of up to two years from the time a borrower's application with RUS is filed
20 until the date that the loan is consummated and financing is made available to the borrower.

21 Navopache is in the process of applying for the line of credit from CFC and will be filing an
22 application with RUS. Navopache has met with RUS and CFC in a series of meetings regarding
23 financing. Both RUS and CFC have not given a written commitment, but neither has indicated any
24 reason for disapproval. In the unlikely event that Navopache does not receive a long-term financing
25 commitment from RUS, it would secure long-term financing from CFC.

26 In Navopache's previous meeting with RUS, RUS recommended that Navopache apply for
27 the long-term debt financing around the same time that Navopache filed its rate case with the
28 Commission. Navopache filed its rate case with the Commission on January 19, 2001. Thus, the

1 RUS finance application should be completed soon and Navopache has indicated it will provide Staff
2 with a copy of the RUS application once filed.

3 The proposed line of credit will include a variable interest rate and a requirement that
4 sometime during each twelve-month period of the loan Navopache will, for a period of at least five
5 consecutive business days, reduce all amounts outstanding to zero.

6 Since the interest rate on the line of credit is variable, Staff estimated Navopache's interest
7 expense and its ability to serve its annual debt. The average variable interest rate charged by CFC
8 between March 2000 and September 2000 was 7.96%. In its analysis, Staff conservatively assumed
9 an average variable interest rate of 8.00% in calculating interest expense associated with the line of
10 credit.

11 Since the line of credit is intended to be a "bridge loan," Navopache will not be required to
12 make any principal payments under the line of credit, but all amounts outstanding will be due and
13 payable when Navopache receives the proceeds from the long-term financing from RUS. Navopache
14 is required to make interest payments on the loan.

15 Capital Structure and Financial Impact

16 According to Navopache's 1999 annual report filed with the Commission, Navopache had an
17 operating income of \$1,316,052. Additionally, as of December 31, 1999, it owed debts to RUS and
18 NRCUF in the amounts of \$24,171,861 and \$8,019,304 respectively.

19 As a measure of financial soundness, Staff examined the effects of the proposed line of credit
20 in relation to Navopache's Debt Service Coverage ("DSC") ratio. That ratio measures the number of
21 times cash flow will cover principal and interest payments. While the CFC does not require
22 Navopache to maintain a minimum DSC, many financial institutions prefer a ratio of 1.25.

23 Navopache anticipates drawing down approximately \$4,109,025 in the first year of the line of
24 credit and \$3,476,225 in the second year. The anticipated interest expense related to the line of credit
25 for the first year would be \$328,722, and the projected DSC ratio is 1.13. While that is below the
26 benchmark of 1.25, it is above 1.00, indicating that Navopache would still be able to service the
27 proposed debt. Navopache's 1999 year-end DSC ratio was 1.28.

28 Navopache's 1999 year-end capital structure was approximately 74.5 percent long-term debt

1 and 25.5 percent equity. The addition of the line of credit will raise the percentage of short-term debt
2 from 0% to 19.6% and total debt from 74.5 percent to 79.5 percent. Historically, cooperatives, like
3 Navopache, have highly leveraged capital structures because they have received lower-than-market
4 interest rates on debt. Therefore, they are able to assume more debt than investor-owned utilities.
5 Based on the foregoing analysis, Staff expects Navopache to generate sufficient funds to support the
6 line of credit and the addition of the line of credit to the capital structure should not increase
7 Navopache's cost of capital.

8 Based on the above, Staff recommended approval of Navopache's proposed financing. We
9 concur.

10 Having considered the entire record herein and being fully advised in the premises, the
11 Commission finds, concludes, and orders that:

12 FINDINGS OF FACT

13 1. Navopache is a non-profit rural electric distribution corporation authorized to provide
14 electric utility service to parts of Apache, Greenlee, Gila and Navajo Counties, Arizona. Navopache
15 also provides electric service to consumers in Catron County, New Mexico. The Navopache has
16 approximately 29,682 customers in Arizona and in New Mexico.

17 2. On October 16, 2000, Navopache filed an application for Commission authorization to
18 obtain an unsecured line of credit totaling \$10,000,000 from CFC.

19 3. On February 26, 2001, Staff filed its Staff Report in the matter, recommending
20 approval of the application without a hearing.

21 4. Navopache published notice of its application on November 28, 2000, in The White
22 Mountain Independent, a newspaper having general circulation in Apache, Greenlee, Gila and Navajo
23 Counties, Arizona and Catron County, New Mexico.

24 5. The line of credit will be used to fund the first two years of a four-year construction
25 plan totaling \$18,434,984.

26 6. The project includes the construction of a new delivery point at the Springerville
27 Power Plant with a twenty (20) mile, sixty-nine (69) kilovolt line to the Round Valley Switching
28 Station.

1 7. The project will improve existing reliability, improve voltage levels, dramatically
2 reduce losses on the system, help Navopache meet expected growth and continue servicing its eastern
3 system in the event the Colorado Transformer, which serves the area, fails.

4 8. Staff Engineering reviewed the proposed capital projects and concluded that they are
5 reasonable, proper and prudent, given the growth being experienced by the utility, and based on their
6 technical study assessments.

7 9. According to Navopache, it will soon have insufficient internal funds to complete the
8 four year work plan and requires immediate financing to continue providing reliable service.

9 10. The line of credit is intended to be a "bridge loan" which will fund the first two years
10 of work until the proceeds from the long-term financing with RUS become available.

11 11. In the unlikely event that Navopache does not receive a long-term financing
12 commitment from RUS, it would secure long-term financing from CFC.

13 12. The proposed line of credit will include a variable interest rate and a requirement that
14 sometime during each twelve-month period of the loan Navopache will, for a period of at least five
15 consecutive business days, reduce all amounts outstanding to zero.

16 13. Since the line of credit is intended to be a "bridge loan," Navopache will not be
17 required to make any principal payments under the line of credit and all amounts outstanding will be
18 due and payable when Navopache receives the proceeds from the long-term financing from RUS.

19 14. Navopache is required to make interest payments on the loan. The anticipated interest
20 expense for the first year is expected to be \$328,722.

21 15. According to Navopache's 1999 annual report filed with the Commission, Navopache
22 had an operating income of \$1,316,052.

23 16. Based on Navopache's 1999 annual report, the terms of the line of credit financing,
24 the estimated interest rate and the projected principal draw downs, Staff projected a DSC ratio of
25 1.13.

26 17. The addition of the line of credit will raise the percentage of short-term debt from 0%
27 to 19.6% and total debt from 74.5 percent to 79.5 percent.

28 18. Staff believes that the proposed financing is for lawful purposes, consistent with sound

1 financial practices, and is in the public interest.

2 **CONCLUSIONS OF LAW**

3 1. Navopache is a public service corporation within the meaning of Article XV of the
4 Arizona Constitution and A.R.S. §§ 40-301 and 40-302.

5 2. The Commission has jurisdiction over Navopache and the subject matter of the
6 application.

7 3. Notice of the application was given in accordance with the law.

8 4. The financing approved herein is for lawful purposes within Navopache's corporate
9 powers, is compatible with the public interest, with sound financial practices, and with the proper
10 performance by Navopache of service as a public service corporation, and will not impair
11 Navopache's ability to perform that service.

12 5. The financing approved herein is for the purposes stated in the application and is
13 reasonably necessary for those purposes, and such purposes are not, wholly or in part, reasonably
14 chargeable to operating expenses or to income.

15 **ORDER**

16 IT IS THEREFORE ORDERED that Navopache Electric Cooperative, Inc. is hereby
17 authorized to obtain an unsecured variable interest rate line of credit totaling \$10,000,000 from the
18 National Rural Utilities Cooperative Finance Corporation.

19 IT IS FURTHER ORDERED that once Navopache Electric Cooperative secures long-term
20 debt financing, which is intended to be used to repay the principle and interest owed under the line of
21 credit, then the authorization for the line of credit contained in this Order shall terminate.

22 IT IS FURTHER ORDERED that Navopache Electric Cooperative, Inc. is hereby authorized
23 to engage in any transactions and to execute any documents necessary to effectuate the authorization
24 granted hereinabove.

25 IT IS FURTHER ORDERED that such authority is expressly contingent upon Navopache
26 Electric Cooperative, Inc.'s use of the proceeds for the purposes set forth in its application.

27 IT IS FURTHER ORDERED that approval of the financing set forth hereinabove does not
28 constitute or imply approval or disapproval by the Commission of any particular expenditure of the

1 proceeds derived thereby for purposes of establishing just and reasonable rates.

2 IT IS FURTHER ORDERED that Navopache Electric Cooperative, Inc. shall file copies of all
3 executed financing documents setting forth the terms of the financing, within 30 days of obtaining
4 such financing.

5 IT IS FURTHER ORDERED that this Decision shall become effective immediately.

6 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

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CHAIRMAN COMMISSIONER COMMISSIONER

IN WITNESS WHEREOF, I, BRIAN C. McNEIL, Executive Secretary of the Arizona Corporation Commission, have hereunto set my hand and caused the official seal of the Commission to be affixed at the Capitol, in the City of Phoenix, this ____ day of _____, 2001.

BRIAN C. McNEIL
EXECUTIVE SECRETARY

DISSENT: _____
PD:dap

1 SERVICE LIST FOR: NAVOPACHE ELECTRIC COOPERATIVE, INC.

2 DOCKET NO. E-01787A-00-0820

3 Paul Michaud
4 MARTINEZ & CURTIS, P.C.
5 2712 N. 7th Street,
6 Phoenix, Arizona 85006
7 Attorneys for Navopache Electric Co-op, Inc.

8 Christopher Kempley, Chief Counsel
9 ARIZONA CORPORATION COMMISSION
10 1200 West Washington Street
11 Phoenix, Arizona 85007

12 Deborah Scott, Director
13 Utilities Division
14 ARIZONA CORPORATION COMMISSION
15 1200 W. Washington Street
16 Phoenix, Arizona 85007
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