

ORIGINAL

OPEN MEETING



0000040513

MEMORANDUM

410

TO: THE COMMISSION

FROM: Utilities Division

DATE: February 8, 2006

RE: IN THE MATTER OF THE APPLICATION OF THE ARIZONA ELECTRIC POWER COOPERATIVE, INC. FOR PERMISSION TO TEMPORARILY EXCEED THE SEVEN PERCENT SHORT-TERM DEBT LIMITATION OF A.R.S. § 40-302.D. (DOCKET NO. E-01773A-06-0007)

Attached you will find the Staff Report that was docketed on February 6, 2006 and a Recommended Opinion and Order which adopts Staff's recommendations related to Arizona Electric Power Cooperative, Inc.'s application for permission to temporarily exceed the seven percent short-term debt limitation of A.R.S. §40-302.D.

Ernest G. Johnson  
Director  
Utilities Division

EGJ:DTZ:lm\CCK

Originator: Daniel Zivan

AZ CORP COMMISSION  
DOCUMENT CONTROL

2006 FEB - 8 A 11: 01

RECEIVED

MEMORANDUM

RECEIVED

TO: Docket Control

2006 FEB -6 A 11: 38

FROM: Ernest G. Johnson  
*for* Director  
Utilities Division

AZ CORP COMMISSION  
DOCUMENT CONTROL

DATE: February 6, 2006

RE: STAFF REPORT FOR ARIZONA ELECTRIC POWER COOPERATIVE, INC. –  
APPLICATION FOR AUTHORIZATION FOR FINANCING (DOCKET NO. E-  
01773A-06-0007)

Attached is the Staff Report for Arizona Electric Power Cooperative, Inc.'s application for authorization for financing. Staff recommends approval.

EGJ:DTZ:tdp

Originator: Daniel Zivan

Attachment: Original and fourteen copies

Service List for: Arizona Electric Power Cooperative, Inc.  
Docket No. E-01773A-06-0007

Michael M. Grant  
Todd C. Wily  
Gallagher & Kennedy, P.A.  
2575 East Camelback Road  
Phoenix, Arizona 85016-9225

Mr. Ernest G. Johnson  
Director, Utilities Division  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, Arizona 85007

Mr. Christopher C. Kempley  
Chief, Legal Division  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, Arizona 85007

Ms. Lyn Farmer  
Chief, Hearing Division  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, Arizona 85007

STAFF REPORT  
UTILITIES DIVISION  
ARIZONA CORPORATION COMMISSION

ARIZONA ELECTRIC POWER COOPERATIVE, INC.

DOCKET NO. E-01773A-06-0007

APPLICATION FOR AUTHORIZATION  
FOR FINANCING

FEBRUARY 2006

## STAFF ACKNOWLEDGMENT

The Staff Report for Arizona Electric Power Cooperative, Inc., Docket No. E-01773A-06-0007 was the responsibility of the Staff member signed below. Daniel Zivan was responsible for the review and financial analysis of the Company's application.

A handwritten signature in black ink, appearing to be 'DZ', is centered on the page.

DANIEL ZIVAN  
PUBLIC UTILITIES ANALYST III

**EXECUTIVE SUMMARY**  
**ARIZONA ELECTRIC POWER COOPERATIVE, INC.**  
**APPLICATION FOR AUTHORIZATION**  
**FOR FINANCING**  
**DOCKET NO. E-01773A-06-0007**

Arizona Electric Power Cooperative, Inc. ("AEPCO" or "Cooperative") filed an application requesting authorization for financing with the Arizona Corporation Commission ("Commission") on January 6, 2006. AEPCO is a Class "A" Arizona cooperative that supplies the power needs of its five Arizona class "A" cooperatives and other customers.

AEPCO requests Commission authorization, pursuant to A.R.S. 40-302.D., to temporarily exceed the statutory short-term borrowing limit of seven percent of total capital through 2006. Specifically, AEPCO requests authorization to increase its short-term borrowing to \$30 million. AEPCO had short-term borrowings of approximately \$15.2 million as of December 31, 2005, and its application anticipates that it will be at the threshold of the seven percent limit (estimated at \$16.3 million) by January 31, 2006. The Cooperative asserts that the larger short-term borrowing limit is needed to finance large under-collections caused by increasing costs of natural gas and purchased power and other operational efficiencies. Absent increased borrowing authority, AEPCO may default on accounts payable obligations to purchased power providers. AEPCO must repay short-term draws within one year.

AEPCO filed an application with the Commission requesting authorization to accelerate the implementation date for the Fuel and Purchased Power Cost Adjustor ("FPPCA") approved in the Cooperative's most recent rate case (Decision No. 68071) from October 1, 2006 to April 1, 2006, to improve its cash flow.

Staff concludes that the proposed use of funds is appropriate and that authorization to increase short-term borrowing to \$30 million for those purposes is lawful and within the corporate powers of the applicant, is compatible with the public interest, and would not impair AEPCO's ability to provide service. Extending the borrowing authorization is also sound practice from the perspective that not extending the authorization has potentially greater detrimental effects for AEPCO and its customers than any temporary cash flow shortfall for servicing the additional requested debt.

Staff concludes that AEPCO will not meet its obligations as they become due beginning in March 2006 without additional borrowing. Further, AEPCO needs additional cash to provide flexibility for its physical hedging program that saves fuel costs for the benefit of customers. In addition, AEPCO needs access to cash for contingencies. AEPCO also needs cash flow to reduce its existing and any additional short-term debt that the Commission may authorize. Accelerated recovery of cash flows via the FPPCA could support these needs for cash.

Staff recommends granting authorization to increase the limit on short-term debt borrowing to an amount not to exceed \$30 million until January 31, 2007, under the terms proposed and for the purposes described in this report.

TABLE OF CONTENTS

	<u>PAGE</u>
INTRODUCTION .....	1
NOTICE .....	1
BACKGROUND .....	1
PURPOSE AND DESCRIPTION OF THE PROPOSED FINANCING .....	1
FINANCIAL ANALYSIS .....	1
COMPLIANCE .....	2
CONCLUSIONS AND RECOMMENDATIONS .....	2

SCHEDULES

Arizona Electric Power Cooperative, Inc. Cash Flow Projections for 2006 .....	Schedule DTZ -1
---	-----------------

## **Introduction**

Arizona Electric Power Cooperative, Inc. ("AEPCO" or "Cooperative"), an Arizona class "A" cooperative located in Benson, Arizona, filed an application requesting authorization for financing with the Arizona Corporation Commission ("Commission") on January 6, 2006.

## **Notice**

Staff counsel has been notified that the Cooperative published notice of its financing application in *Tucson Citizen*, *The Daily Star* and *Kingman Daily Minor* on January 26, 2006. Staff is awaiting the affidavit of publication.

## **Background**

AEPCO is a class "A" Arizona cooperative that supplies the power needs of its five Arizona class "A" cooperatives and other customers. AEPCO's current rates were approved in Decision No. 68071, dated August 17, 2005.

## **Purpose and Description of the Proposed Financing**

AEPCO requests Commission authorization, pursuant to A.R.S. 40-302.D., to temporarily exceed the statutory short-term borrowing limit of seven percent of total capital. Specifically, AEPCO requests authorization to increase its short-term borrowing to \$30 million, or approximately 13 percent of total capital. The Cooperative's application states that "AEPCO has only about \$1 million in short-term debt capacity remaining to support fuel, purchased power and other working capital needs." The Cooperative asserts that the larger short-term borrowing limit is needed to finance large under-collections caused by increasing costs of natural gas and purchased power and its physical hedging program designed to limit future gas costs. AEPCO may default on accounts payable obligations to purchased power providers absent increased borrowing authority. AEPCO must repay short-term draws within one year.

## **Financial Analysis**

AEPCO currently has two sources of short-term borrowing: a line of credit from the National Rural Utilities Cooperative Finance Corporation ("CFC") and a member investment program ("MIP"). As of December 31, 2005, AEPCO had borrowed approximately \$10 million from the CFC line of credit and approximately \$5 million from the MIP for a total of approximately \$15 million. The Cooperative's application anticipates that its short-term debt will be at the threshold of its seven percent of total capital limit (estimated at \$16.3 million) by January 31, 2006. AEPCO asserts that CFC will not grant additional short-term borrowings unless the Commission authorizes such borrowings to exceed seven percent of total capital.

AEPCO's projections show that a cash flow deficit (an inability to meet all obligations as they come due) will occur in March 2006 with its current authorizations (Refer to Schedule

DTZ-1). Granting AEPCO's request to extend short-term borrowing authorization to \$30 million would increase its borrowing capacity by approximately \$14 million. Schedule DTZ-1 shows that AEPCO projects a cumulative cash deficit of \$14.3 million at the end of September 2006. In other words, AEPCO's projections indicate that it would have sufficient cash to meet its anticipated obligations through September 2006 with the additional short-term borrowings of \$14 million. CFC's offer to extend short-term borrowing from \$10 million to \$25 million includes a stop order provision at \$20 million that allows CFC to perform a reevaluation when borrowing reaches \$20 million that could result in discontinuation of further lending.

AEPCO's projections show an additional \$10 million cash flow deficit in the last quarter of 2006 without recognition of Fuel and Purchased Power Cost Adjustor ("FPPCA") collections which the Commission authorized (Decision No. 68071) to begin in October 2006. AEPCO's cash flow projections do not provide for any unexpected contingencies nor do they provide the desired flexibility for purchases under its physical hedging program designed to limit future gas costs.

AEPCO filed an application with the Commission requesting authorization to accelerate the implementation date for the FPPCA approved in the Cooperative's most recent rate case (Decision No. 68071) from October 1, 2006 to April 1, 2006, to improve its cash flow.

Staff concludes that AEPCO will not meet its obligations as they become due beginning in March 2006 without additional borrowing. Further, AEPCO needs additional cash to provide flexibility for its physical hedging program that saves customers fuel costs. In addition, AEPCO needs access to cash for contingencies. AEPCO also needs cash flow to reduce its existing and any additional short-term debt that the Commission may authorize. Accelerated recovery of cash flows via the FPPCA could support these needs for cash.

### **Compliance**

There are no compliance issues with AEPCO.

### **Conclusions and Recommendations**

Staff concludes that the proposed use of funds is appropriate and that authorization to increase short-term borrowing to \$30 million for those purposes is lawful and within the corporate powers of the applicant, is compatible with the public interest and would not impair AEPCO's ability to provide service. Extending the borrowing authorization is also sound practice from the perspective that not extending the authorization has potentially greater detrimental effects for AEPCO and its customers than any temporary cash flow shortfall for servicing the additional requested debt.

Staff concludes that AEPCO (1) will not meet its obligations as they become due beginning in March 2006 without additional borrowing; (2) needs cash to save its customers fuel

costs via its physical hedging program; (3) needs access to cash for contingencies; (4) needs cash flow to reduce its existing and any additional short-term debt that the Commission may authorize; and (5) could have improved cash flow if the Commission were to authorize acceleration of the implementation date of the FPPCA.

Staff recommends granting authorization to increase the limit on short-term debt borrowing to an amount not to exceed \$30 million until January 31, 2007, under the terms proposed and for the purposes described in this report.

Staff further recommends approval of granting liens in favor of the lender as required to secure the borrowings authorized.

Staff further recommends authorizing AEPCO to engage in any transactions and to execute any documents necessary to effectuate the authorizations granted.

Staff further recommends that one copy of the executed loan documents be filed with Docket Control, as a compliance item, within 90 days of the decision in this matter.

Arizona Electric Power Cooperative, Inc.  
 Docket No. E-01773A-06-0007  
 Application for Financing

Arizona Electric Power Cooperative, Inc. Cash Flow Projections for 2006

	Jan-06	Feb-06	Mar-06	Apr-06	May-06	Jun-06	Jul-06	Aug-06	Sep-06	Oct-06	Nov-06	Dec-06
CASH FLOWS FROM:												
OPERATIONS <sup>1</sup>	\$2,929,238	\$695,617	\$1,082,926	(\$9,882)	\$2,214,142	\$1,455,075	(\$1,469,140)	\$1,194,562	(\$2,409)	(\$4,200,512)	(\$505,631)	\$1,446,914
FINANCING ACTIVITIES	\$1,022,481	(\$1,181,162)	(\$5,809,733)	(\$351,821)	(\$1,572,890)	(\$5,580,356)	(\$268,321)	(\$2,469,239)	(\$6,166,090)	(\$411,022)	(\$1,201,308)	(\$5,569,495)
INVESTMENTS ACTIVITIES	\$28,155	\$25,445	\$28,189	\$187,419	\$28,520	\$27,616	\$28,681	\$28,698	\$27,953	\$189,030	\$28,110	\$29,064
TOTAL NET CASH FLOWS	\$3,979,874	(\$460,100)	(\$4,697,618)	(\$174,284)	\$669,772	(\$4,097,665)	(\$1,708,780)	(\$1,245,979)	(\$6,140,546)	(\$4,422,504)	(\$1,678,829)	(\$3,893,517)
BEGINNING CASH BALANCE	\$2,260,236	\$6,240,110	\$5,780,010	\$1,082,392	\$908,108	\$1,577,880	(\$2,519,785)	(\$4,228,565)	(\$5,474,544)	(\$11,615,090)	(\$16,037,594)	(\$17,716,423)
ENDING CASH BALANCE	\$6,240,110	\$5,780,010	\$1,082,392	\$908,108	\$1,577,880	(\$2,519,785)	(\$4,228,565)	(\$5,474,544)	(\$11,615,090)	(\$16,037,594)	(\$17,716,423)	(\$21,609,940)
RESTRICTED FUNDS	(\$2,680,331)	(\$2,680,331)	(\$2,680,331)	(\$2,680,331)	(\$2,680,331)	(\$2,680,331)	(\$2,680,331)	(\$2,680,331)	(\$2,680,331)	(\$2,680,331)	(\$2,680,331)	(\$2,680,331)
ENDING CASH BALANCE	\$3,559,779	\$3,099,679	(\$1,597,939)	(\$1,772,223)	(\$1,102,451)	(\$5,200,116)	(\$6,908,896)	(\$8,154,875)	(\$14,225,421)	(\$18,717,925)	(\$20,396,754)	(\$24,290,271)

<sup>1</sup> Includes the sale of 1,000 tons of SO2 allowances in January, 2006 for \$1,530,000

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25  
26  
27  
28

**BEFORE THE ARIZONA CORPORATION COMMISSION**

JEFF HATCH-MILLER  
Chairman  
WILLIAM A. MUNDELL  
Commissioner  
MARC SPITZER  
Commissioner  
MIKE GLEASON  
Commissioner  
KRISTIN K. MAYES  
Commissioner

IN THE MATTER OF THE APPLICATION )  
OF THE ARIZONA ELECTRIC POWER )  
COOPERATIVE, INC. FOR PERMISSION )  
TO TEMPORARILY EXCEED THE SEVEN )  
PERCENT SHORT-TERM DEBT )  
LIMITATION OF A.R.S. § 40-302.D. )

DOCKET NO. E-01773A-06-0007  
DECISION NO. \_\_\_\_\_  
ORDER

Open Meeting  
February 14 and 15, 2006  
Phoenix, Arizona

BY THE COMMISSION:

FINDINGS OF FACT

1. Arizona Electric Power Cooperative, Inc. ("AEPCO" or "Cooperative") filed an application requesting authorization for financing with the Arizona Corporation Commission ("Commission") on January 6, 2006.
2. AEPCO is a Class "A" Arizona cooperative that supplies the power needs of its five Arizona class "A" cooperatives and other customers.
3. AEPCO requests Commission authorization pursuant to A.R.S. §40-302.D. to temporarily exceed the statutory short-term borrowing limit of seven percent of total capital through 2006. Specifically, AEPCO requests authorization to increase its short-term borrowing to \$30 million.
4. Staff counsel has been notified that the Cooperative published notice of its financing application in the *Tucson Citizen*, *The Daily Star* and *Kingman Daily Miner* on ...

1 January 26, 2006. Staff is awaiting the affidavit of publication for notices published in *The Tucson*  
2 *Citizen* and *The Daily Star*.

3 5. On February 2, 2006, the Cooperative waived its ten day exception period and  
4 requested that this matter be decided by the Commission at the February Open Meeting.

5 6. AEPCO had short-term borrowings of approximately \$15.2 million as of  
6 December 31, 2005, and its application anticipates that it will be at the threshold of the seven  
7 percent limit (estimated at \$16.3 million) by January 31, 2006.

8 7. The Cooperative asserts that the larger short-term borrowing limit is needed to  
9 finance large under-collections caused by increasing costs of natural gas and purchased power and  
10 other operational efficiencies.

11 8. Absent increased borrowing authority, AEPCO may default on accounts payable  
12 obligations to purchased power providers.

13 9. AEPCO must repay short-term draws within one year.

14 10. Staff has determined that the proposed use of funds is appropriate and that  
15 authorization to increase short-term borrowing to \$30 million for those purposes is lawful and  
16 within the corporate powers of the applicant, is compatible with the public interest, and would not  
17 impair AEPCO's ability to provide service.

18 11. Staff has determined that extending the borrowing authorization is also sound  
19 practice from the perspective that not extending the authorization has potentially greater  
20 detrimental effects for AEPCO and its customers than any temporary cash flow shortfall for  
21 servicing the additional requested debt.

22 12. Staff concludes that AEPCO will not meet its obligations as they become due  
23 beginning in March 2006 without additional borrowing. Further, AEPCO needs additional cash to  
24 provide flexibility for its physical hedging program that saves fuel costs for the benefit of  
25 customers. In addition, AEPCO needs access to cash for contingencies. AEPCO also needs cash  
26 flow to reduce its existing and any additional short-term debt that the Commission may authorize.

27 13. Staff has recommended approval of the request to increase short-term borrowing to  
28 \$30 million.

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25  
26  
27  
28

CONCLUSIONS OF LAW

1. The Cooperative is a public service corporation within the meaning of Article 15 of the Arizona Constitution and Title 40 of the Arizona Revised Statutes.

2. The Commission has jurisdiction over AEPCO and over the subject matter of the application.

3. Notice of the application was provided in conformance with law.

4. The Commission having reviewed the application and Staff's Memorandum of February 8, 2006, concludes that it is in the public interest to grant the Company's request to increase short-term borrowing to \$30 million from the perspective that not extending the authorization has potentially greater detrimental effects for AEPCO and its customers than any temporary cash flow shortfall for servicing the additional requested debt.

5. The Cooperative will be required to file one copy of executed loan documents with Docket Control, as a compliance item in this matter, within 90 days of the decision in this matter.

ORDER

IT IS THEREFORE ORDERED that the application of Arizona Electric Power Cooperative, Inc. to increase short-term borrowing to \$30 million be and hereby is granted.

...  
...  
...  
...  
...  
...  
...  
...  
...  
...  
...  
...  
...  
...  
...

1 IT IS FUTHER ORDERED that the Company file one copy of executed loan documents  
2 with Docket Control, as a compliance item in this matter, within 90 days of the decision in this  
3 matter.

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

5

6 **BY THE ORDER OF THE ARIZONA CORPORATION COMMISSION**

7

8

CHAIRMAN

COMMISSIONER

9

10

11

COMMISSIONER

COMMISSIONER

COMMISSIONER

12

13

IN WITNESS WHEREOF, I BRIAN C. McNEIL, Executive  
Director of the Arizona Corporation Commission, have  
hereunto, set my hand and caused the official seal of this  
Commission to be affixed at the Capitol, in the City of  
Phoenix, this \_\_\_\_\_ day of \_\_\_\_\_, 2006.

14

15

16

17

18

\_\_\_\_\_  
BRIAN C. McNEIL  
Executive Director

19

20

21

DISSENT: \_\_\_\_\_

22

DISSENT: \_\_\_\_\_

23

EGJ:DTZ:lh\m\CCK

24

25

26

27

28

1 SERVICE LIST FOR: Arizona Electric Power Cooperative, Inc.  
2 DOCKET NO. E-01773A-06-0007

3 Mr. Michael M. Grant  
4 Mr. Todd C. Wiley  
5 2575 East Camelback Road  
6 Phoenix, Arizona 85016-9225

7 Mr. Ernest G. Johnson  
8 Director, Utilities Division  
9 Arizona Corporation Commission  
10 1200 West Washington  
11 Phoenix, Arizona 85007

12 Mr. Christopher C. Kempley  
13 Chief Counsel  
14 Arizona Corporation Commission  
15 1200 West Washington  
16 Phoenix, Arizona 85007

17  
18  
19  
20  
21  
22  
23  
24  
25  
26  
27  
28