

ORIGINAL



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MEMORANDUM

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TO: Docket Control
Arizona Corporation Commission

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

Date: May 30, 2007

RE: STAFF REPORT FOR THE APPLICATION OF GRAHAM COUNTY ELECTRIC COOPERATIVE, INC. FOR PERMISSION TO TRANSFER CERTAIN OF ITS ASSETS TO THE TOWN OF THATCHER AND TO AMEND ITS CERTIFICATE OF CONVENIENCE AND NECESSITY IN RELATION THERETO. (DOCKET NO. E-01749A-07-0237)

Attached is the Staff Report for the application of Graham County Electric Cooperative, Inc. for permission to transfer certain of its assets to the Town of Thatcher and to amend its Certificate of Convenience & Necessity in relation thereto. Staff recommends approval.

Any party who wishes may file comments to the Staff Report with Commission's Docket Control by 4:00 p.m. on or before June 11, 2007.

EGJ:AII:tdp

Originator: Alexander Ibhade Igwe

Attachment: Original and 13 Copies

Arizona Corporation Commission

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Service List for: Graham County Electric Cooperative, Inc.
Docket No.: E-01749A-07-0237

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STAFF REPORT
UTILITIES DIVISION
ARIZONA CORPORATION COMMISSION

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.
DOCKET NO. E-01749A-07-0237

APPLICATION FOR PERMISSION TO TRANSFER CERTAIN OF ITS ASSETS TO THE
TOWN OF THATCHER AND TO AMEND ITS CERTIFICATE OF CONVENIENCE AND
NECESSITY IN RELATION THERETO.

MAY 30, 2007

STAFF ACKNOWLEDGMENT

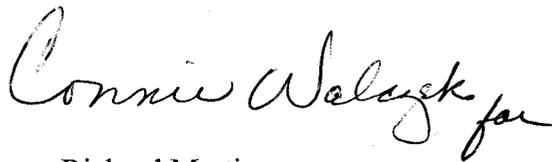
The Staff Report for Graham County Electric Cooperative, Inc., Docket No E-01749-07-0237, was prepared by the Staff members shown below. Alexander Ihhade Igwe was responsible for reviewing the application and performing pertinent financial analysis; Steve Taylor analyzed the engineering issues; and Richard Martinez researched the Consumer Service issues in this proceeding.



Alexander Ihhade Igwe
Executive Consultant III



Steve Taylor
Utilities Engineer



Richard Martinez
Public Utilities Consumer Analyst II

EXECUTIVE SUMMARY
GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.
DOCKET NO. E-01749A-07-0237

On April 11, 2007, Graham County Electric Cooperative, Inc. ("Graham") filed an application with the Arizona Corporation Commission ("Commission") for authorization to transfer certain of its assets to the Town of Thatcher ("Thatcher") and to amend its Certificate of Convenience and Necessity ("CC&N") in relation thereto. This transaction is predicated on a 1961 Agreement, as amended in 1973, which authorizes Thatcher to annex a portion of Graham's certificated area upon fulfillment of the terms of the Agreement. Graham reports that Thatcher has exercised its option pursuant to the 1973 Agreement, and that both entities entered into an agreement on March 26, 2007. Thatcher's request was approved by its citizens in the September 2006 election. The sale/purchase agreement provides for a purchase price of \$731,783.35 and transfer of assets with estimated net book value of \$52,577.87. The proposed transaction will result in an estimated gain of \$679,105.48 to Graham and transfer of approximately 68 of its 6,000 customers to Thatcher.

Staff analysis finds that the proposed transaction will neither result in service degradation in Graham's services territory nor will it have negative financial impact on the affected customers. In fact, Graham's transferred residential customers with an average monthly consumption of 755 KWh will experience a bill decrease of \$1.76, from \$74.96 to \$73.20 without the impact of purchase adjustor, under Thatcher's current tariff. If the impact of purchase adjustor is configured into the calculation, it results in a higher monthly bill decrease from \$86.58 to \$73.20, a saving of \$11.62.

As to the gains resulting from this transaction, Graham contends that it would be more beneficial to reinvest the proceeds in new capital improvements. Graham claims that its proposal is consistent with the current practice of investing internally generated funds in new infrastructure, instead of drawing down on its \$10.80 million credit facility, previously approved by the Commission. Staff finds Graham's proposal to reinvest the gains resulting from this transaction in new infrastructure to be consistent with sound financial practice and in the public interest.

The Cooperative reports that it currently holds \$100 in customer deposit for a customer and that the deposit will be applied as a reduction to the customer's last bill. Staff accepts the Cooperative's proposal to repay customer deposit as a credit to the last bill. However, in the event that the affected customer's last bill is less than \$100, Staff recommends that Graham refund the difference in cash payment.

In conclusion, Staff finds Graham's proposal to transfer certain of its assets to Thatcher and to cancel its CC&N in relation thereto, to be in the public interest. Accordingly, Staff recommends approval with conditions.

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Background

On April 11, 2007, Graham County Electric Cooperative, Inc. ("Graham" or "Cooperative") filed an application with the Arizona Corporation Commission ("Commission") for authorization to transfer certain of its assets to the Town of Thatcher ("Thatcher" or "Town") and to amend its Certificate of Convenience and Necessity ("CC&N") in relation thereto.

Graham is a non-profit, electric distribution cooperative certificated in Decision No. 33006, dated April 6, 1961, to operate electrical systems in most areas of Graham County south and east of the San Carlos Apache Indian Reservation. Graham currently serves approximately 6,000 members.

Thatcher is a municipal corporation which operates an electric distribution system within its corporate boundaries.

The Transaction

Graham proposes to transfer certain of its assets to Thatcher, and to delete its CC&N in relation thereto. This proposal is predicated on a previous Agreement entered into between Graham and Thatcher in 1946, and subsequently amended in 1973 ("The Agreement"). The Agreement grants Thatcher the right to annex certain portions of Graham's service territory, upon issuance of a written notice, payment of a purchase price and fulfillment of other stipulated terms. The Agreement states that upon consummation of a purchase agreement between both entities, Graham would cede the portion of its service territory containing the assets acquired by Thatcher. As a result, Graham will apply for cancellation of its CC&N in relation to the ceded portion of its certificated territory, and Thatcher would immediately assume responsibility for the provision of service to the customers located in that area. The Cooperative reports that the Town has exercised the above option to purchase certain of its assets pursuant to the Agreement. Thatcher's request was approved by its citizens in the September 2006 primary election. On March 26, 2007, Graham and Thatcher entered into a purchase agreement for the sale and transfer of the Cooperative's assets located within the area delineated in Exhibit A of the agreement, for the sum of \$731,783.35. This application seeks Commission authorization to effectuate the above transaction.

Public Notice

On August 29, 2006, Thatcher wrote a letter to its citizens advising them of a ballot measure that would allow the Town to purchase a portion of Graham. The initiative was approved by the citizens of Thatcher in the September 2006 election.

On September 6, 2006, Graham noticed its members of Thatcher's election ballot that, if passed, would allow Thatcher to acquire certain portion of its certificated area. Also, Graham advised its members that passage of the ballot would result in Thatcher becoming the power provider for the affected area.

On March 15, 2007, Graham filed an Affidavit of Publication, indicating that notice of its filing was published on May 6, 2007, in the *Eastern Arizona Courier*, a newspaper of wide circulation around Graham County. Please see Exhibit B attached herewith.

Engineering Analysis

Based on a field review of the physical inventory and electrical arrangement, including discussions with the Graham's General Manager, Staff concludes that transfer of the assets contained in the service area annexed by Thatcher will not have any detrimental impact on service reliability and that the terms are reasonable. Staff's conclusion is contingent on the final separation of all electrical connections between the ceded service area and the adjacent distribution facilities owned by Graham.

Staff has not performed a detailed service reliability study for customers that will be impacted by this Application. However, it appears there will be minimal, if any, reliability degradation due to the implementation of distribution changes brought about by this transaction. Thatcher's present distribution system, south of the affected service area is large and densely populated (in comparison to the service area). Therefore, Staff finds that Thatcher should be able to absorb the new service area with minimal impact on its system. As the service area grows in density, over time, Thatcher would have sufficient opportunity to make the necessary capital upgrades to insure system capacity reliability. Furthermore, the customers that will continue to be served by Graham upon consummation of this transaction should not experience any degradation in service reliability. The actions necessary for Graham to fully disconnect its system from the area being annexed by Thatcher is minimal and restricted to a few locations. Also, it appears that the corresponding work required for Thatcher to ensure provision of reliable service to its newly acquired customers would be routine. Therefore, Staff concludes that the actions necessary to effectuate the disconnection of Graham's electric distribution system from the ceded area and connection to Thatcher's distribution systems will neither be detrimental to service reliability in the service area nor negatively impact the immediate adjoining service areas. Detail Engineering Analysis is attached as exhibit A.

Financial Analysis

Staff's analysis indicates that Graham's proposal to transfer certain of its assets to Thatcher and to cancel a portion of its CC&N in relation thereto will not impair its ability to continue to provide electric distribution service within the remainder of its service territory. Also, Staff finds that this transaction will have no immediate negative financial impact on customers that will be transferred to Thatcher upon consummation of this transaction.

Staff finds that this transaction could result in a net gain of approximately \$679,105.48 to Graham. This finding results from the difference between Graham's reported net book value of its assets that will be transferred to Thatcher, estimated at \$52,677.87 and a purchase price of \$731,783.35. In a response to Staff's data request, Graham proposes to re-invest its anticipated gains as a reduction to future borrowings necessary to fund new capital improvements within its

certificated territory. The Cooperative states that the proposal is consistent with its current strategy of utilizing internally generated funds for capital improvements as against drawing against Commission authorized \$10.8 million line of long-term debt, approved in Decision No. 66382. Graham explains that as a result of its strategy, it has only drawn approximately one-half of the \$10.8 million line of credit, discussed above. Further, the Cooperative argues that while its may seem plausible to utilize the gain as a reduction to Graham's existing debt; such a recommendation could result in negative consequences, such as incurrence of prepayment penalties. The Cooperative contends that it would be more prudent to reinvest the sale proceeds in new capital investments necessary to accommodate growth, spurred by rejuvenation of mining activities within its certificated area. Staff concurs with Graham and recommends that the sale proceed, including the gains discussed above, be utilized for new capital improvements only.

Upon consummation of this transaction, Graham will transfer 68 of its current customers to Thatcher. The Cooperative reports that it currently holds \$100 in customer deposit for a customer and that the deposit will be applied as a reduction to the customer's last bill. Staff accepts the Cooperative's proposal to repay customer deposit as a credit to the last bill. However, in the event that the affected customer's last bill is less than \$100, Staff recommends that Graham refund the difference in cash payment.

Staff's analysis indicates that transfer of electric service from Graham to Thatcher will not negatively impact the customers currently being served by the Cooperative. For example, Graham's current residential customer with an average consumption of 755 KWh, will experience, after transfer to Thatcher, a decrease of \$1.76 in monthly bill, from \$74.96 to \$73.20. If Graham's fuel adjustor costs is configure into the calculation, it results in a higher monthly saving of \$11.62, a decrease from \$86.58 to \$73.20.

Consumer Service Issues

Staff's inquiry confirmed that Graham was in good standing with the Corporations Division of the Arizona Corporation Commission.

A search of Consumer Services database from January 1, 2004 though April, 27 2007, indicates 8 complaints and 2 inquiries. The complaints and inquiries relate to billing and service issues. The complaints and inquiries have been fully resolved and closed.

Conclusion and Recommendations

Staff finds that Graham's proposal to transfer certain of its assets to Thatcher and to amend its CC&N in relation thereto is in the public interest. The projected \$679,105.48 gains will decrease Graham's borrowing for new capital improvements. Further, the customers affected by this transaction will experience a decrease in monthly bills, under Thatcher's tariff.

Staff recommends approval of Graham's request to transfers certain of its assets to Thatcher.

Staff further recommends cancellation of Graham's CC&N in relations to the portion annexed by Thatcher, upon consummation of this transaction.

Staff recommends that Graham refund all customer deposits or prepayments, as a credit to the customer bill and/or cash disbursement, prior to consummation of this transaction.

Staff further recommends that Graham utilize the gains resulting from this transaction for new capital improvements only. Staff recommends that Graham file as a compliance item in this docket within 60 days of Commission order authorizing this transaction, a proposal identifying the specific new project that will be funded with the gains realized from this transaction.

Staff further recommends that Graham complete the separation of its distribution system from the ceded service territory within 90 days of the closing date of this transaction.

Staff further recommends that Graham file a report, as a compliance item in this Docket Control, within 30 days of separation of its distribution systems from the ceded service area, actions taken to separate the systems and a declaration that the customers in the affected area are exclusively being served by Thatcher.

Staff further recommends that the Commission authorize Graham to engage in any transactions and to execute or cause to be executed any documents necessary to effectuate the authorizations requested with the application. Staff recommends that Graham file as a compliance item in this docket, all pertinent documents evidencing the consummation of this transaction, no longer than 30 days from the effective date of transaction.

MEMORANDUM

TO: Alexander Igwe
Executive Consultant III
Utilities Division

FROM: Steve Taylor 
Electric Utilities Engineer
Utilities Division

THRU: Del Smith 
Engineering Supervisor
Utilities Division

DATE: May 8, 2007

SUBJECT: GRAHAM COUNTY ELECTRIC COOPERATIVE, INC. APPLICATION FOR
TRANSFER OF ASSETS TO THE TOWN OF THATCHER (DOCKET NO.
E-01749A-07-0237)

On April 11, 2007, Graham County Electric Cooperative ("GCEC") submitted an Application to the Arizona Corporation Commission ("Commission") for authorization to:

- Sell GCEC electric assets to the Town of Thatcher ("Thatcher") in an area delineated in the Asset Purchase Agreement accompanying the Application.
- Relinquish to the Town of Thatcher the right, obligation and responsibility to provide electric service in the Service Area as defined in the Asset Purchase Agreement accompanying the Application.

Utility Overview

GCEC is a non profit, electric distribution cooperative which supplies service to approximately 6,000 members in Graham County, Arizona. Thatcher is a municipal corporation in the State of Arizona which operates an electric distribution system within its corporate boundaries. GCEC and Thatcher have an Agreement by which Thatcher can acquire (upon payment and other conditions) certain electric facilities of GCEC and thereafter provide electric service to customers in territories annexed by Thatcher. The residents of Thatcher approved the acquisition of the Service Area as defined in the Asset Purchase Agreement (hereinafter the "Service Area") in a 2006 primary election and Thatcher is now exercising its right to acquire GCEC electric facilities and provide electric service in the Service Area.

Staff's Review of the Electric Facilities

Staff inspected the Electric Facilities in the Service Area on April 26, 2007, and makes the following field observations:

1. The Service Area comprises an approximately one square mile area on the north side of Thatcher. It is generally undeveloped and contains approximately 30 residences throughout the Service Area (based on the number of single phase meters in the Application). The Service Area also contains several small businesses along the north side of U.S. Highway 70 and water pump facilities throughout the Service Area (37 businesses and water pumps in total based on the number of three phase meters in the Application).
2. The Service Area is bounded on the south primarily by areas served by Thatcher which have much higher customer densities. A portion of the south bordering area is served by GCEC. The Service Area is bounded on the north by the Gila River which borders an undeveloped area to the north of the River. The Service Area is bounded on the west by a lightly developed area served by GCEC. The Service Area is bounded on the east by an undeveloped area.
3. The Service Area contains electric distribution lines owned and operated by GCEC. The Inventory Items included with the Application include poles, wire, transformers, cable, meters and associated hardware with voltage ratings (where applicable) of 600 volts generally for secondary rated equipment and 13,000 volts generally for primary rated equipment. Staff's review of the Service Area site indicates the Inventory Items listed in the Application appear to be generally commensurate with field observations.
4. The GCEC Inventory Items in the Service Area are used to supply GCEC customers in the Service Area, supply GCEC customers outside the Service Area and comprise a portion of the overall GCEC distribution system for the area. The GCEC facilities in the Service area are predominantly in the south and west portions of the Service Area.
5. Staff was cognizant that the present electrical arrangement could lead to an undesirable "co-mingling" of assets in either the proposed Service Area or present Thatcher served areas that might adversely impact the service reliability of customers in either the GCEC or Thatcher service areas. For a specific case in this Application, it would be undesirable to serve GCEC customers on the south side of U.S. Highway 70 from assets transferred to Thatcher on the north side of U.S. Highway 70 as is the present electrical arrangement. GCEC is aware of this condition and other occurrences and has advised Staff that it will make the necessary disconnects from its distribution system to ensure there will be no "co-mingling" of assets in the proposed Service Area and that GCEC customers will be served through assets owned by GCEC. Conversely, Thatcher will supply its customers in the Service area by assets owned by Thatcher.

6. All GCEC assets in the Service Area appeared to be well maintained, in good condition and built to appropriate standards and using good engineering practice.

Reliability of Service

Staff has not performed a detailed reliability study for customers impacted by this Application; however, it appears there will be minimal, if any, reliability degradation due to the implementation of distribution changes brought about by this Application. The present Thatcher distribution system to the south of the Service Area is large and densely populated (in comparison to the Service Area) and therefore should be able to absorb the Service Area at its present density with minimal impact. As the Service Area grows in density over time, Thatcher should have sufficient opportunity to make the necessary capital upgrades to reliably supply new load. The GCEC customers that will continue to be served by GCEC after the distribution work described in Item 5 above is complete should also not experience any degradation in reliable service. The GCEC actions necessary to fully disconnect its system from Thatcher in a few locations are minimal and corresponding work to ensure reliable service to remaining GCEC customers should be routine. Staff therefore concludes that the actions affecting the area's electric distribution system as part of this Application will have no detrimental affect on customer reliability in the Service Area or areas immediately adjoining the Service Area.

Conclusions and Recommendations

Based on a field review of the physical inventory and electrical arrangement including discussion with the GCEC General Manager, Staff concludes that the Transfer of Assets in the Service Area to Thatcher is reasonable under the terms of the Application and no detrimental impact to service reliability is expected. This is contingent on the final separation of all electrical ties between the Service Area and the adjacent distribution facilities owned by GCEC.

Therefore, Staff recommends that within 90 days of the Closing Date of the Asset Purchase Agreement as described in the Application, GCEC would complete the separation of its distribution system from the Thatcher distribution system occupying the Service Area of this Application. In conjunction with this separation, GCEC would further ensure that no GCEC customers are served through Thatcher distribution facilities and no Thatcher customers are served through GCEC distribution facilities. Staff further recommends that GCEC file as a compliance item in this docket, a report with Docket Control within 30 days of separation of the subject distribution systems describing actions taken to separate the systems and further declaring that GCEC customers in the affected area are reliably and exclusively served through GCEC facilities.

GALLAGHER & KENNEDY

P.A.
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May 15, 2007

HAND DELIVERED

Docket Control
Arizona Corporation Commission
1200 W. Washington
Phoenix, AZ 85007

Re: *Affidavit of Publication; Graham County Electric Cooperative Application to
Transfer Certain Assets to the Town of Thatcher; Docket No. E-01749A-07-0237*

Dear Sir/Madam:

Enclosed are the original and 13 copies of the Affidavit of Publication in this matter confirming published notice in the Eastern Arizona Courier on May 6, 2007. Your assistance is appreciated.

Very truly yours,

GALLAGHER & KENNEDY, P.A.



By: Michael M. Grant

MMG/plp
10430-12/1558416

Enclosures

Original and 13 copies filed with Docket
Control this 15th day of May, 2007.

G&K

