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BEFORE THE ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission
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COMMISSIONERS

MIKE GLEASON - Chairman
WILLIAM A. MUNDELL
JEFF HATCH-MILLER
KRISTIN K. MAYES
GARY PIERCE

IN THE MATTER OF THE APPLICATION OF SULPHUR SPRINGS VALLEY ELECTRIC COOPERATIVE, INC. FOR AUTHORIZATION TO INCUR DEBT TO FINANCE ITS CLEAN RENEWABLE ENERGY BONDS FOR SCHOOLS PROGRAM AND FOR RELATED APPROVALS.

DOCKET NO. E-01575A-07-0501

DECISION NO. 70097

OPINION AND ORDER

Open Meeting
December 18 and 19, 2007
Phoenix, Arizona

BY THE COMMISSION:

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Having considered the entire record herein and being fully advised in the premises, the Arizona Corporation Commission ("Commission") finds, concludes, and orders that:

FINDINGS OF FACT

1. On August 30, 2007, Sulphur Springs Valley Electric Cooperative, Inc. ("SSVEC" or "Cooperative"), an Arizona class "A" public service corporation and non-profit cooperative, filed an application with the Commission for authorization to incur debt to finance its Clean Renewable Energy Bonds for Schools Program ("CREBS Program") and for related approvals.

2. On September 27, 2007, SSVEC filed an affidavit of publication verifying that it had published the public notice of its financing application in the *Eastern Arizona Courier* on September 9, 2007, in the *Sierra Vista Herald/Bisbee Daily Review* on September 11, 2007, and in the *San Pedro Valley News-Sun* and the *Arizona Range News* on September 12, 2007.

3. On November 16, 2007, the Commission's Utilities Division Staff ("Staff") filed its Staff Report, recommending approval of the application.

4. On November 20, 2007, SSVEC filed a Response to the Staff Report. SSVEC had no comments on the substance of the Staff recommendations, but requested that the Commission consider the application at its regularly scheduled December Open Meeting so that the matter could be approved before the end of the year. The Cooperative states that the contractor's bid to install the photovoltaic shade structures at all public schools in SSVEC's service territory will expire at the end of the year and failure to approve the project by then will require a re-bid of the project and result in higher costs to SSVEC primarily as a result of recent increases in the price of steel. SSVEC states further that because of the inter-relationship between the two dockets, the Commission should consider approval of the Renewable Energy Standard Tariff ("REST Plan" or "RES Tariff") at the same time as the current financing request.

5. SSVEC is an Arizona non-profit, member-owned cooperative that provides electric distribution service to approximately 49,000 customers in parts of Cochise, Santa Cruz, Pima and Graham Counties. The Cooperative's headquarters is in Willcox, Arizona.

6. The Commission approved SSVEC's current rates in Decision No. 58358 (July 23, 1993).

7. SSVEC is seeking Commission authorization to obtain debt financing through an $11.48 million credit facility from the National Rural Utilities Cooperative Finance Corporation ("CFC"). SSVEC also requests authorization from the Commission to pledge, mortgage, lien and/or encumber its assets in connection with the CFC credit facility.

8. The purpose of the financing is to construct photovoltaic ("PV") shade structures at all the public schools in SSVEC's service territory as well as at public colleges and universities. This program is a major part of SSVEC's REST Plan that is currently before the Commission for approval in Docket No. E-01575A-07-0310. In its Response to the Staff Report SSVEC states that the source of revenue for payment of the CREBS Program loan will come directly from SSVEC's proposed REST Tariff which has been incorporated into the REST Plan.

9. The CREBS Program is expected to lower the energy bills of 41 schools. The Program will install a total of 41 systems, each system will produce 23 KW of electricity at peak output. SSVEC will not charge the schools for the electricity produced by the PV systems. The

CREBS Program will provide an educational opportunity for the schools, via a cable connection to a computer in the school library which will show students and faculty how the system is working. SSVEC prepared an economic analysis of the school PV systems; depending upon system outputs and annual energy cost increases, SSVEC's cost recovery analysis estimates that the cost recovery, or payback, for the school PV systems will range from 16.7 to 27.8 years.[1]

10. SSVEC received CFC approval for the Credit Facility on July 6, 2007. The Cooperative estimates an interest rate on the loan of approximately 0.5 percent with a maximum term of 16 years. The CFC loan will be subject to a fee of 150 basis points to cover the legal expenses, placement fees and administrative costs. Under the CFC commitment, the funds may be used for reimbursement of qualified CREBS Program project expenses only.

11. The Commission's Engineering Staff has reviewed the SSVEC CREBS Program and Financing Application and finds that the Program is appropriate to meet a portion of SSVEC's Renewable Energy Standard and Tariff requirements.

12. Staff agrees with SSVEC that the CREBS PV program will benefit all of SSVEC's customers who will provide funding through the RES Tariff. SSVEC's customers are the same parties who provide funding for the local schools by means of local taxes. Staff believes that the school PV program was the result of customer focus groups that clearly showed SSVEC customer support for such a program.

13. Staff finds the costs of the CREBS Program to be reasonable.

14. Staff cautions that its conclusions should not be interpreted to imply a specific treatment for rate base or rate-making purposes in the Cooperative's future rate filings.

15. Staff performed a financial analysis of the effect of the proposed debt. As of year end December 31, 2006, the Cooperative had a capital structure consisting of 3.4 percent short-term debt, 62.4 percent long-term debt and 34.2 percent equity. As of December 31, 2006, the Cooperative had

[1] Under SSVEC's analysis, if annual energy costs increase at a 4 percent rate each year, the SSVEC calculations estimate a 17.8 year payback for a perfect system performance and a 19 year payback if the performance is 80 percent of the perfect peak output. The longest payback calculated by SSVEC is 27.8 years, and assumes annual energy costs do not increase at all. Staff's analysis suggests a payback in the range of 28-30 years based on more conservative assumptions.

a Times interest Earned Ratio ("TIER") of 1.80 and Debt Service Coverage Ratio ("DSC") of 1.56.[2] Based on year end 2006 data, the addition of $6.8 million in previously authorized debt, and the proposed new debt of $11.48 million associated with the CREBS Program, the Cooperative's capital structure would consist of 3.5 percent short-term debt, 66.6 percent long-term debt and 29.9 percent equity, and its TIER would drop to 1.61 and its DSC to 1.49. In Docket No. E-01575A-07-0446, SSVEC requested authority to borrow $70.43 million from the CFC to fund its 2008-2009 Construction Work Plan ("CWP"). Staff performed a pro forma analysis that assumed a $35.03 million draw related to the CWP, and based on a term of 35 years and an interest rate of 7.5 percent, determined that based on December 2006 numbers, the Cooperative's projected 2008 capital structure would consist of 2.94 percent short-term debt, 72.92 long-term debt and 24.14 percent equity; and would have a TIER of 1.26 and DSC of 1.37. Staff's projections indicate that with an additional $35 million draw related to the CWP, in 2009, all else remaining equal, the Cooperative would have a capital structure consisting of 2.6 percent short-term debt, 77.1 percent long-term debt and 20.3 percent equity, a TIER of 0.76 and DSC of 1.06.[3]

16. Staff notes that its pro forma TIER indicates that operating income would become insufficient to cover interest expense in 2009, and would be unsustainable in the long-run. Staff states that the DSC indicates that SSVEC will be able to meet all debt obligations with cash generated from operations. Staff notes further that should the Commission approve the proposed RES Tariff, SSVEC would have incremental revenue to service the loan and have a higher DSC, all else being equal.[4]

17. Staff states further that it typically recommends cooperatives have a minimum equity ratio of 30 percent as being appropriate to balance the cost of debt and financial risk. Staff

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[2] TIER represents the number of times earnings cover interest expense on short-term and long-term debt. A TIER greater than 1.0 means that operating income is greater than interest expense. A TIER less than 1.0 is not sustainable in the long term but does not mean that debt obligations cannot be met in the short run.

DSC represents the number of times internally generated cash will cover required principal and interest payments on short-term and long-term debt. A DSC greater than 1.0 indicates that operating cash flow is sufficient to cover debt obligations. A DSC less than 1.0 means that debt service obligations cannot be met by cash generated from operations and that another source of funds is needed to avoid default.

[3] Staff's pro forma analysis reflects the Cooperative's projected figures at current rates, exclusive of the proposed RES Tariff in Docket No. E-01575A-07-0310.

[4] The Staff Report does not estimate the revenues expected to be collected from the proposed RES Tariff.

recognizes that the inclusion of the $75.46 million in new debt for the 2008-2009 CWP in conjunction with the requested $11.48 million in the current application results in an overly leveraged financial position. Staff states, however that there is no other known immediate option to finance the CWP. Staff also notes that in the long-run, increased rates would provide additional equity. Furthermore, the Cooperative expects the RES Tariff to cover repayment of the CREBS Program debt.

18. Staff states that SSVEC has no compliance issues.

19. Staff concludes that issuance of the proposed debt financing for the purposes stated in the application is within SSVEC's corporate powers, is compatible with the public interest, is consistent with sound financial practices and will not impair SSVEC's ability to provide service.

20. Staff recommends that the Commission authorize SSVEC's request to obtain CREBS Program financing through a credit facility not to exceed $11.48 million from CFC and to pledge, mortgage, lien and/or encumber its assets; that SSVEC be authorized to engage in any transaction and to execute any documents necessary to effectuate the authorizations granted; and that SSVEC file one copy of the executed loan documents with Docket Control within 60 days of execution.

21. We find that Staff's recommendations are reasonable and should be adopted, however, our approval is conditioned on the approval of a RES Tariff that would provide funds for repayment of the loan. At our November 27, 2007, Open Meeting we authorized SSVEC to borrow $70.78 million from the CFC for its 2008-2009 CWP, and we directed SSVEC to file a report of its equity projections if it has not filed a rate case before December 31, 2009, and its equity is less than 23 percent of its total capital. That requirement remains in effect and will allow the Commission to monitor the effect of both loan facilities on the Cooperative's capital structure.

CONCLUSIONS OF LAW

1. SSVEC is a public service corporation within the meaning of Article XV of the Arizona Constitution and A.R.S. §§ 40-301, 40-302, and 40-303 and AAC R14-2-1814.

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

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

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

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

ORDER

IT IS THEREFORE ORDERED that Sulphur Springs Valley Electric Cooperative, Inc. is hereby authorized to borrow up to $11,480,000 of long term debt from the National Rural Utilities Cooperative Finance Corporation at an interest rate not to exceed 1.5 percent, for the purposes set forth in the application and set forth herein, conditioned on the approval of a compatible RES Plan and Tariff that include the CREBS Program.

IT IS FURTHER ORDERED that Sulphur Springs Valley Electric Cooperative, Inc. is authorized to pledge, mortgage, lien and/or encumber its assets in connection with the loan approved herein.

IT IS FURTHER ORDERED that Sulphur Springs Valley Electric Cooperative, Inc. is authorized to engage in any transactions and to execute or cause to be executed any documents or modifications to existing documents to effectuate the authorization granted herein, including notes and bonds evidencing or securing the indebtedness authorized herein.

IT IS FURTHER ORDERED that such finance authority shall be expressly contingent upon Sulphur Springs Valley Electric Cooperative, Inc.'s use of the proceeds for the purposes stated in the application and approved herein.

IT IS FURTHER ORDERED that Sulphur Springs Valley Electric Cooperative, Inc. shall file with Docket Control, as a compliance item in this docket, its executed financing documents within 60 days after the date of execution.

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IT IS FURTHER ORDERED that approval of the financing set forth hereinabove does not constitute or imply approval or disapproval by the Commission of any particular expenditure of the proceeds derived thereby for purposes of establishing just and reasonable rates.

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

BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

CHAIRMAN COMMISSIONER

COMMISSIONER COMMISSIONER COMMISSIONER

IN WITNESS WHEREOF, I, DEAN S. MILLER, Interim Executive Director 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 21st day of Dec., 2007.

DEAN S. MILLER
INTERIM EXECUTIVE DIRECTOR

DISSENT

DISSENT ________________

JR:db

SERVICE LIST FOR: SULPHUR SPRINGS VALLEY ELECTRIC COOPERATIVE, INC.

DOCKET NO.: E-01575A-07-0501

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