

OPEN MEETING ITEM



0000085984

ORIGINAL

COMMISSIONERS
WILLIAM A. MUNDELL
JEFF HATCH-MILLER
KRISTIN K. MAYES
GARY PIERCE



Executive Director

ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission
DOCKETED

DATE: JUNE 17, 2008
DOCKET NO: E-01461A-07-0433
TO ALL PARTIES:

JUN 17 2008

DOCKETED BY *mm*

Enclosed please find the recommendation of Administrative Law Judge Jane Rodda. The recommendation has been filed in the form of an Order on:

TRICO 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 **4:00** p.m. on or before:

JUNE 26, 2008

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:

JULY 1, 2008 and JULY 2, 2008

For more information, you may contact Docket Control at (602)542-3477 or the Hearing Division at (602)542-4250. For information about the Open Meeting, contact the Executive Director's Office at (602) 542-3931.

Brian C. McNeil
BRIAN C. McNEIL
EXECUTIVE DIRECTOR

RECEIVED
2008 JUN 17 P 2:20
AZ CORP COMMISSION
DOCKET CONTROL

1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2 COMMISSIONERS

3 MIKE GLEASON, Chairman
4 WILLIAM A. MUNDELL
5 JEFF HATCH-MILLER
6 KRISTIN K. MAYES
7 GARY PIERCE

8 IN THE MATTER OF THE APPLICATION OF
9 TRICO ELECTRIC COOPERATIVE, INC. AN
10 ARIZONA CORPORATION, FOR AUTHORITY
11 TO BORROW THE ADDITIONAL SUM OF
12 \$58,786,000 FROM THE UNITED STATES OF
13 AMERICA (RDUP) AND THE ADDITIONAL
14 SUM OF \$25,194,000 FROM NATIONAL RURAL
15 UTILITIES COOPERATIVE, AND TO EVIDENCE
16 SAID LOANS BY EXECUTION OF LOAN
17 AGREEMENTS, PROMISSORY NOTES AND
18 SECURITY DOCUMENTS REQUIRED BY THE
19 LENDERS.

DOCKET NO. E-01461A-07-0433

DECISION NO. _____

ORDER

14 Open Meeting
15 July 1 and 2, 2008
16 Phoenix, Arizona

17 **BY THE COMMISSION:**

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

20 * * * * *

FINDINGS OF FACT

21 1. On July 23, 2007, Trico Electric Cooperative, Inc. ("Trico" or "Cooperative"), a non-
22 profit member-owned cooperative, filed an application with the Commission for authorization to
23 borrow \$83.98 million from the United States of America through the Rural Utilities Service
24 ("RUS").¹

25 2. On September 13, 2007, the Commission granted intervention to Local Union 1116,
26 International Brotherhood of Electrical Workers, AFL-CIO ("IBEW Local 1116").

27 _____
28 ¹ Trico originally planned to borrow \$58,786,000 from the RUS and \$25,194,000 from the National Rural Utilities
Cooperative Finance Corporation ("CFC"), but subsequently decided to borrow all the funds from RUS.

1 3. On September 13, 2007, Trico mailed affidavits of publication verifying that it had
2 notice of its financing application published in the *Nogales International* on August 28, 2007 and in
3 the *The Daily Territorial* on August 27, 2007. Both newspapers are papers of general circulation in
4 the areas served by Trico. The affidavits were docketed by Staff on June 4, 2008.

5 4. On May 29, 2008, the Commission's Utilities Division ("Staff") filed its Staff Report
6 recommending conditional approval of the requested financing authority.

7 5. On June 13, 2008, the IBEW Local 1116 filed Comments Regarding the Staff Report,
8 expressing its "strong support for the recommended conditional approval for the financing
9 authorization for the reasons set forth in the Staff's Report dated May 28, 2008."

10 6. As of the date it filed its application, Trico provided electric power distribution service
11 to approximately 37,300 customers in a service area ranging from Mt. Lemmon on the north side of
12 Tucson to areas west and south of Tucson, to Sasabe on the Mexican border. The Cooperative
13 expected 38,400 customers by the end of 2007. Portions of its service territory are rural and sparsely
14 populated, but other areas, including Avra Valley, Sahuarita and Three Points are experiencing rapid
15 growth from new subdivisions.

16 7. Trico has no generating capacity of its own and contracts with the Arizona Electric
17 Power Cooperative, Inc. ("AEPSCO") for the majority of its electric power supply.

18 8. Trico seeks to borrow the funds to finance its construction work plan for the period
19 2008 through 2010 as set forth below:

20

21

<u>Year</u>	<u>Construction Budget</u>
2007	\$20,029,700
2008	22,770,162
2009	24,733,604
2010	21,016,364
Subtotal	\$88,549,830
Less: Other funds	4,569,830

26

27

28

Required Loan**\$83,980,000**

9. Trico states that the construction of additional and supplemental facilities is necessary to provide for expected growth in its service territory and to maintain its plant in sound operating condition.

10. The proposed financing consists of a 35-year amortizing loan that provides for multiple draws over an estimated five year period. The expected interest rate is estimated to be 5.0 percent per year, but the actual interest rate will be based on the market rate at the time of each draw. The anticipated yearly draws are set forth as follows:

<u>Year of Draw</u>	<u>Amount Drawn</u>	<u>Year of Maturity</u>
2008	\$10,500,000	2043
2009	18,000,000	2044
2010	18,000,000	2045
2011	18,000,000	2046
2012	18,000,000	2047
2013	1,480,000	2049
Total	\$83,980,000	

11. The following is a summary of Trico's 2007-2010 Construction Work Plan:

<u>Account Name</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>Total</u>
Member Extns.	\$9,785,563	\$8,433,159	\$9,555,462	\$10,655,328	\$38,429,512
Tie Lines	1,862,000	3,488,610	3,054,331	2,107,871	10,512,812
Upgrades, Rebuilds	3,082,000	4,267,290	2,651,189	2,221,514	12,221,993
New Substations	0	927,000	1,591,350	819,545	3,337,895
Misc. Distrn. Eqp.	5,290,656	5,644,337	4,582,423	5,201,745	20,719,161

1	Other Distribution	9,481	9,766	10,059	10,361	39,667
2	Transmission	0	0	3,288,790	0	3,288,790
3					SubTotal	\$88,549,830
4	General Funds					4,569,830
5	Total Project Cost					\$83,980,000

6
7 The Cooperative's Work Plan includes upgrades and additions of transmission and distribution
8 facilities needed for reliable operation of its system. The Work Plan includes new tie lines and a
9 conversion from overhead lines to underground cable to maintain proper voltage on the system. Staff
10 believes the new transmission lines and new distribution tie lines will enable the Cooperative to meet
11 the projected system load growth in a reliable manner.

12 12. Staff reports that Trico's outage hours per customer varied between 2.16 and 2.25 for
13 the 2003-2007 period, showing an average of 2.21 outage hours per customer per year. Staff states
14 this is well within the RUS guidelines of 5 outage hours per customer per year. In addition, Staff
15 reports that Trico's system losses ranged between 5.29 percent in 2003 and 5.17 percent in 2007,
16 which Staff states are well within the industry guidelines of 10 percent per year for rural electric
17 cooperatives.

18 13. Staff's engineering review of the application indicates that the items included in the
19 list of capital projects are appropriate to meet the load growth and will enable Trico to operate and
20 maintain its electric system in a safe and reliable manner, and that the expenditure amounts
21 associated with the projects appear to be reasonable.

22 14. Staff noted, however, that it is not making a "used and useful" determination as part
23 of its review in this proceeding, but rather treatment of the proposed plant improvements for rate-
24 making purposes will be deferred to a future rate proceeding.

25 15. Based on year ended December 31, 2006, financial information, Staff's analysis
26 indicates that as of December 31, 2006, Trico's capital structure consisted of 1.6 percent short-term
27 debt, 71.9 percent long-term debt and 26.5 percent equity. At that time, the Cooperative's Times
28

1 Interest Earned Ratio ("TIER") and Debt Service Coverage Ratio ("DSC") were 1.49 and 1.62,
2 respectively.²

3 16. Staff states that as of December 31, 2006, Trico had \$24,748,000 of unused debt
4 authorization. Staff's pro forma analysis, to account for the issuance of this unused finance authority,
5 yields a capital structure as of December 31, 2006, consisting of 1.6 percent short-term debt, 75.5
6 percent long-term debt, and 22.9 percent equity. The pro forma TIER and DSC for this scenario are
7 1.20 and 1.35, respectively.

8 17. RUS loan covenants require a 1.25 TIER and a 1.25 DSC in two of the past three
9 years.

10 18. Staff believes that the pro forma ratios indicate that Trico has little capacity to support
11 additional borrowing based on its 2006 operating results.

12 19. Staff's financial analysis further modified 2006 operating results to take account of the
13 current request to issue \$83.98 million in additional debt. Staff's pro forma analysis shows that the
14 additional debt would result in a capital structure comprised of 1.4 percent short-term debt, 83.2
15 percent long-term debt, and 15.4 percent equity, and that the TIER and DSC would fall to 0.71 and
16 0.85, respectively. Staff asserts that these results represent a "stress test" because Trico will not be
17 drawing down the entire amount of the new debt all at once, but plans to draw on the funds over a six
18 year period beginning in 2008.

19 20. In the Staff Report, Staff states that although Trico's own financial analysis shows that
20 the Cooperative will have the ability to meet debt service obligations including the newly proposed
21 debt, its assumptions about future results are unknown. Consequently, Staff does not believe Trico's
22 projections are sufficiently reliable to serve as a basis for unconditionally granting the entire
23

24 ² Times Interest Earned Ratio ("TIER") represents the number of times earnings cover interest expense on short-term and
25 long-term debt. A TIER greater than 1.0 means that operating income is greater than interest expense. A TIER less than
26 1.0 is not sustainable in the long term but does not mean that debt obligations cannot be met in the short term.

27 Debt Service Coverage Ratio ("DSC") represents the number of times internally generated cash will cover required
28 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.

1 requested debt authorization.³

2 21. Staff notes that Trico's 2008 capital improvement projects budget is approximately
3 \$20.8 million. Staff believes that issuance of \$20.8 million of additional debt would provide funds to
4 allow the Cooperative to continue its planned capital improvement projects for another year without
5 interruption. Staff's pro forma analysis taking account of the issuance of \$20.8 million of additional
6 debt results in a capital structure consisting of 1.54 percent short-term debt, 77.82 percent long-term
7 debt and 20.64 percent equity, with a pro forma TIER and DSC of 1.02 and 1.18, respectively, based
8 on year-end 2006 results. Staff states that under this scenario, Trico would have sufficient cash flow
9 to meet all obligations, but would need to improve upon its 2006 operating results to meet the RUS
10 requirement for a 1.25 TIER and a 1.25 DSC. Staff acknowledges that because the TIER and DSC
11 requirements apply to two of the past three years, if the Cooperative falls short of these parameters in
12 any one year, it has an opportunity to pursue corrective measures for compliance in subsequent years.

13 22. Staff concludes that it is in the public interest for Trico to have \$20.8 million of new
14 funding available to finance its 2008 budget for capital improvements. Staff also concludes that any
15 borrowing authorizations granted to Trico in this proceeding beyond that needed to satisfy its
16 budgeted 2008 capital improvement projects should be subject to the condition that a pro forma
17 calculation, using its most recent annual financial report (Form 7) reflecting the additional borrowing,
18 results in a 1.25 DSC and a 1.25 TIER unless the Commission specifically grants an exception. Staff
19 additionally concludes, subject to this condition, that Trico incurring up to \$83.98 million of debt for
20 the purposes proposed in its application is within its corporate powers, is compatible with the public
21 interest, is compatible with sound financial practices, and will not impair its ability to provide public
22 service.

23 23. In Decision No. 66779 (February 13, 2004), the Commission approved a \$25,000,000
24 line of credit expressly for the purpose of providing interim financing for capital improvements until
25 permanent RUS funding becomes available. Decision No. 66779 provided specifically ". . . use of
26 the line of credit authorized herein shall be restricted to obtaining interim financing for future capital
27

28 ³ Staff Report at p 3.

1 improvement projects for which the Commission has authorized long-term financing.”

2 24. Staff is concerned that Trico’s use of the line of credit not result in excess borrowing
3 beyond the Cooperative’s ability to service debt.

4 25. Staff believes that if the capital projects associated with the conditional authorization
5 could be considered capital improvements for which the long-term has been authorized, Trico could
6 use the line of credit to incur more debt than would meet financial restrictions. Consequently, Staff
7 concludes that any debt authority that is conditioned or restricted under this Decision should not be
8 used to qualify for interim financing under the line of credit approved in Decision No. 66779.

9 26. Staff reports that Trico has no outstanding compliance delinquencies.

10 27. Staff recommends the Commission authorize Trico (1) to issue debt in an amount not
11 to exceed \$20.8 million to RUS in the form of a 35-year amortizing loan to fund the Cooperative’s
12 budgeted 2008 capital improvement projects; and (2) to issue debt in an additional amount not to
13 exceed \$63.18 million to RUS in the form of a 35-year amortizing loan to fund other capital projects
14 described in its application subject to the condition that a pro forma calculation using its most recent
15 annual financial report (Form 7) reflecting the additional borrowing results in a 1.25 DSC and a 1.25
16 TIER.⁴

17 28. Staff further recommends that any debt issuance authorization conditionally granted in
18 this proceeding shall not satisfy the line of credit restriction specified in Decision No. 66779 that “. .
19 . use of the line of credit authorized herein shall be restricted to obtaining interim financing for future
20 capital improvement projects for which the Commission has authorized long-term financing” unless
21 the amounts drawn on the line of credit when treated as draws on debt authorizations granted in this
22 proceeding would meet the 1.25 TIER and 1.25 DSC conditions.

23 29. Staff further recommends that any unused debt issuance authorization granted in this
24 proceeding terminate on December 31, 2013.

25 _____
26 ⁴ For purposes of this test, Staff recommends the DSC should be calculated as a fraction with operating margin before
27 fixed obligations, depreciation and amortization, and income tax, if any, in the numerator and interest on short-term and
28 long-term debt plus principal repayments due within 12 months in the denominator, and TIER should be calculated as a
fraction with operating margin before fixed obligations in the numerator and interest on short-term and long-term debt in
the denominator. Calculations are to be based on the most recently filed audited financial statements (Form 1) adjusted to
reflect the interest and principal impact of changes to outstanding debt to the date of the calculation plus the proposed
new debt, where interest and principal repayments are annualized.

1 any documents necessary to effectuate the authorizations granted.

2 IT IS FURTHER ORDERED that Trico Power Cooperative, Inc. shall file with Docket
3 Control, as a compliance item in this docket, copies of any executed financing documents related to
4 this authority within 60 days after the date of execution.

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

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

9 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

10
11
12 CHAIRMAN

COMMISSIONER

13
14 COMMISSIONER

COMMISSIONER

COMMISSIONER

15
16 IN WITNESS WHEREOF, I, BRIAN C. McNEIL, Executive
17 Director of the Arizona Corporation Commission, have
18 hereunto set my hand and caused the official seal of the
19 Commission to be affixed at the Capitol, in the City of Phoenix,
20 this _____ day of _____, 2008.

21 _____
BRIAN C. McNEIL
EXECUTIVE DIRECTOR

22 DISSENT _____

23 DISSENT _____

24 JR:
25
26
27
28

1 SERVICE LIST FOR: TRICO ELECTRIC COOPERATIVE, INC.

2 DOCKET NO.: E-01461A-07-0433

3

4 Russell E. Jones
5 Waterfall, Economidis, Caldwell, Hanshaw
6 & Villamena
7 5210 East Williams Circle, Ste. 800
8 Tucson, Arizona 85711

6

7 Nicholas J. Enoch
8 Lubin & Enoch, PC
9 349 North Fourth Avenue
10 Phoenix, Arizona 85003
11 Attorneys fore EBEW Local 1116

9

10 Janice Alward, Chief Counsel
11 Legal Division
12 ARIZONA CORPORATION COMMISSION
13 1200 West Washington Street
14 Phoenix, Arizona 85007

12

13 Ernest Johnson, Director
14 Utilities Division
15 ARIZONA CORPORATION COMMISSION
16 1200 West Washington Street
17 Phoenix, Arizona 85007

15

16

17

18

19

20

21

22

23

24

25

26

27

28