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MEMORANDUM

To: Utah Public Service Commission
From: Division of Public Utilities
Philip J. Powlick, Director
Artie Powell, Manager, Energy Section
Marlin Barrow, Technical Consultant
Charles Peterson, Technical Consultant
Jocelyn Nance, Intern
Subject: Notice from Garkane Energy, Re: Twin Cities Acquisition Notice. Purchase and Sale Agreement. Docket No. 09-028-03.
Date: May 12, 2009

ISSUE

Garkane Energy Cooperative, Inc. (Garkane, or the Company) requests recognition of its acquisition of Twin Cities electrical distribution system and authorization of the Company's purchase and sale agreement. The Public Service Commission (Commission) issued an action request to the Division of Public Utilities (Division) on April 29, 2009 with a due date of May 13, 2009. This memorandum responds to the Commission's action request

RECOMMENDATION (Approval)

The Division recommends that the Commission recognize Garkane Energy's acquisition of Twin Cities' electrical distribution system, and authorize Garkane Energy's Purchase and Sale agreement.

DISCUSSION

Information used in the Division's analysis included: A letter from Carl Albrecht, CEO of Garkane Energy, to the Commission dated March 3, 2009, the purchase and sales agreement drafted on February 5, 2009 and March 25, 2009 between Hildale City, Utah and Colorado City, Arizona dba Twin City Power (Twin Cities) and the Company, an Arizona Corporation Commission (ACC) Opinion and Order,¹ information given on May 7, 2009 to the Division from Michael Avant, Engineering Manager for Garkane, and a Memorandum of Understanding (MOU) dated December 10, 2008 between Rocky Mountain Power (RMP) and the Company.

On December 19, 2008 Garkane asked the Commission for approval to increase their line of credit from \$2 million to \$5 million (see Docket No. 09-028-01). The stated primary purpose for the increase in the line of credit was to enable Garkane to purchase the Twin Cities distribution and transmission facilities. Garkane expected to quickly pay off this short-term loan with proceeds from the sale of the Twin Cities' transmission line to RMP. During this time the Division performed an analysis of the Company's financial statements and found that Garkane is a stable company with the ability to set its own rates and that is able to take on extra debt to finance this acquisition. The Commission approved the increase to Garkane's line of credit on March 30, 2009.

Garkane owns three hydroelectric plants used to satisfy demand, and four diesel plants that are used in emergencies when there are unexpected peaks in demand. Also Garkane has a stable contract with Deseret Power Electric Cooperative (Deseret) with which it will be able to obtain additional power the company will need to serve the Twin Cities.

According to the ACC, Garkane had originally owned the Twin Cities system along with some rural areas in northern Arizona, but sold the Twin Cities system to Hildale and Colorado City in 1994, with Garkane retaining the rural areas including the areas surrounding Colorado City up to

¹ Arizona Corporation Commission, Docket No. E-01891A-08-0598, April 16, 2009

the present. The cities of Hildale and Colorado City acquired the distribution system in 1994 through the sale of municipal bonds. Recently, the Twin Cities have defaulted on their bonds. The bondholders, represented by Wells Fargo Bank, have asked Garkane if it would be willing to purchase the system. The Company has indicated that part of the purchase and sales agreement was that the Company would receive the system free and clear of any prior liabilities. The Company also has told the Division that it does not see any major maintenance problems within the system, but is setting aside \$100,000 annually for the next five years for minor corrections and replacements the Company has identified.

Garkane has entered into a MOU with Rocky Mountain Power to sell a transmission line that is part of the purchase from the Twin Cities. The transmission line is 69kV and runs from the Twin Cities to Hurricane, Utah. The agreed upon purchase price of the transmission line is \$3 million. This will significantly mitigate the financial risk Garkane is assuming by purchasing the Twin Cities distribution system. As reported in the Division's memo in Docket 09-028-01, the Division's analysis showed that Garkane would still be financially stable even if this sale to RMP does not occur.

Both the Company and the Twin Cities customers should benefit from this sale. New tariff sheets submitted to the ACC by the Company show an average decrease of about 14 percent in customer bills over Twin Cities' tariff sheets. This decrease occurs after a surcharge that Garkane will apply to Twin Cities' customers to account for the higher costs of getting power to the Twin Cities area. According to the Company, Twin Cities' books show that the system has an historical depreciated cost of \$7 million, far above the purchase price of \$3 million. However, given the purchase price, Garkane, in all likelihood, will write down the assets to the purchase price when it transfers them to its books.

The Division has not attempted to evaluate the reasonableness of the terms and conditions of the transaction, although these terms and conditions appear to be ordinary. The Division has relied upon the Company's own analysis and the analysis of the sellers.

The Division bases its recommendation for approval on the following factors:

- A. The Company, which has total access to financial information about its operations and budgets, has conducted an evaluation and concluded that this is the most beneficial option available.
- B. The Commission already approved the financing for this acquisition in Docket 09-028-01.
- C. The Company has a signed MOU with Rocky Mountain Power that will allow the Company to recover the majority of the cost of this acquisition.
- D. Due to prior analysis done in Docket 09-028-01 the Division concludes that the Company is stable and should be able to handle a moderate capital expenditure program as well as the property acquisition of the Twin Cities.

Based upon these considerations, the Division recommends that the Commission recognize and authorize Garkane's Twin Cities Acquisition and Purchase and Sales Agreement.

cc: Carl R. Albrecht, CEO, Garkane Energy Cooperative, Inc.
Michele Beck, Committee of Consumer Services
Cheryl Murray, Committee of Consumer Services