



State of Utah
Department of Commerce
Division of Public Utilities

FRANCINE GIANI
Executive Director

THOMAS BRADY
Deputy Director

CHRIS PARKER
Director, Division of Public Utilities

GARY HERBERT
Governor
SPENCER J. COX
Lieutenant Governor

ACTION REQUEST RESPONSE

To: Utah Public Service Commission
From: Division of Public Utilities
Chris Parker, Director
Artie Powell, Manager, Energy Section
Douglas D. Wheelwright, Technical Consultant
Jeffrey S. Einfeldt, Utility Analyst
Subject: Application of Dixie Escalante Rural Electric Association, Inc. dba Dixie Power for Authority to Issue Securities, Docket No. 16-066-01.
Date: August 15, 2016

RECOMMENDATIONS (Approval)

The Division recommends that the Commission approve the request and authorize Dixie Power to issue securities in the form of a \$20,000,000 long term loan with National Rural Utilities Cooperative Finance Corporation (CFC). This loan is in addition to the currently existing loan with CFC of up to \$13,000,000 (outstanding balance as of 12/31/2015 of approximately \$8,823,000) previously approved by the Commission.

ISSUE

Pursuant to Utah Code Ann. § 54-4-31, Dixie Escalante Rural Electric Association, Inc. dba Dixie Power (Dixie) requests authorization for authority to issue securities in the form of a long-term secured debt obligation. The proposed obligation is a long-term loan agreement with National Rural Utilities Cooperative Finance Corporation (CFC) up to \$20,000,000 primarily to

help finance the construction of new transmission and new distribution infrastructure, buildings and related facilities.

DISCUSSION

Dixie-Escalante Rural Electric Association, Inc. is a non-profit, cooperative association organized January 1, 1978 as a result of a consolidation of Dixie Rural Electric Association and Escalante Valley Electric Association for the purpose of providing electric service to rural areas located in southwestern Utah and northwestern Arizona. Dixie has a contract to purchase power from the Western Area Power Administration. Monthly power needs in excess of this allocation are purchased from Deseret Generation and Transmission (Deseret G&T). Additional power beyond that provided by these two sources would be purchased under a contract with the Intermountain Power Project (IPP).¹

Information used in the Division's analysis included the Company's application, along with the audited annual financial reports for Dixie from 2008 through 2015. The Division has had discussions with Chery Hulet, CFO for Dixie Power, regarding certain details of the application and questions regarding the historical financial statements. The proposed loan was approved by the board of directors by resolution on June 1, 2016. Copies of the resolution and board meeting minutes were included with the original application.

Historical Results

Exhibit 1 is a summary of the audited financial results for 2011 through 2015. The income statement on page 1 indicates that Total Revenue has increased 4.66% annually from \$20.8 million in 2011 to \$26.0 million in 2015. Operating Expenses have grown at a faster rate than revenues, rising from \$20.5 million in 2011 to \$27.4 million in 2015, for a 7.38% annual increase. The cost of purchased power represents 62% of operation expenses for 2015 and experienced an average annual increase of 7.1% from 2011 through 2015. Many of the other operational expenses experienced similar percentage increases. The Company has implemented a rate increase for Utah customers effective February 2016 to offset the increase in operating

¹ Dixie Escalante Rural Electric Association, Inc. audited financial statements, March 27, 2013.

expenses. Utah customers represent approximately 90% of the total usage. A similar increase is scheduled for the Arizona customers and should become effective in October of this year. Due to the late implementation of the rate change, the impact of the Utah rate increase will be reflected in future financial statements. The new rates include a wholesale power cost adjustment provision which will allow Dixie to move rates up or down as wholesale prices change. The addition of the power cost adjustment mechanism should help maintain the gross margin closer to historical levels. In addition to the lower gross margin, Dixie has experienced an increase in the operating and maintenance costs and customer related expenses through 2015. This increase in operating expense is primarily due to increased maintenance for repairs to an aging infrastructure. It is anticipated the Company will continue to incur this higher level of maintenance costs in future years. Customer related expenses have increased due to an increase in new customers.

The balance sheet information on page 2 shows a cash position at the end of 2014 of \$3.3 million and a significant decrease to a balance of \$946 thousand at the end of 2015 due to expenditures on capital improvements to update aging facilities and meet the demand of significant new customer growth. In addition to the infrastructure improvements, the Company is building a new headquarters facility which is utilizing cash and has increased short term borrowing.

Other balance sheet accounts of note are the Net Plant which grew at an annual rate of 4.01% from 2011 through 2015. During this same period, Long Term Debt increased at a rate of 0.55% and Total Patrons Equity increased at 3.13% annual rate from \$21.2 million in 2011 to \$23.5 million in 2015.

Page 4 of Exhibit 1 identifies the financial ratios for 2011 through 2015. The Long-term Solvency ratios in 2015 remain strong and are close to historical averages. The profitability ratios show a decrease in the gross and net margins for 2015 due to the increase in operating costs mentioned above. While the margins are lower, the Company remains profitable and is able to meet its obligations and provide a return of patrons' capital in 3 of the past 5 years. Due to the lower margins, the Company paid no Return on Patrons' Capital in 2015.

The Regulatory Capital Structure calculates Long-Term Debt at 25.37% and Equity at 74.63% as of year-end 2015 which is a slightly higher equity percentage than the 71.86% historical average. Based on the historical information, it appears the Company is generally healthy and has been able to meet its current obligations.

CONCLUSIONS

The Division has not attempted to evaluate the reasonableness of the terms and conditions of financial transaction, however, the terms appear to be in line with current market rates. The recommendation for approval is based on the following factors.

1. The Board of Directors has approved the proposed transaction during the June 1, 2016 meeting.
2. The Company has recently increased customer rates and has the ability to raise future customer rates, if necessary, in order to meet its financial obligations.
3. Based upon the financial statements, it appears that Dixie has been financially stable for the past five years and has been able to meet its financial obligations.

The Division recommends that the Commission approve the Application of Dixie Escalante Rural Electric Association, Inc. for Authority to Issue Securities, Docket No. 16-066-01.

cc: Chery Hulet, CFO - Dixie Power
Dane Johnson, Controller - Dixie Power
Michelle Beck, Office of Consumer Services