

(Decision No. 78921)

BEFORE THE PUBLIC UTILITIES COMMISSION  
OF THE STATE OF COLORADO

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RE: INVESTIGATION AND SUSPENSION OF )	INVESTIGATION AND SUSPENSION
TARIFF SHEETS ACCOMPANYING ADVICE )	DOCKET NO. 687
LETTER NO. 27 FILED BY <u>SAN LUIS</u> )	
<u>VALLEY RURAL ELECTRIC COOPERATIVE,</u> )	RECOMMENDED DECISION OF
<u>INC., MONTE VISTA, COLORADO,</u> )	CHRISTIAN O. IGENBERGS,
PROPOSING TO INCREASE CERTAIN RATES )	EXAMINER
FOR ELECTRIC SERVICE. )	
	GRANTING IN PART TARIFF INCREASES

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October 28, 1971  
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Appearances: William O. DeSouchet, Jr.,  
Esq., Alamosa, Colorado,  
for San Luis Valley Rural  
Electric Cooperative, Inc.;  
Robert E. Commins, Esq.,  
Denver, Colorado, for the  
Staff of the Commission.

PROCEDURE AND RECORD

San Luis Valley Rural Electric Cooperative, Inc. (hereinafter referred to by its corporate name or as Respondent), filed with this Commission on June 11, 1971, Advice Letter No. 27, accompanied by 15 revised tariff sheets, whose purpose was to increase Respondent's electric revenues an estimated \$108,344 per annum, or 15.77% over the like 1970 electric revenues. The proposed increase was to become effective on 30 days' notice or on July 15, 1971.

The Commission assigned Investigation and Suspension Docket No. 687 to the within matter.

By Decision No. 78201, dated July 14, 1971, the Commission, on its own motion, ordered that the aforesaid tariff sheets filed by Respondent accompanying Advice Letter No. 27, dated June 11, 1971, be suspended for 120 days or until November 12, 1971, unless otherwise ordered. By the same Decision, the Commission ordered that a public hearing be held in the within matter on September 21, 1971, in the Courtroom of the District Court, County Courthouse in Alamosa, Colorado at 10 a.m.

Notice of the proposed increase in rates was given by Respondent to its customers on June 12, 1971. Following said notice, five letters were received by the Commission from customers of Respondent protesting the proposed rate increases.

Pursuant to law, the Commission assigned Investigation and Suspension Docket No. 687 to Christian O. Igenbergs, Examiner, for the purpose of conducting the hearing and gave due and proper notice of the hearing to all interested persons, firms, or corporations. The hearing was held at the said time and place.

Respondent's Exhibit No. 1 and Staff Exhibits Nos. 2 through 7, inclusive, were tendered and admitted into evidence.

At the conclusion of the hearing, the subject matter was taken under advisement.

Pursuant to the provisions of Chapter 115, Article 6, Colorado Revised Statutes (1963), as amended, Examiner Christian O. Igenbergs now transmits herewith to the Commission the record and exhibits of this proceeding together with a written recommended decision which contains his findings of fact and conclusions thereon, together with the recommended order or requirement.

#### FINDINGS OF FACT

Based upon all the evidence of record, the following is found as fact that:

1. San Luis Valley Rural Electric Cooperative, Inc., is a public utility as defined in Chapter 115-1-3, Colorado Revised Statutes 1963, as amended, and is engaged in the business of purchasing, acquiring, transmitting, distributing, furnishing, and selling electricity to its customers on its lines in the counties of Hinsdale, Mineral, Rio Grande, Alamosa, Costilla, Conejos, and Saguache, State of Colorado, and it owns and operates certain electric transmission and distribution and related facilities in said counties.

2. The Commission has jurisdiction over Respondent and the subject matter of this proceeding.

3. The proposed rates under investigation herein involve the following rate schedules and estimated average percentage increase proposed for each schedule:

<u>Rate Schedule Designation</u>	<u>Customer Description</u>	<u>Proposed Average Percentage Increase</u>
Schedule A 1- $\phi$	Residence, Small Commercial, Public Buildings, Other Public Authorities	17.35%
Schedule A 1- $\phi$ W.H.	Residence, Small Commercial, Public Buildings, Other Public Authorities with water heater	18.58
Schedule A-3 $\phi$	Residence, Small Commercial, Public Buildings, Other Public Authorities with water heater	27.68
Schedule A	Seasonal (Summer cabins, Cellars, Housing Stock Pumps, Sheep Sheds, etc.)	36.92
Schedule A	Intermittent	23.90
Schedule A-E 1- $\phi$ (all electric)	Residences, Small Commercials, Public Buildings, Other Public Authorities and Seasonal Service	9.40
Schedule A-E 3- $\phi$	Residences, Small Commercials, Public Buildings, Other Public Authorities and Seasonal Service	13.20
Schedule A-E	Seasonal	11.90
Schedule A-H	Space heating service only (separately metered)	6.60
Schedule A-W	Water heating service only (separately metered approved water heating service)	18.80
Schedule L.P.S.	Large Power Service	8 66

4. The proper test year for the determination of revenue requirements for the Respondent in this proceeding is the calendar year 1970.

5. The test year revenues claimed by Respondent to be \$1,234,903 should be adjusted upward by a net amount of \$1,896, representing the difference between over-billing a customer \$522 and failure to bill for fuel cost escalation in an amount of \$2,418, as provided by contracts, resulting in an adjusted operating revenue total of \$1,236,799.

6. The test year expenses claimed by Respondent to be \$1,137,910 should be adjusted upward by \$17,623 representing the

annualization of an in-period wage increase and \$20,407 representing an increase in depreciation accruals during the test year as a result of adopting new service lives for transmission and distribution plant, resulting in an adjusted operating expense total of \$1,175,940. There are no out-of-period adjustments to expenses.

7. Respondent claims that its average rate base for the test year is \$4,224,558 consisting of the following items:

<u>Gross Rate Base</u>	<u>Average for 1970</u>	
Utility Plant In-service Plus Construction	\$6,384,948	
Work in Progress		
Materials and Supplies - Electric	73,873	
Prepayments	3,485	
Working Capital Allowance (A)	<u>66,499</u>	\$6,528,805
<u>Deductions</u>		
Accumulated Depreciation	\$2,203,814	
Contributions in Aid of Construction	97,503	
Consumer Advances for Construction	<u>2,930</u>	
Total Deductions		<u>(2,304,247)</u>
Rate Base		<u>\$4,224,558</u>
(A) Working Capital Computation		
Purchased power 15/365	\$ 41,060	
Other operation and maintenance expenses 45/365	<u>49,397</u>	
Subtotal	\$ 90,457	
Less: 1/2 Annual Property Tax Accrual	<u>(23,958)</u>	
Working capital allowance	<u>\$ 66,499</u>	

The proper average rate base for the test period for Respondent, after giving consideration to in-period adjustments for wage increase annualization and depreciation expense as outlined in Finding No. 6 is, in fact, \$4,226,357, consisting of the following items:

<u>Gross Rate Base</u>	<u>Average for 1970</u>	
Utility Plant In-service Plus Construction	\$6,384,948	
Work in Progress		
Materials and Supplies - Electric	73,873	
Prepayments	3,485	
Working Capital Allowance (A)	<u>68,732</u>	
		\$6,531,038

Deductions From Gross Rate Base

Provisions for depreciation and amortization	2,203,892	
Contributions in aid of construction	97,504	
Customers' advances for construction	<u>3,285</u>	
Total Deductions		<u>2,304,681</u>

Rate Base \$4,226,357

(A) Working Capital Computation

Purchased power 15/365	\$ 41,110
Other operation and maintenance expenses 45/365	<u>51,580</u>
Subtotal	\$ 92,690
Less: 1/2 Annual Property Tax Accrual	<u>(23,958)</u>
Working capital allowance	<u><u>\$ 68,732</u></u>

8. The new rate schedules filed by Respondent applied on an unadjusted basis would increase test year operating revenues by an estimated \$108,344 from \$1,234,903 to a total \$1,343,247 and net operating revenues from \$76,740 to a total of \$185,084. The \$185,084 net operating revenues would provide a return of 4.4% on the Respondent's stated average rate base of \$4,224,558.

9. A fair rate of return for a rural electric cooperative, such as Respondent, using the same or similar method of financing, at this time is within a range of 3.4% to 5.6%. The rate schedules proposed by Staff, and admitted into evidence as Exhibit No. 7 will increase test year operating revenues of Respondent by an estimated sum of \$110,099, or from adjusted revenues of \$1,236,799 to a total of \$1,346,898 and the net operating revenues from \$71,642 to a total of \$181,741. Net operating revenues of \$181,741 provide a rate of return of 4.3% on Respondent's adjusted average rate base of \$4,226,357. The rate of return of 4.3% when applied to the adjusted rate base of Respondent is found to be a fair rate of return to said Respondent, providing sums adequate to pay interest on

Respondent's debt and additional sums to build up a more appropriate equity capital position. The aforesaid increase of \$110,099 is therefore found to be just and reasonable.

10. The distribution of the proposed increase among Respondent's customer classifications is shown in detail on Staff Exhibit No. 6 and the proposed rate schedules reflecting such increase are contained in Staff Exhibit No. 7. The distribution of the increase among customer classifications is hereby found to be just, reasonable, and not unjustly discriminatory.

Respondent's presently existing rate schedules listed below are found to be just and reasonable and completely adequate at present rate levels and are therefore not in any need of revision at this time.

<u>Rate Schedule Designation</u>	<u>Customer Description</u>
Schedule A-E 3- $\phi$	Residences, Small Commercials, Public Buildings, Other Public Authorities and Seasonal Service
Schedule A-E	Seasonal
Schedule Y-L	Yard Lights
Schedule L. P-A	Large Power Service

Respondent has not proposed an increase in rates for sales under Rate Schedule I-Irrigation. The Staff study shows that an equitable distribution of fixed and variable costs to this customer classification for the test year resulted in costs which exceeded revenues. An increase in rates under the aforesaid Schedule I, extended to yield additional revenues in the amount of approximately \$26,450, or an increase of 5.5% in existing rates would remedy and equalize the situation and such increase is therefore found to be just and reasonable.

11. The rates proposed by Respondent are hereby found to be unjustly discriminatory.

#### DISCUSSION

Respondent is in urgent need of substantial sums of money for system expansion, renewal, and replacement, and the U.S. Rural Electrification Administration, the Respondent's lender, states that such sums

may be made available only if Respondent's earnings are improved. There can be no doubt that an increase in rates is needed, and it is the considered opinion of the Examiner that this can be best and most equitably accomplished by the increase authorized in the Order, infra.

At the same time, it is also the opinion of the Examiner that since any increase in rates producing a given rate of return on an established rate base is closely associated with the cost of capital and therefore the capital structure of the utility concerned, it behooves us to consider Commission policy with regard to the capital structure of rural electric cooperatives in the State of Colorado and in particular the ratio or relationship between equity and long-term debt, making appropriate suggestions as to any possible changes in such policy if the factual situation should so warrant.

In the Union Rural Electric Association, Inc., Decision No. 71084, this Commission discussed capitalization at some length and expressed the opinion that a desirable equity position ranged from a minimum of 20% to 30% or more. It was stated further that refunding of patronage margins should be accomplished in not less than ten years nor more than 15 years. In March of 1968, the date when the decision issued, this position was entirely reasonable in light of the then current equity positions of many Colorado rural electric cooperatives, their past financial history, and the short-term outlook for additional financing.

Since that time, certain changes have taken place and will be taking place in future years concerning the capitalization and financing of rural electric cooperatives. Of particular importance, in this respect, is the formation of the Cooperative Finance Corporation (CFC) by the cooperatives nationwide to provide supplemental capital to the REA's. Since all of the long-term funds loaned to electric cooperatives no longer will be supplied by the Rural Electrification Administration, the equity portion of each cooperative's capitalization becomes increasingly important. The Rural Electrification Administration has set 40%

as a desirable level for net worth which it feels will provide an indicator of financial stability to the investors in CFC.

The Examiner is in agreement with the goal set forth by the Rural Electrification Administration and therefore considers that henceforth a target of 30% to 45% equity position for Colorado rural electric cooperatives is desirable in view of the changing financing situation emerging for the said cooperatives.

In light of the foregoing, let us now consider the Respondent's capital structure.

Respondent, as of December 31, 1970, the end of the test year in this case, had a membership equity of \$1,115,345 and long-term debt of \$3,711,556, for a total capitalization of \$4,826,901. Thus, equity constitutes 23.11% of total capitalization and debt constitutes 76.89% of the total capitalization.

As stated above, it is the opinion of the Examiner that a 30% to 45% equity position is desirable. At the same time, the Examiner's position with regard to the retention of patronage capital is in accord with the Union case discussed above and thereby remains at 10 to 15 years.

It is easily seen from the evidence presented that Applicant's rate of return of 1.70% for the test year barely covers the composite cost of debt and contributes only .69% as a return on equity as shown below:

		<u>% of Capital</u>	<u>% Rate</u>	<u>Composite Cost %</u>
Equity	\$1,115,345	23.11	.69	.16
Debt	<u>3,711,556</u>	<u>76.89</u>	2.00	<u>1.54</u>
	\$4,826,901	100.00		1.70

This clearly would not provide for the building of equity and the revolving of patronage capital.

To provide funds that would maintain a 30% equity position and a retention of patronage capital for a 15-year period, the following rate of return is required:



	<u>% of Capital</u>	<u>% Rate</u>	<u>Composite Cost %</u>
Equity	30	6.67	2.00
Debt	<u>70</u>	2.00	<u>1.40</u>
	100.00	Rate of Return	<u>3.40</u>

Likewise a 45% equity ratio with a 10 year retention of patronage capital would require a rate of return of 5.60%, determined as follows:

	<u>% of Capital</u>	<u>% Rate</u>	<u>Composite Cost %</u>
Equity	45	10.00	4.50
Debt	<u>55</u>	2.00	<u>1.10</u>
	100.00	Rate of Return	<u>5.60</u>

3.40-5.60

Respondent, of course, has only a 23.11% equity ratio, so to build up to at least a 30% equity ratio, a rate of return in excess of 3.40% is reasonable. It also would appear reasonable, therefore, for Respondent to have a rate of return of between 3.40% and 5.60% to eventually achieve an equity ratio of between 30% and 45%.

Respondent has asked for revenues that would produce a 4.40% rate of return. In the cost of service study prepared by the Staff of the Commission, it was shown that an equitable arrangement of the proposed rates will produce a 4.30% rate of return which appears to be just and reasonable. In addition, the 4.30% is approximately midway between the 3.40% and 5.60% rates of return deemed to be necessary for an orderly growth of equity for the Respondent and it will also provide for the revolving of patronage capital within the 10 to 15 year period prescribed by this Commission.

#### CONCLUSIONS ON FINDINGS OF FACT

Based on the aforesaid findings of fact, it is concluded that:

1. Respondent should be granted a rate increase as hereinafter set forth.
2. Pursuant to 115-6-9 (2), CRS 1963, as amended, it is recommended by the Examiner that the Commission enter the following Order.

O R D E R

THE COMMISSION ORDERS THAT:

1. The proposed new tariffs accompanying its Advice Letter No. 27 dated June 11, 1971, of the San Luis Valley Rural Electric Cooperative, Inc., be, and hereby are, permanently suspended, canceled, and not permitted to become effective.

2. San Luis Valley Rural Electric Cooperative, Inc., Monte Vista, Colorado, be, and hereby is, authorized to file with the Commission the following tariff revisions which are estimated to provide the following percentage revenue increases:

<u>Rate Schedule Designation</u>	<u>Customer Description</u>	<u>Average Percentage Increase</u>
Schedule A 1-ø	Residence, Small Commercial, Public Buildings, Other Public Authorities	15.00%
Schedule A 1-ø W.H.	Residence, Small Commercial, Public Buildings, Other Public Authorities with water heater	10.20
Schedule A-3ø	Residence, Small Commercial, Public Buildings, Other Public Authorities with water heater	15.50
Schedule A	Seasonal (Summer cabins, Cellars, Housing Stock Pumps, Sheep Sheds, etc.)	26.30
Schedule A	Intermittent	31.60
Schedule A-E 1-ø (all electric)	Residences, Small Commercials, Public Buildings, Other Public Authorities and Seasonal Service	1.30
Schedule A-H	Space heating service only (separately metered)	1.80
Schedule A-W	Water heating service only (separately metered approved water heating service)	28.10
Schedule I	Irrigation service	5.50
Schedule L.P.S.	Large Power Service	8.30

3. The new tariffs listed above, to conform to the provisions of this Order, may be filed to become effective on or upon one (1) day's notice in accordance with 115-3-4 (1), CRS 1963, as amended.

4. This Order is subject to such orders and regulations as may be promulgated by the President of the United States, or his Delegate, pursuant to Title II of Public Law 91-379, August 15, 1970, 84 Stat. 799, as amended (generally known as the Economic Stabilization Act of 1970, 12 U.S.C. 1904, footnote).

5. The Commission retains jurisdiction herein to make such further order or orders as it may deem to be necessary.

6. This Recommended Decision shall be effective on the day it becomes the Decision of the Commission, if such be the case, and is entered as of the date hereinabove set out.

7. As provided by 115-6-9 (2), CRS 1963, as amended, copies of this Recommended Decision shall be served upon the parties, who may file exceptions thereto; but if no exceptions are filed within twenty (20) days after service upon the parties or within such extended period of time as the Commission may authorize in writing (copies of any such extension to be served upon the parties), or unless such decision is stayed within such time by the Commission upon its own motion, such Recommended Decision shall become the Decision of the Commission and subject to the provisions of 115-6-14, CRS 1963, as amended.

( S E A L )



THE PUBLIC UTILITIES COMMISSION  
OF THE STATE OF COLORADO

CHRISTIAN O. IGENBERGS

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Examiner  
hbp

ATTEST: A TRUE COPY

*Harry A. Galligan, Jr.*

Harry A. Galligan, Jr., Secretary