COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

EAST KENTUCKY POWER COOPERATIVE, INC. APPLICATION FOR APPROVAL OF THE ISSUANCE OF UP TO $200,000,000 OF SECURED PRIVATE PLACEMENT DEBT, FOR THE AMENDMENT AND EXTENSION OF AN UNSECURED REVOLVING CREDIT AGREEMENT IN AN AMOUNT UP TO $500,000,000, AND FOR THE USE OF INTEREST-RATE MANAGEMENT INSTRUMENTS	)	CASE NO. 2013-00306

ORDER

On August 6, 2013, East Kentucky Power Cooperative, Inc. ("EKPC") filed its application for approval of the issuance of up to $200 million of secured private placement debt, for the amendment and extension of an unsecured revolving credit agreement[1] ("Credit Facility") in an amount up to $500 million[2] and for the use of interest-rate management instruments pursuant to KRS 278.300, 807 KAR 5:001, Sections (4), (7), (14), and (17) and other applicable law.[3] On August 19, 2013, EKPC filed a motion to supplement the application with an executed EKPC Board Resolution, dated August 13, 2013, in which the Board approved the authorization to amend and extend the Credit Facility. By letter dated August 23, 2013, the Commission notified

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[1] Case No. 2011-00204, Application of East Kentucky Power Cooperative, Inc. for Approval of an Unsecured Revolving Credit Agreement for a Term of Up to Five Years and in an Amount Up to $500,000,000 (Ky. PSC July 19, 2011).

[2] The Credit Facility had $275 million drawn down at the time of EKPC's application.

[3] Application, cover letter.

EKPC that all filing requirements were satisfied and the application was considered filed as of August 6, 2013.

PROPOSED INDEBTEDNESS

Issuance of up to $200 million of Secured Private Placement Debt

EKPC intends to use the proceeds from the secured private placement debt to reduce the outstanding balance of its Credit Facility; to redeem early or at maturity certain long-term debt if market conditions are favorable; and to fund estimated future capital expenditures related to its electric generation and transmission business; for such additional expenditures as contemplated by KRS 278.300; or for other lawful corporate purposes.[4]

The Credit Facility is currently being used to provide temporary financing for construction projects, approved regulatory assets,[5] and general corporate purposes until permanent financing can be obtained.[6] EKPC stated that many of these projects can and will be funded through the U. S. Department of Agriculture's Rural Utilities Service ("RUS"); however, some projects, regulatory assets, and funds spent for general corporate purposes cannot be financed through the RUS. EKPC states that Commission approval of the proposed secured private placement debt is necessary to

[4] Application, Exhibit 3.

[5] EKPC has a balance in the Smith 1 regulatory asset account of $150,221,471 as of August 28, 2013, but expects to finance an amount between $90 million and $120 million, after the sale of certain Smith 1 assets, over an approximate term of 10 years. *See* Case No. 2010-00449, Application of East Kentucky Power Cooperative, Inc. for an Order Approving the Establishment of a Regulatory Asset For the Amount Expended on its Smith 1 Generating Unit (Ky. PSC Feb. 28, 2011). Also *see* Exhibit 6 of the application and the response to Item 1.c.(1) of Commission Staff's Initial Request for Information ("Staff's Initial Request"), filed on Aug. 29, 2013.

[6] Application, paragraph 3.

avoid carrying a permanent balance in the Credit Facility.[7] EKPC considers this inappropriate, since the Credit Facility is short term in nature and subject to variable interest rates; therefore, it wishes to use long-term fixed financing to more appropriately finance these activities and relieve the Credit Facility so that it remains available for its intended purpose.[8] EKPC also stated that, due to the increasing level of uncertainty involved in funding available through the RUS, the possibility of additional required environmental facilities, and the current favorable financing environment, it desires to include some additional amount in the private placement to allow for the financing of future capital projects related to production, transmission and environmental improvements.[9]

EKPC seeks regulatory authority from the Commission to issue, in one or more transactions over a period ending December 31, 2014, up to $200 million of secured private placement indebtedness and to enter into all necessary agreements relating thereto. In the original resolution by the Board of Directors, EKPC was authorized to enter into the private placement financing agreement, consisting of tranches having terms of up to 30 years, in a total amount not to exceed $150 million, except that in the case that more favorable than expected pricing is achieved, at the discretion of EKPC's Chief Executive Officer, the private placement issuance may be upsized to an amount not to exceed $200 million.[10]

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[7] *Id.*

[8] *Id.*

[9] *Id.*

[10] Application, Exhibit 6, page 2.

The proposed private placement debt will be issued under an Indenture of Mortgage, Security Agreement and Financing Statement dated October 11, 2012, between EKPC and the U.S. Bank National Association, as Trustee, which was approved by the Commission in Case No. 2012-00249,[11] with a secured indebtedness up to and including $5 billion.[12] As of June 30, 2013, EKPC's total long term debt was $2,558,479,241.[13]

EKPC stated the private placement debt will be sold by auction, through underwriters or agents, or by direct placement with commercial banks or institutional investors through a Dutch auction-type process.[14] EKPC seeks authority to issue the debt at a time or times when it believes it is prudent to do so, subject to any parameters ordered by the Commission, if such financing is approved. EKPC has received estimates of indicative pricing from financial institutions and investors in anticipation of a private placement financing. EKPC anticipates the interest rate will be fixed and the rate of interest on the debt will not exceed by more than 3 percent the yield to maturity of United States Treasury Bonds of comparable maturity at the time of issuance.[15] EKPC also stated that it may agree to specific redemption provisions, if any, at the time of the issuance of the debt.[16]

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[11] Case No. 2012-00249, Application of East Kentucky Power Cooperative, Inc. for Approval to Obtain a Trust Indenture (Ky. PSC Aug. 9, 2012).

[12] Application, paragraph 12.

[13] Application, Exhibit 5, page 9.

[14] Application, Exhibit 2, page 1 and Response to Item 1.(e) of Staff's Initial Request.

[15] *Id.*, page 1.

[16] *Id.*, page 2.

EKPC stated it is not able to determine at this time, whether it would be more advantageous to issue its debt with long-term or some shorter term maturities. EKPC stated it expects to issue debt in tranches having maturities of between 10 and 30 years, but believes it should be allowed the necessary flexibility to adjust its financing programs to developments in the markets for medium- and long-term debt securities when and as they occur in order to obtain the best possible price, interest rate, and terms for its debt, but that no series of debt will have a maturity date exceeding 30 years.[17] In response to an information request from Commission Staff, EKPC stated that because many private placement investors desire average life maturities in the seven- to 15-year range, the pricing is more favorable for such average lives. EKPC will most likely attempt to place the tranche related to the regulatory asset in this range, resulting in a possible final maturity of slightly greater than ten years, but with a lesser average maturity.[18] EKPC requests the Commission allow it to decide at a subsequent date whether there will be more than one series and the maturity of each series of the debt.

Amendment and Extension of Revolving Credit Agreement

EKPC wishes to amend and extend its Credit Facility in order to reduce the interest cost, to extend the maturity from the current date of August 9, 2016 to a date five years from the new closing date, and to allow for the possibility of increasing the total commitment from $450 million to $500 million.[19] EKPC stated that because of the

[17] Application, Exhibit 2, pages 1 and 2.

[18] Response to Item 1.c.(3) of Staff's Initial Request.

[19] Application, Exhibit 2, page 2.

delay regarding the timing of loan advances for the multiple projects funded by RUS, the Credit Facility is essential to maintaining its liquidity.[20]

Due to favorable market conditions, EKPC believes it is advantageous to enter into a five-year arrangement at this time and that financial institutions are open to lending to it under more favorable terms.[21] EKPC will have to pay amendment fees and expenses associated with the proposed changes to the Credit Facility, but it expects they will not exceed 0.2 percent of the Credit Facility commitment.[22] Based on the current outstanding balance of the Credit Facility, EKPC estimates that potential daily savings of approximately $2,000 is possible and net savings over the life of the Credit Facility are expected to be at least $1.5 million, if its request is approved by the Commission.[23]

The National Rural Utilities Cooperative Finance Corporation ("CFC") will continue to be the Lead Arranger and Administrative Agent for the Credit Facility. CFC and the remaining syndicate of lenders have provided EKPC a $450 million Credit Facility and this may be increased by up to $50 million on or prior to the closing, if approved by the Commission. If its application is approved by the Commission, EKPC expects the financial closing date to be in the fall of 2013.

As of June 30, 2013, EKPC had approximately $1,150,000 in deferred financing fees outstanding from its 2011 Credit Facility. It proposes to amortize this outstanding

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[20] *Id.*, page 3.

[21] *Id.*

[22] Application, Exhibit 2, page 4.

[23] *Id.*, pages 3 and 4.

balance, and the new amendment fees and expenses, over the life of the new Credit Facility.

The Use of Interest-Rate Management Instruments

EKPC desires to utilize interest-rate management techniques and to enter into interest-management agreements in an effort to control its overall effective interest costs. In connection with the issuance and management of its debt, EKPC requests authority to enter into, over a period ending December 31, 2014, one or more interest-rate management agreements. The interest-rate management agreements will utilize products currently used in today's capital markets, consisting of interest rate swaps, caps, collars, floors, options, or hedging products such as forwards or futures, or similar products, to manage interest costs. EKPC expects to enter into these agreements with counterparties that are highly rated financial institutions.

EKPC stated that the net fees and expenses in connection with any interest-rate management agreement will be in addition to the costs formerly identified and will not exceed 5 percent of the amount of the underlying obligation involved.[24] EKPC also stated that in the event it enters into an interest-rate management agreement, a copy of any such agreement will be provided to the Commission within 30 days of its execution.[25]

EKPC maintains that since market opportunities for these interest-rate management alternatives are transitory, it requests authority to execute interest-rate management transactions when the opportunity arises to obtain the most competitive

[24] *Id.*, page 5.

[25] *Id.*

pricing.[26] Thus, EKPC seeks approval to enter into the described transactions within the parameters discussed prior to the time it reaches agreements with respect to the terms of such transactions. It maintains that the financial authority requested in its application is consistent with the proper performance of its services to the public, will not impair its ability to perform those services, and is reasonably necessary and appropriate for such purposes.

There are no intervenors in this case. EKPC responded to one request for information from Commission Staff. The matter now stands submitted for a decision based on the evidentiary record.

DISCUSSION

The Commission is well aware of the difficulties associated with RUS financing. In Case No. 2012-00249, the Commission approved EKPC's request to replace its existing RUS mortgage covering most of its property with a trust indenture. Use of the trust indenture allows EKPC greater flexibility to obtain financing from sources other than RUS due in part to RUS's lending and guaranty authority being subject to an annual appropriations process. However, EKPC intends to continue to use RUS financing for certain projects. In Case No. 2013-00259,[27] EKPC has requested Commission approval of a RUS-guaranteed loan to finance an alteration to its environmental controls at its Cooper Station generating facility.

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[26] *Id.*, page 6.

[27] Case No. 2013-00259, Application of East Kentucky Power Cooperative, Inc. for a Certificate of Public Convenience and Necessity for Alteration of Certain Equipment at the Cooper Station and Approval of a Compliance Plan Amendment for Environmental Surcharge Recovery, filed Aug. 21, 2013, paragraph 24.

In Case No. 2012-00192,[28] the Commission approved the request of Nolin Rural Electric Corporation ("Nolin") to refinance 100 percent of its existing RUS debt with $50 million in new CFC debt. Nolin's request was premised on recent and ongoing difficulties with RUS's loan process and the stringent, and inflexible, requirements associated therewith.

EKPC entered into its existing Credit Facility in August 2011.[29] It states that since that time, credit markets have improved somewhat. In addition, EKPC's financial results reflect improvement, and it has obtained an investment-grade credit rating of "BBB" from both Fitch Ratings and Standard and Poor's.[30] Standard and Poor's revised its outlook on EKPC to "Positive" from "Stable" in March 2013.[31]

The improvements in the credit markets, combined with the view that EKPC is less risky today than it was just over two years ago, have allowed it to negotiate more favorable pricing terms for both the proposed secured private placement debt and the amended and extended Credit Facility. The Commission commends EKPC for taking advantage of the financing alternatives available to it, thereby securing savings for itself, its member-owners and their retail consumers.

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[28] Case No. 2012-00192, Application of Nolin Rural Electric Cooperative Corporation for an Order Pursuant to KRS 278.300 and 807 KAR 5:011, Section 11 and Related Sections, Authorizing the Cooperative to Obtain a loan in the Amount of $50,000,000 from the National Rural Utilities Cooperative Financing Corporation (Ky. PSC June 22, 2012).

[29] Application, Exhibit 2, page 3.

[30] *Id.*, page 2.

[31] *Id.*

Given the foregoing, the Commission is persuaded that the proposed secured private placement debt, the amendment and extension of the Credit Facility and the use of interest-rate management instruments will be in the best interests of EKPC, its member distribution cooperatives, and their retail member ratepayers. The Commission will want to monitor EKPC's progress with the secured private placement debt and the use of interest-rate management instruments and will, therefore, require that EKPC provide the Commission with information related thereto.

FINDINGS

The Commission, after consideration of the evidence of record and being sufficiently advised, finds that:

1. The issuance of up to $200 million in secured private placement debt is for lawful objects within the corporate purposes of EKPC, is necessary and appropriate for and consistent with the proper performance by the utility of its service to the public, will not impair its ability to perform that service, is reasonable, necessary, and appropriate for such purposes, and should be approved.

2. Approval of the proposed amendments and extension to the Credit Facility in an amount up to $500 million for a term up to five years is for lawful objects within the corporate purposes of EKPC's utility operations, is necessary and appropriate for and consistent with the proper performance by the utility of its service to the public, will not impair its ability to perform that service, is reasonable, necessary, and appropriate for such purposes, and should be approved.

3. EKPC's proposal to amortize the June 30, 2013 balance in deferred financing fees of $1,150,000 outstanding from its 2011 Credit Facility, and the new

amendment fees and expenses, over the life of the new Credit Facility is reasonable and should be approved.

4. EKPC's proposal to use interest-rate management instruments to reduce interest cost is reasonable and should be approved.

5. The proceeds from the proposed secured private placement debt should be used only for the lawful purposes set out in EKPC's application.

6. The proceeds resulting from the proposed amendments and extension of the Credit Facility should be used only for the lawful purposes set out in EKPC's application.

7. The terms and conditions of the secured private placement financing should be consistent with the terms and conditions described in EKPC's application.

8. The terms and conditions of proposed amendments and extension of the Credit Facility should be consistent with the terms and conditions described in EKPC's application.

IT IS THEREFORE ORDERED that:

1. EKPC's request to issue up to $200 million in secured private placement debt in one or more transactions over a period ending December 31, 2014 is approved.

2. EKPC's request for the amendment and extension of its Credit Facility for up to $500 million for five years from the date of closing is approved.

3. EKPC's proposal to amortize the balance in deferred financing fees and the new amendment fees and expenses over the life of the new Credit Facility is approved.

4. EKPC's proposal to use interest-rate management instruments is approved.

5. The proceeds from the proposed secured private placement debt shall be used only for the lawful purposes set out in EKPC application.

6. The proceeds resulting from the proposed amendments and extension of the Credit Facility shall be used only for the lawful purposes set out in EKPC's application.

7. The terms and conditions of the secured private placement financing shall be consistent with the terms and conditions described in EKPC's application.

8. The terms and conditions of proposed amendments and extension of the Credit Facility shall be consistent with the terms and conditions described in EKPC's application.

9. EKPC shall, within 30 days of the issuance, file with Commission a statement setting forth the date or dates of issuance of the evidences of indebtedness or use of interest-rate management instrument authorized herein, the proceeds of such issuances, the interest rate(s), the maturity date(s), all fees and expenses involved in the issuances of these evidences of indebtedness or use of interest-rate management instruments.

10. Any document filed pursuant to ordering paragraph 9 of this Order shall reference the number of this case and shall be retained in the utility's general correspondence file.

Nothing contained herein shall be deemed a warranty or finding of value of securities or financing authorized herein on the part of the Commonwealth of Kentucky or any agency thereof.

By the Commission

ENTERED
SEP 2 7 2013
KENTUCKY PUBLIC
SERVICE COMMISSION

ATTEST:

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Case No. 2013-00306

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