

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF GREEN RIVER ELECTRIC)	
CORPORATION AND HENDERSON UNION)	
ELECTRIC CORPORATION FOR APPROVAL OF)	CASE NO. 97-156
CONSOLIDATION)	

ORDER

On March 28, 1997, Green River Electric Corporation ("Green River") and Henderson Union Electric Corporation ("Henderson Union") filed a joint application pursuant to KRS 278.020(4) and (5) for approval of their proposed merger and consolidation into a new utility to be named Kenergy Corporation ("Kenergy"). Green River and Henderson Union are nonprofit electric cooperatives, organized under KRS Chapter 279 and engaged in the retail distribution of electric power to member-consumers in western Kentucky. Green River serves approximately 29,000 customers in eight counties and Henderson-Union serves approximately 18,000 customers in seven counties.

Full intervention was granted to NSA, Inc. and Alcan Aluminum Corporation, the largest industrial customers of Green River and Henderson Union, respectively. A public hearing in this matter was held at the Commission's offices on May 19, 1997. Mr. Richard L. Liggett, a member-consumer of Henderson Union, offered public comments regarding the proposed consolidation.

BACKGROUND

The subject of consolidation was first raised in 1993 in a Commission sponsored management audit of Green River and Henderson Union. The audit was performed for the Commission by F.E. Jennings and Co. ("Jennings"), an independent management

consulting firm. Jennings issued a comprehensive audit report in June 1993 that recommended further studies be performed to explore the feasibility of consolidating the entire Big Rivers Electric Corporation ("Big Rivers") system.¹ Although two members of the Big Rivers system declined to participate in any discussions of consolidation, Green River and Henderson Union agreed to such discussions and eventually procured a formal feasibility study.²

A preliminary study was performed at no cost to the utilities by the National Rural Electric Cooperative Association ("NRECA") and the National Rural Utilities Cooperative Finance Corporation. This preliminary study, presented at a joint meeting of the Green River and Henderson Union Board of Directors, recommended further in-depth analysis. This presentation became Phase I of a five phase consolidation process. Eventually, Green River and Henderson Union engaged NRECA to perform a detailed study of the proposed consolidation.

The detailed NRECA Consolidation Study ("Consolidation Study"), completed in October 1996, reviewed virtually every element related to a consolidation of Green River and Henderson Union. The Consolidation Study consists of NRECA's extensive findings and recommendations relating to the proposed consolidation, in addition to an analysis of the economic benefits. An economic model prescribed by the Rural Utility Services of the Department of Agriculture was used to develop a base case financial forecast for use in

¹ The Big Rivers' system consists of four distribution cooperatives: Green River; Henderson Union; Jackson Purchase Electric Cooperative Corporation; and Meade County Rural Electric Cooperative Corporation.

² Application, page 2.

determining the economic benefits of the proposed consolidation.³ The Consolidation Study includes three scenarios relating to the economic benefits of the consolidation. Scenario 1 reflects the immediate impact of consolidation from year one to year 10 of the forecast period and would result in a savings of \$20.5 million. Scenario 2 reflects a phase-in period of 5 years to full realization and results in a savings of \$16.3 million. Scenario 3 reflects a phase-in period of 10 years to full realization and results in a savings of \$11.6 million.⁴

DISCUSSION

Based upon a review of the record, the Commission finds that the proposed consolidation should provide significant long term benefits to the member-consumers of Green River and Henderson Union. The Commission is convinced that the positive financial impact and economies of scale achievable through consolidation will allow Green River and Henderson Union to best serve their member-consumers in the future. The evidence conclusively demonstrates that the consolidated organization, Kenergy, will have the financial, technical and managerial abilities to provide reasonable service to its member-consumers. Kenergy should be able to provide electric service at a total cost that is lower than otherwise achievable without a consolidation.

The record also demonstrates that Green River and Henderson Union have developed a reasonable plan to consummate the consolidation. It is apparent, however, that all issues have not been finalized. The Commission views this consolidation effort as

³ Slater prefiled testimony, pages 8 and 9.

⁴ NRECA Consolidation Study, pages 74 through 78.

a "work in progress." For example, Green River and Henderson Union are committed to effectuate the consolidation without terminating any employees.⁵ Consequently, since a substantial portion of the economic benefits of consolidation are from reduced staffing levels, it will take five to seven years to realize the full potential savings. Similarly, there are numerous organizational and personnel decisions having long term economic implications that must await resolution by Kenergy and its Board of Directors. While many of these issues were identified in the Consolidation Study, there will likely be others that arise as Kenergy begins serving its member-consumers.

The Commission further finds that it has an obligation to monitor the progress of this consolidation and the decisions made by Kenergy on the numerous outstanding issues which will impact the cost and delivery of electric service. In addition, although Green River and Henderson Union have decided that the Kenergy Board of Directors should consist of 13 members, the Commission notes that the Consolidation Study recommended 10 members and the majority of cooperatives under our jurisdiction have fewer than 10. Thus, this issue warrants further review and study by the Kenergy Board of Directors. The Commission also recognizes that, in the near-term, Kenergy may be in a position to adopt technological innovations that are feasible and cost effective. Such measures also warrant serious consideration if cost effective.

To facilitate the Commission's monitoring of this consolidation and the outstanding issues enumerated in the Consolidation Study and this Order, Green River and Henderson Union should file periodic reports describing their progress on these issues and in achieving

⁵ West pre-filed testimony, page 2.

the benefits of the consolidation. The first such progress report should be submitted one year after the consolidation has been consummated. The need for and the timing of subsequent progress reports will be determined after review and analysis of the first report.

The Commission believes that Green River and Henderson Union should be commended for their actions in seriously considering a consolidation and then pursuing it once the benefits became apparent. In summary, we find this consolidation to be in accordance with the law, for a proper purpose, and consistent with the public interest. We encourage Green River and Henderson Union to complete the consolidation in the most practical, efficient and cost-effective manner.

The Commission notes that two other electric distribution cooperatives have recently announced their intent to consolidate. This action is not surprising considering the relatively large number of such utilities under our jurisdiction, their relatively rural service territories, and their relatively small customer bases. The Commission urges electric cooperatives to consider consolidations and other forms of strategic alliances that will achieve economic benefits and enhance the economies of scale necessary to continue to provide high quality service at reasonable costs to your member-consumers.

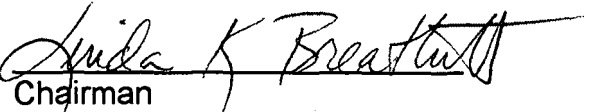
IT IS THEREFORE ORDERED that:

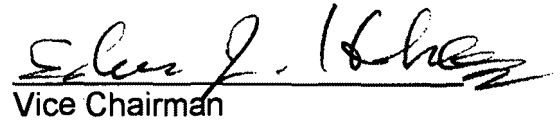
1. The consolidation of Green River and Henderson Union into a new electric distribution cooperative to be known as Kenergy be and it hereby is approved.
2. Within five days after consummation of the consolidation, Kenergy shall file a written notice with the Commission setting forth the date of consolidation.
3. Twelve months after the consolidation Kenergy shall file a report detailing the progress in achieving the benefits of consolidation, the status of all unresolved issues

discussed in the Consolidation Report, the issue of the size of Kenergy's Board of Directors, and an analysis of additional technological improvements.

Done at Frankfort, Kentucky, this 27th day of May, 1997.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:


Executive Director