COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF NOLIN RURAL ELECTRIC COOPERATIVE CORPORATION TO ADJUST THE PAYOUT OF CAPITAL CREDITS IN ACCORDANCE WITH THE COMMISSION'S ORDER OF AUGUST 17, 1995 IN CASE NO. 94-402	)	CASE NO. 2000-482

O R D E R

In Case Nos. 90-064[1] and 94-402,[2] the most recent general rate cases for Nolin Rural Electric Cooperative Corporation ("Nolin"), settlement agreements were approved which required Nolin to use all margins in excess of a 1.50X Times Interest Earned Ratio ("TIER")[3] to rotate capital credits to its members. In its November 1, 1999 Order in Case No. 99-259,[4] the Commission noted the changes in Nolin's financial condition since the establishment of the first settlement agreement, and suggested that Nolin reevaluate the current settlement agreement and seek modification of the provisions for capital credit rotation if necessary. On March 30, 2001, Nolin submitted for filing an

[1] Case No. 90-064, The Notice of Nolin Rural Electric Cooperative Corporation's Revision to its Electric Tariffs.

[2] Case No. 94-402, Application of Nolin Rural Electric Cooperative Corporation Concerning Existing Rates.

[3] The TIER level is exclusive of generation and transmission capital credits ("GTCCs"). Unless otherwise noted, TIER and the equity to capitalization ratio are expressed as excluding GTCCs.

[4] Case No. 99-259, The Application of the Nolin Rural Electric Cooperative Corporation for an Order Pursuant to KRS 278.300 and 807 KAR 5:001, Section 11 and Related Sections Authorizing the Cooperative to Obtain a Loan in the Amount of $4,300,000.00 from the National Rural Utilities Cooperative Finance Corporation.

application seeking authority to modify that portion of the current settlement agreement requiring the rotation of capital credits.

Nolin's application was filed pursuant to the general rate application requirements of 807 KAR 5:001, Section 10; however, Nolin sought no changes in its existing rates for service to members. Nolin cured deficiencies that were identified in the application, and the application was considered filed on May 22, 2001. The Attorney General of the Commonwealth of Kentucky ("AG") has intervened in this proceeding. In its June 11, 2001 Order, the Commission afforded the AG the opportunity to either conduct discovery on Nolin's application or to file comments by June 26, 2001; otherwise, the case would be submitted for a final decision. The AG has neither issued a request for information nor filed written comments on Nolin's filing.

Nolin states that the settlement agreements' goal of reducing its excessive equity to capitalization ratio has been achieved. Nolin notes that in recent years it has had severe cash flow problems, which have made it difficult to comply with the capital credit rotation requirements contained in the settlement agreements. In addition, Nolin has developed an equity management plan that should allow it to avoid a repeat of the financial situation experienced in 1990. For calendar year 1990, when the settlement agreement in Case No. 90-064 took effect, Nolin earned a 3.33X TIER and its equity to capitalization ratio was at 55.95 percent.[5] For calendar year 2000, Nolin showed it earned a 1.41X TIER and its equity to capitalization ratio was 32.86 percent.[6]

[5] Adkins Direct Testimony, Application Exhibit G, at 5.

[6] Id. at 6.

During the time the settlement agreements have been in force, Nolin's equity to capitalization ratio and TIER have both declined to more reasonable levels. However, Nolin's cash flow problems have negatively impacted its ability to make the capital credit retirements required under the settlement agreements. These problems in turn have caused Nolin on several occasions to request this Commission to grant deviations and delays in making the required capital credit retirement to members. The shortage of cash funds to make required retirements of capital credits under the settlement agreement resulted in Nolin filing Case No. 99-259. In that proceeding, Nolin sought authorization to incur long-term debt of $4.3 million to pay capital credit retirements required by the settlement agreement covering 4 calendar years.[7] The issuance of long-term debt coupled with the rotation of capital credits over the past 10 years has had a positive impact on Nolin's equity and has assisted in moving its TIER to a more reasonable level.

The Commission finds that, under the current circumstances, it is reasonable to eliminate the requirement that all margins in excess of a 1.50X TIER be used to retire capital credits to members. Although it is eliminating this provision of the settlement agreements, the Commission reminds Nolin that it still has the obligation to retire capital credits to its members when it is financially able to do so. Nolin has adopted an equity management plan that provides a target range of 1.50X TIER to 2.00X TIER and an equity to capitalization ratio target range of 30 percent to 40 percent. The adopted equity management plan also commits Nolin to make annual payments of capital credits when certain financial conditions are met. The Commission notes that for calendar year

[7] Case No. 99-259, final Order dated November 1, 1999, at 1.

2000, Nolin's TIER was near the target range, while its equity to capitalization ratio was within the target range. In order for the Commission to monitor Nolin's performance under its equity management plan, Nolin should supplement its annual report to the Commission. This supplement should include a schedule of the amount of capital credits paid out during the calendar year and a statement indicating whether the payout achieves the goals of Nolin's equity management plan.

In conjunction with the development of its equity management plan, Nolin prepared extensive modeling analyses and financial forecasts.[8] At a minimum, Nolin will need to periodically prepare financial forecasts to monitor its equity management plan. The preparation of a periodic financial forecast should assist Nolin from repeating the financial condition that existed at the time the first settlement agreement was adopted. The Commission finds that Nolin should prepare such financial forecasts annually and in a timely manner. Nolin should retain the most recent 3 years of annual financial forecasts and make these forecasts available for Commission review upon request.

IT IS THEREFORE ORDERED that:

1. Nolin's request to eliminate the requirement in the settlement agreements adopted in Case Nos. 90-064 and 94-402 to use all margins in excess of 1.50X TIER to retire capital credits to members is approved.

2. Nolin shall supplement its annual report to the Commission with a schedule indicating the amount of capital credits paid out during the reporting year.

[8] Application Exhibit F.

Nolin shall also include a statement indicating whether the calendar year's payout achieves the goals of its equity management plan.

3. Nolin shall prepare a financial forecast annually and in a timely manner to monitor its equity management plan. The annual financial forecasts shall be retained by Nolin for 3 years and made available for review by the Commission if requested.

Done at Frankfort, Kentucky, this 2nd day of August, 2001.

By the Commission

ATTEST:

Thomas M. Dorman

Executive Director