

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

AUTHORIZATION UNDER KRS 278.300 OF	)	
FLEMING-MASON ENERGY COOPERATIVE	)	
CORPORATION OF APPROVAL OF	)	CASE NO.
GUARANTEE OF REVOLVING LINE OF	)	2002-00291
CREDIT FOR FLEMING-MASON SERVICE	)	
CORPORATION	)	

O R D E R

On November 6, 2002,<sup>1</sup> Fleming-Mason Cooperative Corporation (“Fleming-Mason”) filed an application seeking Commission approval allowing it to guarantee a line of credit loan between its subsidiary, Fleming-Mason Service Corporation<sup>2</sup> (“Service Corp.”), and the National Cooperative Services Corporation (“NCSC”). Under the terms of the line of credit, Service Corp. can borrow up to \$750,000 for a term of 60 months. On July 1, 1999, Fleming-Mason’s Board of Directors authorized its President and General Manager to execute an unconditional guaranty of all amounts due under the line of credit between NCSC and Service Corp. On July 1, 1999, Fleming-Mason signed documents providing NCSC with the unconditional guaranty.<sup>3</sup>

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<sup>1</sup> Fleming-Mason originally filed its application on July 29, 2002. The Commission found the application had numerous deficiencies and rejected the filing by letter on August 22, 2002. Fleming-Mason submitted information to cure the deficiencies on September 6, 2002 and November 6, 2002. After providing additional information, Fleming-Mason’s application was accepted and declared filed on November 6, 2002.

<sup>2</sup> Service Corp. is a wholly owned subsidiary of Fleming-Mason that primarily provides wireless broadband services.

<sup>3</sup> Service Corp. signed the line of credit agreement with NCSC on July 1, 1999. See Application, Attachments, Security Agreement dated July 1, 1999.

Since securing the line of credit, Service Corp. has borrowed \$743,041 from NCSC. During Fleming-Mason's last general rate case,<sup>4</sup> the Commission found that Fleming-Mason's guarantee of the line of credit for Service Corp. was not in compliance with the provisions of KRS 278.300(1).

KRS 278.300(1) states:

No utility shall issue any securities or evidences of indebtedness, or assume any obligation or liability in respect to the securities or evidences of indebtedness of any other person until it has been authorized so to do by order of the commission.

Furthermore, KRS 278.300(3) states:

The commission shall not approve any issue or assumption unless, after investigation of the purposes and uses of the proposed issue and the proceeds thereof, or of the proposed assumption of obligation or liability, the commission finds that the issue or assumption is for some lawful object within the corporate purposes of the utility, is necessary or appropriate for or consistent with the proper performance by the utility of its service to the public and will not impair its ability to perform that service, and is reasonably necessary and appropriate for such purpose.

Requiring this prior approval by the Commission ensures that ratepayers will not be obligated to bear the cost of any financings or guarantees that are not necessary, appropriate, or consistent with the utility's provision of service to the public and will not impair the utility's ability to perform that service. Prior to filing this application, Fleming-Mason had neither sought nor been granted approval to be the guarantor of the NCSC line of credit.

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<sup>4</sup> Case No. 2001-00244, Adjustment of Rates of Fleming-Mason Energy Cooperative Corporation, final Order dated August 7, 2002.

The Commission has in two previous cases considered requests by electric cooperatives to approve a guarantee of a loan between a third party and a lending institution.<sup>5</sup> In Case No. 1999-00412,<sup>6</sup> Grayson Rural Electric Cooperative Corporation (“Grayson”) sought approval to guarantee the financing by local banks of geothermal heat pump systems and Electric Thermal Storage units purchased and installed in members’ homes. The Commission approved Grayson’s loan guarantee program, determining that the equipment constituted viable demand-side management alternatives and that it was appropriate for an electric utility to encourage demand reductions through the use of such technologies. The Commission further found that bank loans were made only to members who met the bank’s credit standards and that Grayson had taken reasonable precautions to limit its potential exposure in the event of a member’s default on the equipment loans.<sup>7</sup>

In Case No. 2001-00188,<sup>8</sup> Jackson Energy Cooperative Corporation (“Jackson Energy”) sought approval to guarantee a line of credit between its subsidiary, Jackson Service Plus, Inc. (“Service Plus”), and NCSC. Service Plus signed the line of credit with NCSC in August 1998, which permitted Service Plus to borrow up to \$1,000,000 for

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<sup>5</sup> The Commission notes that, in all three cases, the failure to seek prior Commission approval of the loan guarantee was discovered during the processing of the cooperatives’ last general rate case.

<sup>6</sup> Case No. 1999-00412, Application for the Assumption of Securities by Grayson Rural Electric Cooperative Corporation.

<sup>7</sup> Case No. 1999-00412, March 22, 2000 Order at 3-4.

<sup>8</sup> Case No. 2001-00188, Application for Authority for Jackson Energy Cooperative Corporation to Guarantee a Line of Credit for Jackson Service Plus, Inc. with National Cooperative Services Corporation.

60 months. Service Plus borrowed \$937,750 under the NCSC line of credit and in turn loaned \$855,000 to Jackson Energy Services Corp. (“JE Services”), which used those funds to support its propane venture.<sup>9</sup> At the time the application was filed in Case No. 2001-00188, JE Services had not repaid any of the funds borrowed from Service Plus and consequently Service Plus had not repaid NCSC.

The Commission denied Jackson Energy’s request for authority to guarantee its subsidiary’s line of credit. The Commission stated,

Unlike Grayson, Jackson Energy has not demonstrated that the guarantee of the line of credit for a non-regulated propane business is necessary or appropriate for or consistent with the proper performance of its provision of electric service to its members, will not impair its ability to perform that service, and is reasonably necessary and appropriate for such purpose. Jackson Energy has not shown that Service Plus qualified for the line of credit absent Jackson Energy’s guarantee nor taken precautions to limit its potential exposure in the event of a default by Service Plus. The risk of default is compounded by the financial condition of JE Services and the likelihood that JE Services will fail to repay Service Plus.<sup>10</sup>

The situation presented by Fleming-Mason in this case is essentially the same as the circumstances in the Jackson Energy proceeding. Fleming-Mason has guaranteed a line of credit to its wholly owned non-regulated subsidiary. Fleming-Mason is at risk under the guarantee because Service Corp. has not repaid any of the line of credit from NCSC. Furthermore, based on the information provided in this record, Service Corp. does not have funds available to repay NCSC.

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<sup>9</sup> Service Plus is a wholly owned subsidiary of Jackson Energy that primarily provides home security systems, home monitoring systems, and tree trimming services. JE Services is jointly owned by Jackson Energy and East Kentucky Power Cooperative, Inc.

<sup>10</sup> Case No. 2001-00188, March 28, 2002 Order at 5-6.

The Commission has considered the evidence presented and finds that Fleming-Mason's request for authority to guarantee its subsidiary's line of credit should be denied. Like Jackson Energy, Fleming-Mason has not demonstrated that the guarantee of the line of credit for a non-regulated wireless broadband business is necessary or appropriate for or consistent with the proper performance of its provision of electric service to its members, will not impair its ability to perform that service, and is reasonably necessary and appropriate for such purpose. Fleming-Mason has not shown that Service Corp. qualified for the line of credit absent Fleming-Mason's guarantee. Furthermore, Fleming-Mason has not shown that it has taken precautions to limit its potential exposure in the event of a default by Service Corp.

In the August 7, 2002 Order in Case No. 2001-00244, the Commission expressed its concerns about the ability of Service Corp. to continue as a going concern and the impact a possible failure would have on Fleming-Mason's financial condition. We encouraged Fleming-Mason to review the situation concerning Service Corp. and, if conditions warranted, to consider the divestiture of the wireless broadband operations. Nothing in the record in this case has lessened our concerns, and we again encourage Fleming-Mason to review this situation.

The Commission acknowledges that the distribution cooperatives in Kentucky are evaluating and/or participating in numerous non-regulated business ventures. Generally, this is a new area of activity for these cooperatives. Numerous questions will likely arise concerning the relationship between the regulated cooperatives and these non-regulated activities. The Commission and its Staff are available to work with the regulated distribution cooperatives in seeking answers to these questions.

IT IS THEREFORE ORDERED that Fleming-Mason's request for authorization to guarantee the line of credit between Service Corp. and NCSC is denied.

Done at Frankfort, Kentucky, this 21<sup>st</sup> day of January, 2004.

By the Commission

ATTEST:

  
Executive Director