

“This decision was not made lightly . . .”

Circumstances drive rate increase

By Andrea Blowers

Like any business, Basin Electric has its ups and downs. And, like other businesses, the cooperative does its best to minimize the extremes of those ups and downs.



“We’re impacted by outside forces, both positive and negative. Some we can control, others we can’t. We can control internal costs, but we continue to be adversely impacted by new environmental and industry regulations. We respond and adjust accordingly, and appreciate when things are going well,” says Ron Harper, Basin Electric CEO and general manager.

But, when the negative events get out of hand, the cooperative is forced to make decisions far less ideal than planned. Most recently, that includes an intra-year rate increase. At their July board meeting, following some difficult discussions both internally and with the membership, Basin Electric’s directors approved a wholesale electric rate increase of an average 5 mills to Class A members.

“This decision was not made lightly; it was emotional and it was tough,” Harper says. “However, the covenants of our loan agreements with the Rural Utilities Service require us to generate certain levels of margins. We were projecting we would be approximately \$25 million below those levels.”

Just four short years ago – 2007 – business conditions were different for Basin Electric and its membership. The economy was strong; natural gas prices were holding above \$6 allowing Basin Electric to pay patronage to the membership dividended from the cooperative’s Dakota Gasification Company; Basin Electric was readily able to sell surplus power on the market; and the cooperative’s construction program was in full swing, building for the forecasted growth of its membership.

Fast-forward four years. The economy is limping along following its collapse in 2008; gas prices are hovering around \$4; the cooperative’s construction cycle is coming to a close; member growth continues, but slower in many areas than previously forecast; and impacts of record-setting water levels from snow and rain fall have slowed thermal generation demand, and hindered federal hydropower scheduling and operations. Read “The Power of Water” from the July-August issue of Basin Today: <http://bit.ly/PowerOfWater>.



Paul Sukut, Basin Electric CFO and senior vice president of Finance, says what’s going on right now is more or less a perfect storm.

“We’re coming out of a construction period. Typically, when you come out of a period like that, costs are higher because interest and depreciation on newly

constructed facilities starts being calculated in rates,” Sukut

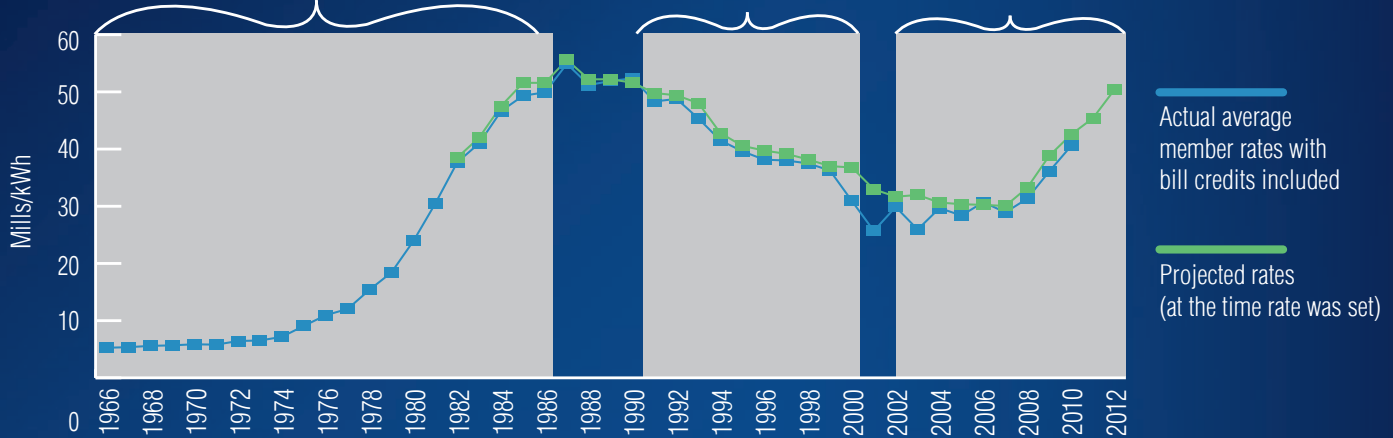
2nd Construction Program

Wyoming Distributed Generation – 2002
 Wisdom Unit 2 – 2004
 Groton 1 & 2 and Culbertson – 2006, 2008 & 2011
 PrairieWinds ND 1 & SD 1 – 2009 & 2011
 Dry Fork Station – 2011
 Deer Creek Station – 2012

Construction Program

LOS Units 1 & 2 – 1966 & 1975
 Spirit Mound Station – 1978
 LRS Units 1, 2 & 3 – 1980, 1981 & 1982
 AVS Units 1 & 2 – 1984 & 1986

Debt refinancing
 Extended depreciation
 of baseload facilities
 Increased surplus
 power prices



says. “At the same time, we’re struggling to sell surplus power in the market because of east-side market limitations. On top of that, the excess water in the Missouri River system. The greatest impact in the short-term has really been the water,” Sukut says.

And, there’s the economy. “We’re trying to come out of a balance sheet recession,” he says. “A classic recession is cyclical, more consumer-driven. What we have has been a balance sheet recession, meaning people’s largest assets, like their homes, went down in value and the debt they had against those assets was too high. It takes much longer to fix that problem.

“It’s really the convergence of all these events happening at once that has brought us to this point,” he says.

Sukut says Basin Electric has not had to consider an intra-year rate increase since 1979. “When we recognized in the first quarter of the year the rates set would not be sufficient, it was important to Ron and the board to ensure the membership was kept in the loop from the beginning.”

Harper and Sukut set up meetings with each Class A member to communicate that a rate increase may need to be considered before January 2012. The two sat down with board members and managers from mid-January to mid-April and explained the issue.

“We received a lot of questions and tried to answer them all,” Sukut says. “We first laid out the problem and then explained that because of our indenture and loan contract with the Rural Utilities

Service, we’re required to meet a certain margin level. Higher margins also have the added benefit of building equity. To the extent our equity reaches certain levels, we will be able to resume distribution of patronage capital back to our membership.”

Harper says the membership has been engaged in the process and has provided feedback. “They said if an intra-year rate increase was necessary, they generally had two requirements. First, they asked that we do it once and work to hold it throughout 2012. The other was to do it as late in the year as possible,” Harper says. “We wanted to take a systematic approach to it, because we understand how this will impact the person at the end of the line. We wanted to monitor how things would play out as the year progressed and take action when we needed to.”

In calculating the rate and the time line, Sukut says, the financial team developed the financial forecast for the following year, just like they do each year. “We went ahead and solved for what we thought we needed in the 2012 rate increase, and determined that could be used to solve for 2011 as well,” he says. “To produce adequate revenue for the year, we calculated the increase would need to be implemented in October.” The wholesale rate increase will be effective Oct. 1, 2011, for 2011-2012.

The membership has basically been supportive, Harper says. “I know rate increases are not easy. The membership owns Basin Electric and they understand to keep it financially strong, the increase is necessary.”