

Pressure of politics

Access to RUS funds **shrinks** with budget cuts, moratoriums

By Julie Slag

Politics – rural electric cooperatives were born in it. Then and now, our survival depends on winning political battles in Washington, D.C.

The battle is always the same: stop those who seek to curtail or shrink funding for power projects in the rural electric program. Tactics usually require delivery of a reality check and an economics lesson with a simple message: Don't shoot the banker.

For decades, cooperatives have been advocates for keeping the Rural Utilities Service (RUS) program in Washington, D.C., viable and funded. Formerly the Rural Electrification Administration (REA), RUS has been rural electric cooperatives' banker since 1935.



Buzz Hudgins

“It is one of the most successful government programs ever put in place,” says Buzz Hudgins, Basin Electric's chief financial officer and senior vice president of Financial Services. “It achieved its initial goal: electrifying much of rural America with affordable power through REA (now RUS) low-cost financing. The RUS Electric Program

continues to play a vital role in maintaining electric infrastructure and reliability, which, in turn, promotes economic growth and sustainability in rural communities.”

However, the RUS Electric Program is being threatened by budget cuts and expanded moratoriums. Such changes could change the way Basin Electric and RUS work together in the future.

A historic partnership

Generation and transmission (G&T) and distribution rural electric cooperatives depend on federal funding of low-interest loans as primary sources of capital for construction and maintenance projects. Recent RUS moratoriums eliminated funding of fossil-fuel based generation projects, which had a direct impact on many G&Ts. But it wasn't always this way.

The history between Basin Electric and RUS is long-standing and successful. Hudgins says it's a



partnership that has existed for almost 50 years through loan guarantees and financing of major construction and operations projects at Basin Electric's generation and transmission facilities.



Steve Johnson

Hudgins and Steve Johnson, Basin Electric manager of treasury services, say the RUS continues to play a role in providing low-cost financing for construction projects and facility upgrades.

“The RUS has been tremendously supportive of not only Basin Electric, but the entire rural electric cooperative program,” Hudgins says. “The federal government,

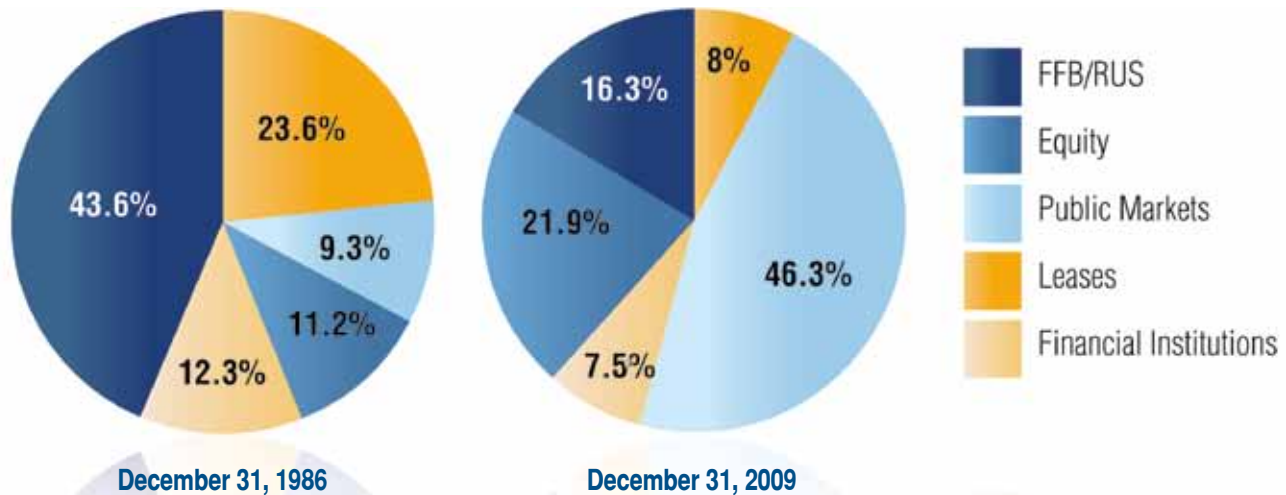
with very few exceptions, has never lost money on the loans to the rural electric program. RUS has been very

successful in providing low-cost financing for us and affordable power for rural America. We need this program to continue.”

\$3.357 billion - Total dollars advanced by REA/RUS to Basin Electric since inception of Basin Electric.

Source: RUS

Basin Electric's Consolidated Capitalization



These charts indicate the change in Basin Electric's capital structure. Two things are especially noteworthy: 1) the growth in Basin Electric's equity, which has contributed to strong bond ratings and, in turn, lower borrowing costs; 2) a shift in borrowing from the RUS to the public and private placement markets. Some of this is due to a commercial paper program used for interim construction financing, and some is due to RUS' inability to lend for coal-based generation.

Both Hudgins and Johnson emphasize how expensive it is to maintain the rural electric program, not just financing at the G&T level. Johnson says Basin Electric member systems are experiencing significant growth such as oil and gas development. "They will need additional transmission build-out, enlargement of substations, and enhanced reliability," he says. "If RUS availability were to be curtailed, distribution cooperatives would need other, more expensive financing."

The recent Good Friday blizzard damage done to Mor-Gran-Sou Electric, Capital Electric and Roughrider Electric transmission and related facilities in North Dakota is a good case-in-point, Johnson and Hudgins say. "If some form of government assistance didn't exist and provide some degree of help, distribution

cooperatives would be turning to the RUS or other more expensive financing to rebuild," Johnson says.

"There are very few cash registers per distribution mile compared to an investor-owned or a municipal utility," Hudgins says. "The program is valuable because it's the primary financing resource for power development in rural areas. RUS is helping make energy affordable in the rural areas of our country."

Hudgins says Basin Electric remains in strong financial condition because of some very good foresight on the part of the Basin Electric board of directors, and this fact is reflected in our excellent bond ratings. "If we were to lose RUS funding, Basin Electric could continue to finance capital projects as dictated by the demand requirements of our Basin Electric family, but not at the low cost we've been able to get from the Rural Utilities Service."

\$915.85 million - Total dollars outstanding in loan applications in 2010.

Source: RUS

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Troubling pressure



Mike Eggl, Basin Electric senior vice president of External Relations and Communications, talks about the impacts of widening the RUS moratoriums on loans for generation:

"The ongoing pressure on RUS is deeply troubling. First, through a combination of legislative and executive decisions, we saw RUS's ability to lend to baseload facilities struck.

"Now, we see that same effort being made in relation to all forms of generation that emit carbon dioxide. This would eliminate any potential for even natural gas development. Not even the strictest climate change bills proposed would eliminate the use of natural gas, and no other entity is being held to this type of standard.

"We believe strongly that both the baseload and the natural gas prohibitions should be eliminated. While it's clear the baseload issue will be much more difficult to change, there is hope the prohibition on natural gas development can be amended. Unfortunately, this fight comes at a time when the administration will be faced with large deficits and programs such as RUS will come under even more pressure."

Johnson says over the past couple years, Basin Electric has submitted several loan applications to the RUS, of which \$807.5 million in funds have been approved.

Another approximately \$1 billion in loan guarantee applications have been submitted to RUS for the Deer Creek Station and the PrairieWinds ND 1 and PrairieWinds SD 1 projects. These applications are awaiting action by RUS, Johnson says.

Hudgins hopes to get RUS approval for the Deer Creek Station project near White, SD, this year. “We applied for funds for the Deer Creek Station some 12 months ago, when we heard RUS may be prohibited from lending for natural gas generation in the future. That piece of the moratorium will not take place this fiscal year. Steve (Johnson) and his team have been working very hard to get that loan application completed.”

Johnson says there is about a one-percent differential between RUS interest and current public market

rates. “Take \$405 million for the Deer Creek Station and apply that one-percent differential – that’s \$4 million in interest expense in the early years that we would save our members by going through RUS and not the capital markets,” he says.

Johnson noted Basin Electric’s for-profit subsidiary, Dakota Gasification Company, is not eligible for RUS

funding, but not because it’s a for-profit corporation. He says any entity that wanted help to electrify rural America was eligible

for funding, including for-profit investor-owned utilities.

“If the purpose of the funds was for rural electrification, you got the money. Eligibility for funding begins with the program’s definition of ‘rural America.’ It’s a defined term based on size and population. Dakota Gas isn’t serving rural America; it’s delivering gas into urban areas, not electricity,

so it’s not eligible for RUS funding,” Johnson says.

Basin-RUS relationship benefits the membership

The bottom line: There would be upward pressure on Basin Electric’s mill rate if it weren’t able to get low-interest financing from RUS, Hudgins says.

Hudgins says Basin Electric has good rapport with RUS. “We have what I consider to be a very special relationship. We work closely with their staff, and we’ve never had a significant problem with them. We find them to be a team of professionals dedicated to their mission. Basin Electric has about a billion dollars in RUS loan applications pending right now, and we have every confidence that we will be able to get those applications approved.”

Johnson says millions of dollars for member systems at the retail electricity level are saved whenever Basin Electric can get relatively low interest rates on money it borrows. “Wholesale power

“Basin has deliberately kept itself strong to be able to access the capital markets. However, RUS is a source of financing we very much do not want to lose.”

Buzz Hudgins, Basin Electric



May 10, 1962: REA Administrator Norman Clapp (seated) signs papers for a \$36.6-million loan to construct the Leland Olds Station Unit 1, Basin Electric’s first power plant.



June 24, 1963: Ground is broken for the Leland Olds Station. (From left) REA Administrator Norman Clapp; Mary (Maud) Olds; Assistant Secretary of the Interior Ken Holum, and John Olds. Mary and John Olds were relatives of economist Leland Olds, former chairman of the Federal Power Commission and advocate for federal support of rural electrification.

costs tend to be a distribution cooperative's largest expense; if these costs can be held down, this helps keep retail rates affordable."

"We view RUS as a banker whose function is similar to other financial relationships Basin Electric has," Hudgins says. Basin Electric's Financial Services staff travel once a year to Washington, D.C., to give RUS staff the same presentation they give to Wall Street rating agencies, banks and lending institutions.

Hudgins says the most significant thing RUS has done for Basin Electric was through the efforts of Wally Beyer, former RUS administrator. "Wally assisted Basin Electric in getting a standard corporate utility indenture in place," Hudgins says. "We were the second G&T to have a standard utility indenture – it has made a big difference for us."

An indenture significantly removes a lot of RUS oversight and control and specifies the circumstances and conditions of when and how Basin Electric issues debt. Basin Electric received approval for their indenture on Jan. 1, 1998. "Several other G&Ts are struggling to get this," he says.

Johnson says RUS staff work in less-than-ideal conditions due to both cuts in staff and funding. "That impacts their workload, as well as having to weather political moves to reduce or eliminate the program. They have a small staff for the amount of work they need to do."

"We like RUS and we work very well with their people," Hudgins says. "We intend to keep this special relationship with them. That's one factor that helps us source low-interest rate financing for the benefit of our membership."

RUS under siege

Hudgins offers a personal perspective. "Ever since I came here to Basin Electric 24 years ago, I have seen attack after attack on the RUS program. When I first got here, Harold Hunter was put in place by Richard Nixon with the express purpose of killing the RUS. That didn't happen.

"But, we continue to see attacks on the program. Fortunately, through our lobbyists (Basin Electric's government relations staff) and the strong political strength of our combined member systems, we've been able to influence and push back these attempts to kill the RUS program."

Recent events in Washington are also troubling, Hudgins says. The administration's Fiscal Year 2011 budget decreases the RUS loan authority to \$4.1 billion from \$6.5 billion in 2010. More troubling is that the budget limits loan funds to renewable energy (only wind and photovoltaic), transmission, distribution, and carbon capture projects on generation facilities. "This means, in addition to halting all RUS lending for baseload nuclear and coal facilities, lending for gas-fired facilities is being eliminated as well," he says. Coal-based and nuclear generation are considered baseload generation.

Johnson says, "It would be unfortunate if the administration extends the moratorium to include natural gas generation, which would effectively limit us to loans for transmission and renewables such as our PrairieWinds ND 1 and PrairieWinds SD 1 projects."

"We hope our government relations division and our friends can turn back that attempt," Hudgins says. "Even though we helped electrify rural areas, the job goes on at all levels of the rural electric program. We need RUS to help Basin Electric and our members continue to provide affordable power to rural America."



Oct. 30, 1978: Robert W. Feragen is sworn in as the ninth REA administrator by U.S. Secretary of Agriculture Bob Bergland. Feragen had served as Basin Electric's director of information from 1964 to 1971.



Basin Electric's Rich Fockler (right) hosts a tour of Leland Olds Station for REA Administrator Harold V. Hunter. Appointed by Pres. Ronald Reagan, Hunter served from 1987 to 1989.