Risk Management Report to Board

Meeting Tuesday, August 15, 2017
Attending: Committee -- Judith Gregory, Frank Willett, Bill Pascoe, David Peterson, Arleen Boyd; Board -- Julie Lindgren, Roxie Melton; Dan Dutton; Staff – Kevin Owens, Brad Prophet; Attorney Larry Martin on phone connection.

Agenda (attached) included major decisions the board will address this month, including possible extension (up to a total of five years) of the two-year contract with Energy Keepers that runs from September 2022 through September 2024. A decision on increasing the approved $1,030,177 cushion of credit with the Rural Utility Service also will be addressed at the August 29 meeting and was discussed by the committee.

Energy Keepers next steps. Because the actual indicative pricing numbers are still confidential this report will not list numbers the committee recommended be taken to Energy Keepers, before the upcoming board meeting, relative to a contract extension following 2024 when the current Energy Keepers contract expires. We expect discussion by the board in closed session. The committee discussed reported industry forecasts that project low wholesale power costs for the foreseeable future. The committee noted concern about power contracts that extend ten years and questioned the exposure if BEC projected load decreased or prices went even lower when we have a set price. Bill Pascoe explained the limited exposure to excess load requirements under our load following contract with Energy Keepers. There was general agreement that prices could go down or up and the upside has more room to grow than the downside has to decrease. The committee reached agreement on a maximum price and a potential two-year or three-year contract extension, which Bill and Kevin will be discussing with Energy Keepers before the board meeting. The parameters the committee recommended would improve the forecast plan projections.

Cushion of Credit potential increase. The committee reviewed a comparison of the impact on BEC financial ratios resulting from the current two-year cushion of credit deposit (and the terms of the CoBank loan that financed that deposit) with the impact on ratios of potential increased loans to increase the deposit. The spreadsheet comparison (attached) used the BEC forecast plan as the basis for calculations of the total impact of projected loans on BEC financial ratios. The initial increase scenario extends the existing loan payments through 2022 and would cover an additional cushion of credit deposit of $1,543,399, bringing the BEC deposit total to $2,573,576 in 2017. The second and third scenarios increase the deposit by 50% and 75% of the additional $1,543,399.

Borrowing the money to finance the deposit produces a gain for BEC because the interest rate on the projected loans is lower than the 5% interest paid by RUS on the deposits. The committee looked at the gain from the cushion of credit scenarios as well as the impact on financial ratios, particularly Debt Service Coverage, which is calculated to dip to1.26 (just over the 1.25 standard lender requirement) in 2019 and 2020 under the full borrowing scenario.

Committee discussed exposure with planned borrowing for new meters, causes for the drop in DSC and the need to run the forecast model to fully reflect the impact of cushion of credit borrowing.

Manager Kevin Owens said that he is not comfortable with a tight DSC margin and noted that the CFC letter of credit is best reserved for unexpected short-term needs and emergencies. He will check with lenders before the board meeting and report on how the DSC exposure in the most aggressive scenario affects their evaluation of BEC and our credit requirements with power suppliers.

Committee recommendation. The 60-day notice to members of potential new loans exceeding two years was issued on July 28, which leaves time for member comments through the September 23 annual meeting. The committee recognizes the exposure with debt service coverage ratios and, based on the scenario results, is comfortable with borrowing an additional $1,157,549 (75% of $1,543,399) for a total of $2,187,965. If, after discussions with lenders and our power suppliers, the manager is confident that financial exposure is not great with the scenario to borrow an additional $1,543,399 the committee recognizes the value of the $139,680 gain from RUS interest that would be applied to RUS loan payments. The committee recommends (before or after a decision is made) having Kim Mikkelsen and Frank run the forecast model to reflect the new debt and possibly include settled numbers for the new TWACS (Two Way Automatic Communication System) meters.

Power supply and distributed generation policies. Bill Pascoe led a review of policies relating to power supply that need to be reviewed from the perspectives of strategic risk management, legal requirements and policy implementation. The consensus on Policies 309, 416, 417,418 and 419 is that they should be examined together in the context of rate structure and power supply planning at the planned board strategy session expected in September or October.

One decision should be addressed at the upcoming board meeting: Should we take action to allow management to delay signing member agreements for community generation (Policy 419) projects until after we identify the strategy for dealing with distributed generation and the rate structures, legal requirements and cost projections that support community projects? The timeframe for reaching a policy recommendation would be before the end of 2017.

The committee reviewed questions Bill had identified for the evaluation of the policies before the strategy session and added several for additional consideration. The updated list will be distributed before the August 29 board meeting.

Meter Upgrades: Kevin Owens reported that he and the staff are eager to move on to replacing the obsolete meters as soon as possible. Kevin will report at the board meeting on data from Anixter, Inc., supplier of TWACS solutions. The committee discussed various software options briefly and Kevin will prepare to outline options as well as preliminary costs projections at the board meeting.

Rate Structure. The ongoing risk management rate structure/rate design discussion focused on needed information for evaluating any proposed changes at BEC. The preliminary list of questions will be distributed before the board meeting. Kevin circulated an outline of one approach to develop further and use as a comparison to alternatives the committee and board will consider going forward. It includes a base charge plus a demand charge with power costs handled as a pass-through. The committee endorses discussion at the strategy session of rate structure objectives, how to identify and measure potential alternatives and a timeframe for decision-making.

Audit Schedule. Julie Lindgren reported that the Finance Committee will be receiving the draft audit before August 24 with questions requested to be forwarded to the auditor by August 25. She is scheduling a Finance Committee meeting with the auditor the morning of August 29.

Time permitted only a brief look at **power "alternatives"** or renewable investment opportunities being sent to BEC members and electricity consumers across the country. Arleen will present a brief description of the contacts being made to BEC members, some of their questions, and some data on what is being offered.

Agenda Risk Management Meeting
Tuesday, August 15, 12:00 P.M.

- Energy Keepers Report
- Distributed Generation Strategy and Policies
    - What do we need to know?
    - Timeframe for strategy and decisions
- Cushion of Credit Update and Numbers
    - Notice to Members
    - CoBank Loan
    - Impact on Financial Ratios
- Meter Upgrade Update
- Rate Structure Discussion
- Annual Meeting Risk Management Message
- Audit Schedule
- Arcadia Power