

## **PRC economist: Kit Carson hike too high**

**By J.R. Logan**

*The Taos News*

Kit Carson Electric Cooperative is asking for too much in a proposed electric rate increase, according to an economist with the state Public Regulation Commission.

John J. Reynolds, a utility economist for the PRC, filed written testimony in the co-op rate case questioning the way the increase was calculated and suggesting that the co-op can do more to cut costs.

Co-op critics have said the PRC economist's testimony confirms many of their suspicions that the co-op is mismanaged. But CEO Lu's Reyes counters that the co-op has made judicious decisions, and he stands behind the rate design.

Reyes has said the increase is based solely on a "cost-of-service study" done by Martin Blake, who was hired as a consultant by the co-op. In rebuttal testimony filed with the PRC, Blake defends his calculations and insists that the proposed hike is reasonable.

The last-minute debate came days before the start of a hearing in front of the PRC hearing officer Lee Huffman on the proposed rates. The multiday hearing began Wednesday (July 6). The PRC has the authority to determine the size of the rate hike, or determine if it is at all warranted.

### **Actual costs**

Under the co-op's current rate-increase proposal, the fixed customer charge for residential residents would increase 105 percent — from \$10 to \$20.50 a month — making it the second-highest customer charge in the state. At the same time, the cost of electricity would decrease slightly.

Reyes has said the rate redesign would cover the necessary costs of lines, poles and other transmission infrastructure so that the co-op can continue to provide service and promote energy efficiency without hurting its bottom line.

But in his testimony, utility economist Reynolds said Blake overstated the cost of installing and maintaining electric infrastructure by using figures that don't reflect Kit Carson's actual costs. As a result, Reynolds said the justification for more than doubling

the fixed rate is “inadequately supported by the data.”

In his rebuttal, Blake said his analysis correctly attributes the cost of poles, towers and fixtures as “fixed costs,” and he said they are accurately represented in the monthly customer charge. Reynolds disagrees, arguing that the proposed increase would give the co-op a reliable profit margin — an estimated \$3.60 per customer each month — that doesn’t reflect the true cost of providing electric service. He said co-op rate-making should be a “zero sum game,” where costs directly reflect customer rates. Otherwise, Reynolds said the co-op could continue to live beyond its means on the backs of its electric customers.

“The proposed rate structure therefore provides no incentive to Kit Carson to contain its costs in the face of stagnant economic conditions,” Reynolds stated in his testimony.

Instead, Reynolds recommended that the fixed monthly cost for residential customers be increased to \$17 a month — a rate hike that would “avoid bill shock to customers” while keeping the co-op solvent.

In his testimony, Reynolds is clear, especially considering that the co-op’s books show it is in “technical default” of its federal loans.

Reynolds stated that Kit Carson Electric has seen operating margins fall sharply since 2008. Meanwhile, starting in 2004, Reynolds said the co-op has made “significant infrastructure improvements” financed with higher debt and member-owned capital.

Since 2004, the co-op’s longterm debt has increased by \$22.9 million (57.3 percent), and Reynolds estimates the coop will owe an additional \$1.1 million in interest payments annually.

If nothing changes, he said, things will only get worse.

“Kit Carson’s financial condition will inevitably worsen as its rising financial obligations along with its relatively fixed expenses exceed its revenues,” Reynolds testified.

Reyes told *The Taos News*

Tuesday (July 5) that the investments were needed to ensure reliable service to co-op customers, and that the co-op is not at financial risk. He also said many of those expenditures were started long before the co-op saw its revenue begin to drop.

‘Constructive suggestions’

In addition to challenging the rate-making methodology, Reynolds also tackled peripheral issues that have become major points of contention codetractors.

After the rate hike was announced, hundreds of coop members protested. Some said

the increase would create a financial hardship, and others said it would unfairly affect energy-conscious consumers. Many protested on the grounds that the co-op's propane and Internet companies were losing ventures, and that spending by the board of trustees was out of control.

Reyes repeatedly denied the allegations, saying the rate increase is based solely on the cost of providing service to customers.

But Reynolds testified that such charges were worth investigating.

"(PRC) staff takes the views of the protesters seriously," Reynolds said. "They may have valid and constructive suggestions to reduce expenses without materially affecting service. The protesters are also members of KCEC, and they came out in significant numbers. Their views must therefore be considered."

Perhaps the most controversial issue has been losses incurred by the co-op's diversified activities, which some call "cross-subsidization" from the electric side.

Reynolds testified that the co-op now has \$10 million of electric ratepayer money in affiliated businesses: \$5.6 million in the propane business, \$2.1 million in the Internet and 2.3 center. That money came from "patronage capital" — essentially a cash reserve account that contains member-owned co-op profits.

Both the Internet and propane companies have lost money overall. But Reyes denies that these are cross-subsidizations. Instead, he has said the diversified activities are "investments" and that they will pay off in the long run.

In his testimony, Reynolds agreed with the co-op's assertion that the rate increase is driven by the cost of providing electricity to customers, but he said without payments from electric ratepayers, the diversified activities could not have been sustained.

He also stressed that patronage capital contributions play a role in rate making because they "provide equity to the cooperative and help minimize borrowing thus reducing the coop's debt load."

In addition to its diversified businesses, the co-op has long faced criticism over compensation paid to its board of trustees.

Those who sit on the 11 member board receive compensation for meetings attended and trips taken for training and other conferences. In 2008, reported trustee compensation totaled \$163,000; in 2009 it was \$194,000; and last year it was \$171,000. Though they aren't the highest numbers in the state for rural electric cooperatives, they put it above the New Mexico average.

Reyes has said trustee and employee expenditures are justified and necessary to keep board members up-to-date on trends and technological advancements. He also said

board expenses make up less than 1 percent of the co-op's revenue requirement.

Reynolds said that though Kit Carson's board expenses have been declining, there was room for improvement. He suggested reducing travel and creating a "clear" per diem policy to "limit the risk of incurring variable travel expenses while setting clear guidelines about KCEC's share of the trustee's or employee's travel expenses."

In rebuttal testimony, Reyes said the co-op has such a plan in place.

Reynolds also said the co-op should reconsider a requested \$155,000 increase over 2009 expenses to go toward labor costs.

"Today's economic conditions dictate that salary increases are currently rare and marginal and that businesses are cutting expenses in general not just labor expenses," Reynolds testified. "Opportunities to restructure labor related expenses as well as other expenses surely exist within Kit Carson."

The co-op says it has already implemented a wage freeze, and it has not filled a number of positions to save money.