

Risk Management – Looking for Trouble ... and Opportunity

Risk Management

The Beartooth Electric Cooperative risk management committee, set up by the BEC Board of Trustees, includes co-op members with valuable experience and expertise. They are working with the board to identify risks and analyze alternatives.

Over the past four years we focused on business alternatives. We took membership in a generation and transmission cooperative off the table. We left Southern Montana Electric, which freed us to secure power at much better rates and opened the door for new financial and business agreements.

As we worked to leave Southern we could forecast reduced expenses and favorable new power contracts. Now we are seeing quantifiable results. Excellent rates for wholesale power at BEC are fixed for the next 7 years. Last year we paid \$5.1 million for power, nearly 50 percent of our total revenue. Our new contracts reduce our power cost significantly, creating opportunity for additional member rate reduction.

We have not yet calculated the amount of our next rate reduction – that requires calculation of the reduced revenue opportunity followed by examination of lower revenue scenarios that ensure plant safety and reliability while improving our financial ratios. Those calculations are underway.

Examining Alternatives

For the first time standalone Beartooth provides a positive benchmark for evaluation of organizational alternatives. We no longer are seeking a solution to overwhelming problems or a way out. We are on solid ground looking at business alternatives to improve our position. “Improve” means to deliver reliable power and quality service at lower rates.

One option is to remain independent: a small co-op with challenges of low density and low growth. We have often reported on those challenges and the fact that it is difficult to lower rates significantly with a widespread system financed by revenue from so few members. To improve economies of scale we have a management agreement with Lower Valley Energy that provides excellent staff without full overhead or long-term personnel obligations. The agreement anticipates assessment of the potential for a merger with BEC becoming part of the larger co-op.

LVE is both a source for improved financial results at the independent BEC and a potential business alternative for the future. In addition to financial improvements resulting from our exit from Southern and new power contracts, we predict financial gains from implementation of efficiencies and best practices by LVE management. Financial gains will benefit an independent BEC and provide data for analysis of the potential benefits of a merger.

Next month we will report on the results of the analysis NorthWestern Energy and BEC have done to assess whether an acquisition could provide a financial advantage for BEC members while protecting the interests of NWE ratepayers as required by law.

Next Steps

BEC has three upcoming steps for you to track. We will: 1) Use the forecast model in January to perform comparative analyses of various rate reduction scenarios for BEC as a standalone cooperative managed by LVE. 2) Perform in March a comprehensive Cost of Service Analysis (COSA) to decide how to fairly lower rates across member classes. 3) Continue to assess the risks and benefits of business alternatives available to BEC.

Southern Connection Update

Our exit from Southern is final. We paid our legally required share of Southern's debt for the Highwood Generating Station (HGS) and are paying expenses we would have paid as a Southern member. We receive Southern's financial statements each month to help us track their progress toward completion of bankruptcy obligations and the potential receipt of payments that could include amounts due to BEC. We continue to monitor Southern's payback of the HGS notes. Once the notes are paid, our obligation to pay expenses ends.

We inform you to generate input and improve decision-making. Please contact any board member or our manager, Jim Webb, for information --- or with suggestions.

Arleen Boyd – Risk Management Chair, District 5 Trustee
Submitted December 9, 2015