

Board Report – June 28, 20116

**Risk Management Meeting, June 17, 2016**

Present: Jack Schutte, Frank Willett, Bill Pascoe, David Peterson, Roxie Melton, Julie Lindgren, Larry Martin, Arleen Boyd. Present by video: Jim Webb, Wade Hirschi.

Wade Hirschi presented the 7-year standalone forecast with the committee. The forecast is based on Wade's use of the CFC Compass model to set key financial ratio targets and use growth, expense, capital outlay and patronage retirement assumptions from the BEC budget analysis to calculate annual revenue requirements for ten years starting in 2016. The model shows that revenue based on current rates with .25% annual kWh sales growth would exceed the minimum revenue required by \$800,000 to \$1 million each year. The committee sees this as indication that a small additional rate decrease could be possible this year and does not see a new COSA required to confirm that, but rather a run of the forecast model with a proposed rate decrease. The committee asked for several additions and corrections to the model, which Wade will prepare for review at a risk management meeting scheduled for July 13. Updates will include filling in Balance Sheet missing data, increasing capital outlay for 2018 and 2019 to reflect a more conservative \$1.5 million for new meters, correcting a few spreadsheet inconsistencies, and creating a more complete cash flow sheet to show beginning and ending cash with the standard sources and uses of cash.

The committee and management discussed proposed uses for the \$1.211 million payment BEC received as its share of the NorthWestern energy repayment of Schedule 3 overcharges to Southern. After discussion the committee recommends using the amount to retire the CFC debt BEC took on to finance prepayment of its share of the Highwood Generating Station notes as a provision of the exit agreement with Southern. Jim and Wade will confirm the loan provisions with CFC and detail a recommendation to the board. They also will seek advice from the BEC auditor regarding whether the amount should be noted as a potential liability due to the appeal NorthWestern is filing to challenge the FERC ruling that required the NWE refund.

The committee reviewed a summary of its previous comments regarding the *EES Evaluation of Consolidation Between Lower Valley Energy, Fall River Cooperative, and Beartooth Electric Cooperative*. The summary was distributed to the board as well. The committee had decided not to examine the study further until after the consolidation reevaluation by FREC and LVE boards is completed. The summary noted that some assumptions and potential conclusions about BEC need verification and the impact of the noted savings on rates must be added to the analysis. The committee reviewed its comments now because the report:

- Provides data that would be used in an analysis of the BEC merger (by E3 if appropriate)
- Is being reviewed by the GDS consultants

- Is posted on the BEC website and needs an explanation of what it represents at this time (a potential work in progress).

The committee examined, as requested by the board, potential actions regarding a potential MOU with Lower Valley and concluded that an MOU likely is not needed at this time because the management agreement provides a path toward making a decision on recommendation of a merger and defines many of the criteria for that decision. The management agreement does not address governance issues or legal requirements that need to be in place for a merger to occur. Jim Webb agreed that the open issues do not require an MOU and could be dealt with between the two boards. Both parties need to understand the legal requirements, governance issues, and process for making a decision to merge. A beginning outline of requirements and process for developing a merger contract is included in the attached MOU document that includes changes made after it was last distributed to the board.

Larry Martin reported on the agreement with Southern and NorthWestern Energy to distribute the BEC share (\$1.112 million) of the NWE refund to Southern (\$ 6.347 million). The Southern board voted to put its share of the refund in an escrow account until resolution of the NWE appeal of the FERC ruling that NWE must repay Schedule 3 overcharges. The BEC refund came directly from NWE on June 17.

Larry reviewed the preliminary conclusions regarding member-voting requirements for a merger or consolidation. He will have a memo for the before the meeting on June 28.

Jack Schutte announced his resignation from the Risk Management Committee and his plan to move to Texas in July. Jack has served on the due diligence/risk management committee since 2012 when it was formed. His experience and expertise have helped the co-op make solid financial decisions and evaluate options effectively. Jack was instrumental in the co-op's ability to work through daunting financial and organizational challenges and get to the very positive position we enjoy today.

The committee will review the independent analysis and governance issues at the next meeting. The committee did not receive the E3 report in time to review it before the June meeting and will examine it for discussion at the July 13 meeting.

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**Southern Montana Electric –**

Southern financials show full payment of the Highwood Generating Station notes in May. Our agreement to contribute to A&G expenses ends with payment of the notes. The BEC Exit Agreement stated:

*A monthly payment to reimburse for A&G expenses beginning the first full month after the Withdrawal Date and continuing through the date when the Restructured Notes are paid in full or otherwise deemed to be satisfied in full (the "Periodic Payments"). Each Periodic Payment shall be due on the 5<sup>th</sup> day of the month and shall be in the amount of \$9,636.61.*

Southern has not reported discussion of intention to close. Following payment of the notes, according to the Southern reorganization plan filed with Bankruptcy Court, any member may seek an exit. There is no indication that any member plans to do that.