

Electric Cooperatives of Oklahoma

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WHAT ABOUT THE FUTURE?

The days of inexpensive energy have ended for all Americans. Electric rates, however have remained stable over the last few years, and forecasts are for this trend to continue into the future.


However, there are areas where improvement can help with energy efficiencies, enabling stable electricity costs to continue. The future of electric rates in Oklahoma will be controlled by our ability to efficiently use our existing generating capacity. This is called “Load Management.”

In the 70’s and 80s, cooperatives had to suffer through high costs of construction, and unusually high rates of interest and inflation, just as everyone else! One bright spot is that Oklahoma’s RECs now have sufficient capacity for several years to come; but, we must use these generating facilities efficiently and effectively.

All but two Oklahoma cooperatives purchase wholesale electric power from a generation and transmission (G&T) cooperative. Oklahoma has two G&T: Western Farmers Electric Cooperative (WFEC) in Anadarko, and KAMO Power, located in Vinita. Tri-County Electric Cooperative, Hooker, purchases its wholesale power from Golden Spread Electric Cooperative in Amarillo, Texas. Northeast Oklahoma Electric Cooperative, Vinita, purchases some of their wholesale power from KAMO Power, but the majority of their energy is supplied by the grand River Dam Authority (GRDA), a state-owned power supplier.

Voluntary load management is an effort to shift electrical usage around “peak” periods of the day. Voluntarily, we can all help “shave” these peaks and thus more efficiently utilize the generation system that currently supplies power to nearly one million Oklahomans. Contact your local REC to find out how you can help!

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**The
Electric Cooperatives
of Oklahoma:**

**They Are
YOUR Business!**

THE 90s— DECADE OF DECISION

Since its birth in 1935, the rural electrification program has evolved into one of the first, and greatest, consumer action programs in America. It hasn't been easy – and Oklahoma's Rural Electric Cooperatives (RECs) still face some of their greatest challenges in the next decade and into the next millennium.

As we all know, times are changing. Customs, attitudes and lifestyles of America's rural people are being transformed and driven by a world economy. Oklahoma's RECs are feeling the effects of change as well. Many of rural electrification's pioneers have turned over the reins of leadership to the next generation; the days of inexpensive energy have faded to memory, and the nature of our membership is changing dramatically. Many of today's new members are "urbanites," choosing to flee the city, yet expecting the convenience of in-town living in a rural environment.

Where does that leave today's Co-ops? What is unique about the Electric Cooperatives of Oklahoma? Does the Cooperative philosophy involve more than just providing electricity to rural areas? Are Cooperatives more than just a "rural utility?" We think so!

Cooperatives are unique among electric service suppliers; they are owned by those they serve, with each consumer being a member/owner with a voice in the affairs of the Cooperative. That voice can be expressed through the election of the governing Board of Directors, and approval of bylaws governing the Co-op. Each member, regardless of power usage, has only one vote. Also, there is a personal communication link in the form of district and annual meetings of the membership. These meetings provide forums for members to talk about matters of concern to them. What other utility allows its "consumers" the ultimate control of the organization? What other form of utility is exclusively owned by the consumer it serves?

In addition, Co-ops offer a wide range of services to their member/owners. Information on electrical use; a home energy audit program to help members improve energy efficiency in their homes; and consulting with members on plans for new homes are all provided, without charge, to members. Also, the Cooperatives are mandated to serve anyone who desires electric

If not for the PCA, your Cooperative would have to raise its rates high enough to cover the worst possible conditions, high "peak demands" and low energy usage. It sometimes takes two years for your Co-op to complete the regulatory process to receive a rate adjustment; without the PCA, there would not be an adjustment to increase the revenue on a per-month basis, depending on need. This would cause the base rate to be unfairly and artificially high, and would collect excess revenues on a monthly basis.

By using the PCA each month, your REC charges you only for the actual costs of wholesale power.



For the last few years, there has been some confusion about how to interpret the PCA. Several definitions used over the years have implied that the PCA is a result of variations in the price of fuel used to generate wholesale power. This is true to an extent, but is not the whole story.

Part of the story lies in the term “Peak Demand.” Peak demand is the highest (or maximum) rate of consumption during a specified period of time. It represents the maximum usage required of the electrical generating facilities which serves your REC. This peak usage may only occur one day, or one hour, out of the year. Even so, it requires that sufficient capacity be available year-round. This capacity is paid for by your distribution cooperative through “demand” charges to the generation and transmission cooperatives, or G&Ts. In Oklahoma, the majority of Cooperatives establish their peak demand during the summer, usually in August or early September. However, it is not uncommon for some Cooperatives to “peak” during the winter.

These two components, fuel (or energy) costs and demand costs, are the major portions of your REC’s cost of purchased wholesale power. **The PCA is the difference between your REC’s actual cost of power (fuel costs plus demand costs) and the base rate established for members by the Cooperative.** The PCA allows your REC to collect adequate revenue to pay their current wholesale power bill. Remember, the PCA is that portion of the wholesale bill that the base rate of the Cooperative fails to recover from its members.

Your Cooperative’s retail rate is the charge per kilowatt-hour (kWh) of electricity consumed by members. The PCA includes both fixed costs (demand charges, depreciation, interest, etc.) and variable costs (primarily fuel). That is why the PCA fluctuates each month. It is prorated on a kWh basis.

When your Cooperative sells a low number of kWhs (usually during the spring and fall), the demand charge (fixed cost) is spread over fewer kWhs and is consequently higher for each kWh of energy. On the other hand, if your REC sells a high number of kWhs (usually in the summer and winter), those constant and ever-present demand charges are spread over a lot of kilowatt-hours (kWhs) and are less for each kWh.

service in their area. What other utility can claim this?

So what is the critical decision of the 1990s? It is one to be made by every person in rural Oklahoma, to recommit ourselves to the Cooperative spirit and philosophy. This spirit put electricity into rural homes when no other utility in Oklahoma was willing to serve the rural areas. This philosophy accepted the fact that serving the sparsely populated countryside with electricity would not be a profitable investment. Thus, Cooperative members banded together and built the lines themselves.

Today, those Cooperatives are still owned by their member-owners. And, they still need the involvement, the ideas and the spirit that only those members can provide.

We need to reaffirm in the next decade our pride and commitment to the program we established in the 1930s-the program that has had such a positive impact on rural America.

YOUR COOPERATIVE PHILOSOPHY

Just 60 years ago, 97 out of every 100 families in rural Oklahoma did not have central station electric service for their homes or farms. By the 1930s, people in towns and cities were enjoying the conveniences of electricity, but for thousands of rural families across the country, electricity was only a dream.

Existing power companies serving urban areas had long refused to extend electric service into rural areas because they felt it would not be profitable.

When Franklin Delano Roosevelt discovered he was paying 18¢ per kilowatt-hour for electricity at his cottage in Warm Springs, Georgia, he was shocked! It was about 4 times the rate he was paying at his home in Hyde Park, New York. That triggered a study of the electric power industry and particularly, the plight of rural areas. When he became Governor of New York, he developed the Power Authority of the State of New York, which conducted studies that proved the feasibility of rural electrification.

Armed with this and his own research, Mr. Roosevelt, as President of the United States, created the Rural Electrification Administration (REA) in 1935. A consumer had opened the door that would provide rural America a better way of life. With the assistance of REA, rural people decided to build power lines themselves.

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They had a heritage of cooperation, having worked and fought together from the early days of the country, creating farms from wilderness, and then defending those farms. They had cooperated to harvest their crops and market them. They knew how to work and fight for the things they needed and believed in.

They were undaunted by the skepticism which greeted their desires to provide themselves with electric power. Despite strong and continued opposition from many of the nation's commercial electric utilities, people who wanted to become electric consumers forged ahead to develop their own rural electric service into the strong and successful example of private enterprise it is today.

Cimarron Electric Cooperative had the distinction of being the first cooperative in Oklahoma to set a meter in early December of 1937, at the home of Earl Harrison. What a Christmas Gift!

From these humble beginnings, the rural electrification movement changed the nature of rural living in Oklahoma and throughout the country. Today, this people-oriented program has grown to 28 successful distribution electric cooperatives in Oklahoma. More than 99% of the rural families in our state enjoy the benefits of electricity in their homes and on their farms. Rural electric cooperatives are a tribute to the men and women of the country's rural communities.

Through their accomplishments of rural electrification, these people improved their standard of living and the agricultural productivity of this great nation.

YOUR REC IS...

A Business - Born of the need and desire of rural people who worked together for their common good to electrify rural America. It is a private non-profit corporation owned by its consumer-members.

Non-Discriminatory - Membership is open to anyone within the Co-op service area who desires electric service.

Democratically Controlled - Each consumer of the cooperative is a member with one vote in the affairs of the cooperative. Members are entitled to attend the cooperative meetings and to exercise their voting privilege in elections of directors, as well as any other business presented to the membership at annual or district meetings.

- Revenues lost to the Treasury due to the special tax benefits of accelerated depreciation and investment tax credits which have been provided to investor-owned utilities; and
- Any direct costs incurred by government in conjunction with RUS insured loans made to RECs at below-market interest rates.

Federal assistance to rural electric cooperatives can be calculated as the difference between the RUS insured loan interest rate (5%) and the average rate on Treasury borrowings times the volume of RUS loans. No costs are attached to the RUS loan guarantees, since they are made on a cost-plus basis.

Assistance to publicly-owned utilities relates to their ability to issue debt securities on which interest payments are not taxed by the federal government. These tax-free bonds are, therefore, issued at comparatively favorable interest rates.

Measuring assistance to the investor-owned segment also revolves around Treasury revenue losses resulting from tax benefits. The tax benefit from accelerated depreciation, for example, reduces the IOU's tax liability and serves, in effect, as an interest-free loan. The investment tax credit further reduces IOU tax payments. In addition, tax legislation passed in 1981 enables stockholders in these systems to reinvest up to \$1500 in dividends in additional stock, thereby deferring any payment of tax until the stock is sold, when it is generally taxed at a much lower capital gain rate. The impact of these provisions on Treasury revenues is estimated at over \$5.1 billion a year.

In conclusion, while all three segments of the electric utility industry enjoy some degree of assistance from the federal government, there is clear evidence that the largest measure of aid presently is going to investor-owned companies.

POWER COST ADJUSTMENT

The power cost adjustment (PCA) is probably one of the most misunderstood portions of the cost of providing electric service to cooperative members. The formal language in Oklahoma Statutes, Title 17, Section 250.9 reads as follows: "Purchased power adjustment clause (PCA) means any mechanism which allows an electric public utility or electric distribution cooperative to adjust its charges above or below the base amount included in its rates based upon changes in costs of wholesale power purchased from others."

WHAT ABOUT INTEREST RATES?

No doubt you have heard someone refer to “those REA 2% loans” and the “sweet deal” that RECs have with the federal government. This misconception has existed for quite some time. In fact, there is NO MORE 2% money available to RECs.

Just what is the average current interest rate on RUS financing?

As explained earlier, the Rural Utilities Service (RUS) does make insured loans at a 5% interest rate. These loans are to distribution cooperatives only, and require a portion of the loan be acquired from non-RUS sources (usually 30%), such as CFC or Co-Bank. Most of the supplemental financing is by CFC, whose long-term rates in 1998 varied from 5.15% to 8.5%.

Eighty-five percent of the money loaned by RUS is at a cost greater than the governments cost of borrowing money. These loans, backed by federal guarantees, are loaned by the Federal Financing Bank to generation and transmission cooperatives.

Blending the two loan programs together provided an overall average cost in RUS financing which could hardly be regarded as “cheap” money, since it is considerably higher than the often claimed “2%.” This effective interest rate is approximately the same as that of investor-owned electric utilities and is slightly higher than that of publicly owned electric utilities.

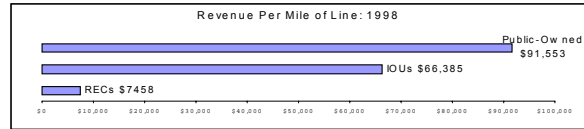
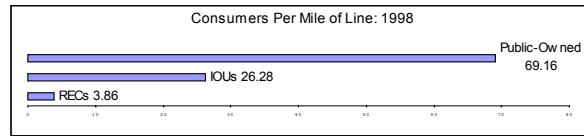
FEDERAL ASSISTANCE TO UTILITIES

The federal government’s financial assistance to all types of electric utilities dates to the industry’s very beginnings, nearly 125 years ago.

Overall federal assistance can be measured in terms of the corresponding loss in revenue to the U.S. Treasury attributable to the varying types of assistance provided to the three major segments of the industry:

- Tax revenues lost to the Treasury resulting from publicly owned utilities’ ability to issue securities on which the interest received by investors is exempt from federal income tax;

Comparison of Consumers & Revenue Per Mile of Line



Truly Non-Profit: It is important to briefly compare the financial position of RECs to investor-owned (IOU) and publicly-owned (POU) utilities. Nationwide, RECs serve only 5.76 consumers per mile of line (3.86 in Oklahoma) compared to 34.85 per mile for IOUs (26.28 in Oklahoma) and 47.76 for POU’s (69.16 in Oklahoma). This means that RECs collect less than one-eighth the revenues of IOUs, and less than one-tenth of revenues compared to POU’s.

In the event of net earnings, each member is allocated a percentage, in the form of capital credits, proportionate to the amount of energy he received. The capital credits may be paid to the members when the financial condition of the Co-op and RUS policies make it possible.

Growing: Today, Oklahoma’s 28 electric distribution co-ops and two generation and transmission (G&T) co-ops operate growing electric systems composed of generating plants, substations and 105,000 miles of line to serve nearly 400,000 meters in all 77 counties in Oklahoma.

Preparing for the Future: Your cooperative is planning ahead, employing all possible power sources: natural gas, oil, coal, solar and wind energy to meet the electrical needs of its members, now and in the future. The task of the rural electric cooperatives is far from complete.

Good for the Economy: Your Co-op, like other businesses, pays taxes. Since income tax is a tax on profit, and RECs are non-profit corporations, they pay no income tax; however, Oklahoma RECs pay a 2% gross receipts tax to the state, which is distributed to local schools in relation to the number of miles of line in each district. For 1997, this tax amounted to nearly \$15 million. RECs also pay social security, unemployment, and gasoline taxes as well as license, franchise fees and other taxes.

WHERE DO WE GET THE MONEY?

Your monthly payments for electric service pay for: (1) the cost of generating, transmitting and distributing electricity to the members; (2) the cost of operating and maintaining over 105,000 miles of line; (3) the principle and interest on RUS and other loans. These are operating expenses, paid with operating income.

Construction of new power plants, substations and other system improvements are financed by loans. The Rural Utilities Service (RUS; formerly REA) serves as primary banker for most rural electric cooperatives. On May 11, 1973, President Nixon signed Public Law 93-32 which removed the rural electric borrowers from complete dependency on federal appropriations. This law opened the door for RECs to borrow capital in adequate amounts. As a trade-off, the cooperatives surrendered the flat 2% interest rate set in 1944.

The principle source of loans for distribution cooperatives is in the form of insured loans. The actual funds used for these loans originate from the Rural Electric and Telephone Revolving Fund. This fund was established in 1973 and its lending and borrowing activity is excluded by law from inclusion in the federal budget. Generally, distribution cooperatives are required to obtain 30% of their loan needs from non-RUS sources.

At the time of its creation, the assets of the fund were comprised of all outstanding REA (now RUS) loans, plus the cash REA had on hand, representing funds which had been provided to REA by Congress, but not yet advanced to borrowers. All together, the initial asset value of the fund totaled nearly eight billion dollars.

In addition, the new law provided that all payments of interest and principal made to REA by Rural Electric and Telephone borrowers would then flow into the fund. These receipts made up the primary source of capital available to REA for new insured loans. This continual “rolling over” of old loan payments into new loan advances is the reason the fund is said to “revolve”.

The other lending program of RUS is “guaranteed loans.” The major source of money to construct generation and bulk transmission facilities are loans guaranteed by RUS.

Without this guarantee, the low equity co-ops would be regarded as high risk in the private money market and thus would have to pay much higher interest rates.

Further cost savings for the generation and transmission cooperatives are achieved by borrowing the funds from the Federal Financing Bank at the government’s full cost of borrowed money, plus a margin. This rate has ranged from 8% to 12% over the past few years. In 1986, REA loan guarantees accounted for approximately 78% of REA’s lending activity for rural electrification.

In the mid-1960s, it became apparent that REA’s loan program was not adequate to meet the growing needs of the nation’s RECs. An independent cooperative financing organization was created to obtain additional capital. The National Rural Utilities Cooperative Finance Corporation, or CFC, was formed in 1969. As of May 31, 1999, CFC has 1057 members—908 of which are electric cooperatives. CFC has a 22-member board of directors representing 11 districts across the country, and employs 186 full-time employees, nearly all of whom work at CFC national headquarters in Herndon, Virginia.

At the end of Fiscal Year 1999, total credit commitments to CFC members exceeded 12.7 billion. Member investments were \$3 billion in 1998, or 21% of total capitalization. CFC has approximately \$4.8 billion in bank lines of credit with 70 domestic and commercial banks throughout the United States, Europe, Canada and Japan.

In addition to CFC, one relatively new source of capital for Oklahoma’s RECs is Co-Bank. This bank is a specialized financial institution which serves only cooperatives, and is district owned by the member/borrower cooperatives. There are 12 district Banks for Cooperatives in the United States. Co-Bank serves co-ops primarily in Kansas, Oklahoma, New Mexico and Colorado.