

HEBER LIGHT & POWER

Executive Summary Report

Introduction

We are pleased to present a summary of the electric cost of service, financial projection, and rate design study for Heber Light & Power (HLP). This report summarizes the Full Report that includes additional information, discussion on study results, and the significant assumptions used in the development of the studies. The purpose of a cost of service study is to identify the following:

- 1) Determine the utility's revenue requirements for fiscal year 2020
- 2) Identify if cross-subsidies exist between rate classes
- 3) Identify cost-based power supply and distribution rates
- 4) Identify the appropriate monthly customer charge for each class
- 5) Identify future rate considerations for Heber Light & Power

Financial Projection Results

In the financial projection study, three targets are considered for a period of five years to evaluate the financial health of the utility.

Fixed Cost Coverage Ratio: Maintaining a fixed cost coverage ratio ensures adequate funds are available to meet debt service payments. The fixed cost coverage includes debt service owned by HLP and fixed costs related to take or pay power supply contracts. For rating purposes, a minimum of 1.40 coverage ratio should be maintained. HLP maintains a strong fixed cost coverage ratio throughout the projection.

Minimum Cash Reserves: The financial projection identifies a minimum cash reserve level to ensure timely replacement of assets, fund operating expenses and annual debt service payments, and to mitigate a utility's exposure to catastrophic events, market risks, changes in fuel costs, or loss of a major customer. The projected cash balance includes monies set aside as rate funded capital by HLP. HLP cash balances are projected to fall short of the minimum targets between 2022 – 2024.

Target Operating Income: In order to fund interest expense on outstanding debt principal and recover the full replacement cost of system assets, a utility must generate a breakeven rate of return. The target operating income incorporates this return into the operating income calculation. Operating losses are projected each year with losses exceeding \$2.0 million in 2024.

Financial Projection Summary – No Increases

Fiscal Year	Projected Rate Adjustments	Fixed Coverage Ratio	Adjusted Operating Income	Target Operating Income	Projected Cash Balances	Recommended Minimum Cash
2020	0.0%	1.92	\$ (473,188)	\$ 2,176,617	\$ 8,046,188	\$ 6,246,482
2021	0.0%	1.79	(531,492)	2,233,032	8,826,787	7,619,590
2022	0.0%	1.66	(978,371)	2,672,276	5,614,019	8,753,636
2023	0.0%	1.60	(1,535,244)	2,698,163	1,598,441	9,628,311
2024	0.0%	1.46	(2,143,574)	3,334,856	(4,574,694)	10,072,511

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HLP fixed cost coverage ratio is strong throughout the projection period. The rate track projected below ensures operating income remains positive with movement toward the target; however, projected cash balances may fall below the recommended minimum in 2023 and 2024. The financial projection should be reviewed once the amount and timing of capital costs, and connection fee revenue can be identified with additional certainty.

Financial Projection Summary – Recommended Rate Track

Fiscal Year	Projected Rate Adjustments	Fixed Coverage Ratio	Adjusted Operating Income	Target Operating Income	Projected Cash Balances	Recommended Minimum Cash
2020	4.0%	2.06	\$ 214,111	\$ 2,176,617	\$ 8,733,487	\$ 6,246,482
2021	4.0%	2.08	921,651	2,233,032	10,970,665	7,619,590
2022	2.0%	2.01	907,184	2,672,276	9,654,171	8,753,636
2023	2.0%	2.03	810,008	2,698,163	8,004,045	9,628,311
2024	2.0%	1.95	690,041	3,334,856	4,696,554	10,072,511

Cost of Service Summary Results

The cost of service study determines costs to provide service to each class of customer and assists in design of electric rates. The table below provides the cost to service each class with projected revenues. The “% change” column is the adjustment necessary to meet projected cost of service requirements. Negative adjustments suggest current rates are collecting more than cost of service and positive adjustments suggest current rates are short of recovering costs spent to serve that customer class.

Cost of Service Summary Results

Customer Class	Cost of Service	Projected Revenues	% Change
Residential	\$ 11,782,845	\$ 9,570,665	23.1%
Residential Solar	314,406	213,018	47.6%
Street lighting	139,463	-	0.0%
Yard Lighting	5,971	6,942	-14.0%
Small Commercial	2,464,627	2,276,554	8.3%
Medium Commercial	2,915,961	3,081,431	-5.4%
Large Commercial	1,602,373	1,893,714	-15.4%
Commercial Solar	7,227	5,569	29.8%
Pumping	180,018	134,580	33.8%
Total	\$ 19,412,891	\$ 17,182,473	13.0%

The study indicates the Medium and Large Commercial, and Yard Lighting classes are paying rates exceeding their cost of providing service. The Residential, Small Commercial, Solar, and Pumping classes are paying rates below their cost of providing service.

Based on UFS experience, HLP’s study results are typical for many utilities around the nation with results showing the commercial classes needing less increases and residential classes greater increases.

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Cost of Service Rates

The table below identifies the cost of service rates for each customer class and includes costs for power supply, distribution, and direct customer related costs. Charging these rates would directly match the cost of providing service to customers. The table compares the current customer charges with the cost-based customer charges and cost-based demand and energy rates for each class.

Total Costs by Customer Class

Customer Class	Current Average	COS Customer		Demand	Energy
	Customer Charge	Charge			
Residential	\$ 12.70	\$ 14.67	\$ -	\$ -	0.1042
Residential Solar	12.70	27.43	-	-	0.1143
Street lighting	-	2.09	-	-	0.0817
Yard Lighting	-	2.09	-	-	0.0556
Small Commercial	8.00	28.53	15.50		0.0215
Medium Commercial	15.20	131.43	16.86		0.0215
Large Commercial	26.90	324.71	16.46		0.0215
Commercial Solar	8.00	54.05	15.50		0.0215
Pumping	7.88	54.46	14.46		0.0215

Residential Customer Charge

The customer charge consists of expenses related to 1) providing a minimum amount of electricity to the residential customer, and 2) expenses related to servicing a meter on the customer premises, in effect determining the cost to deliver a single kWh of electricity to the customer. The methodology used in this study is consistent with methodologies and practices used in the electric industry. The cost of service study identified minimum system charges of \$7.62 and direct costs of \$7.05 for a total monthly customer charge of \$14.67. The total monthly customer charge cost breakdown is listed in the table below and includes minimum system costs (blue) and direct costs (brown).

Monthly Customer Charge Cost Breakdown

Rate Breakdown	Residential
Distribution Customer Costs	\$ 2.27
Transformer Customer Costs	3.98
Substation Customer Costs	1.37
Meter O&M	0.81
Meter Reading	1.10
Billing	4.15
Customer Service	0.99
Customer Charge \$/Meter	\$ 14.67

Based on UFS experience with similar size utilities, HLP's residential cost-based customer charge is lower than most utilities.

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Rate Design Summary

Rates were designed using the recommended rate track as guidance to move slowly toward cost of service. Individual rates are designed with a +/- 2% bandwidth on the overall rate adjustment. Year 1 has an overall adjustment of 4.0%; therefore, no class would see an increase less than 2.0% or greater than 6.0%.

Projected Revenues Under Proposed Rates By Class

Customer Class	Projected	Projected	Projected	Projected	Projected	Projected
	Revenues Under Current Rates	Revenues Under Proposed Rates Year 1	Revenues Under Proposed Rates Year 2	Revenues Under Proposed Rates Year 3	Revenues Under Proposed Rates Year 4	Revenues Under Proposed Rates Year 5
Residential	\$ 9,570,665	\$ 10,030,742	\$ 10,490,818	\$ 10,754,225	\$ 11,030,355	\$ 11,316,008
Residential Solar	213,018	213,018	213,018	213,018	213,018	213,018
Yard Lighting	6,942	7,220	7,508	7,659	7,812	7,968
Small Commercial	2,276,554	2,344,341	2,409,297	2,447,544	2,485,791	2,524,037
Medium Commercial	3,081,431	3,161,514	3,261,859	3,302,020	3,350,477	3,398,895
Large Commercial	1,893,714	1,941,867	1,990,002	2,003,172	2,016,342	2,029,511
Commercial Solar	5,569	5,569	5,569	5,569	5,569	5,569
Pumping	134,207	141,045	149,579	154,082	158,285	163,989
Totals	\$ 17,182,100	\$ 17,845,316	\$ 18,527,650	\$ 18,887,288	\$ 19,267,648	\$ 19,658,995

Projected Rate Change By Class

Customer Class	Projected	Projected	Projected	Projected	Projected
	Percentage Change Year 1	Percentage Change Year 2	Percentage Change Year 3	Percentage Change Year 4	Percentage Change Year 5
Residential	4.81%	4.59%	2.51%	2.57%	2.59%
Residential Solar	0.00%	0.00%	0.00%	0.00%	0.00%
Yard Lighting	4.00%	4.00%	2.00%	2.00%	2.00%
Small Commercial	2.98%	2.77%	1.59%	1.56%	1.54%
Medium Commercial	2.60%	3.17%	1.23%	1.47%	1.45%
Large Commercial	2.54%	2.48%	0.66%	0.66%	0.65%
Commercial Solar	0.00%	0.00%	0.00%	0.00%	0.00%
Pumping	5.10%	6.05%	3.01%	2.73%	3.60%
Totals	3.86%	3.82%	1.94%	2.01%	2.03%

Conclusions

- 1) The cost of service study indicates that some customer classes are paying above cost of service and some below cost of service. The proposed rate designs move toward cost of service in a gradual manner to limit potential impacts on customers.
- 2) The cost of service study indicates that all customer classes are paying customer charges below cost of service. The proposed rate adjustments include movement toward cost-based customer charges. HLP cost of service results are common and the residential cost-based customer charge is lower than similar utilities to HLP.

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UFS Qualifications

Utility Financial Solutions, LLC (UFS) has provided cost of service and rate studies for electric utilities since 2001 and is one of the largest providers of electric rate studies in the country. UFS has provided services to some of the largest and smallest public power systems in the United States, Cooperatives and Investor-Owned Utilities. UFS is an international firm providing rate studies in over 38 states, Barbados, Bermuda and Guam. Examples of some of the electric studies include Nashville, TN; Naperville, IL; Lansing, MI; Rochester, MN; Barbados; and Keys Energy, FL. Mark Beauchamp, the president of Utility Financial Solutions, LLC has been in the utility industry since 1981 and provided electric rate studies since 1990. Due to our reputation, we are instructors for electric cost of service for the American Public Power Association and the National Association of Regulatory Utility Commissioners (CAMP NARUC Program) offered through Michigan State University. Mark is a frequent speaker at regional and national conferences around the nation on industry rate trends and cost of service.