

Capital Credits: The Cooperative Way of Doing Business

Graham County Electric and Graham County Utilities have allocated 2012 capital credits to members.

If you have not received notification of capital credits, you soon will. The following article is intended to answer some of your questions regarding your capital credit allocation.

Unlike many other businesses, cooperatives do not have shareholders who expect to make money from the operation of the company. Instead, consumers of a cooperative are member-owners of the company.

In an investor-owned business, the money remaining after paying all expenses—the net margins—is profit and belongs to the company. Some of the profits are reinvested in the business to provide additional capital, but most are used to pay dividends on stock held by investors.

The primary objective of an investor-owned company is to make a profit. Your rural electric cooperative is different. It is a nonprofit business that exists solely to provide its members with electricity. In a co-op, net margins do not belong to the company; they belong to individual consumers who paid money on their monthly service bills.

In effect, the consumers of a cooperative are the shareholders. Because of that, when the cooperative takes in more money than is needed to run the business, the owners are entitled to a share.

That is the philosophy behind what is known as member equity, or capital credits.

What are capital credits?

Because Graham County Electric Cooperative and Graham County Utilities are cooperatives owned by the members they serve, they do not earn profits. Instead, any revenues over and above the cost of doing business are considered margins.

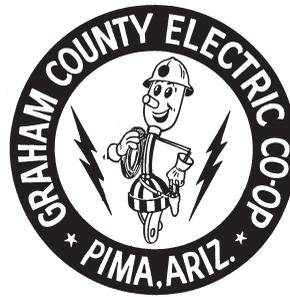
These margins represent an interest-free loan of operating capital by the membership to the cooperative.

To a certain extent, this allows the co-op to finance operations and new construction without borrowing money that would incur interest and necessitate rate increases.

What is the difference between allocated and retired capital credits?

Allocated capital credits appear as an entry on the permanent financial records of the co-op and reflect your equity or ownership in Graham County Electric and Graham County Utilities.

When capital credits are retired, a check is issued to you, and



your equity in the co-op is reduced.

How do I start accumulating capital credits?

Capital credits are calculated for everyone who purchased electricity during a year in which the utility earned margins. No special action is required to start a capital credits account. Membership in the co-op activates your capital credits account.

How are capital credits calculated?

The amount of capital credits you earn in a given year is based on the amount of capital you contribute to the co-op through payment of your monthly bills. The more electricity you buy, the greater your capital credits account.

The sum of your monthly bills for a year is multiplied by a percentage to determine your capital credits.

What percentage is used to determine the amount of my capital credits?

The percentage of your total payment allocated as capital credits varies from year to year, depending on the margins earned by the co-op during the year being considered.

Capital credits are only allocated for years in which the co-op earns margins. Since capital credits are a member's share of the margins, no credits are allocated for years with no margins.

Do I have to be a customer for an entire year to earn capital credits?

No. Capital credits are calculated based on a member's monthly bills. If you are billed for service for even one month, you will accumulate capital credits if margins are earned in that year.

Can I use allocated capital credits to pay my bill?

No. Allocated capital credits may not be used to pay current



bills. Your electric bill is due now. You may not receive capital credits for many years.

Who determines when capital credit allocations may be retired?

The co-op must maintain a certain equity ratio that is set by the Arizona Corporation Commission and our lender, the National Rural Utilities Cooperative Finance Co., to be permitted to retire capital credits.

When that criterion is met, the board of directors decides when or if capital credits will be retired.

What happens to my capital credits when I leave the co-op?

Your capital credits remain on the books in your name until they are retired. Because capital credits may be retired many years after they are earned, you should make sure the co-op always has your current mailing address.

Why not just break-even?

Since the co-op is not in business to make money, it might seem like it should establish a budget and rates that would allow it to merely break even each year, rather than show a profit.

That is not possible—or desirable.

The business of building power lines is expensive and much more so in a rural setting than in a population dense area, such as those owned by investor-owned companies.

Maintaining the lines is subject to outside forces—most notably, the weather.

It would be impossible for an electric cooperative manager to plan the operations of a cooperative so precisely in advance that revenues and expenses come out exactly even at the end of the year.

Like other businesses, electric cooperatives must have money on hand to provide current operating funds and a reserve for the unexpected, such as storm damage.

The past few years brought unprecedented growth and escalated fuel and material costs. Growth requires new power lines and substations to meet load demands.

The cooperative also must have sufficient margins from its operations to repay any principal on loans.

When you receive your Notification of Capital Credits, you will see that for consumers who purchased power in 2012, there is an allocation from Arizona Electric Power Cooperative.

AEPCO is the generation cooperative that supplies the power we deliver to your homes and businesses. As a cooperative, it does business in the same way we do.

More than one-third of Graham County Electric's equity consists of unretired capital credit allocations from AEPCO. ■