

# **EQUITY MANAGEMENT**

**LA PLATA ELECTRIC ASSOCIATION, INC.**

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- What is Equity?
  - Why Retire Equity?
  - Financial Models
  - Retirement Options
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# WHAT IS EQUITY?

- Balance Sheet
  - Shows what LPEA owns and owes at a given point in time
  - Assets = Liabilities + Equity
    - Assets – Liabilities = Members Equity
  - **What is owned – What is owed = What is left**

# WHAT IS EQUITY?

- Capital Credits
  - Member Equity
  - Patronage Capital
  
  - Revenue above the cost of operations assigned back to the member
  - Ownership interest of the cooperative by the members
  - Requirement of being a cooperative
    - Uniform System of Accounts
    - IRS, State of Colorado
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# ALLOCATION

- Policy 205
  - Operating Net Margins – Value Method (\$)
    - Member Gross Purchases ÷ LPEA's Gross Operating Sales X LPEA's Net Operating Margin
  - Non Operating Margins – Quantity Method (kWh)
    - Member kWh Purchases ÷ LPEA's Gross kWh Sold X LPEA's Non Operating Margins
      - G&T Allocations tracked separately
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# WHAT IS EQUITY USED FOR?

- Capitalization of the Cooperative
    - Substations, Poles, Wires, Transformers, Meters, Rolling Equipment, etc.
    - Combination of Debt & Equity
      - Lowering one raises the percentage of the other
  - Financial Benefit of Maintaining  $\geq 40\%$  Equity
    - Discount of 12.5 Basis Points on LT Debt
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## HOW DOES EQUITY AS A % OF ASSETS MOVE?

- Retiring Equity
    - Not a 1 to 1 ratio
      - Both Numerator and Denominator Change
  - Acquiring / Pay-off Debt
  - Margins – Positive and Negative
    - Not 1 to 1 – Assets may move
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## WHY RETIRE EQUITY?

- IRS / State Law
    - Lawsuits in other states against co-ops which did not retire
  - Part of being a cooperative
  - Cost of debt of members vs. Cost of debt of the cooperative
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# FINANCIAL MODELS

- Goodwin Formula
    - Rate of Return on Equity Based on Maintenance of Equity
  - Boatman Theorem
    - Rate of Return on Equity - Growth of Capital = Equity Returned
  - Capital Credits Retirement Cycle
    - Goal in Years
    - 20 Years =  $1/20 = 5\%$
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# RETIREMENT

- Bylaws – Article VII, Section 3
    - FIFO (First In, First Out)
    - Percentage Basis
    - Combination
    - Any other reasonable method
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# RETIREMENT

- FIFO
    - Capital Credits don't get as old
      - Easier to find former members when they aren't as old
      - Retire more to member vs. estate
  - Percentage Basis
    - Newer members get retirement of equity
  - LPEA has been doing 75% FIFO & 25% Percentage Basis
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# DISCUSSION

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