



**FREESTATE ELECTRIC
COOPERATIVE, INC.**

The Outlet

FreeState Electric Cooperative, Inc.

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Member Notice

FreeState Electric Cooperative experienced low sales due to mild weather and has entered into a revenue requirement study. This study will provide the board of trustees a road map for future revenue and the financial requirements of the cooperative.

FROM THE CEO

We Will Get Through This Together

We have all become experts in change over the past two months.

The routine of life we were comfortable with has completely changed. What we consider normal has shifted. That old saying of “the only thing that stays the same is change,” comes to mind. And, we have all made adjustments to get through these uncertain times because life requires it. We do what we have to do to make it all work. Our ability to adjust helps us all in the long run. We are undoubtedly stronger, we are better at reacting, and are ready to handle whatever comes next.

The cooperative is no different. The global COVID-19 pandemic has forced us out of our comfort zone.

This issue of The Outlet is going to address financial transparency and where we are, and how uncertain everything is moving forward. We are not presenting doom and gloom content by any means, but we feel it is right to let our members know that we are seeing some trends that have caused concern about our finances, and that we are realizing that action needs to be taken sooner than later.

There are many factors that have driven a decline in revenue, and we'll discuss that more in this issue, but it seems as though the global pandemic has caused commercial closures that have amplified already low kilowatt-

hour sales due to warmer weather patterns and changes in how our members use energy. We expect this trend to continue.

In the past four years, we have maintained the promise to our members that the consolidation would not change your standard of service or the cost per kilowatt-hour. Members have not seen any adjustment to service charges or rates since 2010 (East District, prior LJEC) and 2012 (West District, previous Kaw Valley). For the past decade, we have worked tirelessly to maintain affordability. No changes in at least a decade is an accomplishment, considering how everything changes much more frequently. For example, the nearby investor-owned utility has increased rates on their consumers 39



Steve Foss

“The investor-owned utility has increased rates on their consumers 39 times in 10 years. FreeState has made no changes in that same time frame.”

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FINANCIAL TRANSPARENCY

Costs and Temperatures Rise

A mild winter. Milder summers. Changing weather patterns put extra pressure on cooperative finances as costs continue to rise.

A milder winter than normal was a bonus for most, but for FreeState it meant kilowatt-hour sales plummeted. In a business whose budget is dependent on the weather, it was anything but good news.

Pair a lack of sales with the COVID-19 pandemic and FreeState was put into a precarious position.

“It seemed like things were coming at us from every direction,” said **STEVE FOSS**, FreeState CEO. “Right before the pandemic hit, we were entering into a revenue requirement study (RRS) and just as we were getting a handle on that and preparing to discuss everything with our membership at the annual meeting, the board had to make the difficult decision to cancel the meeting.”

FreeState joined cooperatives across the country in making the decision to put public health ahead of cooperative business.

“We just couldn’t risk it,” said **JEANINE MURPHY**, board president, regarding the annual meeting. “Our most loyal members are some of those who are most vulnerable and the amount of work that goes into planning a meeting with no apparent timeline of when it would be safe to meet again – we just decided to do what was best.”

“That’s our job,” said Murphy. “To do what is best for the overall health of the cooperative and our communities.”

Foss (and Murphy) said financial health is also a big part of the equation, and that FreeState had been analyzing data and financial forecasts since late 2019. The outlook was not as positive as expected and being transparent with members was also top of mind.

“Sales have been down because our weather has been good,” Foss said. “We had to start looking at what we needed to do in order to make up some ground and we discussed entering into a RRS not expecting a pandemic to break out. But, regardless of the situation we’re in, we want to be upfront with our members and provide information to them that may impact them later, because it’s the right thing to do.”

According to the Energy Information Administration, collected data shows that 2017 was the first year that residential electricity sales fell at a significant rate, and they have contin-

ued a downward trend due to rising temperatures in months that are typically very cold or very hot. There are factors that can contribute to using less electricity. Factors like energy efficiency practices and renewable energy. But, the biggest factor in the change in electricity usage is weather.

Utilities typically see spikes in usage from December to February, and from June to September. These are the coldest and hottest months when heating and cooling are used the most. However, the warming winter temperatures have changed how consumers use electricity.

“Electric demand is highly dependent on weather,” said Foss. “If we look at the heating degree days, which are the daily temperature differences compared with a base temperature of 65 degrees, the past couple of winters have been warmer than normal. And, that coupled with milder summers means we have fewer sales than we budgeted for.”

Foss said that national weather data and heating and cooling degree day data are utilized in financial forecasting for the co-op.

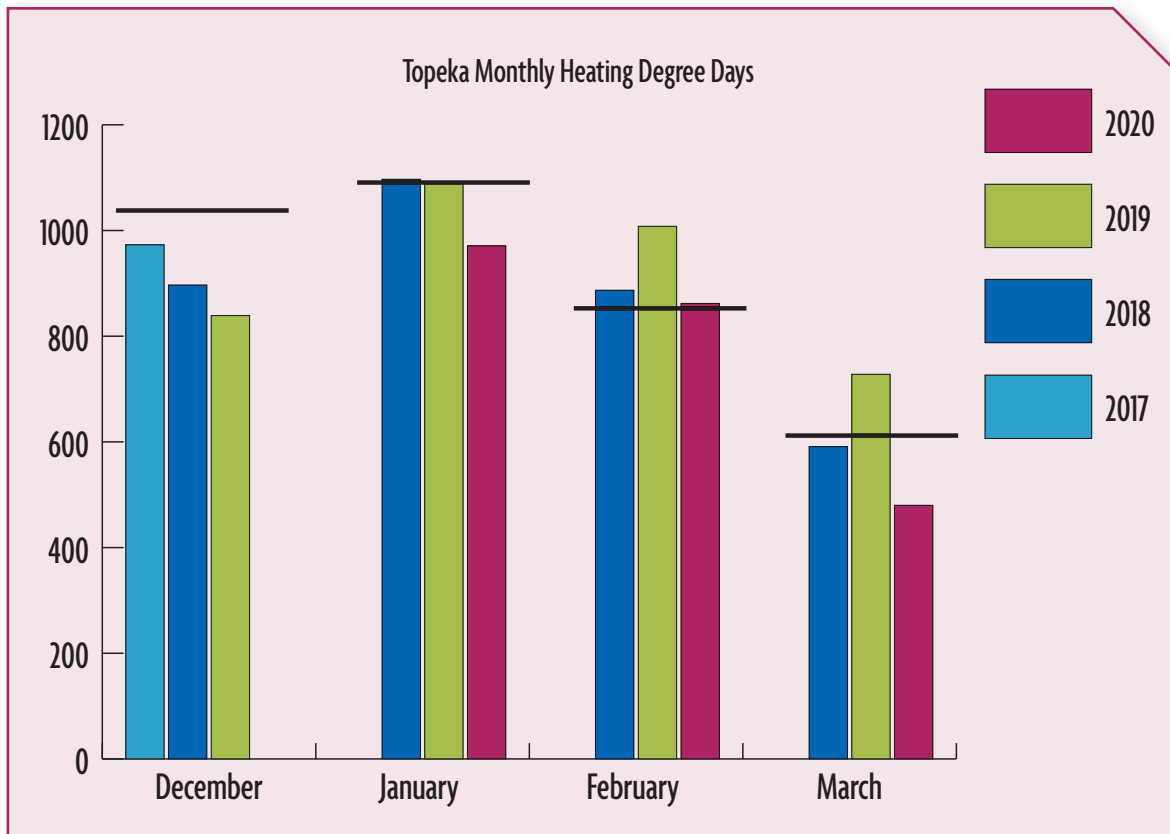
“We use the data to estimate sales and revenue,” Foss added. “But the data we use to forecast with is about 10% in either direction of the actual weather and that is out of our control.”

JILL TAGGART, FreeState’s finance manager, who assists executive management in determining the financial requirements for the co-op, said that relying on weather data to forecast revenue is a practice many utilities have used for decades.

“It’s not a new practice, but FreeState wants to move away from using weather as a primary factor,” Taggart said.

“It’s way too volatile,” added Taggart. “Averages just aren’t as accurate and are not something we want to be dependent on when we forecast our budget in order to meet our financial goals.”

Foss says the board of trustees and executive management along with Taggart have been closely monitoring the variation of revenue. The trend in the numbers made it clear what the cooperative has to do. But when the cooperative will take action remains tentative due to the global COVID-19 pandemic, which has not only impacted residential accounts due to the increase in unemployment and financial uncertainty but



This graph demonstrates the months FreeState typically sees above average sales. The increase in average temperature means FreeState's kilowatt hour sales have declined, putting financial pressure on the cooperative. The graph illustrates the last three years of heating degree day data. The solid black line shows the average for the month. The added pressure has meant cutbacks where possible, and entering into a revenue requirement study to evaluate the financial needs moving forward. This is not a cost-of-service study.

SOURCE: NOAA

has also shut down some of the co-op's largest commercial accounts. Closing the doors on businesses and schools has dropped kWh sales and pushed revenue further down.

"We do know that if we want to make a significant positive impact to our revenue by making just a small adjustment to our electric service charge, we need to do it as soon as possible," Foss said. "But the current timing is terrible. We want to make sure that when we make adjustments, they are small and incremental, but we also want to make sure that our members are not burdened any more than they are now."

"There never is a right time for us to make any adjustments," said Foss. "We want to meet our financial goals, but we want to take care of our members first. They are our priority here."

Foss added that instead of members bearing all the brunt of decreased revenue, the staff at FreeState, along with the trustees started looking at costs and making cuts to everything unless it was a necessity to provide the standard of customer service members expect in a safe manner.

"If it's not necessary we are cutting it," said Foss. "We are going to look at every cost from post-it notes to poles."

The cooperative entered into the RRS to see what adjustments were necessary to the service charge, not the kilowatt-hour rate. Taggart started working on the RRS for FreeState in February when the weather continued an upward trend and sales continued downward. It was clear the numbers were not going to correct themselves.

"This is not a cost-of-service study — that I want to make clear," said Taggart. "This is a way we can get a comprehensive and detailed look at everything so we can determine what our next steps will be."

"Think of this as our financial road map," Taggart added.

Foss said the objective of the study is to determine not only a plan, but how small the adjustments can be to still make an impact without putting a burden on members.

"Our goal from day one has been to push that costly cost-of-service study out as far as we can," said Foss. "This detailed analysis that [Jill] Taggart is doing for us is going to identify ways we can increase revenue while cutting spending to delay a full cost of service study."

Foss says weather was the most significant factor when looking at variances to start the revenue requirement study. FreeState operates as close to cost as possible, but even a small variance in overall revenue can make a big impact on the bottom line and that's what Foss and the FreeState team want to avoid the weather dependency.

The milder winters for the past three years have impacted overall kilowatt hour sales. Comparing the past three years, 2020 (and December of 2019) have been much warmer than average, and that can put financial pressure on the cooperative.

"It is not doom and gloom, by any means," said Foss. "This is a necessary measure for us. Because we must maintain

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FROM THE CEO

Staying Grounded

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times in the past 10 years. FreeState has made zero changes in that same amount of time.

Costs are rising all around us. In the past five years, we have seen a significant increase in operating expenses. The cooperative's operating costs increased by 10% from 2015 to 2019. As I write this, we've had a very mild start to 2020, and an early warmup this spring means the co-op's revenue from kilowatt-hour sales has fallen 5% below our projections for this time of year putting even more pressure on our finances.

We have seen increases in the cost of materials like poles, wire, transformers, and other infrastructure items. Labor costs, transportation, and escalating environmental compliance costs have all impacted the cooperative.

Please know that we here at the cooperative know the timing is never good. We understand that members are facing much uncertainty at this time. An adjustment is imminent and we know we have to do something sooner rather than later, but FreeState is committed to making those adjustments when the outlook has improved. The last thing we want to

do is put additional financial burden on our members.

Our financial goals are important, but our members are more important. You are all the reason we are here. We work for you, and we will continue to do so no matter what lies ahead.

We have taken measures at the cooperative to mitigate costs. We're cutting back on all expenditures, and we've worked to evaluate all of our expenses. We are working on reducing the costs we can control because many of our costs and other factors in distributing electricity are outside of our control.

We live by the cooperative difference — as a cooperative, we are member- and service-driven and operate as close to cost as possible. Our goal is to not make a profit, and we do not make a profit for shareholders. We return overages to our members in the form of capital credits. In the past three years, we have returned over \$2.25 million in capital credits, including a consolidation credit of \$800,000 to all members. We have also returned \$750,000 in margin stabilization to our East District members. We focus on keeping the business financially secure on behalf of all our members so we can provide the safest, most reliable service at the lowest practical cost.

AS ALWAYS, WE ARE HERE TO HELP. IF YOU HAVE QUESTIONS ABOUT THIS CONTENT OR YOUR MEMBERSHIP WE ENCOURAGE YOU TO CONTACT US AT 800-794-1989 OR EMAIL CUSTOMERSERVICE@FREESTATE.COOP.

FINANCIAL TRANSPARENCY

Costs and Temperatures Rise *Continued from page 16C ▶*

financial security and we need to look at all avenues to do that without raising kilowatt-hour rates, and if we can do that with small incremental adjustments to the electric service charge, then that's what we will look at."

In addition to doing the RRS, FreeState has made cuts to the costs the cooperative can control, unfortunately, more than three-quarters of the cooperative's expenses are not controlled by the cooperative.

"Power costs are not something we can control," said Foss. "And, they keep rising. Mix those costs in with the

increased costs of environmental regulations, property taxes, materials, labor and transportation and it just doesn't seem to get any easier."

"The last time we had any sort of change was the last time rates were adjusted," Foss said.

Rates were adjusted in 2010 for the former LJEC (East District) and 2012 for the former Kaw Valley (West District).

"To say we have been able to stay steady for the better part of a decade is quite an accomplishment, especially when everything else we utilize has gone up," Foss said. "Consumer goods

and services just keep getting more expensive, but our cost of electricity has stayed consistent in that amount of time."

"The primary goal of FreeState's board and management is to provide the best member experience and service around," added Foss. "And, we'll continue to do that. However, there comes a time when we must look at making adjustments to meet our financial obligations."

Foss said the board and staff understand that members are seeing a lot of uncertainty at this time and are doing what they can to assist members who are impacted by this unprecedented situation.

Members facing financial hardships due to the COVID-19 pandemic and extended time under stay-at-home orders are encouraged to call the office at 800-794-1989 to discuss assistance options.

Actions Held Due to Pandemic

MEMBERS ARE PRIORITY DURING THIS TIME

As FreeState completes the revenue requirement study, additional information will be forthcoming. The board of trustees recognizes the uncertainty members are facing during the current global pandemic and have elected to reevaluate when adjustments will be made. In the meantime, staff will continue to make spending cuts to prevent member burden and delay adjustments.