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June 30, 2000

FILED

JUN 30 2000

Missouri
Public Service Commission

Mr. Dale Hardy Roberts
Secretary/Chief Regulatory Law Judge
Missouri Public Service Commission
P.O. Box 360
Jefferson City, MO 65102

**Re: Le-Ru Telephone Company
Case No. TF-2000-428**

Dear Mr. Roberts:

Enclosed please find the original plus eight (8) copies of Suggestions in Support of its Request for Financing Authority for filing on behalf of Le-Ru Telephone Company in the above referenced matter. Please note that certain of the exhibit to the Suggestions are marked "Proprietary". Le-Ru has requested that the Commission issue a Protective Order in this case so that this confidential information may be treated in accordance with that Order.

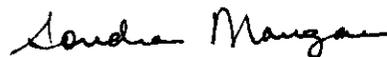
Please bring this matter to the attention of the appropriate Commission personnel. A copy of this filing is being sent to all parties of record.

Thank you for your attention to this matter.

Very truly yours,

BRYDON, SWEARENGEN & ENGLAND P.C.

By:



Sondra B. Morgan

SBM/k

Enclosures

cc: Office of Public Counsel
Mr. Dennis Frey
Le-Ru Telephone Company
Mr. Tim Goodger

**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

FILED
JUN 30 2000

Missouri Public
Service Commission

In the matter of the Application)
of LE-RU TELEPHONE COMPANY)
for authority to borrow an amount)
not to exceed \$9,164,700 from the)
Rural Utilities Service, the Rural)
Telephone Bank and the Federal)
Financing Bank and in connection)
therewith to execute an Amending)
Telephone Loan Contract Amendment,)
Promissory Notes, and a Restated)
Mortgage, Security Agreement and)
Financing Statement.)

Case No. TF-2000-428

**LE-RU TELEPHONE COMPANY'S SUGGESTIONS
IN SUPPORT OF ITS REQUEST FOR FINANCING AUTHORITY**

Comes now Le-Ru Telephone Company ("Le-Ru" or "Company") and for its Suggestions in Support of its Request for Financing Authority states to the Missouri Public Service Commission ("Commission") as follows:

1. On June 7, 2000, the Commission issued its Order Directing Filing and Scheduling Hearing in which it directed the parties to file additional information regarding the proposed financing and scheduled a hearing before the Commission.

2. On June 23, Staff filed the additional information requested by the Commission. Le-Ru has no objection to the information filed by Staff in response to the Commission's Order and offers the following information and Suggestions in Support of its Application for approval of financing.

Le-Ru is a small, local exchange company with approximately 1,471 access lines in two exchanges in Southwest Missouri. The area where the two exchanges are located is experiencing

substantial growth due to the development of the Northwest Arkansas area just across the state line and because the area is now served by a rural water district making development of the area more feasible. Many of the persons moving into the area are retirees or persons building second, vacation homes who are accustomed to high-quality telecommunications services including high-speed Internet.

In planning for the growth in its exchanges, Le-Ru realized that it was necessary for the Company to borrow funds in order to be able to meet the need for more access lines and to upgrade its lines so that its customers could have access to the latest technology including high speed Internet services. Le-Ru began its negotiations with the Rural Utilities Service ("RUS") to obtain this loan in the fall of 1998. As anyone who has borrowed money from RUS can attest, the process involved in obtaining these loans is time-consuming and involves considerable Company resources. The total time involved before final approval and funding is often in excess of two years. Because of the time and work involved, small local exchange companies like Le-Ru typically borrow a substantial sum of money at one time so that the process will not have to be repeated within a few years. However, when a small company like Le-Ru borrows a large amount of money such as Le-Ru has requested in this application, it can "flip" the company's capital structure, and the ratio of equity to debt is reversed. This is the case in this proceeding and is the situation which is causing the Commission and its Staff concern.

When the history of the Company and its previous borrowings is reviewed, however, it shows that the debt to equity ratio is not the determining factor when considering the ability of the Company to meet its debt payments or to continue to operate as a successful telecommunications Company. Le-Ru first borrowed funds from the Rural Electrification

Administration ("REA") in 1982. The Company filed a request for authority to borrow \$1,940,000 with the Commission in Case No. TF-82-190. At that time the Company had an equity ratio of 14.4%, but the pro formas filed with the application showed that after the Company had drawn down all of the funds requested, its equity ratio would drop to less than 3%. The Commission approved the application without comment. In 1993, Le-Ru filed an application with the Commission requesting authority to borrow an additional \$1,610,000 from REA. The pro formas filed with that application showed that the Company's equity ratio would dip down to 24%. The Commission approved this application stating that "even though the resulting levels of equity will be low according to the pro forma capital restructuring, the solid coverage ratios and the nature of the REA debt and low interest costs make the financing reasonable." Order Approving Financing, Case No. TF-93-273, at page 3.

As can be seen from the attached financial schedules, Le-Ru was able to increase its equity ratio to over forty percent in 1994 and has kept it there until the present. (Exhibit 1) Now, in this request for authority to borrow, its projected financials show that after Le-Ru has drawn down the requested funds,¹ its equity ratio will be 17.72%. The Company has prepared projections which show that it will not be able to bring its ratio up to 40% until 2007 (five years after the construction is completed). (Exhibit 2)² As its history shows, however, Le-Ru has been

¹After discussion with Staff, Le-Ru by letter to Mr. David Winter agreed to reduce the total project from \$9,164,700 to \$7,800,606 through the elimination of the proposed business office and warehouse.

²These projections as well as other financial information provided with these Suggestions have been marked "proprietary." Le-Ru filed a Motion for Protective Order with the Commission on June 29 requesting that an order be entered allowing the Company to file this sensitive information as proprietary.

able to repay its debt, operate its Company and provide service to its customers with equity ratios much below 17%. (See Exhibit 1)

Le-Ru appreciates the Commission's concern regarding its equity ratio, but the Company believes that its past history demonstrates that a low equity ratio does not mean that the Company will not be able to operate its business or provide satisfactory service to its customers. RUS and the Rural Telephone Bank as lenders review the Company's financial situation in depth before they approve the loan. These entities are satisfied that Le-Ru will be able to meet its debt obligations and are prepared to lend the funds to Le-Ru. These lenders look at other indicators to determine if a Company is financially sound and if it has the ability to repay the indebtedness. RUS primarily considers the company's cash flow to insure that it will be able to meet its debt service. RUS looks at the company's equity to assets ratio as well and does place restrictions on the company as to the payment of salaries and dividends if the ratio is low, but it does not refuse to advance the funds based solely on a company's capital structure.

Le-Ru believes that the decisions regarding the capitalization of the Company are management decisions which must be made by the Company in deciding how best to operate the Company and provide the best service to its customers. Le-Ru realizes that its equity ratio will be low, but it believes that the borrowing is necessary in order for the Company to construct the facilities necessary to support the increased growth of the area and provide the services and new technology necessary in today's telecommunications market. While a large Company with more investment can perhaps manage to upgrade its facilities without going below a 40 percent equity ratio, a small Company such as Le-Ru simply does not have that ability. If Le-Ru is going to upgrade its facilities, it will have to borrow the money, and the debt from that borrowing will

cause its equity ratio to fall. Le-Ru has made the management decision that this construction is necessary to the Company's future and is in the best interests of its customers.

The Commission has recognized in previous decisions that a Company's equity ratio is a matter within the discretion of the Company's management. *Re Missouri Public Service*, 22 Mo.P.S.C. (N.S.) 193, 195 (1978). Likewise, in *Re Southwestern Bell Telephone Company*, 16 Mo.P.S.C. (N.S.) 379, 382 (1971), the Commission observed that the:

establishment of capital structure is primarily within managements prerogative. It is the obligation of management, who lives with the detailed and exacting problems of corporate financing on a daily basis, to see to it that the corporation maintains its financial ability to meet its public responsibilities.³

In a more recent case, the Commission stated:

The Commission has, in the past, generally avoided interjecting itself in the management of the various investor-owned utilities that it regulates. The Commission currently does not favor becoming engaged in the micro-management of those companies through its regulatory authority.

Re Missouri Gas Company, 3 Mo. P.S.C. 3d 216, 220-221 (1994). A utility's ownership of its business and property includes the right of control and management. In *State ex rel. Harline v. Public Service Commission of Missouri*, 343 S.W.2d 177 (Mo. App. 1960), the Western District Court of Appeals stated that the Commission's powers do not "clothe the Commission with the general power of management incident to ownership. The utility retains the lawful right to manage its own affairs and conduct its business as it may choose, as long as it performs its legal duty, complies with lawful regulation and does no harm to the public

³In the *Southwestern Bell* case the Commission Staff argued that the Company should reduce its equity position because the cost of equity in the Company was more than the cost of debt. This is true in this case as well.

welfare." *Id.* At 182. Thus, the Company should be able to make management decisions which impact its capital structure without unnecessary interference from the Commission through the regulatory process.

The upgrades to be completed with the funds from this financing are needed in order for the Company to be able to provide service to new customers in this area of rapid growth and to provide the improved service necessary so that these customers will be able to have access to high-quality voice and data services. The Company has prepared a summary of the growth patterns for both the Stella and Powell exchanges which is attached as Exhibit 3. This chart shows that the annualized growth percentages for the year 2000 for the Powell exchange is 10.8% and for the Stella exchange is 11.6%.

Although the upgrades could conceivably be completed in steps, it makes economic sense to do them all at once. Like borrowing money from RUS, the planning, engineering, and construction involved is more economical when done all at once. When materials are ordered and construction crews brought in, it makes sense to complete all of the necessary construction at one time. Le-Ru will also be able to see the benefits and increased revenue from more access lines and more services to existing customers if it is able to complete all of the upgrades at one time. As is shown on its annual reports filed with the Commission, the Company has used \$1,369,653 of its own revenues to finance capital expenditure within the last five years. (See, Annual Reports for years 1994-1995 filed by Staff on June 23.) The Company will also spend approximately \$400,000 in 2000 on line upgrades and new service order construction. (See, Exhibit 3, p.1) But in order to complete all of the construction needed in a reasonable time frame, the Company believes that it is necessary to borrow the funds and complete the project as

expeditiously as possible.

In its Order Directing Filing and Scheduling Hearing, the Commission asked Le-Ru to present and address any "benefits, detriments, issues or obstacles" to achieving an equity ratio of 40 percent within years two through five. The Company has prepared schedules showing the amounts necessary to bring the equity ratio up to 40 percent either through a capital infusion or through debt reduction. (See Exhibit 4) As can be seen from these schedules, the amounts necessary to bring the equity ratio up to 40 percent are daunting and cancel any benefits to be gained from the borrowing. For example, in year 2002 after the construction is completed and all of the funds have been drawn down, to bring the equity ratio to 40 percent would require an infusion of equity capital of \$4,275,000 or a reduction in debt of \$6,400,000. These numbers decrease with each additional year, but it is only after five years, or in 2007, that the numbers are low enough to represent a realistic infusion of capital or debt reduction. In its projections previously provided to the Staff, Le-Ru has set out projections for achieving the 40 percent ratio which it believes are realistic and achievable. (See, Exhibit 2) These projections show that the Company will be able to achieve forty percent equity five years after the completion of the construction, or 2007.

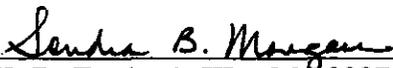
Thus, if the Commission makes the achievement of a 40 percent equity ratio a condition of its approval of the financing, Le-Ru will not be able to complete the financing or the proposed construction. The Company sees no benefits to achieving this ratio earlier, and the detriments will be that the Company's customers will not receive the improved services nor will the Company be able to receive increased revenues from the addition of CLASS services.

In its Order the Commission asked the Staff and Company to provide information

regarding the dividends paid by the Company for the last five years. This was provided to the Commission by Staff on June 23 in Exhibit 6. As can be seen from reviewing this schedule, the Company maintained an equity ratio of at least forty percent while paying the dividends. It should be noted that the dividend paid in 1998 reflects the payment to shareholders from the sale of Le-Ru's cellular interest which was not a part of the Company's revenue from providing telecommunications service. Le-Ru is a subchapter S corporation which means that the Company does not pay federal or state income tax. The corporation's revenues and expenses are passed through to its shareholders who in turn report the revenue and expenses on their individual returns. The tax liability of the shareholders for the last five years is set out on page 2 of Exhibit 6 filed by Staff, and the tax liability of the individual shareholders is paid from the dividends of the Company.

Wherefore, Le-Ru respectfully requests that the Commission consider these Suggestions and the accompanying information attached in the exhibits and grant the relief requested in its Application.

Respectfully submitted,



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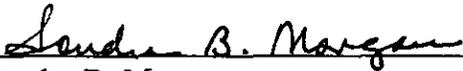
Attorneys for Le-Ru Telephone Company

Certificate of Service

I hereby certify that a true and correct copy of the above and foregoing document was hand-delivered this 30th day of June, 2000 to:

Mr. Mike Dandino
Office of the Public Counsel
P.O. Box 7800
Jefferson City, Missouri 65102

Mr. Dennis Frey
Missouri Public Service Commission
P.O. Box 360
Jefferson City, Missouri 65102



Sondra B. Morgan

LE-RU TELEPHONE COMPANY
 CAPITAL STRUCTURE
 YEAR ENDED DECEMBER 31,

FILED

JUN 30 2000

Missouri Public
 Service Commission

EXHIBIT 1
 Page 1 Of 2

	<u>1999</u>	<u>1998</u>	<u>1997</u>	<u>1996</u>	<u>1995</u>	<u>1994</u>	<u>1993</u>	<u>1992</u>	<u>1991</u>	<u>1990</u>
Long-term debt	\$ 2,901,053	\$ 2,957,293	\$ 2,976,110	\$ 3,005,493	\$ 2,839,532	\$ 2,885,910	\$ 2,747,586	\$ 2,161,443	\$ 2,251,438	\$ 2,339,077
Equity	2,113,037	2,450,471	2,648,391	2,219,965	2,194,149	2,280,889	875,070	895,889	806,507	746,339
Capital	<u>\$ 5,014,090</u>	<u>\$ 5,407,764</u>	<u>\$ 5,624,501</u>	<u>\$ 5,225,458</u>	<u>\$ 5,033,681</u>	<u>\$ 5,166,799</u>	<u>\$ 3,622,656</u>	<u>\$ 3,057,332</u>	<u>\$ 3,057,945</u>	<u>\$ 3,085,416</u>
Equity to Total Capital	42.14%	45.31%	47.09%	42.48%	43.59%	44.1%	24.2%	29.3%	26.4%	24.2%

	<u>1989</u>	<u>1988</u>	<u>1987</u>	<u>1986</u>	<u>1985</u>	<u>1984</u>	<u>1983</u>	<u>1982</u>	<u>1981</u>	<u>1980</u>
Long-term debt	\$ 2,371,181	\$ 2,428,646	\$ 2,476,499	\$ 2,529,983	\$ 2,535,311	\$ 2,530,807	\$ 2,383,220	\$ 990,942	\$ 1,024,977	\$ 1,056,489
Equity	555,184	561,906	558,647	544,873	324,297	269,152	224,845	166,063	114,590	85,918
Total Capital	<u>\$ 2,926,365</u>	<u>\$ 2,990,552</u>	<u>\$ 3,035,146</u>	<u>\$ 3,074,856</u>	<u>\$ 2,859,608</u>	<u>\$ 2,799,959</u>	<u>\$ 2,608,065</u>	<u>\$ 1,157,005</u>	<u>\$ 1,139,567</u>	<u>\$ 1,142,407</u>
Equity to Total Capital	19.0%	18.8%	18.4%	17.7%	11.3%	9.6%	8.6%	14.4%	10.1%	7.5%

	<u>1979</u>	<u>1978</u>	<u>1977</u>	<u>1976</u>	<u>1975</u>	<u>1974</u>	<u>1973</u>	<u>1972</u>	<u>1971</u>	<u>1970</u>
Long-term debt	\$ 1,087,358	\$ 1,043,545	\$ 951,996	\$ 959,876	\$ 656,086	\$ 664,912	\$ 666,104	\$ 622,241	\$ 609,779	\$ 524,902
Equity	84,676	57,328	44,082	40,293	36,176	35,366	32,460	27,121	19,470	15,287
Total Capital	<u>\$ 1,172,034</u>	<u>\$ 1,100,873</u>	<u>\$ 996,078</u>	<u>\$ 1,000,169</u>	<u>\$ 692,262</u>	<u>\$ 700,278</u>	<u>\$ 698,564</u>	<u>\$ 649,362</u>	<u>\$ 629,249</u>	<u>\$ 540,189</u>
Equity to Total Capital	7.2%	5.2%	4.4%	4.0%	5.2%	5.1%	4.6%	4.2%	3.1%	2.8%

Le-Ru Telephone Company Capital Structure

