EUGENE WATER & ELECTRIC BOARD
WORK SESSION
EWEB BOARD ROOM
MARCH 19, 2013
5:30 P.M.

Commissioners Present: John Simpson, President; John Brown, Vice President; Dick Helgeson, James Manning, and Steve Mital

Others Present: Roger Gray, Debra Smith, Dean Ahlsten, Karen Lee, Sue Fahey, Edward Yan, Adam Rue, Michelle Martin, Deborah Hart, Anne Kah, Mark Freeman, Steve Newcomb, Mel Damewood, Lena Kostopulos, Roger Kline, Shelley Stephenson, Dan Morehouse, Cheryl Froelich, Todd Simmons, Tom Williams, Steve Mangan, Brad Taylor, Erin Erben, Megan Capper, Cathy Bloom, Wendi Schultz-Kerns, Lance Robertson, Matt Sayre, Gail Murray, Frank Lawson, Susan Eicher, Mike McCann, Patty Boyle, Dave Churchman, Mark Oberle, Wally McCullough, Sheila Crawford, Kathy Grey, Sibyl Geiselman, and Taryn Johnson of the EWEB staff; Vicki Maxon, recorder.

President Simpson convened the Work Session of the Eugene Water & Electric Board (EWEB) at 5:30 p.m.

RATE ADJUSTMENT FOR DARK FIBER LEASE

Debra Smith, Assistant General Manager, recalled the backgrounder that the Board had received from Dean Ahlsten, Compliance Manager, including the history of what EWEB has done relative to dark fiber. She noted that a consent calendar item will be brought to the Board on April 2 which modifies and adjusts EWEB's rates for this service.

Mr. Ahlsten reviewed a map of current and future fiber optic projects and a map of the Metro Internet project. Ms. Smith explained the multiplexing setup.

With the use of overheads, Mr. Ahlsten reviewed the current and future service provider rate calculations, assuming the rate would escalate with CPI on an annual basis. He then reviewed a dark fiber rate comparison of private companies vs. utilities, the projected dark fiber revenue from EWEB's current users, and the 2013 fiber job queue (active jobs, customer job requests, and EWEB jobs).

In summary:

- EWEB's telecommunications "asset utilization" strategy presently consists of a dark fiber lease-only business model
- Unused fiber is becoming scarce and in some cases is non-existent
- Over half of EWEB's installed fiber optic cable plant, consisting of 120 miles of backbone and 35 miles of lateral cables, is approaching the end of its service life
- Existing customer lease rates vary, making them more complex to administer

- Annual projected dark fiber revenue (post public agency network transition) is approximately $270,000 per year

Staff recommends that the Board standardize on a common rate for public agencies, higher education institutions and medical service providers, which includes all three rate components. K-12 schools would continue to enjoy the steeply discounted (currently 80%) rate consisting of only the operations and maintenance expenses. Staff wishes further discussion with the Board regarding their opinion regarding formal offering of a market-based commercial rate for short-term contracts.

Mr. Ahlsten responded to questions and comments from the Board.

Vice President Brown asked what liability EWEB has if there is a fire in a vault. Mr. Ahlsten replied that the priority for fiber is behind that of electric service, and that EWEB would not be liable.

Vice President Brown asked why EWEB is adjusting the rate now instead of five years ago. Mr. Ahlsten replied that rates are set according to a scale of CPI and then adjusted as needed, and that this adjustment is being done to true up some rate issues that have evolved over time.

Commissioner Helgeson asked if the fiber will have to be replaced at some point. Mr. Ahlsten replied that it has held up well but there can be external factors that affect it, deterioration over time, vibration, etc., but its service life is 20-25 years.

Ms. Smith reiterated that EWEB wishes to offer a consistent set of rates and that technology has changed a lot in the last 15 years, so the question is what EWEB needs to collect today in order to deal with eventual obsolescence.

Commissioner Helgeson said that in his mind, it is the distinction between what EWEB's requirement is to serve and what is driven by market considerations, and still be able to offer a good rate.

Commissioner Mital agreed with Commissioner Helgeson that a multi-pricing strategy seems best.

Vice President Brown voiced the desire for an expanded discussion, as he doesn't want to subsidize for-profit businesses. Ms. Smith replied that this in fact is EWEB's chance to true up and adjust rates for their fiber customers as part of their agreements with them, and that part of this true-up is the question of whether EWEB wants to look at some customers differently, i.e., profit vs. nonprofit.

Commissioner Manning also voiced the desire for further discussion, especially regarding EWEB providing fiber optics vs. only electricity and water.

President Simpson stated that in his mind it is a philosophical question of should EWEB align the rates vs. create different tariffs and encourage the sale of fiber to carriers who pay more than the basic rate.

Ms. Smith noted that EWEB doesn't currently have the resources to be able to do some of this work, but that six years ago EWEB had interested parties and wasn't able to deliver the service, and now that improvements have been made, they are in a better position to do so.

Vice President Brown clarified that he wouldn't have a problem raising the rates of some customers who should be in a totally different category. Mr. Ahlsten noted that the contracts do not stipulate that EWEB can't make rate adjustments.

Ms. Smith stated that staff will look at the various contracts and identify windows of opportunity, and will bring the rate true-up back to the Board on April 2.

President Simpson recalled that LCOG had mentioned the possibility of running fiber through EWEB's steam lines. He wondered how that concept would tie in to the current setup.

Mr. Ahlsten replied that there isn't a lot of tie-in, and that EWEB is currently assessing the feasibility of that, as EWEB may not own that fiber.

General Manager Gray stated that there are constraints that may limit EWEB's ability to change the rate methodology. He added that his strongest advice would be to never go into the fiber optic business on a cost basis because it puts resources at risk for zero upside, but if the service is going to be expanded, the Board needs to make a policy decision about how and why to do it.

Frank Lawson, Systems, Engineering Supervisor, stated that the billing is "contract-centric" and the cost is in the infrastructure, and that it would cost some fiber optic customers approximately $3 million to build their own line, so it is a great deal for those customers. He agreed with General Manager Gray that if EWEB is going to go into the fiber optic business, it needs to be a business, and the investment needs to be made as a business.

Commissioner Mital agreed with General Manager Gray that EWEB is in business to provide electricity and water at the lowest cost possible, and that if there are other business models to pursue to enhance services, that should only be done to subsidize core business, as he doesn't want to give services away.

Vice President Brown commented that it is his understanding that LCOG wants to lease the right of way for steam. General Manager Gray replied that EWEB needs to address the liability issue, for example, if asbestos is found.

Ms. Smith reiterated that staff will return to the Board with a proposal to align rates as per tonight's presentation, and will schedule a later time to discuss the business model. The Board agreed.

ELECTRIC UTILITY FINANCIAL STRATEGIES UPDATE

Using overheads, General Manager Gray briefly reviewed previous Board presentations and discussions regarding long-term electrical utility financial strategies. He then reviewed the agenda and objectives for tonight's presentation.

Using overheads, Ms. Smith reviewed the process to date, i.e., delayed or deferred capital projects, reductions in operation and maintenance (O&M), and elimination of 50 positions in 2012. She reviewed the electric rate drivers and projected BPA and EWEB rate increases for 2013.

Using overheads, Cathy Bloom, Financial Services Manager, reviewed previous Board presentations and discussions regarding electric long-term financial planning. She also briefly reviewed the 2012 electric long-term financial plan assumptions, rate increases resulting from those assumptions, projected reserves and cash balances, and projected debt service coverage ratios.

Ms. Bloom stated that the following financial initiatives were considered in developing the options that are being presented to the Board tonight, in order to improve EWEB's financial health in 2014:

- Capital improvement plan reductions
- Deferral of bond issuances
- O&M reductions
- Asset sales (property, generation or other)
- Board targets for debt service coverage/implied bond rating
- Potential change in electric rate assumption

Using overheads, Mel Damewood, Engineering Manager, summarized the evaluation process for the capital improvement plan (CIP) adjustments and deferrals and the financial impacts of each. He listed some examples of reductions and deferrals for type 1, 2 and 3 capital projects.

Using overheads, Ms. Bloom then reviewed bond issuance deferrals and a summary of the net full-time equivalent (FTE) and non-capital expense changes.

Each department manager then identified the proposed low-risk reductions and high-risk reductions, their related risks, and the cost savings for each, for each of their departments.

General Manager Gray identified the proposed low-risk reductions and high-risk reductions, their related risks, and the cost savings for each, for senior management. He also reviewed the changes in EWEB's organizational structure from 2010-2013, and the potential 2013 organizational structure changes for staff's recommended financial scenario.

Ms. Smith then identified the organization-wide risks from the proposed reductions:

- Reduced services to customers
- Less flexible and adaptable to emergent needs
- Potential for longer outages
- Erosion of employee morale
- Employee retention and recruitment

Ms. Smith also reviewed EWEB's options for asset sales. She noted that generally speaking, asset sales generate "one-time" revenue and not recurring revenue, and therefore they have the potential to reduce borrowing needs or increase reserve levels, but not necessarily have a material influence on ongoing rate levels.

Using overheads, Ms. Bloom reviewed the six financial scenarios that translate to approximate rate increase, change in reserves, and debt service coverage, etc., with a focus on Scenarios 3 and 4, and with Scenarios 5 and 6 as additional options for discussion.

Ms. Bloom then summarized the next steps in the process:

- General Board response and direction tonight in order to further develop 2014 plans
- Water utility discussion (how to deal with "deferral" of a large rate increase)
- 2013 capital budget true-up at the April 2 Board meeting
- Board Financial Work Session on July 16

Staff recommends Scenario #3, Balanced Option A, to help close the financial gap and set the direction for 2014 budget development. Staff noted that they are not requesting approval of the 2014 budget, but clear indication and feedback from the Board regarding direction so that they can continue to develop budget proposals. Scenario #3, Balanced Option A, provides direction for: 1) Board financial policies for financial metric targets; 2) long-term financial plans and budget development; and 3) deferral of bond issuance. If approved, Board policies would be revised for future Board action, and staff would begin incorporating the option into the long-term financial plans and budget development process.

Vice President Brown asked when a good time would be for the Board to make a choice between eliminating more positions or continuing energy education grants. General Manager Gray replied that would be a policy decision.

Vice President Brown asked if 24/7/365 outage/emergency response will be retained. General Manager Gray said it would, but the response time would be longer for any major outage and also for tree trimming, and the reductions would affect reliability. He gave the example of more aggressive tree trimming making some customers angry while risk is mitigated, while less aggressive tree trimming would result in less reliability.

Vice President Brown asked how much of the O&M reductions represents salaries. General Manager Gray replied that the actual reductions represent $11 million and 17 positions, and eliminating those 17 positions would result in a $2.5 million savings. Vice President Brown stated that, according to his math, layoffs could be avoided if each employee would agree to a 5% decrease in pay.

Commissioner Mital asked if the capital improvement plan reductions are separate from the other reductions. General Manager Gray replied that they are, and that there are more deferrals than reductions (i.e., delay of the Carmen-Smith project, etc.). He noted that more detail on the CIP reductions will be provided at the April 2 meeting.

Commissioner Mital stated that the CIP adjustments and deferrals seem to be the biggest lever, and he asked Mr. Damewood if that lever could be pushed any further. Mr. Damewood replied that it could, but there are risks involved. He added that pushing this lever further would mostly affect reliability, and that the more capital is reduced, the more potential work is reduced for engineers, technicians, and possibly some crews.

Ms. Smith stated that there are some items that cannot be eliminated, as the organization needs to remain stable. She added that a lot of the capital work doesn't have an impact on FTE, but if the capital lever continues to be pushed, eventually it will.

Commissioner Mital asked if there will be Board level discussion about delaying the Carmen-Smith relicensing timeline any further. General Manager Gray replied that Carmen-Smith is now 50 years old and there is some work that will need to be done, even without a license, but the six-year clock for completion starts when the license is obtained. He added that the Board will be receiving a backgrounder for further discussion at the April 2 meeting.

Commissioner Mital asked if there are other Board policy decisions that might have some impact on the proposed scenarios that wouldn't have an impact on personnel. Ms. Smith noted that Energy Management Services personnel was impacted severely in both 2012 and 2013 as a result of aligning acquisition targets of the Integrated Energy Resource Plan (IERP). General Manager Gray added that the other policies would be those for energy education grants and low-income funding, but the most powerful policy driver would be lowering EWEB's bond rating from AA to A.

A brief discussion ensued regarding the sale of excess power, the current power market, and the sale of generation assets, and how those could impact the financial scenarios.

The Board was asked for their feedback/direction regarding tonight's presentation:

Commissioner Manning:

- Agrees we can't lay off more employees to get out of this situation, and doesn't want to see that happen - prefers to look at all other options
- No problem with 5% rate increase to offset because he thinks the public can be educated as to where the balance is
- A discussion with all employees is necessary

President Simpson thanked staff for their presentation and all the hours they put in. He recognized and thanked all the employees present at tonight's meeting for their interest, participation, and their dedication to EWEB. He offered the following feedback/direction:

- Wouldn't mind reducing reliability, but not forever (possibly three years). Don't want to take 15 years to recover but would favor the reduction if it can generate ready cash.
- More attracted to Scenario 4B
- Wonders if tree trimming should be less aggressive
- In favor of reducing bond rating from AA to A
- In favor of selling generation resources which are ripe for picking
- Seems like an opportunity for rate smoothing and perhaps more EWEB-generated elbow room to have local rate increases in absence of BPA rate increase in even years, in order to have a more even rate increase assumption
- Don't want to gut Information Services, especially if there are mid-term benefits in technology that can resolve or minimize impact customer service response
- Consider discontinuing public access to meeting rooms
- In favor of 40% reduction in organizational structure
- Morale is important to me – interested in creating opportunities for internal rally
- Very interested in pursuing service territory realignment and asset sales
- In favor of reducing bond rating from AA to A

President Simpson asked what has caused such a large increase in customer service calls, increased hold times, and dropped calls. Mark Freeman, Customer Services/Energy Management Services Manager, replied that the biggest impact has been the recent change to a new on-line bill payment system, as it resulted in 2,000 calls on its first day alone. He said that staff is in the process of researching why general call volume has been up.

President Simpson encouraged Mr. Freeman to continue to research this to reduce the number of calls. General Manager Gray noted that staff is also looking at opportunities to leverage that technology in a different way.

In response to a question from the Board regarding the possibility of 17 FTE reductions, Ms. Smith stated that of those 17, nine are vacant positions, up to four positions are retirements that will happen within the next year, and three positions in Energy Management Services have already been eliminated, with two of those employees having been offered other opportunities.

The Board continued to offer their feedback/direction:

Commissioner Helgeson:

- Appreciates staff for the amount of time spent on the presentation
- The organization needs stability
- Concerned about continuity of operations

- Okay with debt service coverage going to 1.75 (as low as we can go without taking some risk)
- Favors a strategy that splits the remainder between cost reduction and rates
- Comfortable with capital budget reductions that Mr. Damewood and his group have done – good job of balancing risk
- Okay with the O&M non-labor reductions
- Agrees we cannot lay off our way out of this
- Sees this as an opportunity to right-size the organization in terms of efficiency and structure and to position ourselves to move forward
- A bit concerned about two years in a row of reductions but also mindful of managing through attrition
- Concerned about the span of control at senior management level
- Due to EWEB being heavily committed to conservation in the past, don't want to reduce the level of service in Energy Management Services to the point that we can't meet the natural demand of walk-in customers for weatherization or other programs – curious what the natural sustainment level is from a customer demand standpoint
- On the right track regarding asset sales – don't want to lock in losses, especially when we don't get a lump sum up front
- Might be willing to consider more options on the rate side – wouldn't want to just restore cuts, but would like to get a leg up on this conversation for next year

Commissioner Helgeson clarified that it makes sense to ramp down Energy Management Services and recalibrate some programs in light of EWEB's IERP, but that he wouldn't want to do that in such a way as to leave customers without access to programs that help them avoid higher bills.

Commissioner Mital asked for more information on the sale of generation assets. General Manager Gray and Ms. Bloom gave a brief explanation. He then offered his feedback/direction:

- Okay with reducing bond rating from AA to A
- Favors Scenario 5 – a little bit less of a rate increase; need to be cognizant of potential for BPA passthrough
- More comfortable with a bit less in reserves – might force staff/Board to make more difficult decisions about Type 2 and 3 capital projects

Vice President Brown stated that he is okay with reducing the bond rating from AA to A and also okay with staff's recommended debt coverage ratio.

He asked what will happen if EWEB receives the license for Carmen-Smith earlier than predicted. Mike McCann, Hydro License Implementation Project Manager, said that the earliest EWEB would receive it would be in the fall, but the Federal Energy Regulatory Commission (FERC) is currently very busy in Alaska and is not currently working on it, and will probably pick it up in early 2014. He said that it will take six or seven years to implement the fish passage issues, and that the power plant is beginning to fail now, so turbines and generators need to be repaired before the fish passage issues are addressed. He added that the Board will receive an update on Carmen-Smith at the April 2 meeting.

Vice President Brown voiced concern that there will be potential for dumping oil into the water supply. Mr. McCann replied that when the substation is built, the transformers will be located up the hill away from the river, work on the plant will begin after that, and the fish ladder will be deferred until 2017. He added that there is money in the budget for this, and the cost has been pushed out to 2014-16 and beyond.

President Simpson adjourned the Work Session at 8:50 p.m.

Assistant Secretary | President