



MEMORANDUM

EUGENE WATER & ELECTRIC BOARD

Rely on us.

TO: Commissioners Simpson, Helgeson, Manning, Mital and Brown
FROM: Sue Fahey, Finance Manager; Deborah Hart, Budget & Rates Supervisor;
Jerry Reller, Nate Schultz, and Sheila Crawford, Senior Financial Analysts
DATE: July 12, 2016
SUBJECT: Long-Term Financial Plan (LTFP) Update and 2017 Budget Assumptions
OBJECTIVE: Direction on 2017 Budget Assumptions

Issue

Board Policy SD6 and Oregon Statutes require that staff annually prepare balanced budgets for the Electric and Water Utilities for Board approval by the end of the calendar year. Each summer the Board provides direction to staff on the assumptions used to develop the following year's budget.

Background

Over the last several years, both the Water and Electric Utilities have faced financial challenges. Those challenges have been managed by strategically reducing operation & maintenance (O&M) and capital costs, designing prices that increase fixed cost recovery, reducing debt service obligations, and prudently using reserves to strengthen financial metrics. These, along with stronger water sales, have helped stabilize the Water Utility. For the Electric Utility, paying off the Harvest Wind note, using Smith Creek sale proceeds and an additional \$5 million to pay off debt, and refunding \$150 million of bonds have reduced debt service costs. These actions have resulted in significant improvement to the debt service coverage ratio (DSC) which is the Electric Utility's biggest financial challenge.

Discussion

The Strategic Plan continues to build on the three cornerstone concepts approved last year, and revisited in April of this year, to prepare EWEB for the future: Be Flexible and Resilient, Enhance Customer Value, and Focus on People – both Customers and Employees. The following business strategies support the strategic plan:

- **Enhance Affordability:** meet or exceed established financial metrics while keeping average prices below regional industry averages by enhancing utility efficiency, standardization and flexibility.
- **Connect with Customers:** remain aligned with our customers to reflect community values and enhance community vitality and resiliency while preserving affordability.
- **Ready Workforce:** attract, retain and cultivate an empowered, engaged and highly-skilled workforce equipped to perform and adapt as we transform to meet the challenges and opportunities of a changing future.

Management believes that the assumptions used to develop the LTFP incorporate the business strategies.

Overarching Forecast Assumptions

The assumptions used in creating forecasts and budgets greatly influence the results. The following assumptions have been used in developing the current forecasts and are anticipated to be used in creating the 2017 budget.

Both Utilities

- 1% non-labor CPI increase
- Labor/Benefit Increases:
 - 2.4% salary escalation
 - PERS increase – 7 percentage points above current rates on July 1, 2017, 7 percentage points in 2019, 5 percentage points in 2021, and 3 percentage points in July 2023 and 2025
 - Health insurance increase – 5% in 2017, 8% in 2018 and then 10% in subsequent years
- Financial Initiative Adjustments
 - Electric: \$1.7 million ongoing O&M reductions in 2017
 - Water: \$255 thousand ongoing O&M reductions in 2017

Electric:

- Retail load approximately the same as 2016 budget – 2.5 million MWh
- Contribution margin risk tolerance of \$3.2 million which represents 90% generation, 2.5% load reduction or 40% wholesale price reduction
 - Similar contribution margin risk tolerance through 2021, expected conditions 2022-2026
- New large customer load of \$660 thousand in 2017 increasing to \$4.7 million by 2026
- \$24 melded mid-market price curve increasing to \$37 in 2026
- Debt service restructuring with the 2016 bond defeasance and refunding
- Partial year Carmen-Smith generation outages in 2017, 2018, and 2021 respectively
- Bond issuance: \$67 million in 2019; \$19 million in 2022; and \$13 million in 2025, for funding capital work on Carmen-Smith

Water:

- Consumption: 7.6 million kgal, approximately the same as the 2016 budget
- Alternative Water Source (AWS) work begins in 2019
- Bond issuance: \$31 million in 2018; and \$24 million in 2021
- \$850 thousand in additional O&M costs beginning in 2022 to operate AWS
- An additional \$100 thousand for source protection on Willamette beginning in 2017

Long-term Financial Plan Price Assumptions and Outcomes

Electric

The Electric Utility LTFP indicates no overall average price change is needed in 2017. This is the third year in a row that the revenue requirement does not include a general price increase. The 2015 LTFP indicated a 2017 price increase of 3.5%. Through debt reduction and restructuring and financial initiatives, the projected overall average increase has been eliminated. The Electric LTFP outcomes

are included in Attachment 1.

Water

The Water Utility LTFP includes a 3.5% annual price change over the next ten years. This maintains Board targets for financial metrics through the duration of the Financial Plan. The 2015 LTFP projected 3.6% increases for all years throughout the plan. The Water LTFP outcomes are included in Attachment 2.

Recommendation

Management recommends that the Board direct staff to prepare the 2017 budget using the assumptions set forth in this document which includes:

- 3.5% overall average revenue requirement increase for the Water Utility in 2017.
- 0% overall average revenue requirement change for the Electric Utility in 2017.

Requested Board Action

Staff is not requesting Board action at the July 19th meeting; however, staff is requesting that the Board provide clear direction on the assumptions to be used in developing the 2017 budget.

Attachment 1 -Summary of Electric LTFP Price Assumptions and Outcomes

Attachment 2 -Summary of Water LTFP Price Assumptions and Outcomes

Attachment 3 -Average Bill Comparison

Attachment 4 -Average Bill Affordability

Summary of Electric LTFP Rate Assumptions and Outcomes

		2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
Reserves and Cash	\$69,820	\$116,398	\$111,203	\$116,343	\$120,516	\$125,290	\$130,560	\$133,247	\$135,242	\$137,047	\$144,797
Debt Service Coverage Ratio	1.75	1.84	1.87	1.97	1.80	1.67	1.93	1.74	1.62	1.56	1.92
Days Cash		192	185	203	204	213	209	205	199	199	213
Average Rev Requirement Change		0.00%	2.50%	2.75%	3.25%	1.50%	2.50%	2.50%	3.25%	2.25%	3.00%
O&M improvements to support 1.75 DSC		\$0	\$0	\$0	\$0	\$1,800	\$0	\$0	\$1,000	\$1,400	\$0
Total O&M improvements to support 1.75 DSC		\$0	\$0	\$0	\$0	\$1,800	\$1,800	\$1,800	\$2,800	\$4,200	\$4,200
DSC Ratio with O&M Improvements		1.84	1.87	1.97	1.80	1.75	2.01	1.82	1.75	1.75	2.11
	Revenue Requirement Rate Assumptions										Compounded
Rate Schedule	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	10 Yr Total
General Rate Increase			2.00%		1.50%		2.00%		2.00%		7.71%
Carmen/Smith Debt			0.75%	0.75%			0.50%	0.75%	0.25%	0.50%	3.55%
BPA Increase		2.50%		2.50%		2.50%		2.50%		2.50%	13.14%
Avg Rev Requirement Change	0.00%	2.50%	2.75%	3.25%	1.50%	2.50%	2.50%	3.25%	2.25%	3.00%	26.10%

- Retail load approximately the same as 2016 budget – 2.5 million MWh.
- Contribution margin risk tolerance of \$3.2 million
 - Similar contribution margin risk tolerance through 2021. expected conditions 2022-2026
- New large customer load of \$660 thousand in 2017 increasing to \$4.7 million in 2026
- \$24 melded mid-market price curve increasing to \$37 in 2026
- Debt service restructuring with 2016 bond defeasance and refunding
- Partial year Carmen-Smith generation outages in 2017, 2018, and 2021 respectively.
- Bond issuance: \$67 million in 2019; \$19 million in 2022; and \$13 million in 2025, for funding capital work on Carmen-Smith.
- 1% non-labor CPI increase
- Labor/Benefit Increases:
 - 2.4% salary escalation.
 - PERS increase – 7 percentage points above current rates on July1, 2017, 7 percentage points in 2019, 5 percentage points in 2021, and 3 percentage points in 2023 and 2025.
 - Health insurance increase – 5% in 2017, 8% in 2018 and then 10% in subsequent years.

Summary of Water LTFP Price Assumptions and Outcomes (000's omitted)

	Current Target	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
Reserves & Cash	\$11,680	\$25,558	\$27,670	\$32,422	\$19,529	\$17,203	\$18,381	\$16,775	\$16,094	\$15,595	\$13,836
AWS Reserve Balance ¹		\$6,237	\$7,270	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0
DSC	2.00-2.50	3.25	2.76	2.52	2.63	2.42	2.18	2.48	2.55	2.65	2.77
Feb Rate Action		3.5%	3.5%	3.5%	3.5%	3.5%	3.5%	3.5%	3.5%	3.5%	3.5%

Note 1: AWS reserve balances subject to change based on Board approved transfers each spring

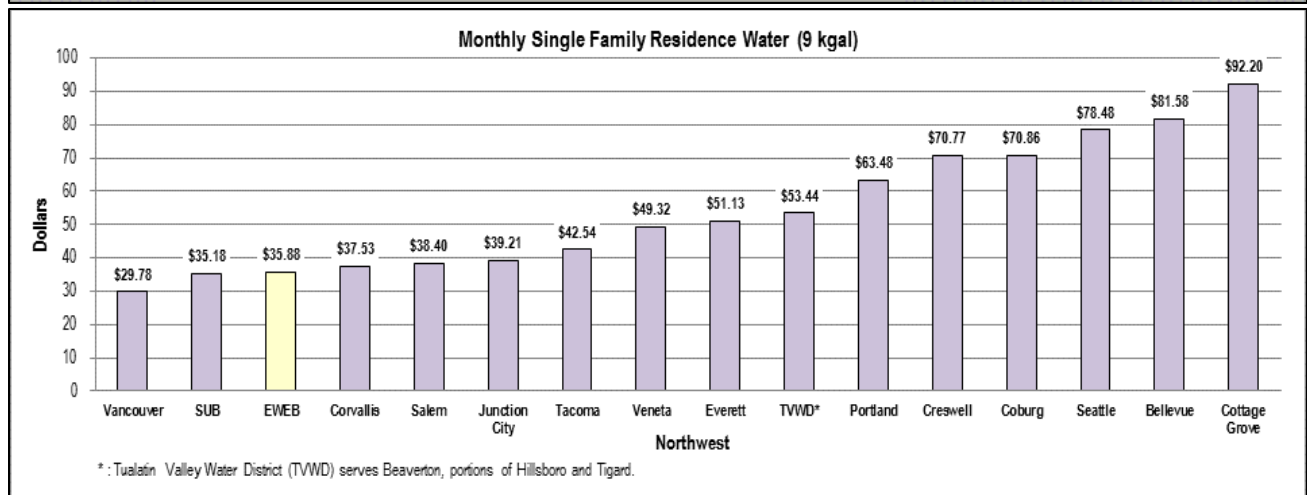
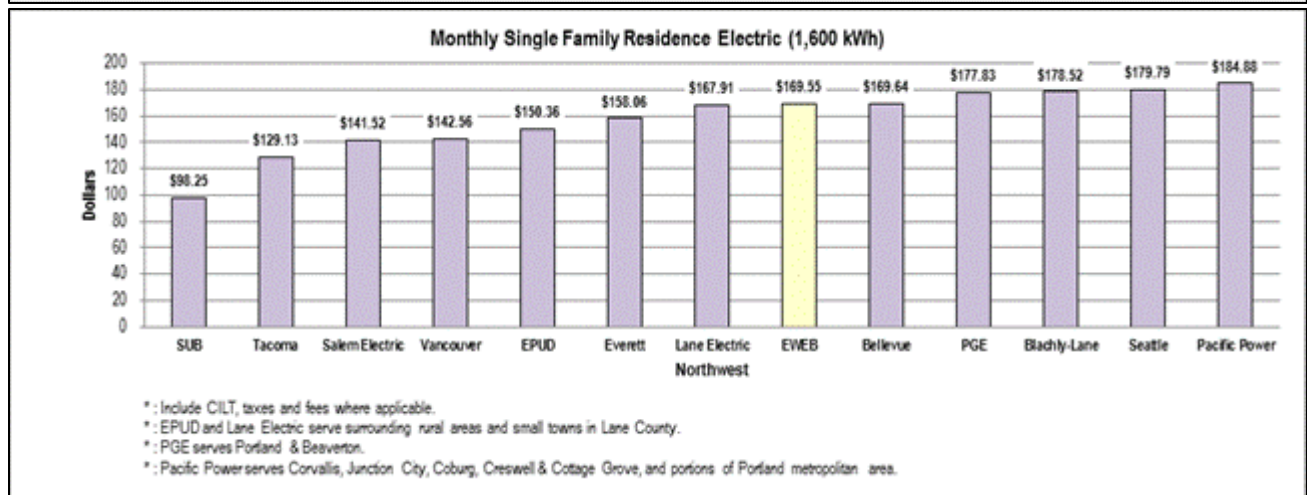
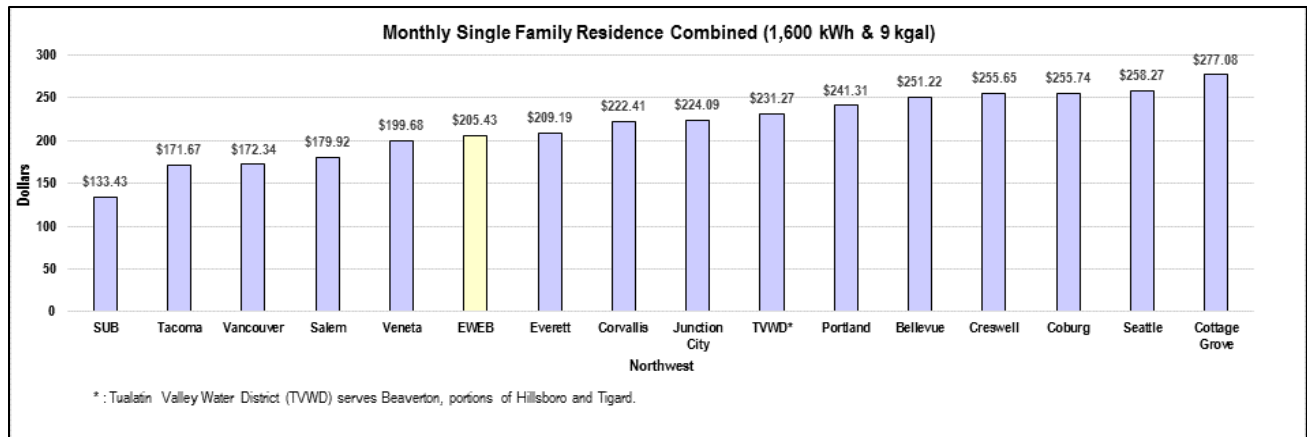
Major Assumptions

- Consumption: 7.6 million kgal, approximately the same as the 2016 budget.
- AWS work begins in 2019.
- Bond issuance: \$30.6 million in 2018; and \$24 million in 2021.
- \$850 thousand in additional O&M costs beginning 2022 to operate AWS.
- An additional \$100 thousand for source protection on Willamette beginning in 2017.
- 1% non-labor CPI increase
- Labor/Benefit Increases:
 - 2.4% salary escalation
 - PERS increase – 7 percentage points above current rates on July 1, 2017, 7 percentage points in 2019, 5 percentage points in 2021, and 3 percentage points in 2023 and 2025.
 - Health insurance increase – 5% in 2017, 8% in 2018 and then 10% in subsequent years.

Reserves and Cash Balances

- Staff is working with consultant to optimize cash balances and bond issuance amounts.

Average Bill Comparison



Average Bill Affordability

Single Family Residence			
	Electric	Water	Total
Average Household Income*			\$ 3,805
Usage	1,600 kWh	9 kgal	
Utility Bill	\$ 169.55	\$ 35.88	\$ 205.43
Utility Bill % of Income	4.46%	0.94%	5.40%
<p>Figures are in monthly averages.</p> <p>*2016 estimate represents an average household income for Eugene. Based on the US Census Bureau 2010 data, escalated by the average of Portland/Salem CPI-U and CPI-W to 2016.</p> <p>Source: Average Household Income based on US Census Bureau medium income. https://factfinder2.census.gov/faces/nav/jsf/pages/community_facts.xhtml</p>			