

EUGENE WATER & ELECTRIC BOARD
WORK SESSION
EWEB BOARD ROOM
500 EAST 4TH AVENUE
MAY 5, 2009
5:30 P.M.

Commissioners present: Ron Farmer, John Brown, Bob Cassidy, Rich Cunningham, and Joann Ernst.

Others Present: Randy Berggren, Sheila Crawford, Dick Helgeson, Patty Boyle, Lance Robertson, Tom Buckhouse, Jim Wiley, Jim Origliosso, Jeannine Parisi, Dean Ahlsten, Debra Smith, Susan Eicher, Brenda Sirois, Garilyn Johnston, and Krista Hince of the EWEB staff; Ruth Atcherson, City of Eugene minutes recorder.

President Farmer convened the work session of the Eugene Water & Electric Board (EWEB).

FIRST QUARTER 2009 GM GOALS

General Manager Randy Berggren highlighted the *2009 GM Goals – 1st Quarter Status Report*. He noted that Goal 5 had been revised to reflect the direction to review all budgeted work and to set priorities for budget reductions, per the Strategic Planning Retreat that had been held in March.

Commissioner Cassidy asked for more information regarding Items (c) and (e) under Goal 1, which had to do with water supply strategies. Mr. Berggren explained, regarding (c), which as part of its work to find an alternate source for water, EWEB had involved trying to work with the Springfield Utility Board (SUB) to create a partnership in a potential new treatment plant. He said SUB had water rights on the Willamette River and an existing treatment plant. In looking at the economics and feasibility for a joint facility, he stated that it was intended to serve as a primary resource for SUB and a secondary resource for EWEB. He related that they had been working with SUB on this for approximately 18 months.

Regarding (e), Mr. Berggren stated that part of the work going forward relative to issues of future policy as EWEB continued to try to expand its wholesale supply initiative, would be to utilize a wholesale power template to identify policy issues that should be addressed in any contract relative to wholesale supply. He said EWEB had three existing wholesale contracts that EWEB planned to use the template for as a test, including the River Road Water District and the Santa Clara Water District. He thought this would show what kind of policy issues existed and to call out policy issues that needed to be addressed.

Commissioner Cassidy asked Mr. Berggren to elaborate on Goal 4 (a), which called for completion of a study for the remaining 78 customer facilities utilizing the steam system along with estimating the cost to convert to alternate fuels. Mr. Berggren replied that staff continued to conduct detailed analysis on the steam line. He noted that some customers were moving forward and staff was monitoring them and trying to evaluate the impacts of what they were doing. He said staff wanted to look at critical steam lines that were on the perimeter of the system and that were highly inefficient, making them the candidates that EWEB would want to decommission in order to improve the efficiency of the system.

In response to a question from Commissioner Cassidy regarding (e)(2) under *1st Quarter Results – Goal 4*, Mr. Berggren said everyone agreed that shutting down the steam plant within three years was better than taking five years to do so. He underscored that they would shut the system down as fast as possible. He explained that staff was still trying to identify funding sources and what it would take to help customers get off the system.

Commissioner Cassidy asked for more of an explanation of (b) under *1st Quarter Results – Goal 5 Revised*. Mr. Berggren clarified that staff had identified an initial goal of reducing 2009 expenses by \$2 million, but staff had also identified other critical work that had not been adequately budgeted, at a cost of \$2.5 million. He was working with \$3.5 million in reductions, \$1.5 million of which would be taken from resources and redeployed to more critical work such as the North American Electric Reliability Corporation (NERC) compliance. He stated that staff would take \$2 million as an actual savings, as a “down payment” on a three-year budget management strategy that aimed to avoid taking a rate action in 2010 for 2011.

Commissioner Cassidy asked if EWEB was anticipating a surplus in the coming budget. Mr. Berggren replied that it would only “barely” be a surplus. Currently, the surplus revenue was estimated at \$3 million altogether, leaving the budget \$1.5 million short though it was still \$3 million over the cost requirement. He explained that this was because they had budgeted the surplus revenue.

In response to a question from Commissioner Ernst, Mr. Berggren confirmed that the contract with Peace Health assured that EWEB would run its steam plant for three years. He considered it to be a standard contract and Peace Health, as EWEB’s biggest steam customer, had given EWEB some ability to spread remaining fixed costs so that it would create more cost stability for the rest of the customers.

Vice President Brown said the State and Junction City had been talking about the provision of water to the new hospital facility. He had heard they were looking at taking water from the Long Tom River. He wondered why they were not talking with EWEB, noting that this could benefit EWEB by helping to further perfect EWEB’s existing water rights. Mr. Berggren responded that staff had spoken with the Mayor of Junction City. He thought the situation could merit “one more knock on the door” to ask if Junction City had fully considered costs. He could not imagine that the economics of the project would not favor EWEB. Water & Steam Division Director Tom Buckhouse added that Junction City was aware that EWEB had the capability to provide water.

President Farmer suggested having a politician and not a technician make contact in Junction City. He felt they needed a strategic plan to do it. Mr. Berggren responded that the politics of Junction City seemed fairly closed. He suggested that staff discuss this and come up with a strategic step to recommend to the Board to ensure Junction City’s engagement in the discussion.

Commissioner Cunningham said he would like to have the General Manager write a one-page description of the type of person that could carry on the legacy of EWEB after Mr. Berggren's retirement.

President Farmer observed that in looking at Goal 2, (c), (d), and (e) indicated only that they were pending. He asked whether the General Manager was confident of EWEB's ability to meet the deadline associated with the Headquarters Master Planning process. Mr. Berggren replied that he was not certain because he did not know how the Board would choose to vote. President Farmer remarked that the deadlines seemed tight. Mr. Berggren concurred.

President Farmer understood that EWEB had identified some sources to help with the steam transition. He said with budgets coming at the current levels and with drastic cutbacks that the State and other jurisdictions were making, he asked if there was any sense as to whether the areas for possible funding resources were at risk. Mr. Berggren replied that staff would not say that it was at risk at this point, but the work different entities had to do to gain access to the stimulus money had gotten in the way for most of the institutions that were working the programs EWEB was seeking access to. He said the Oregon Department of Energy (ODOE) had been occupied with sorting through applications for stimulus funding; EWEB was a little behind from when it expected to hear from ODOE regarding the programs it was interested in. He said EWEB was proceeding with the Request for Proposals (RFP) at this point because of a need to get a sense of what it would cost. He noted that if EWEB did not receive stimulus money or if the State decided that its loan program did not work, EWEB would be facing a funding source issue again.

Employee, Customer, & Community Services Division Director Debra Smith related that Power Resources Division Director Dick Helgeson and Water & Steam Division Director Tom Buckhouse had been working on an alternative scenario that would deploy some internal resources to "jump start" the process. She said they were seeing that customers who were remaining in a strong financial condition were moving off the system. She underscored that this increased the need to stay in front of the issue.

Commissioner Cassidy asked how many customers had "dropped off" from the steam utility since the last update. Ms. Smith replied that the Eugene Hotel and Summit Bank had moved off from the system. She said at this point staff thought they could bridge the gap by taking some capacity in Energy Management Services.

Commissioner Cassidy asked where the tipping point would lie. Mr. Berggren replied that he did not believe the steam customers would all be able to move from the system within three years. He believed that EWEB would be "challenged the whole way." He said until the specific funding was lined up and identified that would close out the last customer, there would be uncertainty about when the last customer would be of the system.

Vice President Brown asked where the County Jail fell in the range of customer size. Mr. Buckhouse replied that the jail was one of the smaller public buildings, but it still represented a fairly significant load.

Vice President Brown asked how much it would cost to renovate the headquarters building. Ms. Smith responded that staff would have access to that numbers at the next meeting. She said the thing that they wanted to do in the short-term would be to have an updated view of the system with a study that would allow EWEB to identify the peripheral customers who were the most expensive. She stated that the goal would be to get at least some customers moved off the system by the next heating season. She estimated that number to be between five and ten of them.

In response to a follow-up question from Vice President Brown, Ms. Smith stated that there was approximately \$400,000 total in the budget for the conversion, \$100,000 for the boiler conversion and \$300,000 for study.

Ms. Smith summarized the situation. She said EWEB had budgeted some money and had been waiting for ODOE to respond to issue the RFP, but had decided to go ahead and issue the RFP. She noted that Key Accounts Manager Mike Logan had his time diverted into working to get stimulus money so the process had been slowed both on EWEB's end and on the end at ODOE. She related that this activity had slowed down and Mr. Logan could return his energies to the steam utility.

FIRST QUARTER 2009 BUDGET AND FINANCIAL PERFORMANCE

Senior Financial Analyst Susan Eicher provided an overview of the *First Quarter Financial Statements* with power points. She stressed that the first quarter of the year was "neither very optimistic nor very pessimistic." She said things were still developing, though they were still projecting the end of the year contribution margin to be somewhat under budget.

Commissioner Cassidy observed that the budget had been based on an 85 percent hydro assumption but was running on a 92 percent of normal hydro year. He asked if EWEB was now basing its budget on the 92 percent level. Ms. Eicher assured him that the budget process had not changed from the 85 percent assumption. She added that one reason they believed the contribution margin to be slightly under the budget was because, though the hydro year was above 85 percent, prices were very low.

Ms. Eicher reported that the working cash was still in "pretty good shape," though it was still under the \$15 million target. She expected it to be at \$15 million once the month of April was closed. She reviewed the reserve funds, noting that the Carmen-Smith Reserve had been replenished. She stated that the biggest differences between March, 2009, and March, 2008, were due to the closure of Hynix and the issuance of rebates. She said all classes of customers were showing some decrease in consumption compared to the previous year.

President Farmer asked if this automatically caused the Contribution In Lieu of Tax (CILT) to go up. Ms. Eicher replied that whatever power EWEB did not need could automatically be placed on the market for sale. She said at present the prices were low and EWEB was not benefiting from it as much as it did previously. She added that EWEB was still above the contribution margin by \$1.1 million.

Ms. Eicher reported that the difference between the net operating revenue and the net revenue had to do with changes in the other revenues and expenses, one of which was attributed to a significant decrease in the yields of the reserve accounts; interest rates were down to 1 percent. She predicted that this would not change soon.

Ms. Eicher related that staff projected a negative variance of approximately \$1.5 million at the end of the year for the electric utility.

President Farmer asked if the budget comparison number included the transfer that had been made out of reserves for the Customer Care Program. Ms. Eicher replied that she had backed out the effects of the program, because they had not been budgeted.

President Farmer surmised that the contribution margin was actually \$700,000. Ms. Eicher responded that generally the utility did not pass budget amendments for contribution margin or revenue items. President Farmer commented that this made things sound “rosier” than they actually were.

Ms. Eicher stated that the capital budget projection did not include budget variances or amendments. She explained that as the budget amendments were passed and the variances were better known, they would come up in future reports.

Regarding the net operating budget, Ms. Eicher reported that it was a little under from what would normally be expected. She said staff was continuing to look for ways to save money.

Ms. Eicher attributed the increased net operating revenues for the water utility to the rate increases.

Commissioner Cunningham ascertained from Ms. Eicher that the water utility’s revenue was down. Ms. Eicher explained that it would be down by a greater amount without the rate increases.

Ms. Eicher stated that they were continuing to watch the economy closely. She related that they had yet to see a forecast indicating that things were starting to go back up in the current year. She said they were monitoring the credit markets, because the budget called for the issuance of bonds. This was still under development. She added that they were working on a line of credit for the Harvest Wind project.

In response to a question from Vice President Brown, Ms. Eicher said it was her understanding that EWEB might have to increase the budget for Harvest Wind to up to \$50 million.

Power Management and Planning Manager Dick Varner stated that originally EWEB was looking for a construction lender, which would have meant that EWEB would have been investing \$15 to \$20 million and then EWEB would buy out when the project was completed. He said that market was not available at this point. He related that at present each utility intended to fund, through commercial operation, their share of the cost, and then they would seek a tax owner to come in and buy the project and commercial operation. He explained that the utilities would then do their pre-purchase of power for their share of the cost. He reported that the current forecast was that EWEB's share would be approximately \$46 million to commercial operation, currently estimated to be in the first weeks of December. He said they were anticipating that a consortium of tax owners would bring between \$100 and \$120 million to the table in order to pay for approximately half of the cost of the facility. He expected that by the end of the year EWEB would be down to \$23 to \$25 million in the project. He added that staff planned to bring the item to the Board on June 2 for an update and they planned to prepare a complete backgrounder that would lay out all of the financing "permutations."

Commissioner Ernst recalled that staff had discussed that the partners in Harvest Wind were having problems gaining funding. Mr. Varner replied that at this point there were no indications from anyone that they were having difficulty coming up with their share of the funds.

Mr. Berggren said part of the reason the contribution margin continued to be close to the budgeted amount was due to the hedging program, which he attributed to the power risk management guidelines. He explained that every year EWEB hedged two years ahead at 85 percent or below with "puts," in which EWEB had the right but not the obligation to place a unit of power on the market. He related that two weeks earlier these "puts" were valued at an amount in excess of \$5 million, which would be a savings on the bottom line. He noted that the Snohomish Public Utility District (PUD) had a 25 megawatt hour (MWH) unit with EWEB at \$100 per MWH in a market in which a MWH was being sold for \$27.

In response to a question from President Farmer, Mr. Berggren stated that the purchased power was \$17.1 million over budget. Ms. Eicher added that EWEB was better than budget on wholesale sales but was worse than budget on purchased power. She said what the Board was seeing was part of the difficulty staff was having in forecasting and budgeting for what the actual power sales would be.

President Farmer asked if staff predicted that the drop in retail sales would be felt after the end of the present year. Mr. Berggren affirmed that EWEB would be "up against it" in 2010.

Commissioner Ernst asked if EWEB was hedging two years ahead on an ongoing basis. Mr. Berggren said that was the practice, but in the present year EWEB had been conditioned on the ability to hedge because of credit constraints and very high markets. He explained that the markets were requiring anywhere from 10 to 15 percent of the value of the deal for the cost of the premium of the insurance. He related that EWEB had run out of hedging partners who actually were credit-worthy enough to do the hedging. He said the 2009/2010 hedging was not completed.

In response to a question from President Farmer, Mr. Varner said there was a significant difference between the prices in 2009 and 2010 and 2011. He related that the 2009 prices per MWH were in the mid-\$30s, 2010 prices were in the mid-\$40s, and 2011 could be in the low \$50s. He underscored that there was a significant difference in the forward curves and “how steeply it comes back.” He added that EWEB did not want to be in the position where, if the market crashed and stayed down for 2010 or 2011, it had to sell in a \$30 market.

Vice President Brown asked how the shut-down of Carmen-Smith would affect the budget. Mr. Varner responded that EWEB had not put money away for the lost generation of the facility, but it had put money away for the capital costs.

Commissioner Ernst asked if the high degree of uncertainty in power costs was driven by the cost of fossil fuel. Mr. Berggren replied that it was driven by the economy. Mr. Varner added that the marginal fuel was natural gas, most of the time, except when the hydroelectric facilities were operating. He said when the demand for natural gas was down, the price of natural gas went down and the price of electricity went down. He averred that as soon as the price of natural gas increased, the price of electricity would increase.

President Farmer adjourned the Work Session at 6:27 p.m.

Assistant Secretary

President