



INTEROFFICE MEMO

EUGENE WATER & ELECTRIC BOARD
CORPORATE SERVICES DIVISION

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TO: Commissioners Farmer, Brown, Cassidy, Cunningham, and Ernst

FROM: Patty Boyle, Fiscal Services Supervisor

July 1, 2009

RE: 2010 Budget Assumptions and Discussion of the Electric Long-Term Financial Plan

ISSUE

The attached provides two views of the Long Term Financial Plan. The evening's discussion will seek to answer the question of what base assumptions should be incorporated into the development of the 2010 Budget?

BACKGROUND

As shown in the table below, in the recent past the Electric Utility has been in the fortunate position to pass through to the customer rate decreases in 2005, 2006 (Nov.) and 2008 and take no action in 2007. The single rate increase since 2005 occurred in May of 2006.

Year	Rate Action	Approximate Change In Average Monthly Bill
May 2009	No Change to Rates	No Change
May 2008	Overall Decrease of 1.8%	Decrease of \$1.50
November 2007	No Change to Rates	No Change
May 2007	No Change to Rates	No Change
November 2006	Overall Decrease of 1.8%	Decrease of \$1.50
May 2006	Overall Increase of 5.8%	Increase of \$5.00
November 2005	Overall Decrease of 2.5%	Decrease of \$2.00
May 2005	Overall Decrease of 1.6%	Decrease of \$1.30

Attached to this memo are two scenarios that forecast the next several years of revenues and expenses. The items included are defined as follows.

Contribution Margin Revenue – This is the bulk of all revenue generated by the Electric Utility. It includes all rate based revenue from power sales to the community as well as revenue generated by selling power to the wholesale market.

Contribution Margin Expense – This category includes all costs associated with the purchase and transmission of power to the place of use as well as the Contribution in Lieu of Tax paid to the Cities of Eugene and Springfield.

Other Revenue - This category records revenue associated with non-power fees such as customer account fees and interest earnings on reserve accounts.

Other Expenditures – The bulk of these costs are driven by Operations and maintenance labor, non-labor costs for materials and supplies, the money contributed to the capital program, the electric utility's conservation program and debt service payments. The category of balance sheet items records a variety of resources and expenses that reconcile the income statement to the balance sheet.

The standard calculation of financial ratios and reserve balances has also been included.

DISCUSSION

In early summer staff typically presents at least two scenarios of what the next several years forecasted financial results appear to be. These scenarios are built using the most current known and forecasted information and Board direction. The purpose of developing these scenarios is to allow the Board to have a broad understanding of the current view of the financial prospects of the organization and to provide high level direction in the development of the prompt year's budget.

In this round of analysis we have developed two scenarios for presentation and discussion. The difference between the scenarios is related to 1) the timing of rate increases and 2) the assumed amount of power generated. There are several things common to both scenarios.

- Like much of the community, EWEB is experiencing the recession economy in the form of decreased demand from all customer classes. Normally a decrease in EWEB load would not have a negative financial impact; rather it is sold to the wholesale market at a higher price thereby generating additional revenue. At this time, the amount of money generated by rates is quite near or slightly above the wholesale market resulting in decreased revenue associated with load loss.
- The price for which we anticipate selling any surplus power is \$10-\$20 MWh lower for the next 1-3 years than the forecast in November of 2008. The impact of this change was largely mitigated by our financial hedging program for 2009. The hedging program purchases 'puts' which lock in the price we can sell power at a future date. Because these prices were locked in, we were able to count on this revenue and for 2009's budget we are largely insulated from a major price drops. Although we will continue to hedge power sales for 2010, the price at which we are able to lock in those sales is much lower than in 2009 and as such we'll count on less revenue.
- The two recently approved power generating facilities, Harvest Wind and Seneca, come on-line in the planned timeframe and at forecast cost. Harvest Wind is anticipated to be in production in late 2009. The total cost of power generated from the project is expected to be about \$1- \$1.5 higher than what that power can be sold for in the next couple of years. Similarly, the Seneca Power Purchase agreement is anticipated to bring power on-line in very late 2010 and will also cost \$1-\$1.5million in the near term. Both of these projects have good economics over their life but do expect to have negative cash flow early on as a result of depressed wholesale markets.

- BPA power costs are also increasing. In November 2008 we assumed that the credit to our power bill as a result of the residential exchange agreement would be \$6 million per year for the next seven federal fiscal years. Subsequently we were notified by the BPA that the credit was only for the 2009 fiscal year and all future years would receive a \$3 million per year credit. Also, the BPA is likely to raise their rates as of October 1, 2009. The current estimate is that their rates will go up by about 6%. In order to cover both of the costs, EWEB rate payers would see a 5.5% – 6.5% rate increase.
- As previously discussed with the Board, the forecast anticipates a large reduction in Tier 1 Power Entitlement from BPA. At today's power values, this reduction will result in a roughly 7% rate increase to customers.
- The second increment of debt to complete the Roosevelt Building is scheduled for issuance in 2010. At this time we anticipate issuing about \$25 million to complete the building. This is about \$3 million lower than previous forecasts and may be lower still based on bids currently being solicited and reviewed.
- There are also a couple of base assumptions for expenses that EWEB can appropriately control. Given the state of the economy and some recent experience we believe we can forgo any inflationary increase in materials and supplies costs for a couple of years. This can be achieved by maintaining most of the budget reductions in 2009 and carefully reviewing all requests for additional funds against the organizational priorities of compliance, safety, sustainability, etc. A small increase in both the number of employees (plus 4) and salaries have been included in this forecast. The collective bargaining agreement for IBEW represented employees has a 4% increase in wages included and 3% increase is being used as a placeholder for non represented employees. Information on non represented employees is due in August and could be lower.

Discussion Specific to Scenario #1

As noted above, two scenarios have been included in your packet. Scenario One assumes that the 2010 budget and the long-term forecast maintain the current policy approach to the timing of rate changes and maintains a 'worst five-year' generation assumption throughout the term of the forecast.

Current Board direction is to 'pass through' costs associated with BPA power as they occur. Practically speaking this means that the decrease in the credit associated with the BPA residential exchange agreement and the increase in BPA power costs would be processed in the fall of 2009 and would appear on customer bills as of November 1, 2009. The estimated rate change is 5.5%-6% to ratepayers.

Current practice is also to view all costs and revenues on the assumption that in any given year there will be sufficient snowpack and run-off to generate at the average of the worst five year period, more simply stated as about 85% of average generation.

Using these two assumptions and holding all other items described above as constant, the utility is expected to generate very small surpluses until 2013 & 2014 where reserves would need to cover deficits of \$14-\$15 million. The cause of those deficits is a combination of lost generation and sales revenue due to the Carmen Smith outage for relicensing work and increase in debt service related to financing that effort.

Discussion Specific to Scenario #2

Scenario Two approaches the timing of rate increases and the generation assumption differently. Knowing that many in our community are impacted by the recession, EWEB management wanted to craft an option that would delay the impact of rate increases and strategically position the organization to have a more likely view of generation.

In this scenario we have modeled the impact of delaying the rate increase associated with BPA power costs to May 2010. This option would put any increase in rates to May 2010 and beyond the heating season. By doing this, the utility would need to make-up the lost revenue by using about \$2 million in reserves to return to a balanced budget. It's important to note that this amount could end up being higher or lower depending changes to the power markets or other budget needs between now and the time the budget for 2010 is complete but given the level of available reserves seems like a reasonable option.

As noted earlier, in late 2011 the utility will take a large decrement in its entitlement to power from BPA under the new contract. At this time, we expect to need about 7% in rate increases to make up for the revenue loss. To smooth that rate impact as much as possible, this scenario moves a scheduled rate increase for EWEB expenses to May of 2012 from May of 2011.

Along with the rate timing changes, this scenario incorporates a much more likely assumption regarding the amount of power EWEB generates. As noted above we typically use the assumption and model roughly 85% percent of average generation in all years. In this scenario we maintain that assumption for 2010 budgeting purposes but also assume in 2011 and beyond generation of approximately 92% of average. The generation assumption of 92% of average is based on the worst 10-year period of generation and while still conservative, much closer to our recent experience. While it provides a view of what is more likely to happen, staff does not suggest modifying the assumption for budget purposes at this time.

Taking the second scenario view of the budget would require either additional cost cutting measures or the use of some reserves in 2010 and possibly 2011 as a result of delayed rate increases. It would also diminish the forecasted need to use reserves in the 2013 and 2014 time period requiring approximately \$11 million.

RECOMMENDATION/ACTION

No action is required at this time. The purpose of this discussion is to inform the Board of the current financial forecast and to have the Board come to general agreement on the basic rate strategy and assumptions going into the budget.

Please feel free to contact me ahead of the meeting to discuss any of the details included in either of these two scenarios.

Electric Long Term Forecast - July 2009 Budget Planning Worksession

85% Average Generation and May & November Rate Increases	2009 Budget	2009 Projected	2010 Proj	2011 Proj	2012 Proj	2013 Proj	2014 Proj	2015 Proj	2016 Proj	2017 Proj	2018 Proj
General Rate Change			May 2%	May 2%	May 2%	May 4%	May 5%	May 3%	May 3%	May 2%	May 2%
BPA Pass Through		November 6%	November 0%	November 7%	November 0%	November 3%	November 0%	November 3%	November 0%	November 3%	November 0%
Net Change in Rates		6%	2%	9%	2%	7%	5%	6%	3%	5%	2%
Contribution Margin Revenue (\$000)											
Residential Retail Rates	80,400	75,100	86,900	90,600	99,200	102,700	109,800	117,300	123,900	130,800	136,800
Small/Medium General Service Rates	45,900	43,600	52,100	54,200	59,800	62,000	66,300	70,800	74,800	79,000	82,600
Large Comm and Industrial Rates	39,700	37,800	39,900	41,600	45,500	46,400	49,100	51,900	54,300	56,800	58,800
Other Retail (Street and Private Lights)	900	900	1,000	1,100	1,900	1,900	2,700	3,600	2,900	3,100	3,200
Wholesale Sales Revenue	53,600	84,800	76,100	68,900	41,000	45,200	44,100	44,200	49,600	50,400	50,800
Total Contribution Margin Revenue	220,600	242,200	256,100	256,400	247,300	258,100	272,000	287,800	305,500	320,100	332,200
Contribution Margin Expense (\$000)											
Purchased Power & Wheeling	97,800	118,300	129,300	129,300	117,700	124,800	129,300	133,400	144,700	149,800	155,100
Thermal Production (IP Fuel Costs)	3,400	1,500	2,800	3,200	3,300	3,400	3,600	1,600	0	0	0
Eugene & Springfield Contribution in Lieu of Taxes	11,200	13,500	12,700	12,500	13,600	14,000	14,500	15,400	16,200	17,000	17,700
Total Contribution Margin Expense	112,400	133,300	144,700	145,000	134,600	142,200	147,400	150,400	160,900	166,800	172,800
Net Contribution Margin	108,100	108,900	111,300	111,400	112,700	116,000	124,600	137,400	144,600	153,300	159,400
Other Revenue											
Miscellaneous Operating Revenue	5,900	6,800	5,800	6,500	8,400	6,500	6,500	6,500	6,500	6,500	6,500
Operating Interest Earnings	5,000	3,700	3,800	3,800	3,300	3,100	2,800	2,700	2,800	3,000	3,300
Total Other Revenue	10,900	10,400	9,600	10,300	11,700	9,600	9,300	9,200	9,300	9,500	9,800
Total Net CM Plus Other Revenue	119,000	119,300	120,900	121,700	124,400	125,600	133,900	146,600	153,900	162,800	169,200
Other Expenditures											
O&M Labor	34,400	33,400	37,100	39,300	41,400	43,700	46,100	48,500	51,200	54,000	55,700
O&M Other	29,100	29,400	29,500	29,900	31,100	32,400	33,700	35,600	37,100	38,600	40,200
Lane Electric Cooperative Payments	400	400	0	0	0	0	0	0	0	0	0
Capital (Net of Bonds and Cust Paid)	18,200	18,200	16,000	16,000	16,600	17,200	18,600	19,400	20,100	20,800	21,500
Debt Service	22,700	22,000	25,700	26,800	27,900	30,600	31,200	32,200	32,500	32,800	33,200
Conservation Program	8,600	8,600	8,900	9,200	9,500	9,800	10,000	10,300	10,700	11,000	11,300
Balance Sheet Changes	1,300	1,300	-200	-300	-500	-400	-1,600	-1,500	-3,100	-3,000	-3,100
Total Expenditures	114,700	113,300	117,000	120,900	126,000	133,300	138,000	144,500	148,500	154,200	158,800
Addition to (Reduction of) Reserves	4,300	6,000	3,900	800	-1,600	-7,700	-4,100	2,100	5,400	8,600	10,400
Equity Draw for Carmen Smith			4,000	14,000	3,000						

Debt to Assets Ratio Target No more than 60%	54%	0%	55%	55%	56%	55%	55%	53%	51%	49%	49%
Debt Service Coverage Above 2.5	2.54	-	2.42	2.60	2.11	1.75	1.88	2.10	2.19	2.32	2.40
Debt service Coverage w/o CILT Above 2	2.05	-	1.92	2.14	1.63	1.30	1.41	1.62	1.69	1.80	1.87
Current Ratio Above two	2.73	-	3.21	3.16	3.07	2.81	2.71	2.70	2.78	2.90	2.90
Operating Ratio Less than .85	0.78	-	0.80	0.81	0.81	0.82	0.81	0.79	0.79	0.78	0.78
Total Reserves w/o Pension	95,051	102,826	102,759	89,531	84,929	77,218	73,098	75,178	80,598	89,198	99,598
Target for Reserves	77,420	77,420	77,420	63,420	58,466	60,069	62,119	64,281	65,885	66,854	67,788

Electric Long Term Forecast - July 2009 Budget Planning Worksession Scenario 2

	2009 Budget	2009 Projected	2010 Proj	2011 Proj	2012 Proj	2013 Proj	2014 Proj	2015 Proj	2016 Proj	2017 Proj	2018 Proj
85% Average Generation and Altered Rate Schedule											
General Rate Change			May 2%	May 0%	May 4%	May 4%	May 5%	May 3%	May 3%	May 2%	May 2%
BPA Pass Through		November 0%	May 6%	November 7%	November 0%	November 3%	November 0%	November 3%	November 0%	November 3%	November 0%
Net Change in Rates		0%	8%	7%	4%	7%	5%	6%	3%	5%	2%
Contribution Margin Revenue (\$000)											
Residential Retail Rates	80,400	74,800	82,000	85,900	95,800	103,400	110,600	118,200	124,800	131,800	137,800
Small/Medium General Service Rates	45,900	43,500	49,000	51,200	57,600	62,300	66,700	71,300	75,300	79,500	83,100
Large Comm and Industrial Rates	39,700	37,600	37,500	37,900	41,400	43,100	45,700	48,300	50,500	52,800	54,700
Other Retail (Street and Private Lights)	900	900	1,000	1,000	1,800	1,800	2,700	3,600	2,900	3,100	3,200
Wholesale Sales Revenue	53,600	84,800	78,000	77,200	52,200	48,000	46,900	47,100	52,700	53,700	54,300
Total Contribution Margin Revenue	220,600	241,600	247,500	253,200	248,800	258,700	272,600	288,500	306,200	320,900	333,100
Contribution Margin Expense (\$000)											
Purchased Power & Wheeling	97,800	118,300	126,800	128,100	116,600	125,200	129,700	133,900	145,200	150,300	155,600
Thermal Production (IP Fuel Costs)	3,400	1,500	2,800	3,200	3,300	3,400	3,600	1,600	0	0	0
Eugene & Springfield Contribution in Lieu of Taxes	11,200	13,500	12,000	11,800	12,900	13,800	14,400	15,300	16,000	16,900	17,600
Total Contribution Margin Expense	112,400	133,300	141,600	143,000	132,900	142,400	147,700	150,800	161,200	167,200	173,200
Net Contribution Margin	108,100	108,300	106,000	110,100	116,000	116,300	124,900	137,700	145,000	153,700	159,900
Other Revenue											
Miscellaneous Operating Revenue	5,900	6,800	5,800	6,500	8,400	6,500	6,500	6,500	6,500	6,500	6,500
Operating Interest Earnings	5,000	3,700	3,800	3,800	3,300	3,300	3,000	2,900	3,000	3,200	3,500
Total Other Revenue	10,900	10,400	9,600	10,300	11,700	9,800	9,500	9,400	9,500	9,700	10,000
Total Net CM Plus Other Revenue	119,000	118,700	115,600	120,400	127,700	126,100	134,400	147,100	154,500	163,400	169,900
Other Expenditures											
O&M Labor	34,400	33,400	37,100	39,300	41,400	43,700	46,100	48,500	51,200	54,000	55,700
O&M Other	29,100	29,400	29,500	29,900	31,100	32,400	33,700	35,600	37,100	38,600	40,200
Lane Electric Cooperative Payments	400	400	0	0	0	0	0	0	0	0	0
Capital (Net of Bonds and Cust Paid)	18,200	18,200	16,000	16,000	16,600	17,200	18,600	19,400	20,100	20,800	21,500
Debt Service	22,700	22,000	25,700	26,800	27,900	30,600	31,200	32,200	32,500	32,800	33,200
Conservation Program	8,600	8,600	8,900	9,200	9,500	9,800	10,000	10,300	10,700	11,000	11,300
Balance Sheet Changes	1,300	1,300	-200	-300	-500	-400	-1,600	-1,500	-3,100	-3,000	-3,100
Total Expenditures	114,700	113,300	117,000	120,900	126,000	133,300	138,000	144,500	148,500	154,200	158,800
Addition to (Reduction of) Reserves	4,300	5,400	-1,400	-500	1,700	-7,200	-3,600	2,600	6,000	9,200	11,100
Equity Draw for Carmen Smith			4,000	14,000	3,000						

Debt to Assets Ratio Target No more than 60%	54%	0%	56%	55%	56%	55%	55%	53%	51%	49%	49%
Debt Service Coverage Above 2.5	2.54	-	2.18	2.53	2.21	1.76	1.89	2.11	2.20	2.34	2.42
Debt service Coverage w/o CILT Above 2	2.05	-	1.71	2.09	1.74	1.31	1.43	1.64	1.71	1.82	1.89
Current Ratio Above two	2.73	-	3.11	3.05	3.02	2.76	2.67	2.67	2.76	2.89	2.89
Operating Ratio Less than .85	0.78	-	0.82	0.82	0.80	0.82	0.81	0.79	0.79	0.78	0.78
Total Reserves w/o Pension	95,051	102,826	97,381	82,906	81,589	74,384	70,764	73,344	79,364	88,564	99,664
Target for Reserves	77,420	77,420	77,420	63,420	57,744	59,841	61,897	64,059	65,638	66,600	67,517