

EUGENE WATER & ELECTRIC BOARD
BUDGET WORKSHOP
EWEB BOARD ROOM
500 EAST 4TH AVENUE
JULY 7, 2009
6:05 P.M.

Commissioners present: Ron Farmer, President; John Brown, Vice President; Bob Cassidy, Rich Cunningham, Joann Ernst.

Others Present: Randy Berggren, Sheila Crawford, Dick Varner, Jim Wiley, Mel Damewood, Debra Smith, Bill Welch, Jim Origliosso, Patty Boyle, Garilyn Johnston, Tom Buckhouse, and Krista Hince of the EWEB staff; Kim Young, City of Eugene minutes recorder.

President Farmer convened the 2009 Budget Workshop for the Eugene Water & Electric Board (EWEB).

UPDATE ON THE FINANCIAL STATUS OF THE UTILITY

General Manager Randy Berggren provided a high-level overview of the financial status of the utility. He noted that typically the utility engaged in a budget workshop in July for the next budget session. He stated that once general agreement was reached among the Board on the basic budget assumptions, staff launched the budget process internally. He observed that the budget process had been affected by the economic conditions, both locally and globally. He said they needed to begin by developing a new set of assumptions around certain areas such as power markets, retail sales and the lost retail sales, and reductions in some of the miscellaneous revenues such as interest earnings and Systems Development Charge (SDC) contributions.

General Manager Randy Berggren stated that staff had been working the 2009 budget to try to increase certainty on the year-end results. He related that staff was still projecting a small surplus contribution margin, estimated at \$5 to \$5.5 million. He pointed out that the accuracy of the surplus contribution margin could vary from week to week because of the variables that drove it. He said the real value of the ten-year financial plan lay in the first five years. He believed that the utility was “in pretty good shape;” the deficit that had been anticipated in 2010 and 2011 had been pushed out to 2013 and 2014. He added that the “good news” was that EWEB had approximately \$15 million above the reserve targets, after \$11 million was returned from the financing of the Harvest Wind project. He said the current view was that the reserves would not change in 2010 and 2011 and that the following two years after that would “look okay.” After that, the Carmen-Smith project would begin, causing a loss of generation and the obligation to spend \$135 million for the relicensing work. He noted that the estimate for the cost contained a high degree of uncertainty, but he anticipated that staff would have a better understanding of it by the end of 2010.

General Manager Randy Berggren related that staff had found \$3.5 million in the 2009 budget in expenses they had prioritized and had reallocated \$1.5 of that to work that had not previously been budgeted, including Carmen-Smith implementation and North American Electric Reliability Corporation (NERC) compliance. He explained that the \$2 million

remaining had been placed in each director's budget and would be reported as a positive variance to the contribution margin.

General Manager Randy Berggren said what had not been reflected in the budget view presented to the Board was that staff had been trying to identify what a five percent reduction in the non-labor operations and management budget would look like. He stated that staff planned to engage this scenario as the budget development moved forward, though it was not included in the current presentation.

General Manager Randy Berggren underscored that the Board should think about the ten-year financial plan as a planning document that helped staff speak to the Board about the long-term rate implications of what was happening. He said the Board would approve the rate impact for 2010. He added that there was probably some value in this planning initiative, given the current economic conditions, to develop some reporting on a periodic basis regarding certain aspects of the assumptions. He thought it would be possible to see things shift by millions of dollars over the course of a year or two. He advised the Board to take the effort to vet and rebuild the plan, and then think about it as highly volatile and potentially subject to significant shifts in its assumptions. He likened the budget assumptions to trying to predict what the stock market would do.

Patty Boyle, Fiscal Services Supervisor, thought one of the best examples of work to be done on reserve levels would be to determine what would be an appropriate reserve while the utility was in the midst of building the \$135 million Carmen-Smith project.

Commissioner Cassidy said he was chiefly concerned with maintaining reserve levels and if this meant the utility needed to raise rates, he would not be afraid to do so.

In response to a question from Commissioner Ernst, General Manager Randy Berggren stated that Mike McCann was assigned to be project manager for the Carmen-Smith project. He spoke briefly about Mr. McCann's work as the Senior Environmentalist in EWEB's Environmental Department and with the engineering firm, CH2M Hill.

Vice President Brown suggested that the Board consider the results of the last eight rate actions. He found it to be a surprising statistic, as most people would say that rates had gone through the roof, though the rates had not been changed. He hoped this could be publicized.

President Farmer reminded the Board that rates had been increased by 40 percent in 2001.

Commissioner Cunningham believed that EWEB would have to tighten its budget to avoid a large rate increase. He wanted to maintain the reserve funds at an acceptable level, but he felt that EWEB was the only government entity that had not taken "a hit" in the last few years. He was concerned that potential rate increases by six percent in November and seven percent in November, 2010, would hit consumers at a time when the largest number of shut-off notices were being put on doors. He thought this should be a cause for concern. He felt this should challenge the utility to be as frugal as possible.

General Manager Randy Berggren concurred. He said the majority of the rate actions were predicated on decisions made in a public context relative to resource acquisitions. He pointed out that they were similar, if not identical, to an impact on the bottom line relative to increased cost that could not be offset in a sustained basis with operations and maintenance. He underscored that it was not possible to offset Bonneville Power Administration (BPA) reductions with budget cuts. He advocated for the Board to do what it could reasonably do. He stressed that the Board was in a good position as a result of six to seven years of Board-level work. He recalled the Draconian actions that were brought about by the Enron debacle and the recession of 2001. He said he could not recommend that the Board should do, for political purposes, what it did not need to do.

President Farmer noted that he had been elected to the Board immediately after the 38 percent pass through from the BPA had been implemented. He recalled that EWEB had borrowed \$30 million to make it through that hump. He said they had reached the position of having the present reserves by changing the water assumption to 85 percent and by making a commitment to pass through rate increases. He urged the Board to keep this in mind as they moved forward. He encouraged everyone to consider the difference between ten-year planning, which was a work in progress from year to year, and the actual budget that the Board passed each year. He emphasized that these were two different perspectives. He thought the most important part of ten-year planning was to look ahead to the really big items on the horizon, so the Board could get a snapshot of how such a project might affect rates. He also encouraged everyone not to overreact to what might be happening in the market at any given point of time. He noted the natural tendency of the Board to react when the market took a dip.

Commissioner Cunningham asked if it would be possible for staff to generate a list of options for what could be trimmed from the budget and what could not be trimmed from it. General Manager Randy Berggren responded that he planned to do so, but would not be able to conduct such an exercise across the entire budget with any certainty. He reiterated that staff was undertaking just such an exercise and would introduce the idea in September with regard to the non-labor operations and maintenance. He underscored that he had intentionally not recommended reductions in labor because of the recently completed International Brotherhood of Electrical Workers (IBEW) contract and the non-represented employees because he did not see sufficient financial justification to do so at present.

Commissioner Cunningham noted that he was meeting regularly with staff in order to have an increased understanding of the budget and he encouraged his colleagues to do the same.

Commissioner Ernst remarked that she was not afraid of a rate increase but she needed to be convinced that EWEB was being prudent in its own budget in this time of economic crisis. She said a lot of people had been forced to “tighten their belt” and she felt that EWEB would also have to do so. She indicated she would join Commissioner Cunningham in meeting with staff regarding the budget.

ELECTRIC LONG-TERM FINANCIAL PLAN AND 2010 BUDGET ASSUMPTIONS

Ms. Boyle presented the long-term financial plan and reviewed the 2010 budget assumptions. Copies of the presentation were provided to the Commissioners. She noted that the conservation efforts were based on the Board’s approved program. She was certain the

Board would update the program and the costs would be reflected in the Conservation Program line of the Contribution Margin Revenue page of the presentation.

Ms. Boyle noted that EWEB was experiencing a lower demand for power, called load loss, in most customer classes. She observed that typically this would not cause a financial consequence because the retail rates were set at a level that was normally found to be lower than what they could sell the wholesale power out onto the market. She underscored that this was not the case at present and EWEB was currently generating less revenue with less load than it normally would. She stated that forecasts brought back this load, in anticipation of economic recovery, and this would reverse itself and rates would become lower than the assumed wholesale rate.

Commissioner Cunningham asked at what point the Board would be “eligible” to have an executive session to discuss salary strategies. General Manager Randy Berggren replied that the utility would have to engage in tangible negotiations.

Mr. Origliosso explained that the financial plan included increases for labor. General Manager Randy Berggren clarified that current practice was to utilize “World at Work” statistics for what the cost of living adjustments (COLA) should be.

Ms. Boyle stated that the “World at Work” survey was published each August. She said the 2010 budget assumption included a four percent increase for IBEW workers, as the contract indicated, and a three percent increase for those employees who were non-represented. She explained that they would recalibrate that number when the “World at Work” survey came out in August, 2010.

Ms. Boyle underscored that wages were not one of the key drivers of the budget. She said wholesale power sales, BPA rates, and what EWEB committed to for debt service were key drivers. She stated that this did not mean that they would ignore wages, but they were in a separate category in terms of fine-tuning the forecast.

Commissioner Cunningham wondered if it would be possible to increase the commercial rates for electricity. Ms. Boyle responded that the Board had yet to face a rate action for electricity. She explained that a great deal of analysis went into the rate structures and included the cost of delivery to the rate classes among other things. She noted that the Board could choose to discuss the rate structure and could request a future rates study.

Ms. Boyle reported that the power trading staff had initiated its annual hedging program in order to lock in what would be expected to be the minimum in revenues associated with wholesale sales. She said staff would be better able to commit to wholesale revenue numbers in September. She noted that at present the floor was pretty low and EWEB was not seeing that the market itself was willing to take much risk and give EWEB good prices.

Continuing, Ms. Boyle said other major issues in the long-term financial plan included new generation facilities. She explained that because they would be selling the power at wholesale levels as the facilities came on it would have a cash impact. She cited the Harvest Wind project and the Seneca generation facility as two examples. She also noted that the BPA had increased costs for operations and had made an adjustment to the residential exchange credit.

Regarding the latter, she related that the \$6 million annual credit that EWEB was originally slated to receive had been reduced to \$3 million. She added that the 2011 BPA contract also reduced EWEB's entitlement significantly. She noted that the depressed price environment made the loss at a lower value but it was still projected to be seven percent.

In response to a question from Commissioner Ernst, Ms. Boyle clarified that the residential exchange had been a court-ordered amount, but the BPA had made an error in its communication to EWEB on what to expect on an ongoing basis. General Manager Randy Berggren added that the error had been regional; all of the affected utilities had been told they would be receiving more.

Ms. Boyle reported that EWEB would be issuing the second portion of the debt for completion of the Roosevelt Boulevard building in 2010 and the cost was incurred accordingly.

Vice President Brown ascertained from Ms. Boyle that there would be savings in the Roosevelt Boulevard project because of the cost escalators that had been included in the budget which were not being realized in the current construction market. General Manager Randy Berggren stated that they had taken approximately \$500,000 off of the original assumption for the debt service costs, which reflected an anticipated finish point estimated at \$76 million currently. Ms. Boyle added that the forecast indicated the clearly known savings and it would be updated as more information was available. General Manager Randy Berggren stressed that they would not know the final cost until the project was completed.

Commissioner Ernst asked if the property sale was "on track." General Manager Randy Berggren replied that staff could not know this at present. Ms. Boyle said the sale of the property was included in previous versions of the long-term financial plan, but it had been clear that it would not necessarily be a likely assumption. She explained that this kept debt service higher, but it also kept capital lease revenues from the water utility up.

Commissioner Cunningham requested a graph that delineated the ten-year projects for Public Employees Retirement System (PERS) contributions. General Manager Randy Berggren replied that staff could provide its best information, but the actual amounts were unpredictable. He anticipated that the PERS costs would increase.

General Manager Randy Berggren stated that in the near-term the majority of the EWEB rate actions would be driven by increased debt service and escalation in labor. He said the bottom line, however, was that the reserves should remain fully funded and that EWEB should continue to collect minimal additions or reductions to reserves. He reiterated that the long-term financial plan would be most impacted by the relicensing work at Carmen-Smith and that the facility would have to go off line while the work was undertaken.

Ms. Boyle said the first rate scenario maintained the current policy perspective, passed through a BPA increase in November, and anticipated a small EWEB increase in the spring. She noted that she had approximated what the BPA rates would be because she did not know for certain what rates they would be pushing. She added that no one knew what those rates would be. General Manager Randy Berggren said they had a high degree of confidence that staff's projection for the rate increase was close.

Ms. Boyle outlined the second rate scenario. She said it represented two changes from the policy perspective; in the out years it assumed a higher level of generation and it provided for a more realistic expectation about it. She related that it provided a platform for discussion on whether to pass through the BPA rate increase or delay it and what consequences that would create. She explained that the absolute cost of pushing the rate increase to the spring was approximately \$5 million and would take EWEB from a near \$4 million surplus to a \$1.5 million deficit. She said in order to reach a balanced budget they would have to get the money from reserves or through cost reductions.

Debra Smith, Director of the Employee, Customer, & Community Services Division, estimated that the Customer Care program would carry over approximately \$500,000 to the next year.

In response to a question from Commissioner Cassidy, Ms. Smith stated that EWEB was developing a proposal for how to use the remaining money and augment existing program offerings for the next fiscal year. She welcomed input from the Board.

In response to a question from Commissioner Cunningham, General Manager Randy Berggren stated that EWEB took its investment in conservation into account. The utility had an abundance of information on the investment made in conservation and the impact on load and, thus, the budget. Mr. Origliosso added that in normal circumstances when there was a great deal of conservation, the utility was able to sell excess power on the wholesale market and benefited from it.

Vice President Brown ascertained from General Manager Randy Berggren that it would require a charter amendment to change the amount paid to the city as a Contribution in Lieu of Tax (CILT) from 6 percent of retail sales and 17 percent of gross wholesale sales. Mr. Origliosso clarified that the only way to change this amount would be if the two parties could agree and neither party was financially disadvantaged by the change.

Ms. Boyle observed that the CILT was a “dearly held” revenue source for the city.

President Farmer asked how far into the future staff felt comfortable with the projections and how far off the projections the actual numbers could be for them to cause discomfort. Mr. Origliosso responded that the actual numbers could stray as much as three to four percent. Ms. Boyle said without the ability to go to the reserves there would not be much flexibility. She noted that the 85 percent hydro assumption had been developed in a time period when there had been no reserve funds and the idea behind the change had been to build them up.

Ms. Boyle asked for the Board to provide her with some feedback as to whether to implement the BPA rate pass through in November or to finance it in order to delay it until the spring.

Commissioner Cassidy supported enacting the rate pass through when it came from the BPA in November.

Commissioner Ernst wanted to meet with staff and discuss the budget further before making the decision.

Vice President Brown said he would not want to take the chance of incurring a \$5 million expense in the current economic environment. He preferred to pass the rate action through in November.

Commissioner Cunningham wondered whether the rate increase could be split more evenly between the November and spring rate actions. General Manager Randy Berggren explained that the impact of only enacting a rate increase of four percent in November would be approximately \$2.5 million.

Commissioner Ernst indicated her support for passing through a six percent BPA rate action in November.

Mr. Origliosso noted that the reason the spring rate action had been suggested in the financial plan was to counter the impacts that costs brought about by the Harvest Wind project and the Roosevelt building project would have on the revenue stream. General Manager Randy Berggren thought it could potentially be mitigated by expense reductions. He said if staff was successful in finding a five percent reduction in non-labor operations and management, the cost could be mitigated for one year.

Commissioner Cunningham said he would be willing to consider the six percent pass through in November provided that there was something in the budget that would help the unemployed and disabled ratepayers to get through this time of economic hardship. He noted that current projections indicated that it would be the third quarter of the next year before they would start to see signs of economic recovery. General Manager Randy Berggren replied that staff intended to discuss this. He added that a one-time savings for a one-time expense would provide a real financial match for a program like the Customer Care Program.

President Farmer called for a short break at 8:10 p.m.

WATER LONG-TERM FINANCIAL PLAN AND 2010 BUDGET ASSUMPTIONS

Ms. Boyle stated that the water utility experienced less variability and, as a result, there was less new information. She said the last forecast anticipated about nine percent in rate increases and, at present, a seven percent rate increase was anticipated.

Senior Financial/Rates Analyst Garilyn Johnston highlighted the long-term financial plan for the water utility and the assumptions for the 2010 budget, aided by power points. She stated that one driver for the seven percent increase was the aging infrastructure. She noted that every water utility faced a similar challenge. She said the water utility was still striving to pay into reserve funds, but had been hit with its portion of PERS liability.

Ms. Johnston stated that water use was down. She was not certain if it was attributable more to conservation or to the economy. She said the utility had ratcheted growth to zero in 2012. Ms. Boyle noted that the utility did not project a great amount of growth in other years, generally around one-half percent.

Ms. Johnston reported that the long-term financial plan included the Roosevelt Boulevard building project. She said the capital lease would come through at about \$1.9 million annually.

She noted that the water utility had a 2011 bond issue planned for capital, though the dollar amount could change before the capital plan was presented on July 21. She stated that there would be another bond in 2017 to address the need for a second source, which would create a large increase to debt service in the 10-year plan.

Commissioner Ernst asked what regulatory agency oversaw the water utility. Tom Buckhouse, Director of the Water & Steam Division, replied that EWEB was the body that held the water utility responsible for the reliability of the water. General Manager Randy Berggren explained that the agencies EWEB had to work with on the water utility side were outcome-based agencies. He said if EWEB did not manage water reliability well, it would have to deal with an entity such as the Department of Environmental Quality (DEQ).

Commissioner Cunningham expressed concern about the projected amount of the bond issue for second source funding. President Farmer commented, in response, that when he had come on the Board the bond issue had been planned for 2010. He predicted that the amount and timing of the bond would likely change again as the 2017 item was more of a placeholder. General Manager Randy Berggren added that he had been working on this issue since he began working for EWEB in 1990. He explained that EWEB was one of the largest water suppliers in the state and had no secondary supply. He stressed that there was a very low probability of something causing the water supply to fail but, should that occur, it would create an extremely high impact.

Ms. Johnston continued her presentation. General Manager Randy Berggren noted that the seven percent rate represented the tail end of a commitment by the Board at a policy level to fund aging infrastructure. He stated that after the seven percent increase, the rate increases were more related to normal inflationary increases at three and four percent.

Commissioner Cassidy commented that EWEB should be more sensitive to reserve funds. He suggested enacting a larger rate increase and having more reserves. General Manager Randy Berggren replied that, with current rates, EWEB would reach its planned reserve target in 2012. He said the Board could choose to expedite reserve building and enact larger rate increases.

Commissioner Cassidy asked for more background information regarding the fire hydrants. General Manager Randy Berggren responded that EWEB would not see any cost, and could realize some potential savings, because the recent agreement meant that city Fire Department personnel would not be “hammering” on the water lines testing the hydrants and EWEB would not have to replace as many water mains. He believed that taking on the interim agreement with the city would save money.

Vice President Brown asked if the program on the McKenzie River that inspected septic tanks in high risk areas and provided for water monitoring would continue to be funded. Mr. Buckhouse affirmed that it would.

Ms. Boyle understood that the Board was expressing a general interest in moving forward with the seven percent rate increase.

In response to a question from Vice President Brown, Ms. Boyle stated that staff would study how to exactly distribute the proceeds from the sale of the riverfront EWEB property. She said the land issues the property faced were complicated and acknowledged that land under the building was owned by the water utility.

President Farmer indicated that he was comfortable with a seven percent rate increase. He acknowledged that water rights were not part of the current discussion, but wanted to underscore his support for moving forward on them expeditiously. He was concerned about not having enough money in the reserves for water at the beginning of the year. He was willing to live with the rates as they were projected because even though a percentage increase to water rates did not create a huge financial impact, the perception of a dramatic increase could feel like “one more stone” on top of the head for people who were currently under financial duress. Regarding the second source funding, he did not think there would be Board buyoff on \$120 million until a more cost-effective solution was found.

Commissioner Ernst expressed discomfort with a seven percent increase.

COMPARATIVE RATE STUDY

Ms. Boyle reviewed the information in the memorandum entitled Comparative Rate Analysis Update dated June 30, 2009. She noted that staff had added some of the other area water suppliers, at the Board’s request. General Manager Randy Berggren noted that Medford sold a large amount of water for agricultural purposes, which brought their rates down.

President Farmer asked staff to speak to the Springfield Utility Board (SUB) rates and why Eugene’s rates tended to be nearly 50 percent higher. General Manager Randy Berggren responded that, in the post-2011 contract the BPA, it was very unlikely that SUB would continue to get exclusively Tier 1 hydroelectric resources. He believed that SUB would be obligated to develop resource Tier 2 requirements at market price. He predicted that this would “level the playing field” to a degree. He also noted that SUB did not do as much in terms of conservation as EWEB did. Ms. Boyle suggested that she follow the SUB budget process.

In response to a question from Vice President Brown, General Manager Randy Berggren stated that SUB was “only” an 80 megawatt system and he speculated that SUB had lost 8 to 10 megawatts in the new BPA contract.

Power Management & Planning Manager, Dick Varner, elaborated on the differences in the BPA contracts for EWEB and SUB. He explained that SUB was a requirements customer. He said what would hit EWEB in 2011 would not hit SUB; SUB would just be responsible for its load growth going forward. He predicted that SUB would get enough power to cover its load as its 2010 level. He stated that as EWEB was a Slice customer, it had signed a contract with the BPA for a fixed amount of power based on a projection of what the load would be going forward. He said EWEB had not experienced this expected load growth due to the recession and the shutdown of Weyerhaeuser’s paper machine and other events. He related that EWEB had “basically cut a really good deal” with the BPA and in 2011 the BPA was taking that good deal back and allocating only what EWEB’s load justified.

In response to a question from Commissioner Cunningham, Mr. Varner said there was a low likelihood of dramatic increases coming from the BPA, as had happened in 2001. He explained that in 2001 the BPA had committed to more supply than it had resources for and had to go to the power market to supply its customers during very expensive markets. He added that the “wild cards” included what would happen with the Snake River dams, the nuclear plant, and the legal decisions regarding the operation of the rest of the Columbia River system. He said any one of those items would be a big number that would hit every utility the BPA served. He related that elimination of the Snake River dams would mean the loss of a \$30 resource and replacement of that resource with \$60 power. He noted that the loss of the nuclear resource would create a similar impact.

Commissioner Cunningham asked what the power from the Seneca biomass generation project was projected to cost. Mr. Varner predicted it would be in the \$80 per megawatt range. He added that it was firm, flat power.

Commissioner Ernst believed that the “push” was growing to remove the Snake River dams and asked what the timeline was on it. Mr. Varner responded that it was all supposition at this point. He said there were interest groups on both sides of the issue and part of it would depend on what Judge Redden or his successor decided to order. He underscored that at present there was no political consensus to do anything.

Commissioner Cunningham asked what assumption the average monthly bills, as portrayed in the comparative rates study, was based on. He could not recall the last time he had an electric bill that amounted to only \$89. Ms. Boyle replied that each customer profile was described in the materials and the average monthly bills were based purely on a system-wide average.

Commissioner Cunningham said he did not want to raise the rates, but he recognized that it was necessary. He wanted to get something put into play so that people who needed help could receive it for their water bills as well. Ms. Boyle responded that they could work with the water utility to make sure that the two utilities go “hand in hand” in the program development.

Commissioner Cunningham remarked that it would benefit the community if the utility could incentivize businesses for job creation by adjusting rates for businesses that created jobs.

President Farmer adjourned the EWEB Budget Workshop at 8:58 p.m.

Assistant Secretary

President