

EUGENE WATER & ELECTRIC BOARD
WORK SESSION
EWEB BOARD ROOM
500 EAST 4TH AVENUE
JUNE 7, 2011
5:30 P.M.

Commissioners Present: John Brown, President; John Simpson, Vice President; Bob Cassidy, Joann Ernst, Rich Cunningham

Others Present: General Manager Roger Gray, Debra Smith, Lance Robertson, Clay Norris, Tom Buckhouse, Patty Boyle, Sheila Crawford, Jennifer Joule, Edward Yan, Andrea Mason, Kathleen Engstrom, and Taryn Johnson of the EWEB staff; Ruth Atcherson, minutes recorder.

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

FINANCE POLICY REVIEW

Director of Customer & Shared Services Division, Debra Smith, explained that the first item ensured that the Board did its due diligence prior to the budget retreat by reviewing the financial policies of the utility. She provided a power point presentation on *Financial Policies*, hard copies of which were provided to everyone present. Regarding *1.1 Rate Sufficiency Policy*, she stressed that the key to the policy lay in the words "*over and above requirements for compliance with existing bond covenants.*" She noted that the municipal bond market was showing signs of improvement, which was good news. She said, regarding *Performance Standards*, that Commissioner Cassidy had commented that debt service coverage of 2.44x might be conservative. She had looked into the standards of several other utilities and thought this was worth reviewing.

Ms. Smith discussed *1.2 Rate Stability Policy* and the *Reserve Targets* associated with it. She underscored that most were not discretionary. She reiterated that the Carmen-Smith reserve fund had been set up to provide equity in the project, but it was considered discretionary in that it was not bound by policy to the one project.

Commissioner Ernst recalled discussing the formation of a similar reserve fund for the Advanced Metering Infrastructure (AMI) project. She thought they could have the same flexibility to put reserves toward it and then later look into a reimbursement resolution. Ms. Smith agreed. She said it could be strategic in terms of what could happen to the debt market and interest rates. She explained that if the Board directed staff to bring a reimbursement resolution forward, it would preserve the Board's right to do so and the discussion could happen at a later date.

Vice President Simpson asked what right a reimbursement resolution would preserve. Ms. Smith responded that this resolution would state that they could go back 60 days prior to the day it was approved and when such time the utility issued debt it could reimburse itself for

money spent out of cash on hand. She stated that debt had been issued at a couple of different points for the Roosevelt Operations Center (ROC), as an example, and then there was sufficient cash on hand and the utility decided to fund the remaining costs out of the operating fund and passed a reimbursement resolution. She said when Financial Manager Cathy Bloom returned later in the month from the debt the utility was currently issuing, the utility would reimburse itself for the cash spent. She stressed that passing the resolution did not oblige the Board, it simply preserved the right to reimburse.

In response to a question from Commissioner Cunningham, Ms. Smith stated that the utility was not able to issue its own bonds because the overhead of managing them was too much.

In response to a question from Commissioner Ernst, Ms. Smith explained that when the utility issued debt it was required to be for a very specific purpose and if the money was not used completely as specified, the remainder was not used for another purpose. She suspected that AMI would be financed by a combination of debt and reserves. She said the timing of projects would be in a more long-range plan.

President Brown asked what percentage of the EWEB rates was made up by interest. He noted that the Springfield Utility Board (SUB) had the lowest rates and it also had no debt. Ms. Smith replied that EWEB staff had compiled a specific comparison of SUB and EWEB and she could provide copies of it to the Board. She was not certain what the exact percentage of rates was related to interest.

Vice President Simpson asked if EWEB had reached the Carmen-Smith reserve fund target. Ms. Smith responded that there had been a couple of designated funds that had no target and Carmen-Smith had been one of them. She said the other one was the retirement fund.

Commissioner Cunningham asked if EWEB intended to raise reserve levels through rate actions. Ms. Smith assured him that this was not the case; rates were set in order to balance the budget.

Ms. Smith noted that the water utility currently had exceeded its capital reserve target because they knew there were substantial investments in the water utility infrastructure in the coming years.

General Manager Gray said maintenance would never be funded with bond proceeds; current practice was to fund it completely with rates and capital reserves that were funded by rates. He explained that the Carmen-Smith project would provide an inter-generational benefit and because of this the use of bond funding could be justified.

Ms. Smith discussed the *1.4 Retirement Benefits Funding Policy*. She said the important thing to remember about the policy was that if EWEB assumed a certain Public Employees Retirement System (PERS) contribution rate and the actual rate was less than that, regardless of how the utility did on a contribution margin basis, the difference would be put into the account and the Board would have the opportunity to advise staff on how to utilize the excess funds.

Continuing, Ms. Smith highlighted *2.1 Cost Management Policy*, which stressed the obligation to manage costs, and *2.2 Budget Policy*.

In response to a question from Vice President Simpson, Ms. Smith clarified that operating income was after the operations and maintenance expenses and net income included interest expense, other revenues, and interest earnings.

Ms. Smith highlighted *2.3 Debt Policy* and the *Performance Standards* associated with it. She stated that the debt to asset ratios for EWEB were "fairly conservative." She reviewed *2.4 Billing and Collection Policy* which dictated the utility's collection standard.

Moving on to risk policies, Ms. Smith discussed *3.1 Enterprise Risk Management Policy* and *3.2 Power Risk Management Policy*. She also highlighted *4.1 Financial Entity Policy* and *4.2 Capitalization Policy*. She said EWEB capitalized its labor costs for capital projects. Patty Boyle, Fiscal Services Manager, added that there was just under \$10 million in capitalized labor costs out of a \$70 million labor budget.

President Brown asked why they were not discussing the coal gasification that could cost between \$20 and \$40 million. Ms. Smith replied that majority of the expense was being borne by EWEB's partners and the agreement was confidential. She said if the Board was interested in the information, it could call an Executive Session to discuss it.

ZERO BASED BUDGETING 101

Ms. Smith invited Andrea Mason to join her before the Board. She said Ms. Mason had enjoyed a long tenured career with EWEB and was now providing leadership in the Zero Based Budgeting process. She stated that the purpose of the discussion was to "manage expectations" and to ensure that she and Ms. Mason were doing the work most helpful to the Board.

General Manager Roger Gray explained that the change in budgeting process would take between three and seven years, beginning with a change at EWEB's cultural level. He noted that EWEB did not have the business systems in place currently to support this approach.

Ms. Smith provided a power point presentation on Zero Based Budgeting, hard copies of which were provided to everyone present.

Vice President Simpson asked if the process was grounded and cast from the Board in 2010 or whether it would be dynamic. Ms. Smith responded that staff was developing scenarios and they were intended to change and to be tweaked as they saw the results in the operational cycle.

Commissioner Cassidy surmised that in this type of budgeting they would look at each department and asking what its mission was, how well it was being done, and if it could be done better.

Ms. Smith reviewed the *2011 ZBB Budget Timeline*, and pointed out that the utility had formed division work groups which had met in March and April on just what Commissioner Cassidy had called out.

General Manager Gray said he would characterize the process of Zero Based Budgeting as looking at the multitude of decisions to make, but staff planned to distill this to some scenarios with basic decisions to make initially. He stated that it would be a multi-year process to integrate it into the utility's culture.

Vice President Simpson asked what the General Manager's authority was to make this change. General Manager Gray responded that the Board would make decisions about the different areas of budgeting, but there had not been specific direction to the General Manager to adopt Zero Based Budgeting. He had sensed frustration in the 2010 budgeting process from the Board and thought this effort would reduce that frustration.

Vice President Simpson indicated that he favored this approach.

Ms. Smith reviewed the work that the employee groups had done to form the organizational scenarios. She said the Board would have the opportunity to look at the scenario impacts on things like the organization's debt service coverage ratio and rates. She related that staff's idea of success for the July 12 financial retreat would be for the Board to direct staff to return with no more than two scenarios, that they would then have built a budget for them. She stated that they would return in October with a budget consistent with the scenarios selected by the Board.

Commissioner Cassidy asked that the scenarios be "kind of specific and kind of realistic." Ms. Smith assured him that they would be so.

General Manager Gray predicted that there would be "people impacts," but he thought they would be at the level that they could be addressed through attrition as opposed to lay-offs.

Vice President Simpson commented that he would prefer, if they were basing budgeting on scenarios, not to call it Zero Based Budgeting. He asked if the actual process of doing the budget in this manner would cost more than the prior budgeting method. Ms. Smith was not certain, but she did consider it to be a great investment. She stressed that Zero Based Budgeting was a planning and decision-making model that asked departments to go back through all of their expenditures in order to be very clear about what the organization and Board could expect as outcomes for the inputs authorized to the departments' individual budgets.

President Brown adjourned the Work Session at 7:16 p.m.

Assistant Secretary

President