



MEMORANDUM

EUGENE WATER & ELECTRIC BOARD

Rely on us.

TO: Commissioners Brown, Carlson, Mital, Simpson and Helgeson

FROM: Sue Fahey, Chief Financial Officer; Deborah Hart, Interim Finance Manager;
Adam Rue, Interim Fiscal Services Supervisor; Jerry Reller and Nate Schultz
Senior Financial Analysts

DATE: September 21, 2018

SUBJECT: 2019 Draft Budgets and Long-Term Financial Plans Update

OBJECTIVE: Direction on 2019 Budget and Price Changes

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 preceding calendar year. The foundation of the Electric and Water Utilities' budgets are the long-term financial plans (LTFP), which help ensure that the budgets approved provide long term financial stability for both utilities. Staff has prepared draft 2019 budgets and updated LTFPs for the Board's consideration. Based on Board direction provided at the October 2rd meeting, staff will develop budgets and price proposals for consideration at the November 6th Board meeting, and approval at the December 4th meeting.

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, reducing debt service obligations, and prudently using reserves to strengthen financial metrics. Strong water sales, cost controls, and debt reduction have bolstered reserve levels and greatly improved the financial stability of the Water Utility. The Electric Utility has used reserves to defease debt and reduce borrowing for the Carmen-Smith relicensing capital project. These actions coupled with other debt restructuring and cost containment have resulted in significant improvement to the debt service coverage ratio (DSC) which historically has been the Electric Utility's biggest financial challenge.

Discussion

A primary focus for 2019 and beyond is updating our infrastructure that supports our strategic direction in improving resiliency and fostering customer confidence, as well as our core values of Safety, Reliability, Responsibility and Community and allows EWEB staff to effectively respond to emergencies or unexpected events.

At the July 10, 2018 Board meeting, Commissioners directed staff to upgrade our meter infrastructure and deploy smart meters to all customers by the end of 2021 in order to take advantage of benefits such as leak and power quality detection monitoring, remote meter readings,

and better information to aid restoration efforts. This has been built into the 2019 budgets and updated LTFFP.

EWEB continues to focus on fostering customer confidence by aligning sustainable spending levels to customer-owners' expectations. In 2017, EWEB developed an affordability target (percentage of utility cost to median household income) of 3.2%. Based on the most recent available data, EWEB customers spend 3.87% of median household income on their electric and water bills, down from 4.06% last year. Within the framework of delivering safe and reliable water and electricity, Management is committed to prudent stewardship of our customer-owners' financial and natural resources. Management believes the assumptions used to develop the LTFFP balance financial responsibility, operational resiliency, and affordability.

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 2019 budget. Utility specific assumptions are noted on Attachments 1, 2 and 3.

Both Utilities

- 2.0% non-labor CPI increase
- Labor/benefit increases:
 - 3.5% wage escalation
 - PERS – Pay down unfunded liability by \$36 million resulting in no employer rate change in 2019 (2016 advisory valuation indicated EWEB's independent employer increase would be 8 percentage points), 5 percentage point increases in July 2021, 2023, 2025 and 2027
 - Health insurance increase – 2% in 2019 and then 8% in subsequent years
- Shift in Shared Services allocation to 80% Electric/20% Water, from 82%/18%, respectively. The split is based on share of total plant in service, revenues, and direct labor. Since 2012, the Water Utility's proportionate share of the total in each category has steadily risen.
- Affordability Initiative savings of \$1.8 million in 2020 and 2021 combined
- Efficiency gains of \$4 million in 2020 thru 2026 from deployment of smart meters

At the July Board Meeting, the Board directed staff to prepare the draft 2019 budgets based on the assumptions presented. Since July, the following assumptions have changed:

Both Utilities

- \$4.7 million capital decrease for AMI – Electric and Water – due to extending implementation from 2 to 3 years
- \$500,000 increase to capital for renovations related to consolidating operations
- \$350,000 decrease for health insurance. EWEB's 2019 premiums are projected to increase 2% compared to 6% in July

Electric

- \$700,000 increase in Electric contribution margin due to higher projected wholesale prices
- \$500,000 added for efficient electrification customer incentives
- \$900,000 decrease in O&M for renovations related to consolidating operations, which are now budgeted in capital

- \$1.5 million shift from Capital to O&M. Adjusting for changes in overhead and labor for capital work due to refinements in the capital budget. The July draft LTFP included assumptions around percentage of labor as well as overhead rates. The capital budget now has labor specifically budgeted to projects, and overhead rates have been refined to reflect the nature of the capital work that was budgeted

Water

- \$1.6 million shift from O&M to Capital. Adjusting for changes in overhead and labor for capital work due to refinements in the capital budget
- Construction of a secondary treatment plant moved from 2026 to 2023

Long-term Financial Plan Price Assumptions and Outcomes

Electric

The Electric Utility LTFP indicates no overall average revenue requirement change is needed in 2019. Four out of the last five years the Electric Utility has had no increase in revenue requirement. Other than the biannual BPA increase, revenue requirements are not projected to be higher in 2020. Through debt reduction and cost-saving initiatives, the Electric Utility is above its debt service coverage target, which has been a challenge in the past. The Electric LTFP outcome is included in Attachment 1. Financial metrics are within Board targets for all years of the plan. Attachment 1 includes a contribution margin risk factor of \$3 million, which is sufficient to cover a 10% reduction in generation, a 2.4% reduction in load, or a 47% wholesale price reduction. Management believes that this is a prudent assumption, sufficient to cover risk in most years, with strong cash reserve balances that could be used to cover additional shortfalls, if necessary. Attachment 2 provides financial metric information if wholesale prices decreased 20%.

Water

The Water Utility is forecasting no additional revenue requirement through 2021. This is the second year with no overall increase in revenue requirement. Days Cash averages more than 400 days and reduces throughout the LTFP as reserves are used to smooth price impacts. All other Board approved financial metrics remain within target across the ten year plan. The Water LTFP outcome is included in Attachment 3.

Recommendation

Management recommends that the Board direct staff to prepare the 2019 proposed budgets using the assumptions set forth in this document. This includes a no overall average price impact for both utilities, but may include class adjustments based on the cost of service analysis, the results of which will be presented at the November 6, 2018 Board meeting.

Requested Board Action

Management is not requesting Board action at the October 2nd meeting; however, staff is requesting that the Board provide direction on the assumptions included in the draft budget. At the November 6th Board meeting, Management will present the budgets and price change proposals which are scheduled to be approved at the December 4th meeting.

Attachment 1 - Summary of Electric LTFP Price Assumptions and Outcomes

Attachment 2 – Summary of Electric LTFP Outcomes with 20% Wholesale Price Decrease

Attachment 3 - Summary of Water LTFP Price Assumptions and Outcomes

Attachment 4 - Median Household Income (MHI) %

Summary of Electric LTFP Revenue Requirement Assumptions and Outcomes (000's omitted)

<u>Key Metrics</u>	<u>Current Target</u>	<u>2019</u>	<u>2020</u>	<u>2021</u>	<u>2022</u>	<u>2023</u>	<u>2024</u>	<u>2025</u>	<u>2026</u>	<u>2027</u>	<u>2028</u>
Reserves and Cash	\$83,720	\$136,700	\$134,600	\$133,800	\$137,900	\$140,600	\$145,100	\$144,100	\$149,600	\$156,600	\$159,400
Debt Service Coverage Ratio	1.75	2.17	2.15	2.89	2.13	2.05	2.13	2.06	2.34	2.43	2.17
Days Cash	>150 Days	252	258	262	253	251	249	243	249	262	265
Average impact resulting from change in revenue requirement		0.00%	2.50%	1.50%	3.75%	2.00%	2.50%	1.00%	2.50%	0.00%	2.50%

Revenue Requirement Assumptions:

<u>Price Schedule</u>	<u>Compounded 10 Year Total</u>	<u>2019</u>	<u>2020</u>	<u>2021</u>	<u>2022</u>	<u>2023</u>	<u>2024</u>	<u>2025</u>	<u>2026</u>	<u>2027</u>	<u>2028</u>
General Rate Increase	4.57%			1.50%		2.00%		1.00%			
Carmen/Smith Debt	1.25%				1.25%						
BPA Increase	13.14%		2.50%		2.50%		2.50%		2.50%		2.50%
Average impact resulting from change in revenue requirement	19.75%		2.50%	1.50%	3.75%	2.00%	2.50%	1.00%	2.50%		2.50%

Key Assumptions

- Retail load approximately the same as 2018 budget – 2.4 million MWh and flat in the out years with customer growth offset by conservation
- 2019 contribution margin risk tolerance of \$3.0 million which represents 90% generation, 2.4% load reduction or 47% wholesale price reduction
 - Similar contribution margin risk tolerance through 2023, expected conditions 2024-2028
- \$23 melded mid-market price curve increasing to \$35 in 2028
- Partial year Carmen-Smith generation outages in 2019 and 2023
- \$1.4 million contribution margin reduction due to increased Snake and Columbia River dam spills for fish migration
- Bond issuance: \$40 million in 2021 funding Carmen-Smith capital work
- \$1.0 million per year contribution to meter replacement reserve starting 2021 based on 12 year estimated life
- 2.0% non-labor CPI increase
- Labor/benefit increases:
 - 3.5% wage escalation
 - PERS – No change in 2019, 5 percentage point increases in July 2021, 2023, 2025 and 2027
 - Health insurance increase – 2% in 2019 and then 8% in subsequent years
- \$27.4 million to pay down PERS liability
- \$850,000 decrease in O&M due to shift in Shared Services allocation
- \$500,000 for efficient electrification customer incentives
- \$4.7 million combined Affordability Initiative and Efficiency Savings through 2026

**Summary of Electric LTFP Revenue Requirement Assumptions and Outcomes (000's omitted)
20% Wholesale Price Reduction**

<u>Key Metrics</u>	<u>Current Target</u>	<u>2019</u>	<u>2020</u>	<u>2021</u>	<u>2022</u>	<u>2023</u>	<u>2024</u>	<u>2025</u>	<u>2026</u>	<u>2027</u>	<u>2028</u>
Reserves and Cash	\$83,720	\$135,300	\$132,600	\$130,300	\$132,700	\$130,100	\$131,100	\$126,600	\$128,700	\$132,900	\$137,400
Debt Service Coverage Ratio	1.75	2.08	2.11	2.79	2.04	1.76	1.91	1.84	2.13	2.25	2.28
Days Cash	>150 Days	249	238	240	230	218	208	198	200	209	221
Average impact resulting from change in revenue requirement		0.00%	2.50%	1.50%	3.75%	2.00%	2.50%	1.00%	2.50%	0.00%	2.50%

Revenue Requirement Assumptions:

<u>Price Schedule</u>	<u>Compounded 10 Year Total</u>	<u>2019</u>	<u>2020</u>	<u>2021</u>	<u>2022</u>	<u>2023</u>	<u>2024</u>	<u>2025</u>	<u>2026</u>	<u>2027</u>	<u>2028</u>
General Rate Increase	4.57%			1.50%		2.00%		1.00%			
Carmen/Smith Debt	1.25%				1.25%						
BPA Increase	13.14%		2.50%		2.50%		2.50%		2.50%		2.50%
Average impact resulting from change in revenue requirement	19.75%		2.50%	1.50%	3.75%	2.00%	2.50%	1.00%	2.50%		2.50%

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

<u>Key Metrics</u>	<u>Current Target</u>	<u>2019</u>	<u>2020</u>	<u>2021</u>	<u>2022</u>	<u>2023</u>	<u>2024</u>	<u>2025</u>	<u>2026</u>	<u>2027</u>	<u>2028</u>
Reserves & Cash	\$12,680	\$27,400	\$27,400	\$24,700	\$25,100	\$26,100	\$29,800	\$32,400	\$27,600	\$23,500	\$19,000
AWS Reserve Balance		\$5,600	\$5,200	\$4,900	\$4,500	\$0	\$0	\$0	\$0	\$0	\$0
AMI Reserve		\$0	\$0	\$300	\$800	\$1,400	\$2,000	\$2,600	\$3,100	\$3,700	\$4,300
Total Cash Reserves	\$12,680	\$33,000	\$32,600	\$29,900	\$30,400	\$27,500	\$31,800	\$35,000	\$30,700	\$27,200	\$23,300

Bond Funding						\$50M					
DSC	2.00-2.50	3.77	3.84	3.90	3.71	2.93	2.54	2.60	2.69	2.77	2.80
Days Cash	> 150 days	610	610	560	512	460	495	527	447	380	308
Average impact resulting from change in revenue requirement		0.00%	0.00%	0.00%	3.00%	3.00%	3.00%	3.00%	4.00%	4.00%	4.00%

Key Assumptions

- 7.8 million KGAL consumption
- Contribution margin risk tolerance of \$750,000
- 2.0% non-labor CPI increase
- Labor/benefit increases:
 - 3.5% wage escalation
 - PERS – No change in 2019, 5 percentage point increases in July 2021, 2023, 2025 and 2027
 - Health insurance increase -- 2% in 2019 and then 8% in subsequent years
- \$8.6 million to pay down PERS liability
- \$850,000 increase in O&M due to shift in Shared Services allocation
- Contributions to AMI reserve starting 2021 based on 20 year estimated life
- Bond issuance: \$50 million in 2023 for secondary treatment plant (\$40 million) and Type II Capital (\$10 million)
- \$4 million System Development Charge reserve draw for debt service payments in 2020 and 2021
- \$1.1 million combined Affordability Initiative and Efficiency Savings through 2026

Median Household Income (MHI) %

Background

The Board has requested staff provide bill affordability information. To prepare this information, *Assessment of Affordability of Residential Rates* (Glenn Barnes and Shadi Eskaf; Environmental Finance Center at the University of North Carolina, Chapel Hill; 2016) was used.

The approach uses the local community's median household income (MHI) and is based on the following data:

1. Monthly water and electric bill at average residential consumption per month
2. Annual bills at same level of use
3. Median Household Income in 2016

Currently, there is no national standard for what affordable percent (%) of MHI value is or is not. When using this assessment, consideration must be given to financial sustainability of the utility as a whole in addition to affordability of price. Setting artificially low prices may produce financial constraints to reinvesting in the system and eventually harm public health through poor product quality and service.

To address the limited income customer-owner bill impact, EWEB has maintained a customer care program for many years that provides assistance for bill payment and weatherization programs.

Included below are the combined average water and electric bill for residential customers (water is 7 kgal and electric is 1050 kWh) in Eugene, Portland, Medford, Vancouver, Tacoma, Seattle, and Everett. This average is annualized and compared as a percentage of MHI.

Eugene, Oregon

	<u>Current Prices</u>
Monthly water & electric bills at overall average residential consumption (Overall average residential : water consumption 7 kgal; electric consumption 1050 kWh)	\$144.50
Annual bill at same level of use	\$1,734
Median Household Income (MHI) in 2016 for Eugene, Oregon	\$44,859
Water & Electric % MHI	3.87%

Portland, Oregon

	<u>Current Prices</u>
Monthly water & electric bills at overall average residential consumption (Overall average residential : water consumption 7 kgal; electric consumption 1050 kWh)	\$187.43
Annual bill at same level of use	\$2,249
Median Household Income (MHI) in 2016 for Portland, Oregon	\$58,423
Water & Electric % MHI	3.85%

Medford, Oregon

Monthly water & electric bills at overall average residential consumption
(Overall average residential : water consumption 7 kgal; electric consumption 1050 kWh)

Annual bill at same level of use

Median Household Income (MHI) in 2016 for Medford, Oregon

Water & Electric % MHI

Current Prices

\$133.22

\$1,599

\$44,130

3.62%

Vancouver, Washington

Monthly water & electric bills at overall average residential consumption
(Overall average residential : water consumption 7 kgal; electric consumption 1050 kWh)

Annual bill at same level of use

Median Household Income (MHI) in 2016 for Vancouver, Washington

Water & Electric % MHI

Current Prices

\$126.32

\$1,516

\$52,004

2.91%

Tacoma, Washington

Monthly water & electric bills at overall average residential consumption
(Overall average residential : water consumption 7 kgal; electric consumption 1050 kWh)

Annual bill at same level of use

Median Household Income (MHI) in 2016 for Tacoma, Washington

Water & Electric % MHI

Current Prices

\$140.75

\$1,689

\$53,553

3.15%

Seattle, Washington

Monthly water & electric bills at overall average residential consumption
(Overall average residential : water consumption 7 kgal; electric consumption 1050 kWh)

Annual bill at same level of use

Median Household Income (MHI) in 2016 for Seattle, Washington

Water & Electric % MHI

Current Prices

\$188.13

\$2,258

\$74,458

3.03%

Everett, Washington

Monthly water & electric bills at overall average residential consumption
(Overall average residential : water consumption 7 kgal; electric consumption 1050 kWh)

Annual bill at same level of use

Median Household Income (MHI) in 2016 for Everett, Washington

Water & Electric % MHI

Current Prices

\$150.55

\$1,807

\$50,933

3.55%