

RIVERSIDE PUBLIC UTILITIES

Board Memorandum

BOARD OF PUBLIC UTILITIES

DATE: APRIL 23, 2018

ITEM NO: 14

SUBJECT: RIVERSIDE PUBLIC UTILITIES PROPOSED BUDGET FOR FISCAL YEARS 2018/19 AND 2019/20

ISSUE:

Recommend that the City Council approve the Riverside Public Utilities Department (RPU) proposed budget for Fiscal Years (FY) 2018/19 and 2019/20.

RECOMMENDATIONS:

That the Board of Public Utilities recommend that City Council:

1. Approve the Electric Funds (including Public Benefits Fund) proposed FY 2018/19 budget totaling \$385.1 million in revenues, \$396.6 million in operating expenditures and \$32.7 million in capital improvements and proposed FY 2019/20 budget totaling \$399.8 million in revenues, \$416.8 million in operating expenditures and \$34.7 million in capital improvements. The difference between revenues and expenditures including capital improvements will be covered by bond proceeds and reserves;
2. Authorize the use of the Designated Electric Fund Capital Repair/Replacement Reserve for technology replacements in the amount of \$200,000 per year for FY 2018/19 and FY 2019/20;
3. Authorize the use of the Designated Electric Fund Dark Fiber Reserve for dark fiber leasing operating expenses in the amount of \$600,000 per year for FY 2018/19 and FY 2019/20;
4. Authorize the use of the Designated Electric Fund Mission Square Improvement Reserve for Mission Square facility improvements in the amount of \$600,000 and \$225,000 for FY 2018/19 and FY 2019/20, respectively; and
5. Approve the Water Funds (including Water Conservation Fund) proposed FY 2018/19 budget totaling \$76.6 million in revenues, \$70.7 million in operating expenditures and \$22.8 million in capital improvements and proposed FY 2019/20 budget totaling \$81.7 million in revenues, \$75.3 million in operating expenditures and \$18.9 million in capital improvements. The difference between revenues and expenditures including capital improvements will be covered by bond proceeds and reserves.

BACKGROUND:

On December 8, 2015, City Council approved the move to a two-year budget in the context of a five-year plan. The rationale for a two-year budget is that sound financial management includes multi-year financial planning. In addition, a two-year budget process will be more efficient and will allow time in the second year for long-term planning and focus on performance measurement and reporting. The Electric

and Water Funds five-year financial plans (5-Year Plan) prepared for this budget process include the Electric and Water Funds five-year rate proposal, which was conceptually approved by City Council on January 18, 2018.

DISCUSSION:

BUDGET OVERVIEW

The proposed two-year budget has been developed to continue to maintain the level of quality electric and water services to our customers and to support the following objectives:

1. Support City Council Riverside 2.1 strategic priorities with an emphasis on customer service and customer value.
2. Meet RPU's strategic goals in the areas for customer experience, reliability and resiliency, affordability, sustainability, operational excellence and strong workforce.

The following are key challenges in developing this two-year budget:

1. Revenue uncertainty due to Electric and Water Funds 5-year rate proposal in process. Final rate recommendations will go to the City Council on May 22, 2018 with new rates effective July 1, 2018. The proposed budget includes revenue from rate proposal.
2. Current capital projects are funded from reserves, with bond funds depleted in prior years. Reserve levels continue to decrease, the water fund is estimated to be at minimum reserves by June 30, 2018. New bond issuances are necessary in FY 2018/19, pending approval of rate proposal.
3. Regulatory constraints and mandates, including the latest renewable percentage and clean water standards, have caused increased supply costs.
4. Increased personnel costs with CalPERS costs outpacing salaries.
5. Significant capital needs due to aging infrastructure and equipment.

The proposed two-year budget and 5-Year Plan have been developed to be in line with the rate proposal as conceptually approved the Board of Public Utilities (Board) and City Council.

Budget Assumptions and 5-Year Plan

On April 5, 2018, RPU presented to the Budget Engagement Commission (BEC) the department's budget assumptions and 5-Year Plan as part of the City's budget process. The 5-Year Plans for the Electric and Water Funds are included in Attachment 2 and 3 of this report. The major budget assumptions and revenue and expenditure categories are detailed in the staff report to the BEC and is also included in Attachment 1 of this report.

Planned Use of Reserves and Line of Credit

RPU will need to utilize restricted, designated and undesignated reserves to balance the proposed two-year budget. As provided in RPU Fiscal Policies, the use of reserves to balance the budget is permitted in the event a balanced budget is not attainable. If the use of reserves is expected to continue beyond one year, the planned use of reserves must be developed as part of a strategic financial plan. The use of electric and water reserves in the proposed two-year budget is planned within the rate proposal. The financial strategy within the rate proposal is to draw down reserves to minimum required levels in order to keep the proposed rate increases as low as possible. In addition, as part of the rate proposal, RPU is proposing the use of a line of credit (LOC) to reduce the necessary required cash levels. With a LOC, RPU is able to meet the overall liquidity and target minimum reserve levels acceptable by bond rating agencies and maintain current bond ratings. RPU plans to obtain a LOC of approximately \$40 million for the Electric Fund and approximately \$25 million for the Water Fund.

Revenue and Expenditure Budget Summary

The following is the budget summary for the Electric Funds, including Public Benefits:

Electric	FY 16/17 Actuals	FY 17/18 Projected	FY 18/19 Proposed	FY 19/20 Proposed
Electric Fund - Revenues	\$369,513,673	\$372,664,665	\$375,938,932	\$390,350,694
Public Benefits (PB) - Revenues	8,879,976	9,116,923	9,133,894	9,443,790
Total Electric Revenues	\$378,393,649	\$381,781,588	\$385,072,826	\$399,794,484
Use of Bond Proceeds	0	0	22,429,000	27,586,000
Use (Incr.) of Electric Fund Reserves	(8,666,661)	17,207,859	15,162,869	17,959,379
Use (Incr.) of PB Fund Reserve	(1,277,883)	(64,333)	6,598,327	6,207,446
Total Electric – Revenues and Other Financing Sources	\$368,449,105	\$398,925,114	\$429,263,022	\$451,547,309
Electric Fund - Expenditures	\$360,847,012	\$389,872,524	\$413,530,801	\$435,896,073
Public Benefits - Expenditures	7,602,093	9,052,590	15,732,221	15,651,236
Total Electric Expenditures, Including Capital Improvements	\$368,449,105	\$398,925,114	\$429,263,022	\$451,547,309

The following is the budget summary for the Water Funds, including Water Conservation:

Water	FY 16/17 Actuals	FY 17/18 Projected	FY 18/19 Proposed	FY 19/20 Proposed
Water Fund - Revenues	\$67,008,437	\$70,575,161	\$75,617,303	\$80,710,703
Water Conservation (WC)- Revenues	1,119,729	868,845	953,822	995,783
Total Water Revenues	\$68,128,166	\$71,444,006	\$76,571,125	\$81,706,486
Use of Bond Proceeds	0	0	11,617,000	12,899,000
Use of Water Fund Reserves	10,210,332	20,458,399	4,656,346	0
Use of WC Fund Reserves	214,995	238,938	698,290	747,667
Total Water – Revenues and Other Financing Sources	\$78,553,493	\$92,141,343	\$93,542,761	\$95,353,153
Water Fund - Expenditures	\$77,218,769	\$91,033,560	\$91,890,649	\$92,443,584
Water Conservation - Expenditures	1,334,724	1,107,783	1,652,112	1,743,450
Total Water Expenditures, Including Capital Improvements	\$78,553,493	\$92,141,343	\$93,542,761	\$94,187,034

Further details on revenues and expenditures are included in the attached 5-Year Plans for the Electric and Water Funds. Use of reserves and bond proceeds are included in the 5-Year Plans, Presentation and are discussed below.

CAPITAL IMPROVEMENT PROGRAM

As part of the budget process, RPU has prepared a Five-Year Capital Improvement Program (CIP) for FY 2018/19 to 2022/23. CIP project costs for FY 2018/19 and 2019/20 are incorporated into the proposed two-year budget. Subsequent years are for planning purposes. The proposed two-year CIP for the Electric and Water Funds is \$67.4 million and \$41.7 million, respectively, comprised of capital projects as presented to the Board and City Council in the November 2017 and January 2018 rate proposal joint workshops and is outlined in the presentation. Funding for CIP is a combination of bond

proceeds, developer contributions, rates and reserves.

OPERATING BUDGETS

The proposed two-year operating budget reflects a rollover budget for the most part with non-discretionary costs such as power supply and production costs budgeted as necessary to serve customer load and consumption. The proposed budget is supported by revenues within the rate proposal and planned use of reserves. No new full-time equivalent (FTE) positions were added. The Electric Fund has a reduction of 14 FTEs. Five positions were eliminated due to the restructuring of RPU's executive management, and reductions in the Workforce Development and Customer Engagement divisions which will realize a savings of approximately \$1.0 million per year. Nine positions were transferred to the Human Resources Department and City Manager's Office/Communication Division as part of the efficiency reorganization to ensure the highest quality service to our customers. As outlined in the report provided to the Board on RPU's Operational Improvements and Efficiencies at this same meeting, it was determined that these non-core services are best served by City departments to provide greater support to RPU in the areas of recruitment, training and communication.

Electric Fund

Revenue Budget

The primary source of revenues for the Electric Fund is retail sales, which will fund 73% of Electric expenditure budget. Current revenue sources including other non-retail revenues will not be adequate to cover Electric Fund's expenditure budget, which is anticipated with the rate proposal. Bond proceeds of approximately \$22.4 million and \$27.6 million will be utilized to fund a major portion of the capital improvement projects for FY 2018/19 and FY 2019/20, respectively. Various reserves will be utilized to cover the balance of the expenditures, as planned with the rate proposal.

Expenditure Budget

The Electric Fund's proposed two-year budget reflects a 7.6% (\$30.3 million) and 5.2% (\$22.3 million) year-over-year increase for FY 2018/19 and 2019/20, respectively. The increase is primarily due to:

- Increase in power supply costs reflecting a projected increase in the transmission costs charged by the California Independent System Operator (CAISO), increase in renewable energy costs, new renewable projects coming online, increase in costs from contractual agreements, and higher market energy prices. Power supply costs represent 48% of the total Electric budget.
- Increase in personnel costs reflecting the 2016 City Council approved Memoranda of Understanding (MOUs) that tie pay increases to the performance of the City's key revenue sources and the increase in CalPERS and other benefit costs.
- Increase in debt service costs due to the issuance of new bonds to fund capital improvement projects.
- Increase in Public Benefit programs to further promote energy efficiency and to increase support for low- and fixed-income customers through expanded eligibility and outreach.

As part of the rate setting and budget development process, all divisions were tasked with reviewing their non-personnel budget and reduce costs where possible. Non-personnel reductions reflected in the Electric expenditure budget are approximately \$2.7 million and \$2.8 million for FY 2018/19 and 2019/20, respectively, for a total of \$5.5 million in savings. These savings include professional services, energy charges, greenhouse regulatory fees, various maintenance costs, and miscellaneous other costs.

As planned with the rate proposal, a portion of the Electric expenditure budget will be funded by various reserves. The following restricted and designated reserves are proposed to be utilized for the two-year

budget, with the balance to be funded from unrestricted, undesignated reserves:

Reserve	Budgeted Expenditure	FY 2018/19	FY 2019/20
Restricted Regulatory Requirement Reserve	EV & LED Streetlight CIP Projects	4.5 M	0.5 M
Restricted Regulatory Requirement Reserve	Renewable Power Supply	2.8 M	2.8 M
Restricted Regulatory Requirement Reserve	ICE Bear Energy Storage Project	2.0 M	2.0 M
Designated Capital Repair /Replacement Reserve	Technology equipment replacement	0.2 M	0.2 M
Designated Dark Fiber Reserve	Dark fiber leasing operating expenses	0.6 M	0.6 M
Designated Mission Square Improvement Reserve	Facility improvements	0.6 M	0.2 M

The Restricted Regulatory Requirement reserve accumulates the proceeds from the sale of greenhouse gas (GHG) allowances under the California Cap-and-Trade Program, which contain regulations restricting the use of these proceeds. The budgeted expenditures identified above have been determined as qualified uses. The planned use of Regulatory Requirement reserve is approximately \$14.6 million for the proposed two-year budget, including CIP projects.

The Designated Capital Repair/Replacement reserve accumulates funds for repair and replacement of facilities, vehicles, and technology outside of CIP. The Electric Fund proposes utilizing \$400,000 from this reserve to fund technology equipment replacement for the two-year budget.

The Designated Dark Fiber reserve was established to capture the dark fiber leasing activities for both revenues and expenditures. Annual revenue is approximately \$600,000; and \$600,000 in expenditures have been budgeted per year for the operation and maintenance of the dark fiber network to be paid from the designated reserve.

The Electric expenditure budget also includes supplemental requests of \$879,000 and \$504,000 for FY 2018/19 and 2019/20, respectively, for rehabilitation of facilities at Mission Square that are critical to the operation of the building and employee and tenant safety. Of the amount, \$279,000 per year for minor improvements will be covered by lease revenues. The balance of \$600,000 and \$225,000 for FY 2018/19 and FY 2019/20, respectively, for capital improvements will be covered by the Designated Mission Square Improvement Reserve.

The Designated Electric Reliability Reserve was established to accumulate amounts received from retail customers through the Reliability Charge for the purpose of funding debt service for transmission and internal generation projects. To keep the proposed rate increases as low as possible, the rate proposal plans for the use of the Electric Reliability Reserve to cover the balance the approved available budget of approximately \$72 million for the Riverside Transmission Reliability Project (RTRP) in lieu of issuing additional debt.

SCPPA Expenditure Budget

On February 21, 2017, City Council received an update on RPU's participation and involvement in Southern California Public Power Authority (SCPPA) and the associated benefits. City Council directed staff to provide a detail of proposed expenditures included within RPU's annual budget to the Board and include this information in the budget recommendation to City Council.

Included in the proposed Electric expenditure budget are \$34.9 million and \$35.6 million of expenditures expected to be procured through SCPPA for FY 2018/19 and FY 2019/20, respectively, of which 89% will

be for power supply, 10% will be for Public Benefit energy efficiency programs, and the remaining 1% will be for various other SCPPA member services. Other SCPPA member services include training, power resources grid management, industry association fees, legislation & regulatory, and energy efficiency program support. Total proposed expenditures through SCPPA is approximately 8% of the total Electric expenditure budget.

Water Fund

Revenue Budget

Similar to the Electric Fund, the primary source of revenues for the Water Fund is retail sales, which will fund 68% of the Water expenditure budget. Current revenue sources including other non-retail revenues will not be adequate to cover the Water Fund's expenditure budget, which is anticipated with the rate proposal. Bond proceeds of approximately \$11.6 million and \$12.9 million will be utilized to fund a major portion of the capital improvement projects for FY 2018/19 and FY 2019/20, respectively. Unrestricted, undesignated reserves will be utilized to fund the balance of the expenditures.

Expenditure Budget

The Water Fund's proposed two-year budget reflects a 1.5% (\$1.4 million) and 0.7% (\$0.6 million) year-over-year increase for FY 2018/19 and 2019/20, respectively. The increase is primarily due to:

- Increase in personnel costs reflecting the 2016 City Council approved MOUs that tie pay increases to the performance of the City's key revenue sources and the increase in CalPERS and other benefit costs.
- Increase in debt service costs due to the issuance of new bonds to fund capital improvement projects.

The proposed budget also reflects operating efficiencies with the installation of solar networks to reduce electricity costs for water pumping, which will generate approximately \$800,000 in savings per year. In addition, the Water Fund divisions have identified \$411,000 and \$65,000 for FY 2018/19 and FY 2019/20, respectively, in non-personnel reductions and these reductions have been reflected in the proposed two-year budget numbers. No supplemental requests have been added to the Water expenditure budget.

ELECTRIC AND WATER FUNDS - NEW DEBT ISSUANCE

As part of the rate proposal, the Electric and Water Funds are planning to issue new debt of approximately \$103.1 million and \$52.2 million, respectively, in FY 2018/19 to fund capital improvement projects over a three-year period. In general, new bonds are issued with proceeds to be used over a three-year period with the next new bond issuance expecting to occur in FY 2021/22 for continual support of the capital improvement program as outlined with the rate proposal. The debt service costs of these new bond issuances have been incorporated into the proposed two-year budget and the 5-Year Plans.

ELECTRIC AND WATER RESERVES

The use of reserves to balance the proposed two-year budget and the 5-Year Plan for the Electric and Water Funds is consistent with the rate proposals. With the proposed use of the line of credit, the Electric Fund is projected to maintain its target minimum reserve level as established by RPU Cash Reserve Policy through FY 2021-22. Reserve levels will drop slightly below target minimum in FY 2022-23 which is consistent with the rate proposal and is allowed so long as the Electric Fund has plans to return reserves to the minimum target level within three years. As part of the rate proposal, the Electric Fund is projected to return its reserve level to minimum target within two years, by FY 2024-25. The rate proposal also takes into consideration the effect of the use reserves on key financial metrics, such as

days cash on hand and debt service coverage. For the 5-Year Plan, the Electric Fund is projected to be able to maintain the financial metrics as set by the RPU Fiscal Policies.

For the Water Fund, the proposed use of a line of credit will allow the Water Fund to utilize reserves to balance its budget for FY 2018-19 and still maintain its target minimum reserve level. For FY 2019-20 and subsequent years in the 5-Year Plan, it is necessary that the Water Fund increases its unrestricted, undesignated reserve level in order to maintain the financial metrics, such as debt service coverage, as set by the RPU Fiscal Policies. While there is an increase in unrestricted, undesignated reserve, the Water Fund will require to maintain the line credit in order to continue to meet its target minimum reserve level in FY 2019-20 and subsequent years.

The Chief Financial Officer/Treasurer concurs with the report recommendations.

FISCAL IMPACT:

The Electric Funds (including Public Benefits Fund) proposed FY 2018/19 budget totals \$385.1 million in revenues, \$396.6 million in operating expenditures and \$32.7 million in capital improvements and proposed FY 2019/20 budget totals \$399.8 million in revenues, \$416.8 million in operating expenditures and \$34.7 million in capital improvements. The use of designated electric reserves in the next two fiscal years will be:

1. \$400,000 from Designated Capital Repair/Replacement Reserve
2. \$1.2 million from Designated Dark Fiber Reserve
3. \$825,000 from Designated Mission Square Improvement Reserve

The Water Funds (including Water Conservation Fund) proposed FY 2018/19 budget totals \$76.6 million in revenues, \$70.7 million in operating expenditures and \$22.8 million in capital improvements and proposed FY 2019/20 budget totals \$81.7 million in revenues, \$75.3 million in operating expenditures and \$18.9 million in capital improvements.

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Approved by: Todd L. Jorgenson, Interim Utilities General Manager

Approved by: John A. Russo, City Manager

Approved as to form: Gary G. Geuss, City Attorney

Attachments:

1. Budget Engagement Commission Staff Report
2. Electric Fund 2018-23 Five-Year Financial Plan
3. Water Fund 2018-23 Five-Year Financial Plan
4. Presentation