

RIVERSIDE PUBLIC UTILITIES

Board Memorandum

BOARD OF PUBLIC UTILITIES

DATE: May 23, 2016

ITEM NO: 17
File 16-1604

SUBJECT: APPROVAL OF RIVERSIDE PUBLIC UTILITIES UPDATED FISCAL POLICIES

ISSUE: The item for the Board of Public Utilities (Board) consideration is a recommendation to the City Council to approve Riverside Public Utilities (RPU) Fiscal Policies.

RECOMMENDATION:

That the Board recommend that the City Council:

1. Approve the updated RPU Fiscal Policies; and
2. Direct staff to annually review the Fiscal Policies and update, at a minimum, once every three years to reflect needed changes to policy.

BACKGROUND:

Importance of Fiscal Policies

The adoption of strong fiscal policies are the cornerstone of sound financial management. The goals of solid fiscal policies for RPU are:

- Promote long term financial stability by establishing clear and consistent financial reporting guidelines.
- Ensure that RPU will maintain its financial health in order to meet its strategic goals.
- Development of cash reserve and budgeting policies.
- Provide guidelines for capitalization of RPU assets.
- Provide funds to maintain and invest in its utility infrastructure.
- Enhance short and long-term financial credit quality by helping to achieve the highest possible credit and bond ratings.
- Provide guidance and controls for effective investment of RPU funds in accordance with City investment policies and State law.
- Provide the Board and City Council with a framework for measuring fiscal performance of RPU against established parameters and guidelines.
- Link long-term financial planning with day-to-day operations.
- Document the Board and City Council philosophy for effective ratemaking and recovery of RPU costs of electric and water service.

Policy History

In June 2001, the Board and City Council approved the existing RPU Fiscal Policy. The approved policy documented and adopted financial goals for both the water and electric utilities and established policies for long-term, as well as day-to-day operations of both utilities. The policy covered operating and capital

budgets, debt policies, investments, risk management, and accounting and reserve policies.

In August 2015, RPU engaged Baker Tilly Virchow Krause (Baker Tilly) to review RPU's 2001 Fiscal Policy, perform a gap analysis of the current fiscal policy and industry best practices, provide recommendations on all areas that should be included in an updated fiscal policies document and prepare draft fiscal policies for RPU.

Baker Tilly's gap analysis highlighted that the 2001 policy was effective in covering many areas needed for effective fiscal policies; however, there were some gaps and omitted areas in the policy compared to current best practices in the Utility industry and with RPU's peer utility group. The 2001 policy was written at a very high level in some areas but in more deep detail in others. Baker Tilly recommended to prepare a policy document that is consistent in its depth would be more appropriate. While the existing policy provides good information and guidelines, updating it in detail and for a move towards best practices would be appropriate.

In addition, Baker Tilly recommended that the revised policy should provide more specific and comprehensive goals should be established. While the current policy provided good information, updating the policy adding a couple of areas such as debt service coverage and cost allocation; and provide more discussion of specific guidelines in each area would be a move towards improved fiscal policies in line with best practices within the Utility industry.

Revised Policy

Baker Tilly worked with staff to prepare the updated RPU Fiscal Policies that conform to best practices and standards within the utility industry. This policy will establish guidelines to provide a framework for the financial management of the Electric and Water utilities.

Under the revised Fiscal Policies, there are ten major components to RPU's financial management:

- 1) Financial Reporting. A strong system of internal controls ensures reliable financial reporting, effective and efficient operations, and compliance with applicable state and federal laws and regulations.
- 2) Cash Reserves. Properly designed reserve policies send a positive message to ratepayers, investors, and regulatory and credit rating agencies that the City is committed to maintaining the long-run fiscal strength of RPU.
- 3) Operating and Capital Budgeting. Sound budgeting processes are needed to provide a control framework for management and governance oversight of the operation of RPU. Budget practices allow for proper planning and accountability for meeting spending targets and key performance indicators.
- 4) Asset Capitalization Policy. Capitalization policies allow for uniform treatment of classification of expenditures, proper operating and capital budgeting, classification of work orders, recording of fixed assets and electric and water plant retirements in the RPU continuing property records.
- 5) Debt Management. A debt management policy improves the quality of decisions, articulates policy goals, provides guidelines for the structure of debt issuance, and demonstrates a commitment to long-term capital and financial planning. Adherence to a debt management policy signals to rating agencies and the capital markets that a government is well managed and therefore is likely to meet its debt obligations in a timely manner.
- 6) Credit Rating. Maintaining high credit ratings from the major rating agencies, such as Standard and Poor's (S&P), Fitch Ratings, and Moody's, is crucial in meeting RPU's goals of providing utility services to the citizens of Riverside at the most economical cost. Higher ratings equate to reduced borrowing cost and greater financial flexibility particularly in unstable financial markets; consequently, maintaining or improving the electric and water credit ratings is a high priority.
- 7) Investments. Prudent investing will allow the City to generate returns that can be used as a revenue source, while allowing for safety of principal for its future use.

- 8) Risk Management. Managing enterprise risk is a control measure for ensuring that assets and operations are safeguarded and that proper mitigation plans are in place for the sustainability of RPU.
- 9) Forecasting and Financial Planning. Long-range forecasting is an integral part of developing RPU strategic objectives and ensuring that user rates will support current operations and long-term goals.
- 10) Revenue Development and Monitoring of RPU Customer Rates. Ratemaking principles guide an entity in the development or revision of current or future rate setting in a manner consistent with the Utility's overall strategy. In addition, the development of a cash basis revenue requirement for water and electric services will ensure full recovery of costs, allocate costs equitably across customers, and maintain rate competitiveness in our service territory.

Due to the their importance and nature, inquiries by the public, and the cost of service studies/10-year proforma work underway, the RPU Cash Reserves Policy was brought forward individually prior to the overall updated RPU Fiscal Policies. This allowed for a full independent discussion on this specific policy by the Board, City Council Finance Committee and ultimately the full City Council. On March 22, 2016, the City Council approved the RPU Cash Reserve Policy. We have incorporated the approved policy into the Fiscal Policies document in order to have a comprehensive document related to the financial health of RPU.

Russ Hissom, Partner at Baker Tilly, will be making the presentation of their report and the proposed updated RPU Fiscal Policies.

FISCAL IMPACT:

While not having an immediate direct impact on the current financial health of RPU, adoption of these fiscal policies sets guidelines and parameters for ongoing activities that will direct the financial management of RPU for the future.

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

Attachments:

1. Baker Tilly Report on Fiscal Policies
2. Proposed Riverside Public Utilities Fiscal Policies
3. Baker Tilly Presentation