RECOMMENDATION
Staff and the Utilities Advisory Commission (UAC) recommend that Council approve changes to certain Utilities reserve fund guidelines. Specifically, staff and the UAC recommend that the development of an assessment of the risks facing each fund be undertaken as part of the annual budget and retail rate development and approval process. This annual assessment will be compared to the established guideline levels to assist in the determination of the Rate Stabilization Reserve level target for each fiscal year.

Additionally, the following minor changes to the guidelines of the following Utilities Fund Reserves are recommended:

1. For the Electric, Gas, Water and Wastewater Collection Emergency Plant Replacement Reserves, establish a minimum guideline level equal to the greater of: 1) the City’s liability insurance coverage deductible or 2) the amount that covers the most expensive item of equipment which, if lost, would cause interruption in the normal activity of that utility;

2. For the Electric Supply Rate Stabilization Reserve, change the minimum and maximum guideline levels equal to 50% and 100% of the annual supply purchase cost, respectively;

3. For the Gas Supply Rate Stabilization Reserve, change the minimum and maximum guideline levels equal to 35% and 75% of the annual supply purchase cost, respectively; and
4. For the Electric Distribution, Gas Distribution, Water and Wastewater Collection Rate Stabilization Reserves, change the minimum and maximum guideline levels equal to 20% and 50% of the annual sales revenue, respectively;

The table below summarizes the proposed changes to the Emergency Plant Replacement (EPR) and Rate Stabilization Reserve (RSR) guidelines.

<table>
<thead>
<tr>
<th>Reserve</th>
<th>Existing Guidelines</th>
<th>Proposed New Guidelines</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Electric, Gas, Water and Wastewater Collection EPRs</strong></td>
<td>No minimum (maximum, as stated in the City Charter, is = 5% of the book value of the fund’s capital in service)</td>
<td>Minimum = greater of: 1) the City’s liability insurance coverage deductible or 2) an amount covering the most expensive critical item</td>
</tr>
<tr>
<td><strong>Electric Supply RSR</strong></td>
<td>Maximum = 103% of purchase cost Minimum = half of maximum</td>
<td>Maximum = 100% of purchase cost Minimum = 50% of purchase cost</td>
</tr>
<tr>
<td><strong>Gas Supply RSR</strong></td>
<td>Maximum = 75% of purchase cost Minimum = half of maximum</td>
<td>Maximum = 75% of purchase cost Minimum = 35% of purchase cost</td>
</tr>
<tr>
<td><strong>Electric Distribution RSR</strong></td>
<td>Maximum = 38% of sales revenue Minimum = half of maximum</td>
<td>Maximum = 50% of sales revenue Minimum = 20% of sales revenue</td>
</tr>
<tr>
<td><strong>Gas Distribution RSR</strong></td>
<td>Maximum = 40% of sales revenue Minimum = half of maximum</td>
<td>Maximum = 50% of sales revenue Minimum = 20% of sales revenue</td>
</tr>
<tr>
<td><strong>Water RSR</strong></td>
<td>Maximum = twice the minimum Minimum = sum of: 1) 15% of sales revenue; plus 2) sales revenue decline due to abnormal weather</td>
<td>Maximum = 50% of sales revenue Minimum = 20% of sales revenue</td>
</tr>
<tr>
<td><strong>Wastewater Collection RSR</strong></td>
<td>Maximum = twice the minimum Minimum = sum of: 1) 15% of sales revenue; plus 2) sales revenue decline due to abnormal weather</td>
<td>Maximum = 50% of sales revenue Minimum = 20% of sales revenue</td>
</tr>
<tr>
<td><strong>All RSRs</strong></td>
<td>Target = midpoint between minimum and maximum</td>
<td>Target to be established following an annual evaluation of risks to each fund as part of budget preparation</td>
</tr>
</tbody>
</table>

**BACKGROUND**

On September 19, 2006, the Council Finance Committee directed staff to work with the Utilities Advisory Commission (UAC) to develop recommendations for changes to the policies, guidelines, or purposes of the following Utilities Fund Reserves [CMR:358:06]:

1. Emergency Plant Replacement Reserve for the Water, Electric, Gas, and Wastewater...
Collection Funds;
2. Supply Rate Stabilization Reserve for the Electric and Gas Funds;
3. Distribution Rate Stabilization Reserve for the Electric and Gas Funds; and
4. Rate Stabilization Reserve for the Water and Wastewater Collection Funds.

The attached memorandum to the UAC contains staff’s recommendations for the selected reserves and the rationale for the development of the recommendations, which were presented to the UAC at its December 6, 2006 meeting.

COMMITTEE REVIEW AND RECOMMENDATIONS
At its December 6, 2006 meeting, the UAC considered staff’s recommendations on changes to the Utilities Reserves Policies and Guidelines. After discussion, Commissioner Dawes made a motion to accept staff’s recommendation with the proviso that, for the rate stabilization reserves, if the target balance resulting from the risk assessment is below the minimum guideline level, that appropriately conservative risk assumptions should be used. This motion died for the lack of a second. After further discussion, the UAC unanimously approved staff’s recommendations.

ENVIRONMENTAL REVIEW
Approval of the recommended changes to the Utilities reserves does not constitute a project that would require environmental review.

NEXT STEPS
If the recommendations are approved, staff will provide the annual risk assessment for each fund and make recommendations regarding the reserve levels for each reserve fund during the budget and retail rate development process as described in the report to the UAC.

ATTACHMENTS
1. Report to the UAC for its December 6, 2006 meeting: Changes to Certain Utilities Reserve Guidelines
2. Excerpt of December 6, 2006 Utilities Advisory Commission notes

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