TO: HONORABLE CITY COUNCIL
FROM: CITY MANAGER DEPARTMENT: UTILITIES
ATTENTION: FINANCE COMMITTEE
DATE: APRIL 17, 2007 CMR:202:07

SUBJECT: UTILITIES ADVISORY COMMISSION RECOMMENDATION TO APPROVE A RESOLUTION ADOPTING AN ELECTRIC RATE INCREASE FOR FISCAL YEAR 2007-08, AND STAFF RECOMMENDATION TO APPROVE, IN CONCEPT, THE ADOPTION OF AN ELECTRIC RATE INCREASE FOR FISCAL YEAR 2008-09

RECOMMENDATION
Staff and the Utilities Advisory Commission (UAC) recommend that the City Council adopt the attached resolution to:

(a) Approve a 5 percent increase to electric retail rates, for Fiscal Year (FY) 2007-08, effective July 1, 2007, which will increase annual revenues by $4.4 million; and,

(b) Approve the changes to the Electric Utility Rate Schedules, as attached.

In addition, for biennial budgeting purposes, staff recommends:

(c) Approval, in concept, of a 9.1 percent system average electric rate increase for FY 2008-09, which will increase annual revenue by an additional $9.2 million.

DISCUSSION
Revenue
Compared to FY 2005-06, electric sales for FY 2006-07 are projected to remain flat. Revenue levels will also be flat for FY 2006-07, since there were no increases in electric rates implemented for this fiscal year.

Sales projections indicate that the flat sales trend will continue in FY 2007-08, and beyond due to limited customer growth and the impacts of energy efficiency efforts. Expenses are expected to increase which leads to the proposed rate increase.
Staff is recommending a 5 percent electric rate increase to be effective July 1, 2007. This represents an annual revenue increase of $4.4 million which will be applied to the distribution rates of all customer classes. The driving factors for the rate increase are the increased costs of operating and maintaining the distribution system as discussed in the attached Utilities Advisory Commission report. Another 10 percent revenue increase, or $9.2 million, is proposed, to be “approved, in concept,” for FY 2008-09.

**Distribution Expenses**

Since there were no electric rate increases in FY 2006-07, the increases in the distribution and supply operating budgets were funded through scheduled draw downs of the Electric Distribution Rate Stabilization Reserve (E-DRSR) and the Electric Supply Rate Stabilization Reserve (E-SRSR).

There were, however, unanticipated expenses of $2.2 million for retiree medical and Workers’ Compensation liabilities starting in FY 2005-06. These retroactive expenses were funded from the E-DRSR during Fiscal Year 2006-07. Current projections show that without a rate increase, the E-DRSR balance will fall below the Minimum Guideline level at the end of FY 2007-08 by $5.2 million.

Operating expenses for electric distribution, the Capital Improvement Program (CIP), and electric supply costs are projected to increase for Fiscal Year 2007-08. While the increases in supply costs can be funded through a continuing draw down of the E-SRSR, the drawing down of the E-DRSR to fund FY 2007-08 operating expenses would negatively impact the E-DRSR by reducing its balance to $535,000. This will leave the Electric Utility vulnerable to financial losses from either unexpected failure of physical infrastructure or an unanticipated shortfall in sales.

The proposed revenue increase of 5 percent, or $4.4 million, will mitigate this funding problem by compensating for the increased distribution expenses (including increased Electric Public Benefits Program funding, as required under state law), and to provide additional funds to bring the E-DRSR to an adequate level.

The proposed revenue increase will result in a projected end-of-year balance for FY 2007-08 of $4.6 million in the E-DRSR. This is below the Minimum Guideline level, but above the “Annual Risk Assessment for Reserves” target of $4 million. To bring the E-DRSR balance to the Minimum Guideline level would require an additional 3.2 percent rate increase, or $2 million in additional annual revenue.

**Supply Expenses**

Due to very favorable hydro conditions, the ending balance of the E-SRSR for FY 2005-06 was $9.8 million over the Maximum Guideline level approved by the City Council. Continuing
increases in electric supply costs for Fiscal Year 2007-08 will be funded through a draw down of
the E-SRSR, with no rate increase to cover increased supply expenses recommended at this time
for Fiscal Year 2007-08.

The proposed “approve, in concept” 10 percent increase to electric retail rates for Fiscal Year
2008-09, representing a $9.2 million increase in revenue, is designed to allow the E-SRSR to
remain above the Minimum Guideline level, and to bring supply costs and revenues back into
alignment.

**UTILITIES ADVISORY COMMISSION REVIEW AND RECOMMENDATIONS**

On April 4, 2007, the UAC voted 4 to 0, with one absent, to recommend that the City Council:

(a) Approve a 5 percent increase to electric retail rates, for FY 2007-08, effective July 1,
2007, which will increase annual revenues by $4.4 million; and,

(b) Approve the changes to the Electric Utility Rate Schedules, as attached.

The UAC voted to withhold recommending approval, in concept, of a 10 percent system average
electric rate increase, or $9.2 million in additional revenue, for FY 2008-09, feeling that future
costs were too uncertain at this time. The UAC also suggested that recommendation for approval
of the specific rate schedules be sought during the approval process.

**ALTERNATIVES**

Staff evaluated the impact of financial alternatives to the recommended $4.4 million revenue
increase. Postponing the increase to a future date would result in: a) a projected E-DRSR balance
below both the Minimum Guideline level of $5.8 million by $5.2 million, and the $4 million
target of the “Annual Risk Assessment for Reserves” by $3.5 million; and, b) would result in a
much larger proposed rate and revenue increase for FY 2008-09.

**RESOURCE IMPACT**

Approval of this proposed rate increase will raise the Electric Fund sales revenues by
approximately $4.4 million for FY 2007-08.

This 5 percent revenue increase will be fully allocated to electric distribution revenue and will
result in a projected end-of-year balance for FY 2007-08 of $4.6 million in the E-DRSR. This is
below the Minimum Guideline level of $6.6 million, but above the “Annual Risk Assessment for
Reserves” target of $4 million.

There is no recommended change to electric supply revenue for FY 2007-08. The projected E-
SRSR balance at the end of FY 2007-08 is $43.7 million. This is above the Minimum Guideline
level of $30.3 million, but slightly below the “Annual Risk Assessment for Reserves” target of
$44.2 million.
Approval, in concept, of a 10 percent rate increase for FY 2008-09, or $9.2 million in additional revenue, would raise the E-SRSR balance 1.8 percent above Minimum Guideline level of $32.5 million by $600,000.

POLICY IMPLICATIONS
This proposed rate increase meets the Utilities Strategic Plan objective of providing superior financial performance to the City and competitive rates to customers. These recommendations do not represent a change in current City policies.

ENVIRONMENTAL REVIEW
The adoption of the resolution does not constitute a project under the California Environmental Quality Act. Therefore, no environmental assessment is required.

ATTACHMENTS
A: Resolution
B. Electric Rate Schedules E-1, E-1-G, E-2, E-2-G, E-3, E-4, E-4-G, E-4-TOU, E-7, E-7-G, E-7-TOU, E-14, E-16, E-18 and E-18-G
C. Report to the UAC for its April 4, 2007 meeting: Recommended FY 2007-08 Electric Rate Increase
D. Minutes of the UAC meeting of April 4, 2007

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