



CITY OF HEALDSBURG CITY COUNCIL AGENDA STAFF REPORT

MEETING DATE: June 5, 2023

SUBJECT: Consider adoption of electric rates for fiscal years 2023-24 through 2026-27

PREPARED BY: Terry Crowley, Utilities Director

STRATEGIC INITIATIVE(S):
Maintain and Improve Infrastructure and Facilities

RECOMMENDED ACTION(S):
Adopt a Resolution rescinding Resolution No. 9-2016 following the October 2023 utility billing and adopting electric rate increases and updated rate schedules.

COMMUNITY ENGAGEMENT/OUTREACH:
This is the third in a series of presentations regarding Healdsburg's electric cost of service analysis (COSA) and rate development. The intent of this item is to adopt electric rates previously discussed during the March 6, 2023 and April 17, 2023 council meetings. The potential adoption of electric rates was also publicly noticed in the Press Democrat.

BACKGROUND:
In 2016, the City Council adopted a resolution approving annual rate increases for fiscal years (FY) 2016-17 through FY 2018-19. As those increases have now ended and costs have increased, City staff along with EES Consulting began the process of performing a Cost-of-Service Analysis (COSA) for a new series of electric rates for FY2023-24 through FY2026-27. The COSA helps ensure fair and reasonable cost recovery amongst the City's various customer classes (residential, small, and medium commercial and industrial) while also ensuring the City's Electric Enterprise has adequate funding to continue to operate.

Since the final approved rate increase in FY 2018-19, the city has used electric revenues and unrestricted reserves to maintain daily operations, increased the department's operating reserve to 50% of annual operating costs plus a \$4 million capital reserve, and completed large capital improvement projects such as Healdsburg Avenue & Mill Street Undergrounding (\$2.6 million) and the Badger Substation upgrades (\$5.0 million). However, FY 2022-23 and 2023-24 budgets show the fund entering a deficit. Extreme inflation, energy market volatility, and desired

community improvements necessitate rate increases to ensure fund stability.

During the March 6 and April 17 Council meetings staff presented an overview of the rate setting process and financial challenges facing Healdsburg's electric department. With Healdsburg's electric rates 50% lower than PG&E and Sonoma Clean Power (SCP), Healdsburg electric customers receive significant savings on their monthly energy bills. Healdsburg's lower electric rates result in communitywide savings of over \$12 million annually. The proposed rate increases over the next four years will reduce these savings but still allow the City to provide reliable energy, community driven projects, and substantial savings over both PG&E and SCP.

DISCUSSION/ANALYSIS:

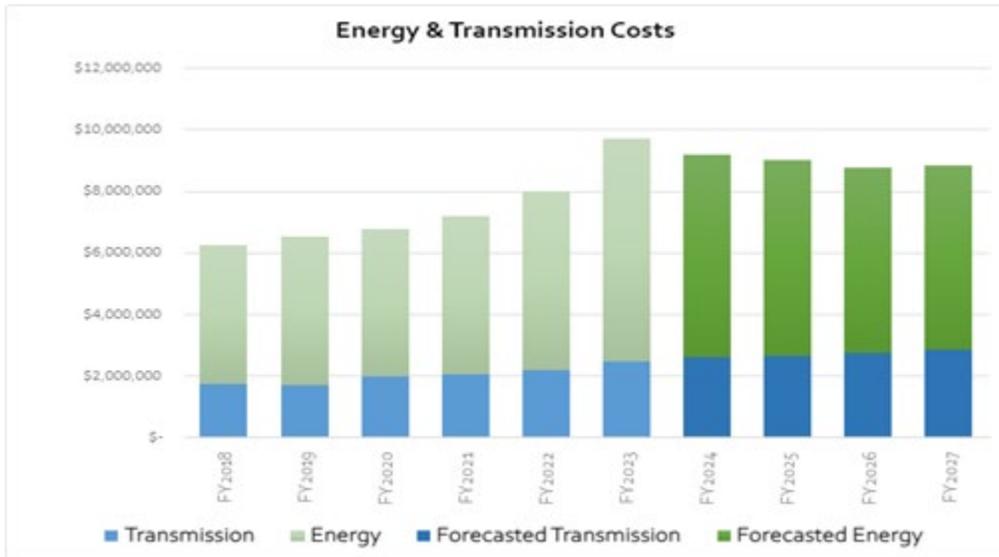
During the initial phases of the COSA, EES Consulting reviewed and developed revenue requirements for FY2023-24 through FY2026-27. The table below lists each year's revenue requirement and represents the cost forecasts for the coming years. As shown, costs will increase over the next several years and therefore the City's cost recovery requirements (rates) will need to increase.

FISCAL YEAR	FORECASTED REVENUE REQUIREMENT	PERCENT INCREASE
FY 2023-24	\$14.0 mil	16%
FY 2024-25	\$16.0 mil	14%
FY 2025-26	\$17.4 mil	8%
FY 2026-27	\$18.6 mil	7%

The revenue requirements assume a use of fund reserves and represent the rate revenues required to cover forecasted costs in each of the major cost categories: Generation, Transmission, Distribution, and General. Energy and transmission costs, utility undergrounding projects, and inflationary constructions costs are large drivers increasing revenue requirements.

Energy and Transmission Costs

Multiple years of drought, inflation, and necessary plant repairs and maintenance have all resulted in cost increases for energy. From FY2017-18 to FY2021-22 the City's energy prices have increased 29% and energy costs for FY2022-23 are expected to come in 26% over FY2021-22 costs. Forecasts for energy costs, without the addition of new renewable or other clean energy sources, are expected to lower from the peak in FY2022-23 but remain roughly 50% higher than energy prices seen in FY2017-18. Compounding this are increased transmission costs; the cost necessary to bring power from the City's various generation plants within California to Healdsburg. In FY2017-18 the City paid just over \$1.7 million for transmission services. For FY2022-23 these costs are estimated to exceed \$2.5 million, a 43% increase over 6-years. Continuing to increase, transmission charges are expected to reach \$2.8 million in FY2026-27.



Healdsburg's energy and transmission costs have seen recent and rapid increases in costs. The forecast for future years indicates they will remain higher than the historic average.

O&M and Planned Capital Improvements

The rapid increase in material costs has and is expected to continue to outpace inflation. Following COVID equipment prices have seen increases between two to five times their historical pricing. Over the next four years the City will need to prepare to spend more on materials. While material costs are a small portion of the electric department's internal costs, they will contribute to overall cost increases.

Additionally, is planning to fund succession planning efforts as a result of anticipated staff retirements. In most cases this will require a brief overlap of positions to transition knowledge. While this will temporarily increase the department's costs it is a necessary cost to recruit and transition new employees and maintain continuity in communitywide services.

To minimize the near-term costs and impact of rate increases, staff have removed three large projects shown on the current Capital Improvement Plan: the South Healdsburg Back-tie, Badger Substation Bank Replacement, and the Reconductor of Grove Street north of Dry Creek. This work can be deferred with a limited but increased risk of planned and unplanned outages. Removing these projects eliminates just over \$1.6 million of capital improvement projects from the four-year cost-of-service analysis and will have the effect of reducing rate increases.

The proposed rate increase will continue to fund a grant match for seismic retrofitting (liquefaction) at the Badger Substation, undergrounding of Grove Street between Dry Creek Road and Grant Street, and undergrounding portions of Healdsburg Avenue between Parkland Farms to just south of the Community Center. Over the next four years, these projects are estimated to have a combined cost of \$6.9 million with most of the funding going to undergrounding projects planned in FY2024-25 and FY2025-26. Each of these projects contribute to the need for increased rates but will return measurable benefits to the community. Timing of the projects, and the corresponding revenue requirement, is based on the need to complete undergrounding work in advance is other planned improvements to those areas.

COSA Revenue Requirement Results

The table below summarizes the COSA results and illustrates the forecasted revenue requirements that need to be recovered by electric rates. These costs have been reduced by eliminating the forementioned capital projects but will support community improvements such as the undergrounding projects planned for Healdsburg Avenue and Grove Street.

Rate Adjustment Plan	2023	2024	2025	2026	2027
Proposed Rate Adjustment		16.0%	14.0%	8.0%	7.0%
Revenue with Rate Adjustment	\$12,064,804	\$13,995,172	\$16,010,818	\$17,352,755	\$18,633,055
Other Revenue (op and non-op)	\$232,519	\$238,519	\$245,675	\$253,045	\$260,636
Total Revenue	\$12,297,323	\$14,233,691	\$16,256,493	\$17,605,800	\$18,893,691
Purchased Power & Transmission (NCPA)	\$9,470,050	\$9,173,804	\$8,984,866	\$8,761,614	\$8,810,075
Operations & Maintenance	\$6,383,947	\$6,416,240	\$6,648,899	\$6,434,450	\$6,177,090
Capital Improvement Program	\$35,000	\$62,500	\$1,410,000	\$4,488,750	\$900,000
Total Expenses	\$15,888,997	\$15,652,544	\$17,043,765	\$19,684,814	\$15,887,164
Surplus (Deficit)	(\$3,591,675)	(\$1,418,853)	(\$787,272)	(\$2,079,014)	\$3,006,527

The above table shows the preliminary revenue requirements for the next four fiscal years. A significant jump in energy and transmission costs, along with planned capital improvement projects are driving a need to increase electric rates.

The proposed rate increase will, over time, correct the planned deficit of FY2023-24, adjust revenues to account for increases in wholesale power costs and transmission services, and fund undergrounding projects along major thoroughfares. The proposed rate increase also benefits the community by improving long-term revenues to support future projects. The projected “surplus” in 2027 is deemed necessary to meet the fund’s reserve policy and re-establish the financial resilience of the enterprise after the deficits of the current and future years.

Proposed Rate Increases

As developed from the COSA, Attachment A details the proposed electric rate schedules for the coming fiscal years. Incorporated into the proposed rate increases are rate adjustments indicated by the cost allocation methodology applied within the COSA model. In developing these rates, the timing of future capital projects and the use of fund reserves help minimize the magnitude of the overall increases. As a generalized summary, the following table illustrates three of the proposed electric rate increases for various customer usages levels.

Multi-Family Rate (D-1)								
	Monthly kWh Usage (kWh)	Old Rate	FY2024 New Rate			Four Year Average		
Low Usage	150	\$26.78	\$29.11	\$2.33	8.7%	\$34.72	\$3.59	11%
Average Usage	272	\$43.37	\$47.85	\$4.47	10.3%	\$55.03	\$4.83	10%
High Usage	450	\$67.59	\$75.18	\$7.59	11.2%	\$84.67	\$6.63	9%
Single-Family Rate (D-1)								
	Monthly kWh Usage (kWh)	Old Rate	FY2024 New Rate			Four Year Average		
Low Usage	350	\$53.98	\$63.10	\$9.11	16.9%	\$74.32	\$8.06	12%
Average Usage	484	\$72.21	\$83.67	\$11.46	15.9%	\$96.63	\$9.41	11%
High Usage	700	\$101.59	\$116.85	\$15.25	15.0%	\$132.59	\$11.60	10%
Small Commercial Rate (C-1)								
	Monthly kWh Usage (kWh)	Old Rate	FY2024 New Rate			Four Year Average		
Low Usage	950	\$165.36	\$194.38	\$29.01	17.5%	\$228.96	\$24.01	12%
Average Usage	1120	\$191.74	\$223.82	\$32.08	16.7%	\$261.22	\$26.06	12%
High Usage	1350	\$227.44	\$263.66	\$36.23	15.9%	\$304.86	\$28.82	11%

Annual Rate changes are for general reference and actual changes will depend upon each individual customer's monthly consumption. Over the four year period rates will increase by an average of between 10 and 12% per year.

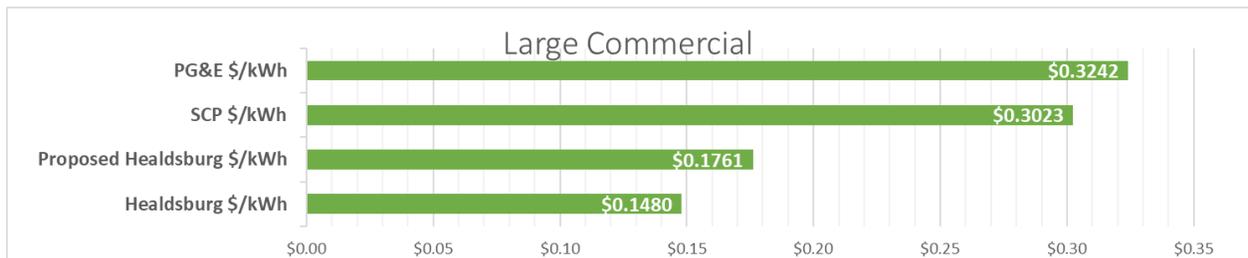
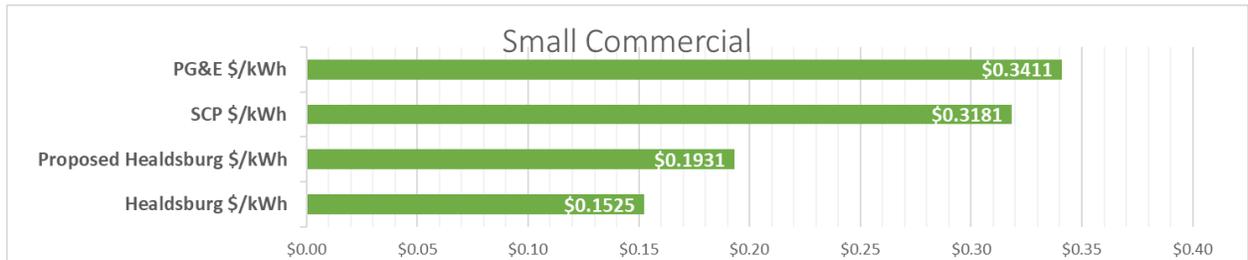
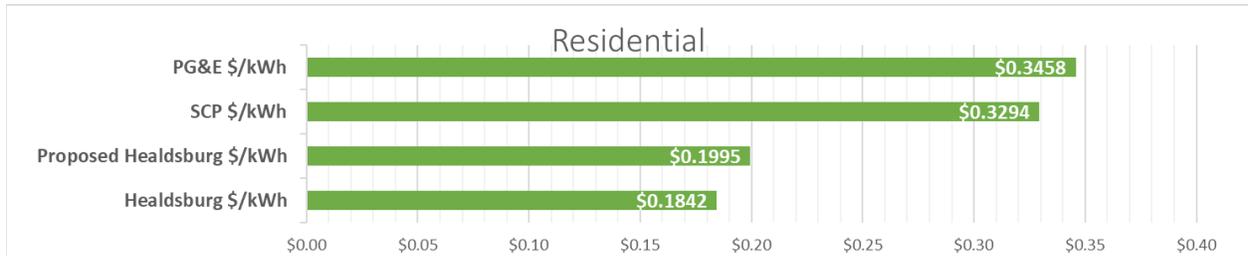
As discussed in the COSA, each rate class can have varying increases. As each rate class, or customer grouping, consumes energy differently and therefore changes how the City incurs costs to provide service. For example, multi-family customers tend to have a lower demand per customer than single-family homes. The proposed establishment of differing monthly fees for single and multi-family customers more fairly allocates costs to maintain the electric system year-round. Additionally, a focus on increasing the monthly customer charge, rather than the per unit cost of energy, better recovers fixed costs that are independent of the amount of energy supplied.

Certain charges within the commercial and residential rates are proposed to be removed. For residential customers, the highest residential tier rate has been removed. Removal of this rate follows a utility trend of narrowing the residential per-unit charge as it better represents how utilities incur energy costs. For all customers, there is a focus on gradually increasing the fixed monthly customer charge. The intent of this charge is to represent the costs of providing a service connection and maintaining access and availability to the power grid. For small energy users within a rate class, this will result in a proportionally larger rate increase but more fairly collects costs incurred to operate and maintain the electric system.

Staff have updated the Electric Rate Schedules to further define each rate class and associated electric rates. The Rate Schedule includes application guidelines, definitions of each rate component, details of available rate modifiers, and the proposed costs. This allows for clarity and consistency in the application of electric rates. The Rate Schedule also defines rate modifiers such as net-metering (solar), Healdsburg's Green Rate, demand charges, and time-of-use rate application. Updated Rate Schedules are included at Attachment B to the staff recommended resolution.

Savings over Pacific Gas & Electric & Sonoma Clean Power

The City's electric rates are currently 50% lower than PG&E and SCP and these low rates result in community-wide savings of \$12 million each year. If adopted the proposed rates will reduce these savings but would still provide substantial savings PG&E and SCP current electric rates. The three charts below compare Healdsburg's current and proposed electric rates against PG&E and SCP. The comparison shows Healdsburg maintaining a 41 to 46% savings over the neighboring service providers. With the proposed rates the yearly savings will be \$11 million and create total savings over the four years of between \$53 to \$66 million.



PG&E & SCP's proposed average rates compared to Healdsburg's current and proposed rates. With the proposed rate increases, Healdsburg will continue to have lower electricity rates and provide measurable savings to the community.

ENVIRONMENTAL STEWARDSHIP:

Maintaining the financial stability of the City's electric enterprise will allow the support of the City electrification of the transportation and building sectors to reduce greenhouse gas emissions. If adopted, the proposed rates increases will also prepare the electric enterprise financially to increase the capacity of the electric grid in support of increased future use of electric vehicles and building electrification.

ALTERNATIVES:

The City Council may choose not to approve the electric rate increases or lower the percent rate increase indicated by the COSA. If the Council chooses this option, the City's Electric Enterprise

it would also be necessary to adjust the forecast of future investments in order to balance costs and revenues while meeting reserve requirements.

FISCAL IMPACT:

The proposed electric rates will gradually increase the Electric Enterprise revenues to fund operational costs, complete planned capital replacements, and re-establish reserves to ensure the long term health of the enterprise. In FY2023-24 approximately \$400,000 of the operating reserves would be used to support operations and over FY2024-25 and FY2025-26 \$3.1 million of the capital reserve funds will support expediting the planned capital projects. The proposed rates will facilitate a full recovery of all reserves in FY2026-27 and ensure ongoing funding for future projects in subsequent years. The chart below illustrates the effect of the proposed rates on the fund balance in the Electric Fund.

	Electric Fund			
	FY 23-24	FY 24-25	FY 25-26	FY26-27
Beginning Working Capital	\$ 13,678,162	\$ 12,259,310	\$ 11,472,037	\$ 9,393,023
Revenue	14,233,691	16,256,493	17,605,800	18,893,691
Expenditure - Operations	15,590,044	15,633,765	15,196,064	14,987,164
Expenditure - Capital	62,500	1,410,000	4,488,750	900,000
Estimated Ending Working Capital	\$ 12,259,310	\$ 11,472,037	\$ 9,393,023	\$ 12,399,550
Change in Working Capital	\$ (1,418,853)	\$ (787,272)	\$ (2,079,014)	\$ 3,006,527
<u>Components of Fund Balance</u>				
Reserve Policy (50%)	\$ 7,795,022	\$ 7,816,883	\$ 7,598,032	\$ 7,493,582
Reserve Policy (\$4 Million Capital)	\$ 4,000,000	\$ 4,000,000	\$ 4,000,000	\$ 4,000,000
Pension Stabilization	\$ 882,291	\$ 889,291	\$ 896,291	\$ 903,291
Remaining Working Capital (Reserve Use)	\$ (418,003)	\$ (1,234,136)	\$ (3,101,300)	\$ 2,677

ENVIRONMENTAL ANALYSIS:

This Resolution is not subject to the California Environmental Quality Act (“CEQA”). This action is not a project within the meaning of the CEQA Guidelines Section 15378 and 15061(b)(3) as it has no potential for physical effects on the environment because it involves an adoption of certain rates and/or charges imposed by the City and does not commit the City to any specific project.

ATTACHMENT(S):

- Resolution
- Attachment-A Proposed Electric Rates
- Attachement-B Proposed Electric Rate Schedule FY2023-24
- Healdsburg Electric Cost of Service Study