



STAFF REPORT

TO: Board of Directors
THRU: Mark Foree, General Manager
FROM: John Erwin, Scott Estes, Kim Mazeres and Jeff Tissier
DATE: 10 September 2011
SUBJECT: **Preliminary revenue requirement and request for Board direction to staff to move forward with a proposed rate adjustment process and schedule**

Recommendation

Staff recommends the Board direct staff to begin the process of gathering public input by presenting to the Standing Advisory Committee (SAC) and at other public meetings/workshops the cost study and proposed rate adjustment. Subsequent to those meetings, staff will present its recommendations and findings to the Board for the first reading of proposed rate adjustments at the November 16, 2011 meeting.

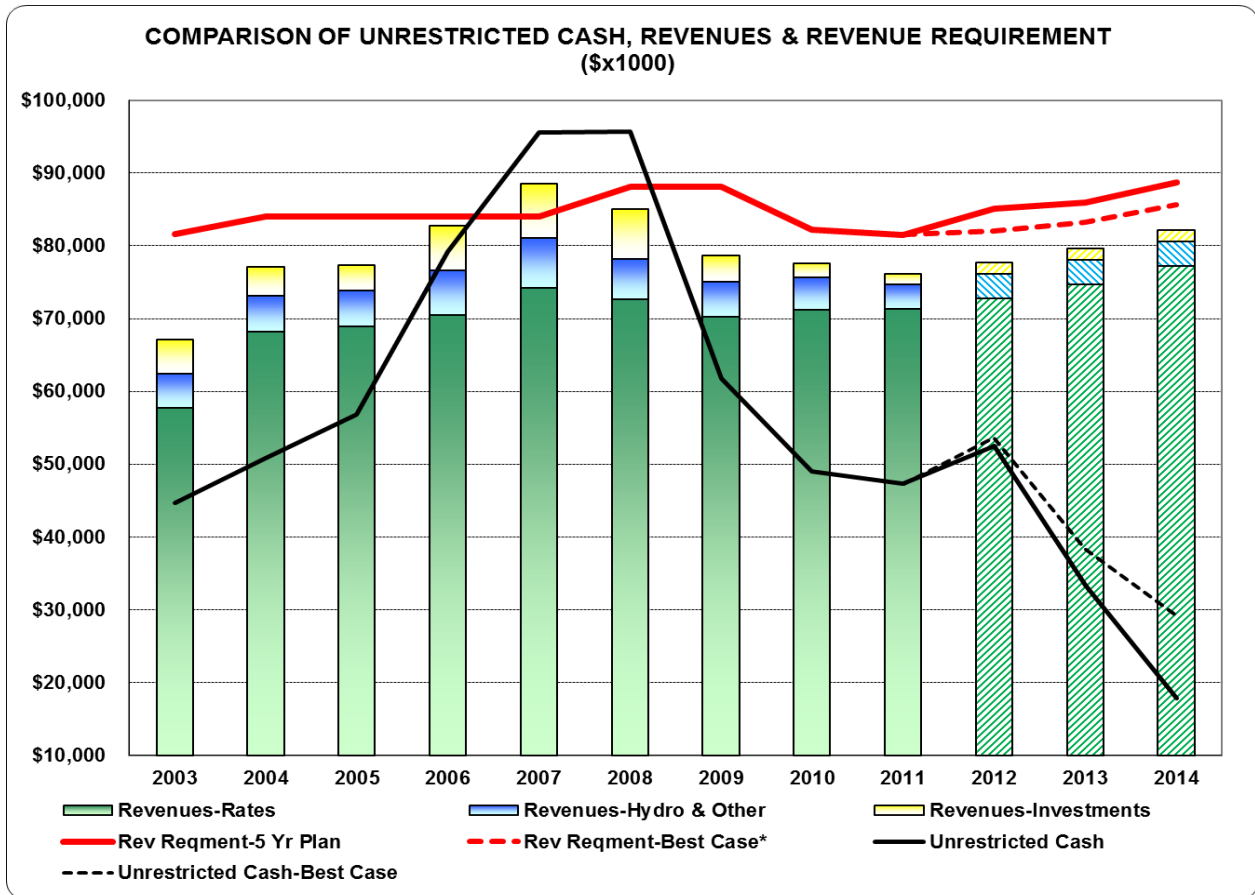
Discussion

In January 2009 staff presented its revised 5-year (FY2010-FY2014) funding plan requirements. The Board adopted a two-part rate adjustment, a 4.5% overall increase effective June 2009 and a 4.5% overall increase effective June 2010; these increases sought to achieve total revenues of \$77.9 million through FY2011. These rate adjustments were part of the ongoing process since TMWA's inception to monitor and analyze its financial health. This was and continues to be important particularly as the utility attempts to close a significant gap between the cost to serve customers and revenues to support the cost of service, with the goal being to ensure TMWA can achieve revenues sufficient to cover its costs, i.e., revenue sufficiency.

Although Phase 1 provided some modest relief to TMWA's financial picture, Phase 2 of the increase did not provide any additional incremental water sales revenue due to a combination of the current economic malaise, no growth in customers, and cooler weather patterns over the past three years resulting in reduced demand for water. FY2009 TMWA water sales were \$70.2 million which increased to \$71.2 million in FY2010. Preliminary FY2011 water sales results are \$71.3 million. Of an expected \$6.0 to \$7.0 million in incremental water sales revenue expected to be generated from the two-phase water-rate increases, TMWA has only realized approximately \$1.0 million. Offset by dismal sales performance TWMA personnel have been diligent in significantly reducing operating expenses, from a peak of \$40.5 million in FY2009 to \$33.2 million in FY2011, a net reduction of \$7.2 million, or 18% over two years. This reduction in costs exceeded the loss in incremental water sales revenue expected from the last rate adjustment. It is management's opinion that FY2011 operating expenses approximate the lowest

level of expenses going forward without degradation in customer services. If TMWA had realized the additional water sales revenues coupled with the aforementioned operating expense reductions revenue sufficiency would have been achieved in FY2011.

The following graphic illustrates the lack of revenue sufficiency over the course of TMWA’s history by comparing fiscal revenues to the revenue requirement.



* Best Case assumes annual inflation of 2.5% on FY2011 O&M and R&R components of revenue requirement.

The graph illustrates that although cost cutting actions have been taken which reduced the amount of revenues necessary to cover annual cash outlays (the red line), the gap between customer-rate-required-revenues and all revenue sources will continue to grow resulting in declines in unrestricted cash balances (the black line) by fiscal year 2014. Revenues from customer rates (the green bars) have been declining since 2007 but were stabilized somewhat with the rate adjustments in 2009 and 2010. However, with the lack of new customers growth coupled with customers using less water due to cooler weather and/or discontinuing service completely, TMWA continues to rely on its unrestricted cash reserves to close the revenue requirement gap. Investment income (the yellow bars), which benefitted TMWA between 2006 and 2008, has diminished substantially since 2007 and will continue to do so as unrestricted cash balances are depleted and rates of return on investments remain at historic low levels due to the current market conditions. Other revenues (the blue bars) include declining inspection and new business fees as a result of declines in new services; and hydroelectric generation which

increased slightly in recent years due to abundant Truckee River water supplies combined with much greater plant availabilities.

Rate Adjustment Timeline

Consistent with the Board adopted rate adjustment calendar (see attached calendar), staff proposes to present its cost study and rate adjustment proposals to the Standing Advisory Committee and other public meetings / workshops beginning October 2011 through January 2011. Staff will present and discuss the rate adjustment proposals at the November 16, 2011 Board meeting for its first reading, along with any customer issues or concerns received from the public meetings. Staff will also be providing for a first reading several revisions to Rules 1 through 6 at that meeting.

Date	Organization	Item
Tue, Sep 6	SAC	Part 1 of Rates Training
Wed, Sep 21	BOARD	Present rate adjustment calendar and revenue sufficiency
By Fri, Sep 23	Staff	Finalize calendar for rate adjustments
By Fri, Sep 23	Staff / O&A	Finalize special one-panel bill insert for all customers regarding workshop and Board meeting dates and times. Insert to run October 3 to October 28
Tue, Oct 4	SAC	Present revenue sufficiency analysis and do Part II Training
By Wed, Oct 12	O&A	Send in display notice of Customer Workshop to RGJ & Sparks Tribune for publication on November workshops
By Fri, Oct 14	Staff/O&A	Finalize November bill insert notifying customers of final public hearing for adoption of rate adjustment and rules revisions
Wed, Oct 19	BOARD	Presentation on preliminary Rates proposals and including cost-of-service study
Wed, Oct 26	RGJ	Display Notice of Customer Workshop published in RGJ & Sparks Tribune (<i>10 working days before workshop</i>)
By Fri, Oct 28	Corinne	Send in legal notice of first public hearing (November 16) to RGJ & Sparks Tribune
Tue, Nov 1	SAC	Present/ public workshop final Funding Plan and Rate Proposal
Wed, Nov 9	PUBLIC	Proposed date of Customer Workshop on Rate Adjustment
By Fri, Nov 4	RGJ	Legal Notice of first public hearing on proposed rate adjustment and rules revisions published in RGJ, Sparks Tribune and on TMWA website (<i>10 days before first hearing</i>)
Mon, Nov 14	Corinne	Send in legal notice of final public hearing (January 18) and adoption of rate adjustment and rules revisions to RGJ & Sparks Tribune for publication on
Wed, Nov 16	BOARD	First Public Hearing and Reading on proposed rate adjustment and rules revisions – proposed evening meeting
Fri, Nov 18	Corinne	Post copies of proposed rate adjustments and rules revisions approved at First Public Hearing and post Notice of Final Hearing date, time and location. Post in all the same locations as agenda is posted, and on TMWA Website.
Mon, Dec 14	RGJ	Legal Notice of final public hearing for adoption of rate adjustment and rules revisions published in RGJ, Sparks Tribune and TMWA website (<i>30 days in advance of final hearing</i>)
Tue, Dec 6 and/or Jan 3	SAC	Update on rate adjustment and rules revisions
Wed, Jan 18	BOARD	Final Public Hearing & adoption of rate adjustments and rules revisions
Feb 2012	Staff	Rate adjustments and rules revisions effective Cycle 1 billings
Tue, Feb 7	SAC	Report of Board Action on rate adjustment and rules revisions