



ROCHESTER PUBLIC UTILITIES

Public Utility Board Agenda Rochester Boards & Commissions - Public Utility Board August 6, 2024 4:00 p.m.

Attending and Viewing the Meeting

This is a special budget review meeting of the Rochester Public Utility Board.

Attend in-person at 4000 E River Rd NE, RPU Community Room, Rochester, MN or via [MS Teams](#).

Call in audio only number: 347-352-4853 Conference ID: 428 902 155#

A recording is made available after the meeting at the [City's website](#).

Call to Order/Roll Call

- 1. *Approval of Agenda***
- 2. *Regular Agenda***
- 3. *Informational***

3.A. Recommended 2025 Water and Electric Utility Budget Updates

No action required. Staff will be available to present and receive input on the proposed budgets.

Final budget approval will be requested during the October 29, 2024, Board meeting, followed by a request for final Council approval on December 2, 2024.

4. *Board Policy Review*

4.A. [Board Policy 27. Contribution in Lieu of Taxes](#)

Review and receive comments on the draft revised policy.

5. *Other Business*

6. *Adjournment*



REQUEST FOR ACTION

Recommended 2025 Water and Electric Utility Budget Updates

MEETING DATE:

August 6, 2024

ORIGINATING DEPT:

Rochester Public Utilities

AGENDA SECTION:

Informational

PRESENTER:

Peter Hogan

Action Requested:

No action required. Staff will be available to present and receive input on the proposed budgets.

Final budget approval will be requested during the October 29, 2024, Board meeting, followed by a request for final Council approval on December 2, 2024.

Report Narrative:

The Board approved the 2024 and 2025 operating budgets, capital projects budgets and multi-year projects continuing beyond 2025, and proposed rate adjustments at the October 24, 2023, Board meeting. The City Council approved the recommended budgets and rate tariffs for both 2024 and 2025 in December 2023.

The current budget review is updating the 2025 operating and capital budgets, however this update does not request any change to the general rate adjustment approved in 2023 for the Water or Electric funds. Management does anticipate some specific rate change recommendations in line with the recommendations that were presented to the Board during the March 27, 2024 board meeting.

Water Utility (in thousands):	2025 Original	2025 Updated
Revenue	\$16,220	\$15,370
Capital (Rate Funded)	\$ 5,239	\$ 5,539

Historically, the water utility has funded capital projects through rates each year between \$2.5M and \$3.0M. The 2025 proposed rate funded capital expenditures of \$5.539M compared to the original 2025 budget of \$5.239. The major capital initiatives that are putting upward pressure on our Water Utility rates are City Road related projects, the approved Advanced Metering Infrastructure (AMI) project, water main replacement and the addition of \$500K contingency for opportunistic capital project that the Utility could undertake when work is being done to support the Mayo Bold Forward Unbound initiative. We are working to increase the water main replacement to \$1M per year to address reliability and aging water infrastructure. The other item that will inflate the capital budget in future years is the inclusion of subscription assets in the year that we enter into a software-related subscription. These assets will be capitalized and then amortized over the life of the subscription. There is no impact due to subscription assets to the water capital budget in 2025.

The main drivers for the Water budget are:

- Growth in customers (0.9%) and consumption (2.3%) for 2025. This is due to the assumption of average weather and rainfall.
- The adopted AMI project will require an investment of \$15.6M over five years. This represents an increase of \$1M over the original budget. This increase represents a project contingency that was not included in the original budget request. The increase in operating costs is expected to be offset by cost savings and additional revenue authorized in the original budget once fully deployed.
- Increased inflation, vendor and supplies availability
- Water main replacements to address aging infrastructure
- City planned street reconstruction
- Development in the downtown (DMC) area affecting water infrastructure
- Distribution system expansion
- Mayo’s Bold Forward Unbound initiative
- Water conservation programs and education

For the water utility, management is recommending no change from the 5.5% general rate adjustment plus an AMI related increase in the customer charge of \$1.32 per month that has been approved for 2025. This is a monthly increase of \$1.67 per month for the average residential customer in 2025.

Electric Utility (in thousands):	2025 Original	2025 Updated
Revenue	\$199,093	\$200,722
Capital (Rate Funded)	\$ 15,662	\$ 15,429

The current electric utility budget shows slow and steady growth of both customers (2025: 0.8%) and consumption (2025: 2.3%). The approved 2025 budget includes two incremental full-time positions. There is a planned spend down of up to \$50M of cash reserves as part of the 2030 resource plan. Of this amount \$12M is anticipated to be spent in 2025.

The approved AMI metering system for our electric customer would require an investment of up to \$15.6M over the next 5 years. This is an increase of \$2M over the originally approved budget and reflects the inclusion of a project contingency which was not included in the originally approved budget. The operating expense is expected to be offset by cost savings and additional revenue from a more accurate metering system.

The recommended 2025 budget includes an additional \$1M contingency for the Electric Utility. The contingency could be used for opportunistic capital project that the Utility could undertake when work is being done to support the Mayo Bold Forward Unbound initiative. The rate funded capital includes an additional \$344K related to the capitalization of subscription assets. This is due to a change in accounting standards in 2023 where software subscriptions are capitalized and amortized over the life of the asset.

Major assumptions:

- In 2026 and 2027 there is an anticipated reduction in the wholesale power costs, due to the retirement of the debt on Sherco 3 by SMMPA in 2026. These funds would normally be passed back to customers through the power cost adjustment; however, the intent is to request Board action effective in 2026 to retain these funds to offset the increase in interest expense due to the 2030 power resource plan borrowing during construction between 2025 and 2030.
- An increase in debt starting in 2026 through 2029 totaling \$457.8M. This debt, besides funding construction includes issuance costs and required debt reserve funds to support the implementation of the 2030 resource plan (Scenario 2) shared with the Board during the July 30, 2024, meeting. The forecast bonding also includes a potential investment in transmission upgrades (\$30.9M). While the specific configuration of the resources and financing may change,

we are showing the projected costs related to the purchase of capacity to offset the capacity currently provided through the SMMPA contract which ends in 2030. The debt service on the transmission investment is offset by additional transmission revenues.

- Cash reserves are expected to go down at the end of 2025 due to the completion of the planned Marion Road substation and the beginning of the spend down of up to \$50M related to the 2030 power resource plan.
- The Debt Coverage Ratio is above our target of 3.0 times in 2025, however this ratio is projected to be below target as debt is issued. Once the 2030 transition is completed and the new generation assets and debt are on the Electric Fund's balance sheet, we expect to maintain a long-term debt coverage ration that will be closer to 1.5 times. This is an important metric when considering future borrowing needs.

Significant business drivers for the 2025 Electric Utility budget are:

- The beginning of the 2030 Power Resource Plan implementation, including anticipated spend of \$12M in reserves.
- Inflation, vendor and supplies availability
- Labor Inflation
- Rate funded capital expenditures of \$14.7M
- The Marion Road substation and feeder system completion
- Electric AMI meter system
- Continued investments in distribution system expansion and reliability, including the new Marion Road substation, tree trimming, new services, and replacement of aging infrastructure

Management is recommending no change to the already approved general rate increase of 4% in 2025. The impact to the average residential customer is \$4.30 per month in 2025. As identified earlier, there are some rate items that were reviewed with the Board in March 2024 and the expansion of the current electric service assured program that will be reflected in the recommended 2025 rate tariff.

Both Utility budgets reflect the need to meet financial targets based on the Utility Method of rate setting:

- Change in Net Assets (Net Income)
- Debt Service Coverage Ratio
- Equity Percent
- Minimum cash reserves per Board policy

For the recommended rate changes, management will review the proposed rate design changes during the September 24, 2024 Board meeting and seek Board approval to give public notice of the proposed rate changes.

Members of the public may provide comments to the RPU Board directly or at the regularly scheduled August, September, or October Board meetings.

Prepared By:

Peter Hogan

Attachments:



REQUEST FOR ACTION

Board Policy 27. Contribution in Lieu of Taxes

MEETING DATE:

August 6, 2024

ORIGINATING DEPT:

Rochester Public Utilities

AGENDA SECTION:

Board Policy Review

PRESENTER:

Tim McCollough

Action Requested:

Review and receive comments on the draft revised policy.

Report Narrative:

Attached is the redlined version of the **Contribution in Lieu of Taxes** policy that the Board ad hoc group reviewed on August 2. It contains the suggested edits that resulted from that August 2 meeting.

Prepared By:

Erin Henry-Loftus

Attachments:

[Board Policy 27 Contribution in Lieu of Taxes -Redlined Version.pdf](#)



POLICY 27: Contribution in Lieu of Taxes

POLICY OBJECTIVE:

The Rochester Public Utility Board operates utility enterprises owned by the City of Rochester for the benefit of its consumer ratepayers. The Board's responsibility is to deliver adequate, reliable service to these ratepayers at an economic cost. The Board recognizes, however, that the services of City government are used in the operation of a utility enterprise. Accordingly, the Board desires to contribute to the City general fund annually a "fair share" amount of money which represents the cost of City government to be paid by the Board's consumer ratepayers. This amount of money will be designated as a "Contribution in Lieu of Taxes."

POLICY STATEMENT:

The Board desires to establish a method of determining the "Contribution in Lieu of Taxes" which fairly compensates the City for services provided, ~~which can be estimated for budget purposes~~, and which eliminates the potential use of utility enterprise funds for meeting the revenue requirements of City government. Recognizing that any policy which affects the financial operation of the utility enterprises ~~must be reviewed periodically with respect to changing conditions~~, the Board ~~initially~~ establishes the following guidelines for determining the annual "Contribution in Lieu of Taxes" to the City general fund:

1. "In Lieu of Tax Payments" will be computed on commodity sales of the electric and water utilities.
2. Commodity sales units are defined as kilowatt-hours (kWh) for the electric utility and one-hundred cubic feet (CCF) for the water utility.
3. The base unit amount for calculation of the payment will be \$0.~~0056000959~~/kWh for the electric system and \$0.~~0525208132~~/CCF for the water system as of January 2024.
4. ~~Change to the base unit amount would only occur if a given utility has a rate increase.~~ The base unit would be increased by the percentage increase in the Consumer Price Index (CPI) from the previous January through December reporting period. The effective date of increase would coincide with the utility rate increase date.

Commented [TM1]: The suggested changes recognize some recent challenges in the ability to accurately forecast for budgetary planning purposes the future budget PILOT expenses/revenues. The revisions to this policy are paired with some internal procedure changes to improve the forecast accuracy.

Commented [TM2]: The changing conditions of the previous 5 years are a more variable CPI environment and some commodity volume variations year to year during the pandemic and post-pandemic recovery period.

RELEVANT LEGAL AUTHORITY: The City of Rochester, MN Home Rule Charter Chapter 15.05, Subd. 3 and Section 15.07, Subd. 1

EFFECTIVE DATE OF POLICY: January 1, 1984
DATE OF POLICY REVISION: ~~June 29, 1999~~ August 27, 2024

Commented [TM3]: The target meeting to approve the changes to policy 27 is the Aug 27, 2024 in parallel with the 2025 budget approvals.

POLICY REVIEW: _____
Board President Date