

DATE: June 20, 2024

TO: Environmental Services Commission

FROM: Lucy Liu, Utilities Director
Scott Edwards, Utilities Deputy Director
Scott Pickard, Acting Fiscal Manager

SUBJECT: Utilities 2025-2026 Operating Budget Proposals

ACTION REQUIRED

No action by the Commission is required at this time. This is an informational briefing.

BACKGROUND / ANALYSIS

This is a continuation of a series of briefings to facilitate the Commission's review of the proposed Utilities Department 2025-2026 operating budget and rates, and 2025-2034 capital investment program (CIP).

Commission previously reviewed:

- January: Utilities Asset Renewal Forecast;
- February: Utilities financial policies;
- April: Utilities 2023 financial performance results and department-proposed 2025-2034 CIP Plan;
- May: Operations & maintenance/CIP field tour; and
- June: 2025-2030 Utilities Early Outlook Financial Forecast, and Utilities 2025-2034 CIP budget proposals and Utilities CIP community engagement results.

On June 20, staff will review the following with the Commission:

- Utilities 2025-2026 operating budget proposals.

Additional details on the operating budget proposals are included as attachments to this memorandum.

Guiding Principles for Budget and Rates Development

The 2025-2026 Utilities operating budget proposals represent department requests for the financial resources necessary to implement our services, strategies, and policies over the next biennium. Utilities consists of enterprise funds, which must operate on a self-sufficient basis without relying on general taxation. Utility rates are the primary funding source for this budget, and as a result, each budget proposal is developed with prudent financial management and efficient service delivery in mind to ensure ratepayer value.

The 2025-2026 operating budget proposals were developed in alignment with the following principles:

- Align with Council strategic direction: Utilities budget proposals align with Council strategic direction by:
- Supporting the City's vibrant economy by providing reliable utilities access to services;
 - Protecting and preserving Bellevue's utility infrastructure as part of the Council's priority for High-Quality Built and Natural Environment, addressing the challenges of population growth and sustainable resource use;
 - Maintaining utility services and infrastructure that directly preserve and improve public health; and
 - Being a high-performing organization, leveraging innovation and technology to enhance customer service, improve service delivery, and achieve cost efficiencies.

- Adhere to City financial policies: City financial policies serve as the foundation for developing the Utilities Department budget and rates. Adherence to these policies has enabled the department to be recognized as a leader in the industry, provide competitive utility rates, and achieve financial sustainability.

Consistent with City financial policies, the budget proposals are based on:

- Funding the full cost of providing utility services now and in the future;
 - Funding the full cost of wholesale services;
 - Maintaining sufficient reserves to protect the solvency of the utility funds;
 - Investing in capital infrastructure and/or the deposit of funds in an infrastructure Renewal and Replacement (R&R) Account to ensure current and future users of the utility system pay their proportional share of system costs; and
 - Maintaining predictable, smooth, and uniform rates.
- Regulatory compliance: Utilities services are subject to significant regulatory requirements from the State Department of Health, Department of Ecology, the federal National Pollutant Discharge Elimination System (NPDES), and more. Maintaining compliance with these various requirements is of paramount importance.
 - Preserve aging utility infrastructure: The City's utility infrastructure, valued at about \$10 billion across the three piped utilities (based on replacement costs in 2023 dollars), is well past its mid-life, and increased maintenance and capital investments are inevitable. System failures are on the rise. The proposed 2025-2034 capital program will focus largely on the renewal and replacement of aging infrastructure.
 - Lean operations: A lean budget is proposed to maintain current service levels, implement strategies from prior budget decisions, fund external financial obligations, and meet regulatory requirements.

2025-2026 Utilities Operating Budget Proposals

The Utilities operating budget proposals are detailed in Attachment A. The following are key highlights of the Utilities 2025-2026 operating budget requests:

- ❖ **Maintain current service levels to the community.** Utility services are essential to the health and economic well-being of the community. The proposed budget includes proposals to maintain current levels of service:
 - **Wholesale costs.** The budget proposals include funding for wholesale costs for drinking water supply from Cascade Water Alliance (Cascade) and wastewater treatment from King County. Per City policy, increases or decreases in the cost of drinking water supply and wastewater treatment are passed directly through to ratepayers. Cascade's wholesale costs to Bellevue Utilities are projected to decrease by -0.4% in 2025 and increase by 2.4% in 2026. Because these wholesale costs are only a portion of the Water utility's overall expenses, the retail impact of the projected costs to Bellevue water customers is a -0.2% decrease in 2025 and 0.9% increase in 2026.

King County's wholesale cost to Bellevue Utilities is projected to increase by 5.75% in 2025 and 7.0% in 2026. Like the Water utility, wholesale treatment costs represent only a portion of the Sewer utility's overall expenses. Accordingly, the retail impact of the projected costs to Bellevue sewer customers is a 3.3% increase in 2025 and 4.0% increase in 2026.

- **Inflationary cost pressure.** As part of the budget development process, Utilities has evaluated its base funding requirements and right sized expenses following recent years of higher inflationary pressures. However, the department is unable to fully absorb rising costs for the 2025-2026 biennium, with budget proposals reflecting necessary increases to continue providing current service levels.
- ❖ **Sustainably manage aging infrastructure.** The sustainable management of aging infrastructure is critical to the delivery of reliable utility services. The operating budget includes the staffing, planning, and engineering costs necessary to support delivery of that capital program, in addition to the replacement of shorter-lived assets such as vehicles and major software systems. Key elements include:
 - **Operating transfers to CIP and R&R.** These budget proposals together represent the funding strategy for the Utilities CIP. Rate revenues are the primary funding source for capital investment and long-term renewal and replacement. Consistent with the City financial policies, the level of rate capacity needed across these two proposals is guided by the long-term renewal and replacement needs of the utilities. In order to keep pace with rising construction costs, and as the Sewer and Storm and Surface Water utilities transition into active system infrastructure replacement, these proposals include an increase of approximately \$5.3 million in 2025 and \$5.9 million in 2026, in total across the three piped utility funds.
 - **Replace obsolete assets.** For the 2025-2026 biennium, the department is replacing multiple vehicles, including two vactors, and eight heavy duty and flat-bed trucks.
- ❖ **Service enhancements.** The proposed budget includes key enhancements to improve service levels for Bellevue Utilities customers.
 - **Solid Waste Community Outreach.** One-time funding to conduct strategic outreach, with the intent to enhance composting and recycling outcomes. This strategic marketing campaign would highlight resources available to the community at no additional charge, including indoor countertop compost containers. These resources would provide convenience for the public and assist with increasing landfill diversion.
 - **Solid Waste Contract Consultant Services.** The City's contract with Republic Services ends in June 2028, and Utilities will conduct a competitive solicitation for future citywide solid waste services. This one-time funding will provide consultant services to conduct research, community engagement, and Request for Proposal development, issuance, and evaluation. Through a competitive process, the new contract will seek to enhance solid waste services and improve recycling outcomes for the Bellevue community.
 - **Water Distribution System Leak Detection Cycle.** Funding to transition the City's leak detection cycle from a current 10-year interval to a 5-year interval. Leak detection mitigates water loss and works to prevent catastrophic pipe failures by identifying and addressing leaks early. Switching to a 5-year interval supports water conservation, reduces repair costs, and reduces unplanned service disruptions. A more frequent pipe inspection cycle will improve water system efficiency, enhance service reliability, and better protect our resources and the community.
 - **Water Quality Services.** Funding is requested to expand and enhance water quality outreach, pre-inspection scheduling, post inspection data entry, and record keeping. Water Quality & Pollution

Prevention programs ensure internal and external regulatory compliance for the Water, Wastewater, and Storm and Surface Water utilities.

- **Process Improvements (Lean Initiatives).** One-time funding to implement certain lean initiatives, including Asset Management Program level of service and key performance indicator assessments for the three (3) piped utilities; gap analysis and data assessment for the department's use of the work management software system; and project portfolio management software optimization. These initiatives will improve how Utilities uses data and software systems to better inform business decisions and enhance efficiency and effectiveness in CIP development and delivery.
- **Merchant Service Fees.** Utilities budget requests include reduced funding for Merchant Fee expenses. Previously, Merchant Fee costs were absorbed by Utilities and subsequently shared by all customers through utility rate charges. This request aligns Utilities' business process with standard industry practice, ensures full cost recovery for our services, and enhances service equity by appropriately assigning Merchant Fee costs to those benefiting from using a credit card for utility bill payment.

Utilities Staffing

The staffing necessary to deliver the current service levels and enhancements identified in this budget are as follows: 179 full-time employees (FTEs), partially allocated to the capital program, and 4 limited-term employees (LTEs).

Key staffing changes for the department's budget requests include:

- **Capital Project Delivery.** As part of a strategy for reducing long-term costs to the ratepayers the department is requesting three (3) new FTEs to perform currently outsourced project planning, program development, and project management functions in-house. This includes a Planning Senior Engineer, Design Project Manager, and CIP Delivery Program Manager. In addition, the department is requesting to convert an existing LTE Construction Inspector to an FTE Construction Inspector to maintain field inspection coverage.
- **Storm and Surface Water (SSW) Operations and Maintenance.** The department is requesting a lead field worker to address increasing year-over-year inspections, maintenance, and repairs. This is due to the complexity of facilities, more stringent NPDES requirements, and a backlog of work orders generated by the video inspection program. This position would lead a team of skilled workers and increase the SSW capacity to respond to workload demands.

Next Steps

- July 11:
 - Comprehensive Financial Policies review
 - Recommendation from the Commission to the City Manager regarding Utilities 2025-2026 operating budget requests and 2025-2034 CIP budget requests.
- September 5:
 - Preliminary Budget and Rates Forecast
 - Budget and Rates Public Hearing.
- September 19:
 - Budget and rates recommendation to the City Council.

POLICY ISSUES

The proposed operating and capital budgets support Council strategic direction and adhere to the City's financial policies, which guide how the Utilities Department conducts its business and sets its budget and rates.

FISCAL IMPACT

Utilities 2025-2026 operating budget requests represent the financial resources necessary to implement the services, strategies, and policies of the Utilities Department.

ATTACHMENTS & AVAILABLE DOCUMENTS

- A. 2025-2026 Operating Budget Proposals
- B. Proposed 2025-2026 Utilities Operating Financial Statements