

CITY COUNCIL STUDY SESSION

Budget Update - Utilities Department Proposed 2023-2024 Operating Budget and Rates, and 2023-2029 Capital Investment Program Plan.

Toni Call, Director, 452-7863

Evan Phillips, City Budget Manager, 452-2831

Finance & Asset Management Department

Nav Ota, Director, 452-2041

Utilities Department

DIRECTION NEEDED FROM COUNCIL**INFORMATION ONLY**

Staff is seeking feedback regarding the Utilities Department's proposed 2023-2024 operating budget and rates, and 2023-2029 Capital Investment Program (CIP).

RECOMMENDATION

N/A

BACKGROUND & ANALYSIS

On March 7, Council held a budget workshop where staff briefed Council on the process and milestones of developing the budget, provided a discussion of economic pressures, challenges to the City's fiscal sustainability, and long-range capital planning needs for parks and recreation, among other related topics. Council provided valuable input on the Budget Guiding Principles that assisted the City Manager in developing the 2023-2024 Preliminary Budget.

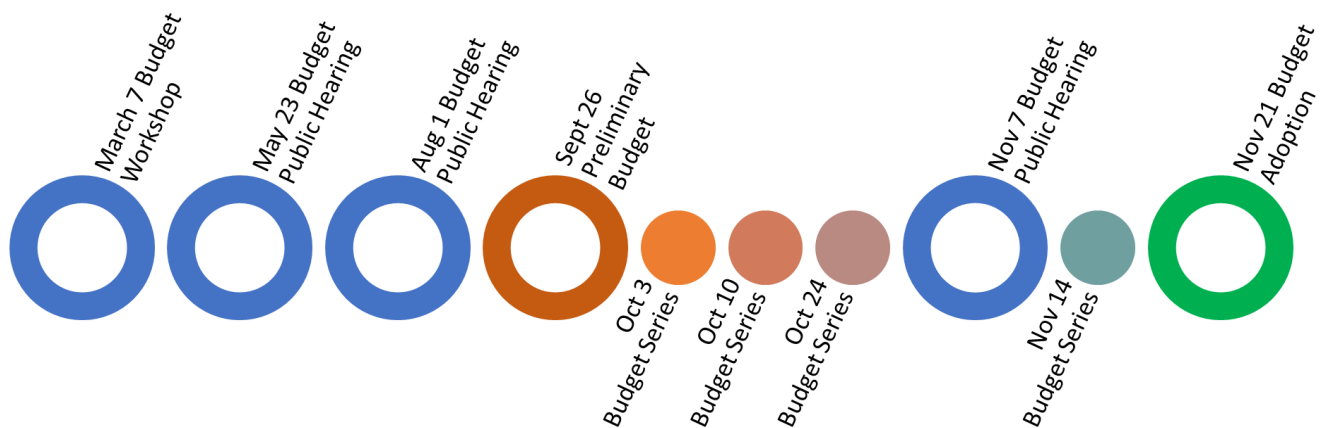
On May 23 and August 1, Council held public hearings that also informed preparation in advance of the City Manager's Preliminary Budget. Thus far, a couple dozen public testimonies (written and verbal) have been received on numerous budgetary issues. The Preliminary Budget document encloses a summary listing of all testimonies.

On September 26, the City Manager and staff provided an overview of the 2023-2024 Preliminary Operating Budget and the 2023-2029 (CIP) Plan. Answers to City Council questions received during the September 26 meeting and all subsequent meetings can be found in Attachment I, "Council Questions and Responses," commonly referred to as the "Memory Bank".

On October 3, City staff presented additional information on the 2023-2024 Preliminary Operating Budget including investments in public safety, homelessness, allocation of American Rescue Plan Act funding, and the implementation of a clean, safe, and vibrant City program. These investments seek to meet the challenges of being a growing and urbanizing city.

The third and final public hearing is scheduled for November 7, which will provide another formal opportunity for the public to offer testimony to the Council regarding the Preliminary Budget. The public is also invited and welcome to submit comments in writing to the City's Budget Manager, Evan Phillips, at EPhillips@BellevueWA.gov or the City Clerk at CityClerk@BellevueWA.gov by 3 p.m. on November 7, 2022. Public feedback is welcome at regular Council meetings during Oral Communications prior to the business agenda. As always, the public may at any time communicate informally to Council by calling, meeting with, or writing to Councilmembers.

Tonight, staff will present the Utilities Department proposed 2023-2024 operating budget and rates as well as the 2023-2029 CIP plan for Council feedback and direction.



The Utilities Department operates as a business enterprise within the City structure. As a business, rates are the primary source of funding for utility functions. Utility revenues do not generally grow without rate increases, and there is limited potential to increase revenues from population or economic growth.

Utilities is a capital-intensive industry. The City of Bellevue owns, operates, and maintains over \$3.5 billion of utility infrastructure assets, with over 1,600 miles of pipeline and numerous reservoirs and pump stations, to provide clean and safe drinking water; safely convey wastewater away from homes and businesses; and safely manage stormwater to protect property and the environment. Most of this infrastructure is past mid-life. As infrastructure ages, it becomes less reliable, and more failures occur. As a result, the cost to maintain, repair, rehabilitate, and replace infrastructure increases.

Council Priorities and Key Council-Adopted Policies Guiding Budget Development

Development of the proposed 2023-2024 Utilities Department operating budget and 2023-2029 CIP was guided by Council priorities and Council-adopted policies:

Council priorities: The Utilities Department proposed operating and capital budgets support Council priorities in the following strategic target areas:

- **Economic Development:** by continuing to provide reliable, high-quality utility services to the

community.

- High Quality Built & Natural Environment: by protecting and renewing utility infrastructure and the natural environment.
- High Performance Government: by keeping a long-term perspective and leveraging innovation and technology to enhance customer service, improve service delivery, and achieve cost efficiencies.
- Achieving Human Potential: by offering rate relief programs, as allowed by state law, to assist low-income residents in paying for utility services.

Council-adopted policies: The Waterworks Utility Financial Policies serve as the foundation for development of the Utilities Department budgets and rates. Adherence to these policies have enabled the Department to be recognized as a leader in the industry, provide competitive utility rates, and achieve financial sustainability. Consistent with Council-adopted policies, the proposed budget is based on:

- Predictable, smooth, and uniform rates
- Full cost of wholesale services
- Full cost of providing utility services now and in the future
- Sufficient operating reserves to protect the solvency of the utility funds
- Investment in capital infrastructure and/or deposit of funds in an infrastructure Renewal and Replacement (R&R) account to ensure current and future customers who use the utility systems pay their equitable share of system costs

Rigorous Budget Review Process

Fiscal stewardship is an essential element of Utilities budget development. The 2023-2024 proposed budget and rates were developed with a lens on delivering reliable and high-quality services to customers, maintaining long-term financial sustainability, responsibly maintaining and replacing aged infrastructure, and ensuring competitive customer rates.

The budget before Council has gone through a rigorous process with multiple layers of review to ensure these objectives are met. This includes budget review and scrutiny by the Utilities Department leadership and the City Manager's Office. Additionally, the proposed budgets and rates have been thoroughly reviewed by the Environmental Services Commission. Utilities is the only department in the City whose operating and capital budgets and rates are reviewed by a board or commission.

Community Engagement

In addition to the CIP online open house, numerous Commission meetings, and the public hearing conducted by the Commission on the proposed Utilities budgets and rates, the Department conducted outreach on the proposed budgets and rates with the Bellevue community. This included a presentation to community members on October 4, and a presentation/discussion with the business community is scheduled for October 12.

Utilities Budget Challenges

The Utilities Department faces the following key challenges in the upcoming biennium:

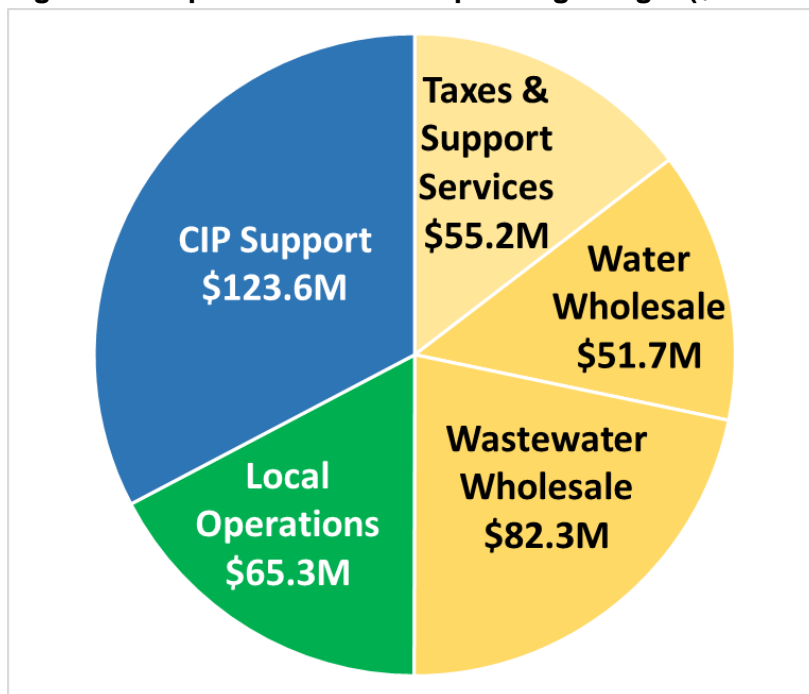
- Increases in wholesale water supply and wastewater treatment costs
- Aging infrastructure and the need to maintain, repair, and adequately fund renewals and replacements in a timely and cost-effective manner to minimize customer impacts, overall costs, and risk of expensive emergency repairs
- Regulatory requirements, and mandated projects and programs
- Extraordinary inflationary conditions affecting both operating and capital costs

With this as context, the proposed 2023-2024 Utilities operating and capital budgets were prepared with high consideration towards rate affordability and capitalizing on opportunities to improve business processes while leverage efficiencies where possible to ensure ratepayer value.

Key Budget Components

The three key cost drivers for the proposed 2023-2024 Utilities operating budget are increases to fund: 1) external costs including wholesale costs for water supply and wastewater treatment, taxes/franchise fees, and interfund payments for City support services; 2) infrastructure funding for current capital investment programs and future infrastructure renewal and replacement needs; and 3) maintaining current service levels and service enhancements for local operations.

Figure 1: Proposed 2023-2024 Operating Budget (\$378.1M)



Excluding reserves

External Drivers

Wholesale Costs

Wholesale costs, the single-largest cost center for the Utilities Department, represent approximately 35 percent of the department's total operating budget, or about \$134 million for the 2023-2024 biennium. These costs include payments to Cascade Water Alliance for water supply and regional capital facility charges, and to King County for wastewater treatment. Cascade's wholesale costs to Bellevue Utilities are projected to increase by 3.3 percent in 2023 and 2.3 percent in 2024. King County's wholesale cost to Bellevue Utilities is projected to increase by 5.75% in both 2023 and 2024. These costs are established by Cascade Water Alliance's Board and King County Council, respectively. Consistent with Council-adopted policies, the proposed budget fully funds wholesale cost increases; thereby, ensuring funding for local operations is not degraded.

Taxes and Internal Service Provider Payments

Taxes and interfund payments represent approximately 15 percent or about \$55 million for the 2023-2024 biennium. The amount of taxes is based on the amount of revenue collected and the tax rates assessed by the State and cities. Interfund payments represent costs Utilities pays to the General Fund for support services.

Local Drivers

Capital Investment Program (CIP) Plan

Locally, the next largest cost driver for the Utilities Department is the CIP and the cost to renew and replace infrastructure, representing approximately 33 percent of the total operating budget for the Utilities Department, or about \$124 million for the 2023-2024 biennium.

The City's utility infrastructure is aging, and increased capital investments are inevitable. The future capital program will focus largely on renewal and replacement of this aging infrastructure. The Utilities Department has a strategic Asset Management Program to prioritize infrastructure replacements at the optimal time to minimize costs and maintain service delivery to the community. The proposed CIP is developed in close coordination with other City departments and agencies to leverage cost efficiencies and minimize disruptions to the community during construction.

Over the 2023-2029 planning period, the City's investment in the proposed Utilities CIP totals \$317.5 million, as follows:

- *Aging infrastructure*: \$262 million, or 83 percent of the proposed CIP, is for investments to address aging infrastructure needs. Examples of projects include water main replacements (\$111.5 million), sewer system trunk rehabilitation (\$26.8 million), sewer pump station improvements (\$23.3 million), and storm system conveyance repairs and replacements (\$19.8 million).
- *Environmental preservation*: \$41 million, or 13 percent of the proposed CIP, is for environmental preservation and flood protection projects. Example projects include the storm system flood control program (\$11.7 million), and Factoria Blvd. stormwater conveyance improvement project (\$7.3 million).
- *Operational efficiencies*: \$11 million, or 3 percent of the proposed CIP, is funding to support operational efficiencies, including building an additional operational facility to maintain service

delivery to the community (\$10.0 million).

- *Capacity for growth*: \$4 million, or 1% of the proposed CIP, is to increase utility system capacity to accommodate growth. Example projects include water storage availability for downtown (\$4.2 million).

Long-range infrastructure renewal and replacement (R&R) planning

The estimated replacement value of Bellevue's water, sewer, and stormwater infrastructure is approximately \$3.5 billion. In 1995, in recognition of the enormity of this future cost, City Council established the infrastructure R&R Account. The purpose of the R&R Account is two-fold:

- 1) Achieve customer equity such that each generation of customers who benefit from the utility systems pays their fair share of the system costs; and
- 2) Create a "savings account" to help smooth peaks in future infrastructure expenditures, producing more stable and consistent rates.

Bellevue Utilities is better prepared than most utilities to meet increasing infrastructure resource requirements due to the Council's foresight to establish the R&R account and the use of long-term infrastructure financial planning to accumulate funds necessary to replace Utilities infrastructure as it ages. This allows Utilities to amortize major pending liabilities over a long-time span, while maintaining current service levels, keep rate increases gradual and uniform, and maintain intergenerational equity.

The water utility is currently in active replacement and thus, does not require as high reserves. Sewer and storm infrastructure, while facing similar challenges, are in very early stages of repair and replacement and will require significant investment in the future. See Attachment B for additional detail on the proposed 2023-2029 Utilities CIP.

Local operations budget

Local operating costs include personnel, supplies, and professional service expenses necessary to carry out the daily operating and maintenance functions of the Utilities Department. This cost category represents approximately 17 percent of the Utilities Department budget, or about \$65 million for the 2023-2024 biennium.

A lean budget is proposed to maintain current service levels and meet regulatory requirements. Fiscal stewardship through operational efficiency and prudent management of utility financial resources is a high priority for Utilities leadership.

See Attachment A for additional detail on the 2023-2024 proposed Utilities operating budget.

Utility Rates

The following table summarizes the rate adjustments in 2023 and 2024 necessary to support the Utility Department's proposed operating and capital budgets, as well as the forecasted annual rate adjustments for the period 2025 to 2028. The projected rates for 2023-2028 were developed using Council-adopted policies as the foundation with the goal of achieving both predictable and gradual rate increases.

Table 1: Proposed and Projected Water Rate Increases 2023-2028

Rate Drivers	2023 Proposed	2024 Proposed	2025 Projected	2026 Projected	2027 Projected	2028 Projected
Cascade	1.7%	1.1%	1.0%	1.5%	1.5%	1.5%
Local	4.2%	3.6%	3.7%	3.7%	3.7%	3.7%
Total	5.9%	4.7%	4.7%	5.2%	5.2%	5.2%

Table 2: Proposed and Projected Sewer Rate Increases 2023-2028

Rate Drivers	2023 Proposed	2024 Proposed	2025 Projected	2026 Projected	2027 Projected	2028 Projected
King County	3.7%	3.6%	3.5%	3.5%	3.5%	5.4%
Local	4.0%	3.2%	3.3%	3.3%	3.3%	3.2%
Total	7.7%	6.8%	6.8%	6.8%	6.8%	8.6%

Table 3: Proposed and Projected Storm Rate Increases 2023-2028

Rate Driver	2023 Proposed	2024 Proposed	2025 Projected	2026 Projected	2027 Projected	2028 Projected
Local	5.3%	5.3%	5.3%	5.3%	5.0%	5.0%
Total	5.3%	5.3%	5.3%	5.3%	5.0%	5.0%

Table 4: Proposed and Projected Combined Water, Sewer, & Storm Rate Increases 2023-2028

Rate Drivers	2023 Proposed	2024 Proposed	2025 Projected	2026 Projected	2027 Projected	2028 Projected
Wholesale	2.4%	2.1%	2.1%	2.3%	2.3%	3.2%
Local	4.3%	3.7%	3.8%	3.8%	3.7%	3.7%
Total	6.7%	5.8%	5.9%	6.1%	6.0%	6.9%

Total Rate Impact to Customer

The total monthly utility bill for the typical single-family residential customer for water, sewer, and stormwater services is \$197.44 in 2022. With the above proposed rate increases, the total monthly bill for the typical single-family resident would increase by 6.7 percent or \$13.18 in 2023 and 5.8 percent or \$12.19 in 2024. The following table summarizes the combined water, sewer, and stormwater utility bill drivers for 2023-2024. Attachment C details the rate drivers for each fund individually and in total.

Table 5: Typical Residential Combined Water, Sewer, & Storm Utility Monthly Bill Rate Drivers

	2023 Bill	2024 Bill
Prior Year Monthly Bill	\$197.44	\$210.62
2023 Rate Drivers		

Wholesale	2.4%	\$4.71	2.1%	\$4.48
Local				
<i>CIP / R&R</i>	<i>2.4%</i>	<i>\$4.82</i>	<i>2.2%</i>	<i>\$4.69</i>
<i>Taxes / Interfunds</i>	<i>1.3%</i>	<i>\$2.58</i>	<i>0.8%</i>	<i>\$1.65</i>
<i>Operations</i>	<i>0.6%</i>	<i>1.07</i>	<i>0.7%</i>	<i>1.37</i>
Local	4.3%	\$8.47	3.7%	\$7.71
Total increase		\$13.18		\$12.19
Typical Monthly Bill	6.7%	\$210.62	5.8%	\$222.81

Bellevue's utility rates are competitive with neighboring jurisdictions. See Attachment D for a bill comparison with neighboring jurisdictions. Given Bellevue's long-range financial policies and proactive infrastructure funding plan, our rates will be even more competitive in the future.

Rate Relief Programs to Serve Low-Income Residents

The City offers two rate relief programs, as allowed by state law, to assist low-income residents in paying for utility services. One program is tailored to meet the needs of low-income seniors and permanently disabled residents and offers a 70 percent bill discount on core utility services. In addition, the Emergency Assistance Program provides temporary bill relief to low-income residents, regardless of age or physical ability, who are experiencing a financial shock. Approximately 1,100 customers are served by these programs.

Environmental Services Commission Recommendation

The Environmental Services Commission (Commission) advises the City Council on water, sewer, stormwater, and solid waste utility programs in the areas of planning, budgeting, ratemaking, CIP financing, and policies. The Commission is comprised of seven members, appointed by the Mayor with the concurrence of Council, who reside within the Bellevue Utilities Department's service area. In this role, the Commission embodies the interests of utility ratepayers throughout the service area, including Bellevue, Beaux Arts, Clyde Hill, Hunts Points, Medina, Yarrow Point, and sections of the City of Kirkland.

The Utilities Department proposed budget has been reviewed in detail by the Commission over nine meetings. Additionally, the Commission received public input on the proposed Utilities CIP through an online open house. The Commission also held a public hearing on the proposed operating and capital budgets and rates on September 1. The Commission's budget review culminates in a budget and rates recommendation to the City Council.

The Commission unanimously recommends the proposed budgets and rates, and the letter of support is provided in Attachment E. The Commission Chair will be present at the October 10 Council meeting to present the Commission's recommendation.

Future Policy Considerations

The Commission also deliberated on the following policy issues:

1. Monthly billing, and
2. Recovery of credit card costs.

Staff will bring these items to Council for consideration early next year.

Council Budget Calendar

Date	Budget Item(s)
March 7	Council Budget Workshop
May 23	Initial Public Hearing
August 1	Second Public Hearing
September 26	2023-2024 Preliminary Operating Budget & 2023-29 Capital Investment Program (CIP) Plan Overview
October 3	Overview of investments in: Public Safety, Homelessness, the American Recovery Plan Act (ARPA) and, Safe Clean, Vibrant City
Tonight	Utility Rates Overview and Other Areas of Interest as Requested
October 24	Development Services Rates Overview, Human Services Commission Recommendations, Community Development Block Grants (CDBG), the Environmental Stewardship Initiative (ESI) and Equity, Diversity and Access
November 7	Final Public Hearing
November 14	Tentative Council Direction for Adoption
November 21	Tentative Budget Adoption

Preliminary Budget Council Required Actions

There are several items that will be required to adopt the 2023-2024 Operating Budget and the 2023-2029 CIP Plan which include:

Ordinance/Resolution Title	Brief Explanation
Human Services Commission Recommendation Ordinance	Adopt funding recommendations for allocations to human services agencies
Community Development Block Grant (CDBG) Recommendation Ordinance	Adopted recommended spending plan for Community Development Block Grant funds
2023 Development Services Fee Ordinance	Set Development Services 2023 Rates
2023-2024 Utility Rates Ordinances (3)	Set the Utilities 2023-2024 Rates
2023 Property Tax Banked Capacity Resolution	Preserve the full levy amount available to the City
2023 Property Tax Ordinance	Adopt 2023 property tax levies (RCW 35A.34.230 and RCW 84.55.092)
Business & Occupation Tax Ordinance	Adjust the taxable gross receipts rate
2023-2024 Budget Ordinance	Adopt "umbrella" budget ordinance which includes appropriation approval by fund, 2023 pay plans and, summarizations of grants and donations accepted that are less than \$90,000

Note: The fire inspection fee ordinance is not needed this year as there is no change. Additionally, a substantial need ordinance is not needed for property taxes as the implicit price deflator surpasses 1 percent.

POLICY & FISCAL IMPACTS

Policy Impact

In accordance with Council-adopted financial policies, utility rate increases are needed to maintain, operate, and invest in utility infrastructure to ensure reliable service delivery to water, sewer, and stormwater customers.

Chapter 35A.34 RCW – Biennial Budgets: State law specifies requirements that must be followed in budgeting each of the City’s funds. Key areas covered include:

- Preparation and filing of a preliminary budget by the Chief Administrative Officer, i.e., City Manager;
- A “budget message” from the Chief Administrative Officer explaining the content, financial policies, and major proposed changes;
- A public hearing on the proposed preliminary budget conducted before adoption of a final budget, which shall be held on or before the first Monday in December;
- Balanced expenditure and revenue estimates for each of the City’s funds; and
- Council adoption of the budget prior to beginning of the ensuing fiscal biennium, i.e., January 1, 2023.

Fiscal Impact

The 2023-2024 Utilities operating budget, totaling \$378.1 million, represents the financial resources necessary to implement the strategies and policies the Utilities Department uses to address key business challenges. The Utilities CIP budget, totaling \$317.5 million, represents investments in capital infrastructure in the next seven years critical to ensuring the integrity of the water, sewer, and storm utility system infrastructure in order to maintain current levels of service delivery to the community.

OPTIONS

N/A

ATTACHMENTS

- A. Utilities Proposed 2023-2024 Operating Budget
- B. Utilities Proposed 2023-2029 CIP Budget
- C. Utilities Proposed 2023-2024 Typical Residential Monthly Bill by Rate Drivers
- D. Utility Bill Comparison
- E. ESC 2023-2024 Budget and Rates Recommendation to Council
- F. City Manager’s Transmittal Letter
- G. 2023-2024 Preliminary Budget Executive Summary
- H. 2023-2024 Fund Appropriation List
- I. Council Questions and Responses (Memory Bank)

AVAILABLE IN COUNCIL LIBRARY

N/A