

CITY COUNCIL STUDY SESSION

Budget Update - Utilities Department Proposed 2021-2022 Operating Budget and Rates, and 2021-2027 Capital Investment Program Plan.

Nav Ota, Director, 452-2041

Lucy Liu, Assistant Director, 452-4445

Utilities Department

Toni Call, Director, 452-7863

Keyi Lu, Assistant Director, 452-4190

Finance and Asset Management Department

DIRECTION NEEDED FROM COUNCIL

DIRECTION

This is the fourth presentation regarding the 2021/2022 Preliminary Budget. Tonight, staff seek feedback regarding the Utilities Department proposed 2021-2022 operating budget and rates, and 2021-2027 capital investment program (CIP) plan and direction to prepare Utilities Rates Ordinances for final adoption. Final adoption will take place as part of the adoption of the City's budget in December.

RECOMMENDATION

Move to direct staff to prepare Utilities Rates Ordinances for adoption as part of the budget adoption package, tentatively scheduled for December 7.

BACKGROUND & ANALYSIS

Background

The City Manager transmitted his Preliminary 2021-2022 Operating Budget and the 2021-2027 Capital Investment Program (CIP) Plan on October 19. This is the fourth in a series of several discussions to review the budget prior to tentative budget adoption on December 7. A tracking of Council requests and responses can be found in Attachment H.

The 2021-2022 biennial budget totals \$1.7 billion. This total includes \$1.1 billion in operating budget (\$474 million in general fund, \$212 million in internal service and other operating funds, \$457 million in Enterprise Funds), \$74 million in special purpose expenditures (such as grants, donations and debt, among others), and \$523 million for the 2021-2022 portion of the General and Utilities CIP.


The impacts of COVID-19 are substantial and will last well into the 2021-2022 biennium. The general fund that supports the majority of the City operations, was required to reduce costs or increase revenues by \$32 million over the two years (\$16 million annually). The preliminary budget includes strategies of cost containment, one-time bridge structures, and revenue adjustments to address this gap.

Further information regarding the overall preliminary budget can be found in the Executive Summary located at https://bellevuewa.gov/sites/default/files/media/pdf_document/2020/2021-2022%20Preliminary%20Budget%20Executive%20Summary.pdf

Tonight, staff will present the Utilities Department proposed 2021-2022 operating budget and rates, and 2021-2027 CIP plan for Council feedback and direction.

There may be other areas that Council also wishes to explore.

Overall Council Process and Previous Meetings



Jun. 22	Budget Workshop
Jul. 27	Initial Public Hearing
Sep. 21	Second Public Hearing
Oct. 19	City Manager's Preliminary Budget
Oct. 26	Development Services, upcoming process
Nov. 2	Human Services; Follow up on Council Question re: Sales Tax Allocation
Tonight	Utility Rates, Council Interests
Nov. 16	Fire Inspection, Council Interests
Nov. 23	Public Hearing, Council Direction for Adoption
Dec. 7	Tentative Budget Adoption

Council held a budget workshop on June 22 where staff briefed Council on the process and milestones of developing the budget and provided scenarios regarding the impact of COVID-19-related events in the near term (2021-2022), over the general fund forecast six-year period (2021-2026), and seven-year (2021-2027) CIP. Council provided feedback in order to assist the City Manager in developing his preliminary budget. The packet information is available here:

<https://bellevue.legistar.com/LegislationDetail.aspx?ID=4576307&GUID=73EC1B4A-FA96-48A3-B417-399955664CEA>.

Council held public hearings on July 27 and September 21. Thus far, Council has received 58 public comments (oral and written submissions) on numerous issues. The preliminary budget document provides a summary listing of all public comments.

On October 19, the City Manager presented his \$1.7 billion 2021-2022 Preliminary Budget and 2021-2027 CIP plan to the City Council, including a \$16 million reduction to the general fund in 2021. The packet information is available here:

<https://bellevue.legistar.com/LegislationDetail.aspx?ID=4671513&GUID=129403E5-D01A-46BA-9167-6713969122E3>.

On October 26, staff provided a presentation on proposed amendments to development permit fees and rates and to the Issaquah and Renton school impact fee schedule for Council consideration and adoption. Council directed staff to prepare Ordinances that amend 2021 permit fees and rates and school impact fees as presented for adoption on December 7 as part of the budget adoption package. The packet information is available here:

<https://bellevue.legistar.com/LegislationDetail.aspx?ID=4675780&GUID=1C1DE5F3-4E72-4CD7-A094-2FC94CCB88C6>

On November 2, staff provided an update on the Human Services Commission's recommendations for 2021-2022 Human Services funding and 2021 Community Development Block grants. Council directed staff to prepare ordinances approving the Human Services Commission's recommendations for 2021-2022 Human Services funding and 2021 Community Development Block Grant funds for adoption as part of the budget adoption package. Staff also provided a Capital Investment Program (CIP) update to address the policy question of the sales tax allocation between CIP and the general fund and summarized overlapping areas addressed in the "memory bank." The packet information is available here:

<https://bellevue.legistar.com/LegislationDetail.aspx?ID=4681143&GUID=37D2945F-58F6-4BDF-A252-D502086E77C6>

The third and final public hearing is scheduled for November 23. Those wishing to provide testimony to the Council regarding the budget at the public hearing may sign up to speak during that evening's Regular Session, or submit comments in writing to the City's Budget Manager (ephillips@bellevuewa.gov) or City Clerk (cityclerk@bellevuewa.gov) by 3 p.m. on November 23. Feedback is also welcome at other meetings during Oral Communications.

Preliminary Budget Council Required Actions

There are several items that will be required to adopt the 2021-2022 budget:

Ordinance Title	Brief Explanation
2021-2022 Human Services Funding Ordinance:	Adopt Human Services Commission's funding recommendations for allocations to human services agencies
2021-2022 Fire Inspection Fee Ordinance:	Adopt Fire Inspection Fee schedule
Basic Life Support Transport Fee Ordinance:	Adopt BLS transport Fee increase
2021 Community Development Block Grant (CDBG) Ordinance:	Adopt Human Services Commission's recommendations for use of 2021 CDBG funds
2021 Development Services Fee Ordinance:	Set Development Services' 2021 rates
2021-2022 Utilities Rates Ordinances:	Set the 2021-2022 Utility Rates

2021 Property Tax Banked Capacity Resolution:	Preserve the full levy amount available to the City
2021 Substantial Need Ordinance:	To allow property tax increase or to bank the capacity of the 1 percent maximum as allowed by statute (RCW 84.55.0101)
2021 Property Tax Levy Ordinance:	Adopt 2021 property tax levies (RCW 35A.34.230 and RCW 84.55.092)
2021-2022 Budget Ordinance:	Adopt “umbrella” budget ordinance which includes appropriation approval by Fund, 2021 pay plans, and summarizations of grants and donations accepted that are less than \$90,000

Utilities Department Background

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 storm and surface water 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 operate, maintain, rehabilitate, and replace infrastructure increases.

COVID-19 Efforts

The COVID-19 pandemic has highlighted the importance of utility services. Because water is critical to public health, the Utilities Department implemented efforts at the onset of COVID-19 to ensure City customers continue to have access to utility services during the pandemic. These include implementing a moratorium on water shutoffs for non-payment, suspending late payment fees, and providing payment plans and bill assistance programs for customers in financial need.

Additionally, efforts were implemented to address the impacts of COVID-19 on the Department. Measures were taken to protect staff so they can continue to safely serve the community. In anticipation of revenue impacts, the Utilities Department took immediate action to control costs to avoid potential customer rate impacts.

Rigorous Budget Review Process

Fiscal stewardship is an essential element of Utilities' budget development. The 2021-2022 proposed budget and rates were developed with an eye towards delivering reliable, high-quality services to

customers, maintaining long-term financial sustainability, responsibly maintaining and replacing aged infrastructure assets, and ensuring competitive rates for the ratepayer.

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 that has its operating and capital budgets reviewed by a board or commission.

Environmental Services Commission Recommendation

The Environmental Services Commission (Commission) advises the City Council on water, wastewater, storm and surface water, 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 members represent 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 eight 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 October 7. The Commission's budget review culminates in a budget and rates recommendations to the City Council.

The Commission unanimously recommends the proposed budgets and rates. The Commission's letter of support is provided as Attachment C. The Commission Chair will be present at the November 9 Council meeting to present the Commission's recommendation.

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 several outreach efforts on the proposed budgets and rates with the Bellevue community. This included presentations and discussions with neighborhood leaders in October and Bellevue Essentials participants in early November.

Council Strategic Direction and Key Council-Adopted Policies Guiding Budget Development

Development of the proposed 2021-2022 Utilities Department operating budget and 2021-2027 CIP was guided by Council strategic direction and Council-adopted policies:

Council strategic direction: Utilities' proposed operating and capital budgets support Council strategic direction by:

- Supporting the City's economic development.
- Protecting and renewing utility infrastructure and natural resources, as part of the City's high quality built and natural environment.

- Continuing to be a high performing organization 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-approved policies: The Waterworks Utility Financial Policies serve as the foundation for development of the Utilities Department budgets 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 Council-adopted policies, the proposed budget is based on:

- The 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 R&R account to ensure that current and future customers that use the utility systems pay their equitable share of system costs.
- Predictable, smooth and uniform rates.

Utilities Budget Challenges

COVID-19 is anticipated to impact utility revenues in 2021-2022. Recognizing that COVID-19 is a dynamic situation, the Utilities Department's goal is to address these impacts by containing costs that are within its control and using available reserves. To mitigate customer impacts, the Department is not proposing rate increases for local operations and has lowered planned contributions to the capital facilities renewal and replacement (R&R) account in the 2021-2022 biennium.

In addition to the financial impacts of COVID-19, the Utilities Department faces the following ongoing challenges which serve as the backdrop for the Department's budget formulation:

- Increase in wholesale water supply and wastewater treatment costs;
- Aging infrastructure;
- Utility infrastructure capacity needed to accommodate population growth and support economic development; and
- Regulatory requirements, and mandated projects and programs.

With this as context, the proposed Utilities operating and capital budgets were prepared with a watchful eye towards competitive rates, now and into the future, and to capitalize on opportunities to improve business processes and leverage efficiencies where possible to ensure value to the ratepayer.

Key Budget Components

The two key cost drivers for the proposed 2021-2022 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; and 2) infrastructure funding for current capital investment programs and future infrastructure renewal and replacement needs. Due to cost containment, local operations is not a cost driver in the 2021-2022 biennium.

Wholesale Costs

The single largest cost center for the Utilities Department is wholesale costs. These include payments to the Cascade Water Alliance for the cost of purchasing water supply and regional capital facility charges and payments to King County for wastewater treatment. Consistent with Council-adopted policies, the proposed budget fully funds wholesale cost increases, thereby ensuring funding for local operations are not degraded. Wholesale costs represent approximately 38 percent of the total operating budget for the Utilities Department, or \$123.2 million for the 2021-2022 biennium.

Local Costs

Capital Investment Program (CIP) Plan

Aside from wholesale costs, the next largest cost driver for the Utilities Department is the CIP and the cost to renew and replace infrastructure, representing approximately 30 percent of the total operating budget for the Utilities Department, or \$95.1 million for the 2021-2022 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. Over the 2021-2027 planning period, the City's investment in the proposed Utilities CIP totals \$235.6 million. 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.

The following table provides a summary of the projected CIP expenditures by year and driver for the seven-year CIP period. See Attachment B for additional detail on the proposed 2021-2027 Utilities CIP.

Table 1: 2021-2027 CIP Expenditures by Driver (\$000's)

	2021	2022	2023	2024	2025	2026	2027	Total
Aging Infrastructure	\$30,920	\$26,010	\$24,590	\$26,160	\$25,740	\$28,320	\$31,160	\$192,900
Environmental Preservation	\$10,370	\$8,620	\$2,860	\$870	\$1,300	\$1,760	\$1,870	\$27,650
Capacity for Growth	\$1,150	\$210	--	\$1,600	\$1,250	\$1,170	\$1,620	\$7,000
Maintain Service Delivery	--	--	\$4,000	\$4,000	--	--	--	\$8,000
Total – Utility CIP	\$42,440	\$34,840	\$31,450	\$32,630	\$28,290	\$31,250	\$34,650	\$235,550

The proposed Utilities 2021-2027 CIP includes the following investments:

- **Aging infrastructure:** \$192.9 million, or 82 percent of the proposed CIP, is for investments to address aging infrastructure needs. Examples of projects include small diameter water main replacements (\$81.3 million), water reservoir rehabilitation (\$23.4 million), sewer system pipeline major repairs (\$25.7 million), sewer pump station improvements (\$15.3 million), sewer pipeline replacements (\$5.7 million), and storm system conveyance repairs and replacements (\$13.1 million).

- **Environmental preservation:** \$27.7 million, or 12 percent of the proposed CIP, is for environmental preservation and flood protection projects. Example projects include the storm system flood control program (\$9.5 million), and Factoria Blvd. stormwater conveyance improvement project (\$9.3 million).
- **Capacity for growth:** \$7.0 million, or three percent of the proposed CIP, is to increase utility system capacity to accommodate growth. Example projects include water storage availability for downtown (\$4.1 million), and new water facilities for the NE Spring Blvd. Corridor (\$2.9 million).
- **Maintain service delivery:** \$8.0 million, or three percent of the proposed CIP, is funding to build an additional operational yard to maintain service delivery to the community.

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 Utilities Capital Facilities Renewal & Replacement (R&R) Account. The purpose of the R&R Account is two-fold: 1) achieve customer equity where each generation of customers that use the utility systems pay their fair share of system costs, and 2) create a "savings account" to help smooth peaks in future infrastructure expenditures.

The long-range infrastructure funding plan is premised on building rate capacity to provide sustainable investment in capital infrastructure. This rate capacity is the main source for Utilities capital funding needs. The R&R Account balance serves as a supplemental source of capital funding when needed.

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 longer 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.

Table 2: R&R Account Ending Fund Balance (\$000's)

	2021	2022	2023	2024	2025	2026	2027
Water	\$ 29,480	\$ 31,164	\$ 35,843	\$ 38,722	\$ 46,538	\$ 52,968	\$ 56,972
Sewer	\$ 95,847	\$106,637	\$115,815	\$126,256	\$139,493	\$155,323	\$173,165
Storm	\$ 70,079	\$ 75,927	\$ 87,103	\$101,242	\$115,706	\$130,051	\$145,768
Total	\$195,406	\$213,728	\$238,761	\$266,220	\$301,737	\$338,342	\$375,905

Lean Operating 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 17 percent of the Utilities Department budget, or \$54.1 million for the 2021-2022 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. As a result of cost containment efforts, no rate increases are proposed in this biennium to support local operations of the water, sewer, and storm and surface water utilities.

Staffing changes are proposed to meet business needs. One new staff person is proposed to implement a Source Control program as mandated by the National Pollutant Discharge Elimination System (NPDES) permit. Additionally, staffing reductions are proposed due to advanced metering infrastructure (AMI) implementation. Nine LTEs were previously added to support AMI implementation. Five of the LTEs will be eliminated in this biennium and four will be eliminated in 2023 when the project is completed. In addition to LTEs, two meter reader FTE positions will be eliminated in this biennium. The following table summarizes the staffing changes included in the proposed 2021-2022 operating budget.

Table 3: Proposed Staffing Changes

	FTEs	LTEs
Senior Engineering Technician (NPDES)	1.00	--
AMI Implementation	(2.0)	(5.0)
Total Change	(1.00)	(5.0)

Taxes and Internal Service Provider Payments

Taxes and interfund payments represent approximately 15 percent or \$49.4 million for the 2021-2022 biennium. The amount of taxes is based on the amount of revenue collected and the tax rates assess by the State and cities. No changes to the State and city tax rates are assumed in the proposed budget except for an increase to the State business and occupation tax rate. Interfund payments represent costs that Utilities pays to the General Fund for support services.

See Attachment A for additional detail on the 2021-2022 proposed Utilities operating budget.

Utility Rates

The following table summarizes the rate adjustments in 2021 and 2022 that are necessary to support the Utility Department's proposed operating and capital budgets, as well as forecasted annual rate adjustments for the period 2023 to 2026. The projected rates for 2021-2026 were developed using Council's policies as the foundation with the goal of achieving both predictable and gradual rate increases.

Table 4: Proposed and Projected Utility Rate Increases 2021-2026

	Water Utility	Sewer Utility	Storm Utility	Combined Utility
2021 Proposed	3.5%	4.1%	3.5%	3.8%
2022 Proposed	3.5%	4.5%	3.3%	3.9%
<i>2023 Projected</i>	<i>4.3%</i>	<i>7.6%</i>	<i>4.3%</i>	<i>5.9%</i>

<i>2024 Projected</i>	<i>4.3%</i>	<i>2.3%</i>	<i>4.5%</i>	<i>3.4%</i>
<i>2025 Projected</i>	<i>4.5%</i>	<i>7.8%</i>	<i>4.5%</i>	<i>6.1%</i>
<i>2026 Projected</i>	<i>5.1%</i>	<i>2.9%</i>	<i>5.2%</i>	<i>4.1%</i>

Total Rate Impact to Customer

The total monthly utility bill for the typical single-family residential customer for water, sewer, and storm and surface water services is \$183.05 in 2020. With the above proposed rate increases, the total monthly bill for the typical single-family resident would increase by 3.8 percent or \$6.91 in 2021 and 3.9 percent or \$7.48 in 2022. The following table summarizes the combined water, sewer, storm and surface water utility bill drivers for 2021-2022.

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

	2020 Bill		2021 Bill	
Prior Year Monthly Bill	\$183.05		\$189.96	
Wholesale Costs	2.2%	\$ 3.93	1.8%	\$ 3.32
Local				
CIP/R&R	0.6%	\$ 1.07	1.7%	\$ 3.50
Taxes/Interfunds	1.0%	\$ 1.91	0.4%	\$ 0.66
Operations	0.0%	\$ -	0.0%	\$ -
Total Local	1.6%	\$ 2.98	2.1%	\$ 4.16
Total Increase	3.8%	\$ 6.91	3.9%	\$ 7.48
New Monthly Bill		\$189.96		\$197.44

Even with these rate increases, 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, the City's rates will be even more competitive in the future.

Rate Relief Programs to Serve Low-Income Residents

The City offers three financial relief programs, as allowed by state law, to assist low-income residents in paying for utility services. Approximately 1,100 households are served by these programs. 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. The City also offers a rebate of a portion of utility taxes paid to the City to all qualified low-income residents.

In addition, the City introduced a new Emergency Assistance Program in 2019 which provides temporary bill relief to low-income residents, regardless of age or physical ability, who are experiencing a financial shock, such as from COVID-19.

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 storm and surface water 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 the beginning of the ensuing fiscal biennium, i.e., January 1, 2021.

Fiscal Impact

The 2021-2022 Utilities operating budget represents the financial resources necessary to implement the strategies and policies the Utilities Department uses to address key business challenges. The Utilities CIP budget represents investments in capital infrastructure in the next seven years that are 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

1. Direct staff to prepare Utilities Rates ordinances for adoption as part of the budget adoption package, tentatively scheduled for December 7.
2. Provide alternative direction to staff.

ATTACHMENTS & AVAILABLE DOCUMENTS

- A. Utilities Proposed 2021-2022 Operating Budget
- B. Utilities Proposed 2021-2027 CIP Budget
- C. Environmental Services Commission 2021-2022 Budget and Rates Recommendation to Council
- D. Utility Bill Comparison
- E. City Manager’s Transmittal Letter
- F. 2021-2022 Preliminary Budget Executive Summary
- G. 2021-2022 Fund Appropriation List
- H. Council Questions and Responses (Memory Bank)

AVAILABLE IN COUNCIL LIBRARY

N/A