EID 2011 – 2012 Operating Budget

The El Dorado Irrigation District Board of Directors adopted the District's current operating budget during the December 13, 2010, regularly scheduled Board meeting.

Estimated revenues and expenses and other relevant information pertaining to the budget are contained in the following Agenda Item Summary that was prepared for the December 13 meeting.

EL DORADO IRRIGATION DISTRICT

Agenda Item Summary

	Approvals (initial):
Board Meeting Date: December 13, 2010	**Preparer** _______
Date Prepared: November 29, 2010	**Division Head** _______
Prepared by: Mark Price, Tony Pasquarello	**Department Head** _______
Agenda Title: Operating Budget	**Finance Manager** _______
Subject: 2011-2012 Operating Budget Adoption	**General Manager** _______

ACTION ITEM NO._____
December 13, 2010

EL DORADO IRRIGATION DISTRICT

Subject: 2011-2012 Operating Budget Adoption

Previous Board Action:

March 20, 2000: The Board adopted a multi-year operating budget process.

December 15, 2008: The Board adopted the 2009-2010 operating budget.

November 23, 2009: The Board adopted the 2010 operating budget.

February 8, 2010: The Board adopted the revised 2010 operating budget.

Board Policies/Administrative Regulations:

BP 3010: It is the responsibility of the General Manager to inform the Board about financial operations of the District so the Board can make informed decisions and fully discharge its legal responsibilities in a fiscally sound manner. The Board shall adopt a two-year operating budget and may modify it prior to the end of the year.

AR 3011: It is the responsibility of the General Manager to develop the budget based on the priorities and needs of the District and its customers. The budget and any budget modification shall:

1. include, but not be limited to, operating expenses, debt, construction, and reserve funds;
2. meet all legal requirements;
3. support the District's mission;
4. maintain prudent levels of reserves in water, wastewater, hydroelectric, and recreation to fund contingencies that meet the District's debt service requirements;
5. allow the District to meets its financial obligations, including bond covenants;
6. be consistent with a financial plan that guides the District in satisfying its multi-year commitments; and
7. encourage public participation through required disclosures and public hearings.

Responsibility for overseeing the budget development process is assigned to the Director of Finance. Once the annual budget is prepared, the Board shall act on it.

Summary of Issues:

January 1, 2011 marks the beginning of the District's two-year operating budget cycle. This cycle is very different from the last two-year budget adopted in 2008. Now, the environment is one of a stagnant economy and the full impacts are in place from the significant actions the Board took over the past 18 months to reduce the District's workforce, decrease employee benefit costs, hold the line on wages, increase the power generation and rate revenues, and provide short-term debt relief to ease the impact to the District' ratepayers.

To review, on November 23, 2009, the Board adopted a revised 2010 budget that included proposed increases in water, wastewater, and recycled water rates. Concurrent with the budget adoption, the Board directed staff to issue a Proposition 218 notice for the proposed rate increases cited above. The notice was mailed December 16 and 17, 2009.

Staff's rate proposal was then modified as a result of community workshops and the Proposition 218 public hearing and protest procedure. An ongoing initiative to increase power generation revenues reached sufficient certainty to revise the projected revenues in the budget. The proposed contract negotiated with PG&E was presented to the California Public Utilities Commission and approved at its November 19, 2010 meeting.

Staff identified a means of restructuring the District's existing debt earlier this year to reduce the debt burden by approximately $4 million in each of the fiscal years 2010, 2011, and 2012. Staff proposed substantial additional cuts and deferrals to the District's 2010-2014 Capital Improvement Program (CIP), to delay and reduce the need for additional future borrowing which was adopted with the 2011-2015 CIP plan at the November 8, 2010 Board meeting. Finally, staff believed that the then 2010 projection of $3 million in Facility Capacity Charge (FCC) revenues should be reduced to $1.5 million.

Staff also worked to identify and implement – with Association concurrence where required – additional reductions to operating expenses, including reduced PERS contributions by the District on behalf of the employees during 2010 and 2011, an across-the-board wage freeze in 2011, additional retirements of eligible employees and layoff of some employees which reduced staff by another 14 positions.

With the changes to the originally proposed 2010 budget via these initiatives, staff was able to develop a revised "Plan B" proposal for rate increases, consisting of an 18% increase in 2010, 15% in 2011, and 5% in 2012, plus two additional annual increases of 5% to be authorized but not implemented without further public Board action. The Board held its public hearing on the proposed rate increases on February 4, 2010 and adopted the revised staff-proposed rates.

Turning to the forthcoming budget, at the November 8, 2010 Board meeting, District staff discussed with Board members in a workshop format the necessity of an extremely tight operating budget for 2011-2012. Included in those discussions were the financial challenges the District faces due to the current financial market situation, the District's cash-flow status, and overall economic conditions.

For the 2011 budget year staff was asked to develop a budget which was less than or equal to that finally adopted for 2010. The challenge staff encountered was absorbing wage increases earned in 2010 as a result of the annual employee review process, and the increase in financial guarantee costs for the District's variable-rate debt. The proposed 2011 budget shows only a $137,000 increase, or 0.3% over the $42,643,000 operating budget adopted for 2010, and a staffing level of 227 positions - down from 304 in late 2008.

Staff Analysis/Evaluation:

In anticipation of each two-year budget cycle and mid-cycle review, staff prepares projected operating revenues and expenses for Board consideration. The Finance Department estimates revenues based on relevant economic factors such as interest rates, investments, and market trends. At the beginning of the budget review, Finance staff also provides department heads and division managers with actual operating costs for the past two years through the most recent month of the current year, along with projections to the current year's end. Based on past and current expenditures, operational commitments for the coming year, and workload indicators, staff develops proposed budgets for the upcoming year.

Analysis of revenue projections for fiscal years 2010, 2011 and 2012:

Table 1 compares the revenue projections for 2010, 2011, and 2012.

The revised revenue projections for 2010 are significantly lower than those adopted for 2010, primarily because of the lower anticipated amount of income projected from water rate revenues. There were a few contributing factors to the lowered rate revenue which included:

- significant late spring rains
- a milder summer compared to prior years
- the adoption in early 2009 of a revised rate structure shifting from a 55% fixed charge 45% variable charge for consumption to a 30% fixed/70% variable
- the adoption of the 18% rate increase

The revenue projections for 2011 assume water consumption recovers some due to more "normal" weather conditions in 2011.

The projections are outlined in Table 1, which reflects the revised lower 2010 income and increases for 2011 and 2012 related to the approved rate increases.

Table 1: Revenue Projections for 2010, 2011, and 2012 (in millions of dollars)

	2010 Adopted Budget	**2010 Revised Projections**	**2011 Revised Budget**	**2012 Proposed Budget**
Water sales and services[2]	$ 23.073	$ 17.800	$ 21.800	$ 22.577
Wastewater sales and services[2]	18.641	16.913	19.661	20.362
Recycled water sales	1.052	0.647	0.756	0.781
Hydropower sales	6.000	7.500	8.000	8.000
Wholesale contract-Placerville			0.423	0.432
Investment income	1.200	0.885	0.902	0.850
FCCs [1]	1.500	0.444	2.000	3.000
Debt surcharges	2.291	1.940	1.979	1.979
Property tax	10.429	10.400	10.400	10.452
IPP and cross connection			0.425	0.425
Other income	1.100	1.550	1.580	1.582
Recreation	1.040	1.000	1.050	1.039
FEMA reimbursement	0.000	0.162	0.170	0.250
Total revenues	**$ 66.326**	**$ 59.241**	**$ 69.146**	**$71.729**

(1) 2010 revised projections for FCCs reflect the current trend of FCC sales. Projections for 2011 and 2012 reflect the anticipated slow recovery in construction.
(2) 2011 and 2012 projections include the 15% and 5% rate increases previously adopted.

Analysis of 2010, 2011, and 2012 budget and expense projections:

Table 2 compares the adopted 2010 Board-adjusted budget and 2010 year-end expense projections to the 2011-2012 proposed budgets by departments. As illustrated in Table 2, the proposed 2011 operating budget is expected to be almost identical to the 2010 adopted budget with the increase tied to the expected increase in cost of the letter of credit fee currently being negotiated. The 2012 proposed budget represents roughly a 3% inflation adjustment to the 2011's proposed budget.

Table 3 identifies expenses by type. Reflected in salaries and benefits is a projected further savings of $0.75 million in 2011 due to the April 2010 staff downsizing by which the reorganization eliminated fourteen positions, including the department head for the former Natural Resources department and the elimination of four positions in our state-certified laboratory whose services were contracted out to a private firm. The District's current staff of 227 employees represents a 14.5% decrease since January 1, 2009 and a 34.8% decrease from January 1, 2008.

Table 2: 2010 Adopted Operating Budget Expenses vs. 2011-2012 Proposed Budgets by Department (in millions of dollars)

Departments	**2010 Adopted Budget**	**2010 Projected Expenditures**	**2011 Revised Budget**	**2012 Proposed Budget (3.0% inflation)**
Office of the General Manager	$ 3.143	$ 2.674	$ 3.199	$ 3.295
Communications	0.558	0.500	0.569	0.586
Finance	5.894	5.391	6.728	6.930
Human Resources	2.482	2.152	2.272	2.340
Information Technology	2.659	2.467	2.538	2.613
Engineering	3.896	3.887	4.416	4.549
Drinking Water Operations	10.036	7.877	10.536	10.853
Wastewater Operations	9.162	9.233	8.893	9.160
Recycled Water Operations	0.327	0.408	0.449	0.462
Hydroelectric	3.359	3.138	3.652	3.762
Natural Resources (1)	2.299	2.116	-	-
Recreation	1.064	1.058	1.073	1.105
Grants	(0.345)	(0.218)	(0.171)	(0.176)
CIP labor offset	(2.462)	(2.309)	(2.547)	(2.623)
Developer reimbursement offset	(0.176)	-	(0.155)	(0.160)
Other post-employment benefits	-	-	-	-
Letter of credit fee	0.747	0.747	1.328	1.328
Total	**$ 42.643**	**$ 39.121**	**$ 42.780**	**$ 44.024**

Note: The above departmental structure reflects the April 2010 reorganization, which has been fully implemented.

(1) Reassignments of this department's functions are reflected in the proposed Engineering, Finance, Operations and Office of the General Manager budgets for 2011 and 2012.

Table 3: 2010 Adopted Operating Budget Expenses vs. 2011-2012 Proposed Budgets by Expense Type (in millions of dollars)

	2010 Adopted Budget	2010 Projected Expenditures	2011 Revised Budget	2012 Proposed Budget
Salaries	$ 17.869	$ 17.334	$ 17.296	$ 17.815
Benefits	10.103	9.419	9.912	10.209
Materials and Services	16.907	14.148	17.117	17.631
Grants	(0.345)	(0.218)	(0.171)	-
CIP and Devel. Reim. Labor Offsets	(2.638)	(2.309)	(2.702)	(2.959)
Other post-employment benefits	-	-	-	-
Letter of credit fee	0.747	0.747	1.328	1.328
Total	**$ 42.643**	**$ 39.121**	**$ 42.780**	**$ 44.024**

The proposed 2011 expenses are currently projected to be slightly higher than the 2010 adopted budget which is primarily driven by an anticipated increase in the letter of credit guarantee fee and offset by a reduction in total salaries and benefits.

The proposed 2011 expenses are currently projected to be roughly $3.6 million higher than the 2010 projected year-end expenditures. The 2011 budget increase is driven by the before-mentioned letter of credit guarantee fee plus Materials and Services expenditures. The contributing factors to the Materials and Services variance include:

- Electricity expense ($900k). Increased budget due to the El Dorado Hills Water Treatment Plant being powered off in January through March 2010 for construction and maintenance.
- Consulting and Contractual Services ($800k). Increased budget due to contractual services related to water efficiency per Prop 50, USBR, and CalFed grants. Additional increases due to IMS, Engineering services, Wastewater SFL lab contract, and Hydro Electric 4(E) permit requirements.
- Repairs and Maintenance ($515k). Increased budget due to Wastewater filter cover supplies and miscellaneous Water, Wastewater, and Hydro Electric services deferred from 2010.
- Compliance Requirements ($265k). Increased budget due to FERC land use.
- Training ($120k). Increased budget due to additional district wide training classes focusing on safety and loss prevention, plus individual department training needs deferred from 2009/2010.
- Chemicals ($100k). Increased budget due to 2010 being a low water consumption year. 2011's budget assumes water consumption and required chemicals will return to normal levels.

Debt service coverage:

The Installment Purchase Agreements associated with the District's debt issuances require the District—to the fullest extent permitted by law—to fix, prescribe, and collect rates and charges so that revenues exceed operating expenditures, including debt payments, by 1.25. The District may make adjustments from time to time in its rates and charges, but cannot reduce those rates and charges unless the District's net revenues from reduced rates and charges will at all times be sufficient to meet the debt service coverage of 1.25. Table 4 shows that projected debt service coverage for 2011 will meet requirements.

Table 4: Revised debt service coverage for 2010 and 2011 (millions of dollars)

	2010 Adopted Budget	2010 Revised Projection	2011 Revised Budget
Estimated revenues	$ 66.326	$ 59.241	$ 69.146
Estimated operating expenses	(42.643)	(39.121)	(42.780)
Net revenues	$ 23.683	$ 20.120	$ 26.366
State loans (preexisting)	1.079	1.079	1.079
Available net revenues	22.604	19.041	25.287
Debt service (1)	17.104	15.010	20.305
Debt service ratio	1.32	1.27	1.25
Internal (1.0) debt service ratio	1.23	1.24	1.15

(1) Debt service in 2011 is projected to be higher due to a full year of interest paid by the district on its 2009A debt and an anticipated interest rate increase related to the 2008A variable rate debt.

Table 5 compares projected debt service coverage for 2011 and 2012. Column 2 shows the District will also meet the required debt coverage in 2012 compared to the 2011 budget under the proposed operating budget if revenues and expenditures remain as currently projected. Column 3 reflects a potential bond sale of $60 million issued at mid-year at 6%, thereby reducing the debt service coverage to 1.17 for 2012 and the internal coverage test to 1.04.

Table 5: Projected debt service coverage for 2011 and 2012 (millions of dollars)

	2011 Revised Budget	2012 Proposed Budget	2012 Proposed Budget w/ Bond Sale
Estimated revenues	$ 69.146	$ 71.729	$ 71.729
Estimated operating expenses	(42.780)	(44.024)	(44.024)
Net revenues	$ 26.366	$ 27.705	$ 27.705
State loans (preexisting)	1.079	1.079	1.079
Available net revenues	25.287	26.626	26.626
Debt service (1)	20.305	21.023	22.823
Debt service ratio	1.25	1.27	1.17
Internal (1.0) debt service ratio	1.15	1.13	1.04

(1) Debt service for 2012 is projected to be higher because of an anticipated higher interest rate on the VRDO debt.

Beginning with the sale of the 1996 Revenue Bonds, the District has been allowed to include FCC revenue in meeting its debt coverage requirements. As reflected in Table 6, the District exceeded the 1.25 coverage requirement every year except for FY 2004 when the State of California took local property tax revenues to help meet the State's debt and FY 2009. However, if the District had not received any FCCs during those years, the coverage test would not have been met—except for FY 2006, when the District received approximately $8.0 million in reimbursements from the Federal Emergency Management Agency.

One of the initiatives staff proposed in February 2010 was a new 1.0 debt coverage test. This test is identical to the bond test of 1.25, except it excludes FCCs from the calculation. By creating budgets to meet this test the District is placed in a better position to meet all of its obligations for a given year, including operating expenses and debt payments, without the reliance on FCC income or using reserves.

Table 6: Debt service coverage FY2003-2009 (millions of dollars)

Fiscal Year	Net Revenues	Debt service	Coverage	FCCs	Coverage if FCCs excluded
2003	$13.044	$7.414	1.76	$12.775	0.04
2004	10.312	11.435	0.90	9.835	0.04
2005	18.578	11.624	1.60	15.884	0.23
2006	36.284	15.561	2.33	11.470	1.59
2007	27.349	15.276	1.79	15.237	0.79
2008	25.919	17.792	1.46	11.453	0.81
2009	12.125	14.755	0.82	1.099	0.75

Five-Year Forecast
As part of the current year budget process staff is now presenting a five-year financial forecast. The forecast has regularly been prepared but has not been presented as part of the budget process in the past. These forecasts were used mainly for management purposes and for inclusion in to any bond documents that were being prepared at any given time. Table 7 below reflects staff's current five-year forecast for the District, which will be updated once the current cost of service study is completed.

Table 7: 2011-2015 Five-Year Forecast (millions of dollars)

	Projected 2011	**Projected 2012**	**Projected 2013**	**Projected 2014**	**Projected 2015**
Cash balance - January 1	$ 96.5	$ 85.7	$ 127.7	$ 113.6	$ 85.5
Total Debt Proceeds	-	60.0 [1]	-	-	-
Total revenues	69.2	71.7	78.0	80.4	85.6
Total maintenance and operation costs	42.8	44.0	44.8	45.8	46.6
Net revenues	26.4	27.7	33.2	34.6	39.0
Pre-existing state obligations	1.1	1.1	1.1	1.1	1.1
Net revenues available after preexising obligations	25.3	26.6	32.1	33.5	38.0
Senior debt service	20.3	22.8	27.8	26.9	28.5
total CIP [2]	15.8	15.8	18.4	34.7	29.4
OPEB - one time partial funding [3]	-	6.0	-	-	-
	-	-	-	-	-
Cash balance - December 31	$ 85.7	$ 127.7	$ 113.6	$ 85.5	$ 65.5
Senior debt service coverage	1.25	1.17	1.15	1.25	1.33
Alternative senior debt coverage					
Total FCCs in revenue above	2.00	3.00	7.00	7.00	10.00
$$$ of FCCs removed from calculation	2.00	3.00	7.00	7.00	10.00
Potential senior debt coverage	1.15	1.04	0.90	0.99	0.98

[1] Potential $60 million bond sale (90% water / 10% wastewater)
[2] Adopted 2011-2015 CIP plan at 80%
[3] Potential partial funding of OPEB liability

Conclusion
The 2011-2012 operating budget process presents a number of challenging financial issues because of ongoing national, state, and local economic conditions. Like all of EID's two-year budgets, staff approached the process first and foremost with the priority of maintaining a reliable level of service to customers that protects public health and safety, and the environment. Staff believes this objective will be achieved under the proposed 2011 operating budget. Staff also believes that if the projected revenues are met and the belt continues to be tightened by staff while meeting the budget expectations then there will be enough net revenue in 2011 and 2012 to meet the 1.25 coverage requirements in the District's bond covenants and enough revenue, excluding FCCs, to meet our internal 1.0 test.

Board Decision/Options:

Option 1: Adopt the El Dorado Irrigation District 2011-2012 operating budget in the amount of $42.780 million for 2011 and $44.024 million for 2012.

Option 2: Take other action as recommended by the Board.

Option 3: Take no action.

Staff/General Manager Recommendation:

Option 1: Adopt the El Dorado Irrigation District 2011-2012 operating budget in the amount of $42.780 million for 2011 and $44.024 million for 2012.

Supporting Documents Attached:

Appendix 1: Cash Flow Projection for 2011
Appendix 2: Total District Summary of Materials and Services by Account
Appendix 3: Office of the General Manager Materials and Services by Account
Appendix 4: Human Resources Materials and Services by Account
Appendix 5: Communications Materials and Services by Account
Appendix 6: Finance Materials and Services by Account
Appendix 7: Information Technology Materials and Services by Account
Appendix 8: Engineering Materials and Services by Account
Appendix 9: Water Operations Materials and Services by Account
Appendix 10: Wastewater Operations Materials and Services by Account
Appendix 11: Recycled Water Operations Materials and Services by Account
Appendix 12: Hydroelectric Operations Materials and Services by Account
Appendix 13: Natural Resources Materials and Services by Account

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Appendix 1: Cash Flow Projections for 2011 (millions of dollars)

	2009	Projected 2010	Projected 3/31/2011	Projected 6/30/2011	Projected 9/30/2011	Projected 12/31/2011	Total Projected 2011
Beginning cash balance	$57.43	$122.48	$96.50	$85.84	$85.87	$86.30	$96.50
Total revenues	63.09	59.24	14.69	14.69	25.77	14.00	69.15
Bond proceeds	120.30						
Operating expenses	45.75	39.12	10.70	10.70	10.69	10.69	42.78
Debt payments	21.25	16.10	10.69		10.69		21.38
CIP expenditures	51.34	30.00	3.96	3.96	3.96	3.96	15.84
Ending cash balance	$122.48	$96.50	$85.84	$85.87	$86.30	$85.65	$85.65
Debt service coverage ratio	0.82	1.27				1.25	1.25