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To: Mayor Ted Wheeler
Commissioner Nick Fish
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Commissioner Chloe Eudaly
Commissioner Dan Saltzman
Auditor Mary Hull Caballero

Subject: Budget Submissions for the Bureau of Environmental Services and the Portland Water Bureau

Date: January 30, 2017

The Portland Utility Board (PUB) serves as a citizen-based advisory board for the Bureau of Environmental Services (BES) and the Portland Water Bureau. We submit this initial budget letter in compliance with City practice for budget advisory committees, and in response to our specific duties to:

“advise the City Council, on behalf of and for the benefit of the citizens of Portland, on the financial plans, capital improvements, annual budget development and rate setting for the City’s water, sewer, stormwater, and watershed services. The Board will advise Council on the establishment of fair and equitable rates, consistent with balancing the goals of customer needs, legal mandates, existing public policies, such as protecting water quality and improving watershed health, operational requirements, and the long-term financial stability and viability of the utilities. (3.123.010)”

Over the course of 2016, the PUB held 12 regular and 12 subcommittee meetings, and participated in four tours of utility facilities to deepen our understanding of the opportunities and challenges facing both utilities. We reviewed preliminary 2017 operating budget information and the major additions and adjustments to the five-year capital improvement plans (2017-2022) for both bureaus. We look forward to providing additional feedback to City Council upon receipt of the final budget decision packages and the City Budget Office (CBO) analysis. We anticipate participating in the budget work sessions in March, the utility rate hearing in May, as well as discussing budget issues with the Mayor if requested, as the budget develops.

The PUB receives significant support from both bureaus’ directors and staff, the ex-officio members, Commissioner Fish and staff, as well as the City Budget

Office and our analyst Melissa Merrell. We are grateful for their collective efforts to help us understand and navigate the complexities of these utilities.

The PUB identified five overarching themes regarding utility management and operation for the City Council to consider, including:

- Facilitating inclusive strategic planning efforts to align and prioritize operating and capital expenditures
- Responding to increases in regulatory and community expectations
- Creating a culture of open communication and transparency
- Addressing long term affordability and equity of rates, and
- Ensuring operating and capital improvements are based on consistent, legally defensible policies

Each theme and the PUB's observations are highlighted below.

Strategic Planning

- **Bureau of Environmental Services:** Under the direction of Director Jordan, BES is conducting a holistic examination of its core functions and processes to create a roadmap for the future that encompasses a financially sound bureau with clear systems for prioritization and decision-making. The plan, as envisioned, will align budgeting decisions with program priorities and performance indicators. The PUB appreciates the work of Assistant Director Uchiyama to include us in this process and fully supports the bureau's efforts to create a plan with clear goals, objectives, and metrics that will guide future investments. The PUB supports the bureau's intention to set a course for known and stable rate increases in the range of the rate of inflation. We are optimistic that the bureau will continue to make choices that will increase its financial and system sustainability and manage the cost burden to its customers.
- **Water Bureau:** The bureau has an expired strategic plan and intends to begin a similar process to that of BES by early spring 2017. The PUB recognizes the bureau has two large infrastructure projects and regulatory concerns with lead and copper that demand significant attention in the near term, but encourages the bureau to prioritize its strategic planning, with an emphasis on addressing long-term rate stability and affordability while maintaining high quality water services. The PUB encourages the bureau to facilitate an inclusive (internal and external) and transparent process to continue to build trust with the community.

Regulatory Compliance and Community Expectations

- **Bureau of Environmental Services:** The Portland Harbor offers a moderately-high degree of uncertainty regarding potential cleanup obligation for the City. BES is the lead entity for the City on this issue, is monitoring the developments, and will work with appropriate City staff to address EPA's requirements. The PUB is confident BES is the appropriate lead entity for the City on this river-based cleanup and is confident there will be close collaboration with the Mayor's office to address city-wide issues.
- **Water Bureau:** The quality of community drinking water received significant national and local attention over the last year. As a result, there has been increased scrutiny regarding the bureau's water treatment and corrosion control. The PUB received several briefings from Director Stuhr and staff and they continue to work with the Oregon Health Authority and Environmental

Protection Agency to identify required future actions. The PUB supports and looks forward to continued open dialogue as the bureau receives the results of the corrosion control study and the evaluation of the Lead Hazard Reduction Program. We support the bureau sharing the results with the public and educating them on their responsibilities to reduce the risk of exposure within their homes.

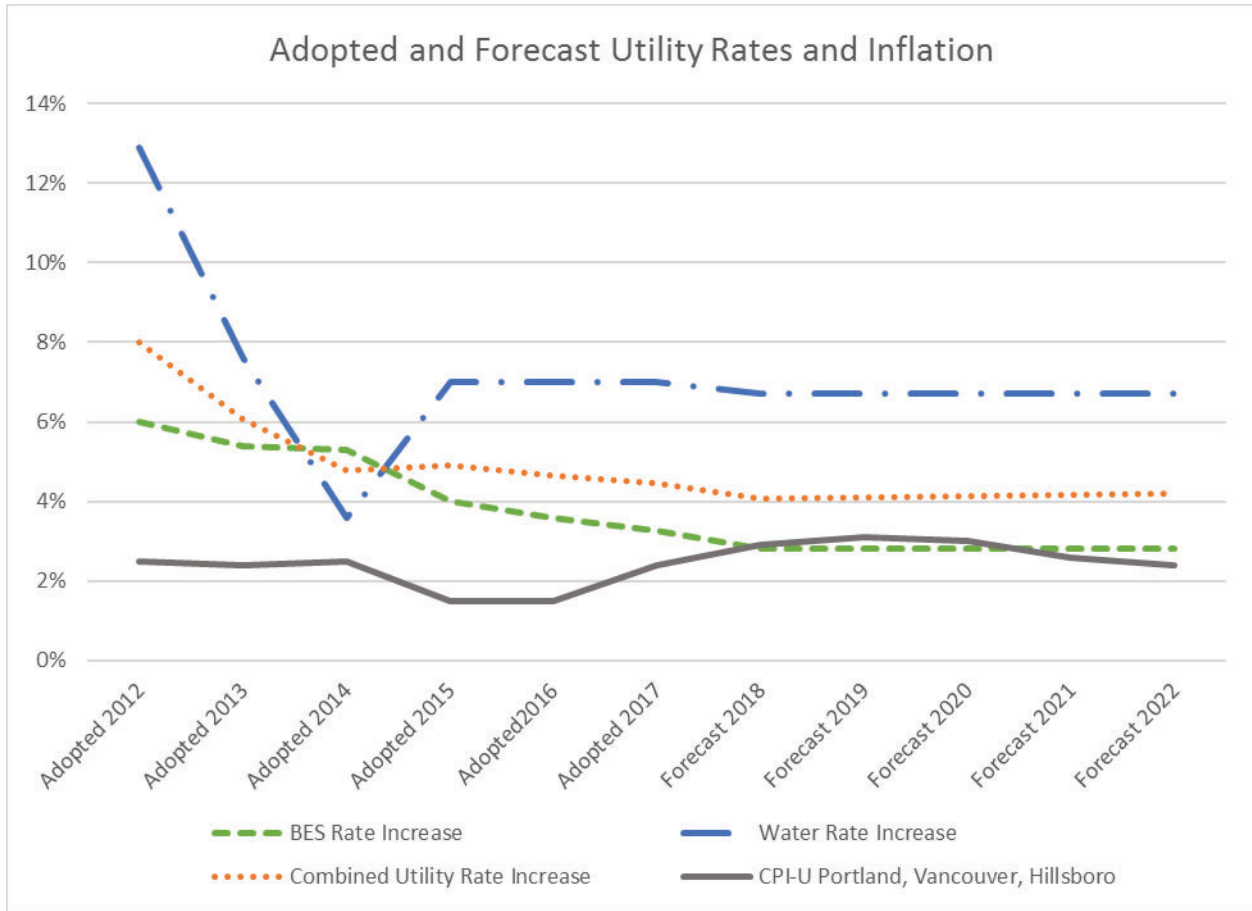
Communications and Transparency

- Bureau of Environmental Services and the Portland Water Bureau: Creating a culture of open, proactive communication, and transparency in both bureaus is ongoing work and PUB is sensitive to public perception of the bureaus. As highlighted in last year's letter we continue to support, *"framing the vision for the bureaus, to strengthen and maintain the public trust, and fine-tuning the bureaus' cultures to ensure that they are more inclusive, transparent, and cooperative, will encourage meaningful community dialogue and understanding that will serve the bureaus in the future."* While project-level communications appear to run smoothly, the Auditor's 2016 Community Survey indicated that respondents who feel "Good" or "Very Good" has declined by 4 to 5 percentage points from 2012 for questions related to the Water Bureau and hovered at or below 50% for questions related to BES. A recent Water Bureau survey of customers indicates that 79% of customers rated their satisfaction as "Satisfied" or "Very Satisfied." Among customers who called the Water Bureau, 66% rated their satisfaction as "Satisfied" or "Very Satisfied." It appears there may be ongoing public concern with both utility bureaus. The PUB has concerns that neither of these tools may be adequately reaching or reflecting the voices of the most vulnerable in the city. We appreciate the Water Bureau briefing of their findings and look forward to learning more about their strategies for addressing concerns identified in that process. The PUB is willing and committed to serving as a conduit to the public, but needs that role to be reinforced through bureau actions and communications. To date, we have seen limited general public participation at PUB meetings. We will work with the bureaus in the upcoming year to identify alternative outlets of citizen engagement to help address any ongoing or emerging concerns.
- City Council: The PUB's role as a citizen oversight commission requires it to have an active role in advising the Council on decisions related to the two utility bureaus. As our August 8, 2016 memo to City Council regarding the disruption of the Council approved process to sell Terminal 1 North revealed, there is opportunity to improve communications between the Council and the PUB. We respectfully request that the Council recommit itself to protecting the interests of its utility customers and proactively engage the PUB early and often in ideas that may impact either utility's obligations or budgets.

Affordability and Equity

- The affordability of the combined water, sewer, and stormwater bill is an ongoing concern for many citizens. The combined cost of service for the City's utilities is rising faster than the rate of inflation. The combined average monthly bill for the typical single family household for FY 2016-17 for water and wastewater is \$103.63, about 2.0% of median household income for the City of Portland (and well below 4.5%, at which point the EPA considers it unaffordable). However, flat local wages for a portion of city residents and rising housing costs exert pressure on the perception of affordability. With BES's current financial position and planning efforts, it anticipates being able to maintain its rate increases near the level of inflation (under

approximately 3%) over the long term. Projections for the Water Bureau have retail rate increases at 6.7% for the next five years due to several large seismic resiliency projects and costs related to the renovation of the Portland Building. The PUB encourages the Water Bureau, through its strategic planning process, to continue to evaluate the tradeoffs and choices keeping affordability concerns a priority.



- Rates are driven both by capital investments and operating budgets associated with staffing. The PUB is closely reviewing BES’s request for 18 new positions and Water’s request for 5 new positions, given the long term cost of PERS assigned to each new full FTE. We appreciate the Water Bureau’s detailed explanation of need presented at the December meeting, and are reviewing the written materials provided by BES. PUB anticipates having additional questions as the budget packages are completed and considered by the Council. However, the staffing numbers noted above exclude the additions made during the Budget Monitoring Process (BMP) in Fall 2016 of five (5) new staff for BES and three (3) for Water. Current budget guidance is that changes made during the BMP should be reserved for “urgent and unforeseen needs.” While we appreciate the needs of each bureau to remain flexible in assessing their staffing needs due to unforeseen challenges, PUB is concerned that staff additions should undergo full evaluation of need in the context of overall programs that happens during the regular budget process.
- The PUB has a standing subcommittee discussing the Low Income Discount Program, to consider

how to offer some bill relief to lower income customers. However, that discussion has confirmed the challenges of providing bill relief to lower income customers who do not have a direct billing relationship with the Water Bureau, leading to an inequitable program in terms of both access and bill relief. A wholesale re-evaluation of how to address affordability and equitable access for those with an inability to pay for basic services is needed in the upcoming year. The PUB is committed to examining this issue further.

Budget Pressures and Policy Consistency

The recent rulings in the *Anderson v. City of Portland*, pending any appeals, relieves the pressure and work associated with defending past city actions. However, it will be important to continue to remain vigilant about spending decisions of the two bureaus. As budgets throughout the City and State remain tight, there is a tendency of other general obligation bureaus and entities to turn to the utilities to request “partnership” funding, fee-for-service, or other intergovernmental agreements. PUB sees this as one of our main purposes – to continue to examine current and new spending to make sure it is in the best interest of the ratepayers. We look forward to continuing to work with Council and staff to provide the needed outside perspective for budgeting decisions early in decision processes.

In addition to being vigilant about proper spending of rate funds, the costs and benefits to the broader public regarding upgrades to private property may need closer examination and scrutiny by the PUB and Council to provide policy clarity and consistency. As part of the strategic planning and assessments in both bureaus, the PUB encourages them to critically evaluate their assumptions regarding levels of service to determine if they are still appropriate in light of climate change, citizen expectations, risk management, and limited budgets.

Budget To Date Highlights

The PUB and its budget subcommittee reviewed the preliminary decision packages and projected rate impacts, but is reserving detailed comment until the packages are complete and the CBO has completed its analysis. In general, however, we would like to highlight a few elements for the Council.

- **Bureau of Environmental Services:** As part of the strategic planning process, the bureau is working to identify an optimal plan for investing in its systems and infrastructure. This will require a bold look at the existing business practices of the bureau’s capital work. The current bureau assessment is that they need to more than double the amount of capital work that is completed each year to address aging infrastructure and amount of inventory ranked as “very poor/critical.” This increased investment in capital and systems will require significant financial resources and strategic shifts in staffing. The current financing model relies heavily on debt financing most capital work in the near term but has assumed a shift to mostly cash financing in the out years. To pay for the proposed large increase in capital work, the bureau now recommends a financing model with closer to half of the CIP financed with debt and half with cash. As most of the capital assets of the bureau have extended useful lives, debt financing ensures an equitable share of the cost burden between today’s residents and future residents who will benefit from the investment. The shift will also allow the bureau to make the necessary investments without placing all of the cost on current residents through large rate increases.

BES highlighted significant needs at both of its wastewater treatment facilities in the next five years to meet permit obligations and address operational efficiencies. They are also completing

extensive analysis in storm water systems planning, in an effort to prioritize expansion of the stormwater system and repair and replacement of aging infrastructure to meet future drainage needs in the City.

BES is also continuing its evaluation of the biogas project. Last year PUB joined the CUB in raising concerns about the proposed biogas and food waste project at Columbia Boulevard Wastewater Treatment Plant. PUB and CUB staff have been engaged with bureau staff throughout the year as analysis and planning for these projects has progressed. The PUB acknowledges that a successful project would be financially beneficial to the bureau, but there are also risks and costs associated with the project and its base assumptions, and PUB again encourages the bureau to carefully evaluate the tradeoff of investing in this project at the expenses of others more closely aligned to the core mission of the bureau.

- **Water Bureau:** The bureau is proceeding with two large capital improvement projects - Washington Park to upgrade its reservoir and a new Willamette River Crossing. Both projects are designed to reduce the potential disruption to water supply to the west side of Portland in the event of a large earthquake. The scope and cost of the Washington Park project has grown and the PUB encourages the Council to assist us in monitoring the projects' progress and budgets closely.

The Council committed in 2015 to completing multi-year preservation work of the former reservoirs at Mt. Tabor. The PUB was encouraged by the Council's decision last year to use General Fund resources to fulfill this obligation. The PUB does not support using ratepayer funds to pay for historic preservation activities at Mt. Tabor and expects the Council will continue to meet this obligation with General Fund resources.

Conclusion

The PUB views this opportunity to comment on the bureaus' budget submissions as the first of several touch points throughout the annual budget and planning processes. We look forward to providing you further advice as these processes continue through the spring. Thank you, and all the cooperating City staff, for your time and consideration. We look forward to continuing the discussions.