

To: Mayor Ted Wheeler
Commissioner Nick Fish
Commissioner Amanda Fritz
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 XX, 2018

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)”

The PUB held five board meetings and two subcommittee meetings to review the FY 2018-19 proposed operating budgets, major additions and adjustments to the five-year capital improvement plans, and decision packages 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. We are grateful for their collective efforts to help us understand and navigate the complexities of these utilities.

The PUB considers the following values when providing input and making recommendations to the Council:

- Affordability

- Efficiency of Operations and Value to Customers
- Assistance to Low-Income Residents
- Protection of Public Health and Watershed Health
- Improvement and Sustainability of Infrastructure
- Regulatory Compliance
- Equity
- Service Delivery
- System Resiliency
- Transparency and Public Engagement

These values are not presented in any particular order and tension can exist between these values. PUB members particularly feel the tension between the need of the bureaus to increase capital investments to address system maintenance and the burden that ongoing annual rate increases place on customers. PUB encourages and has asked the bureaus to make explicit the consequences of rate constraints to increase public awareness of this issue. PUB feels strongly that this needs to be a component of the public dialog to align expectations and find the optimal levels of investment for the bureaus and the public.

Annual Rates of Increase

The bureaus submit budget requests that comply with guidance from the Mayor and Commissioner-in-Charge. City Council ultimately approves those budgets and the necessary increases to rates to support those budgets during the annual budget process.

Annual rates of increase for the typical single-family household in Portland over the past 10 years have increased more than three times faster than commonly used benchmarks for increases including inflation, median household income, median family income, and changes in per capita income. There are challenges to using inflation or other economic benchmarks when considering increases in utility charges. Increasing regulatory requirements and past underinvestment may mean that utilities need to invest more than inflationary increases would permit. An example is the requirement that Portland reduce combined sewer overflows which required significant rate increases over the last 10 years for capital investments but resulted in improved water quality in the Willamette River. While a lower rate of increase this year would translate to savings of \$1 or \$2 monthly for the typical single-family household, those incremental increases compound over time. Given the City Council approved rates of increase over the last 10 years, typical monthly single-family household bills are \$25 more than they would have been if rates had increased in line with inflation over that period.

Acknowledging the scarce resources of many Portlanders, PUB members encourage City Council to be mindful of the multiyear impact of rate increases and the cumulative impact on customers.

Budget Prioritization and Rate Options

The Mayor's FY 2018-19 budget guidance directs the Portland Water Bureau and the Bureau of Environmental Services (BES) to identify efficiencies and reductions to limit rate increases. It further directs them to work with the PUB to develop prioritized reduction options for Budget Committee and City Council consideration. Budget guidance provided to the bureaus from Commissioner Fish on November 20, 2017 included an expectation that the requested budgets will "reflect good value at a fair price in any proposal for a rate increase. As in recent years, the proposed combined retail rate increase shall be below 5%."

The co-chairs requested the bureaus prioritize requests necessary to comply with the following categories: regulatory compliance, maintenance and improvement of asset health, bureau equity goals, and alignment of bureau activities with strategic planning goals. In addition, to demonstrate the relative priority of requests and the benefits that Portland customer would receive from the additional burden of increased rates, the co-chairs requested the bureaus to identify line items in their requested budgets that would not be funded if the City Council were to approve combined annual rate increases of 3% and 4% in addition to their planned requests in line with the Commissioner's guidance of a combined increase below 5%. This information allowed the board to have substantive deliberations about the tradeoffs of the programs and the additional burden on Portland's utility customers. PUB members recognize the amount of work such exercises require and appreciate the time and consideration of the many staff required to provide responses. The bureaus provided helpful information on the budget items that would and would not be included in their budgets if combined rates of increase were further constrained. PUB members found this exercise valuable in highlighting the tradeoffs of the costs of investment and benefit for Portland residents.

The board will reserve its recommendation on individual decision packages until after the City Budget Office reviews and recommendations are complete. PUB members encourage the bureaus to use the budget process to communicate the value of the investments over inflation and benefits that the residents of Portland receive and are committed to the working with the bureaus to do so.

Affordability

The affordability of the combined water, sewer, and stormwater bill is an ongoing concern for PUB members. The combined average monthly bill for the typical single-family household for FY 2018-19 for water and wastewater will be \$113.30 if requested rates of increase are approved.

There is no agreed upon standard for what rates are 'affordable' or 'unaffordable' for any given community. Rates may be measured against economic measures of inflation or changes in income. PUB considered several indicators in its discussions and agreed that budget requests should be viewed in context of core requirements to invest in infrastructure and meet new

regulations. However, there is concern that the growth in the cost of service greatly exceeds growth in household income measures.

In the mid-1990s, EPA developed a benchmark to test rate impacts on customers. Using that guide, water and wastewater bills that are 4.5% or more of the median household income would have a large economic impact on residents on a community wide level. Including the proposed rates of increase, the typical single family residential utility bill would be about 2.0% of median household income for the City of Portland. However, there are concerns regarding the use of a single indicator that may not reflect the impact to lower income households as well as economic and other trends over multiple years. Flat local wages for a portion of city residents and rising housing costs exert pressure on the perception of affordability.

PUB members consider a component of affordability to be reasonable costs to customers with known and predictable rate impacts. Reasonable must be viewed in context of accumulated costs over time and the value of the service provided. PUB members encourage both bureaus and the City Council to continue to evaluate the tradeoffs and choices of investments to keep affordability concerns a priority.

The proposed annual rates of increase in the 5-year financial plan for the Water Bureau have increased from the plan included in the FY 2017-18 Adopted Budget. The major driver for this increase is the direction from City Council, supported by the PUB, to pursue a filtration plant to address regulatory requirements related to *cryptosporidium* and other potential risks to the Bull Run Watershed. The filtration plant will be a substantial capital investment that will significantly impact rates for many years. Resolution 37309 agreed to by City Council on August 3, 2017 included direction “that during the annual rate-setting process the Portland Water Bureau will make every effort to minimize rate impacts while following the intent of this resolution.” PUB members requested information from the bureau on how they have minimized that impact and the bureau identified some work that would be delayed or foregone.

With City Council’s approval, both bureaus have added large capital projects in recent years and additional large investments limit the bureaus’ ability to respond to future needs. Rates are driven both by capital investments and operating budgets associated with staffing. The PUB is closely reviewing BES’s request for 22 new positions and Water’s request for 21 new positions, given the long-term cost of PERS assigned to each new full FTE. The PUB encourages both bureaus to look for efficiencies, vacancies savings, or foregoing lower priority activities within their existing budget before requesting additional rate resources.

PUB requests the bureaus use the upcoming budget process to revisit the cost drivers and assumptions underlying their requests with a goal of trimming individual budget requests to contribute to a rate projection that emphasizes affordability for all Portland residents. PUB members encourage the bureaus to use the next four weeks to dialogue and explore jointly what detailed budget reductions can be identified.

Equity

In 2015, the City of Portland adopted citywide racial equity goals to end racial disparities within city government; to strengthen outreach, public engagement, and access to City services for communities of color and immigrant and refugee communities; and to collaborate with communities and institutions to eliminate racial inequity in all areas of government. The PUB supports these goals and looks forward to an update on the bureaus' implementation of their Racial Equity Plans that were created last year. As part of its deliberation on individual budget requests, the PUB will consider the equity implications of requests and how increased resources will further the bureau and citywide equity goals.

Assistance Programs

The City Council resolution that directed the Water Bureau to pursue filtration also directed "that the Portland Water Bureau will seek to optimize and enhance its discount programs to lessen the impact of rising water rates on low-income customers." The bureaus have multiple programs to provide financial assistance to low-income Portland residents. Compared to other utilities, these programs are generously designed, though few and decreasing numbers of residents are participating in the programs. PUB members feel these assistance programs are vital and commend the work of the bureaus to improve outreach and scope of the assistance programs. Members are supportive of improvements but have concerns about some of the proposals and will continue to work with the bureau during the budget process to address those concerns. Members will provide its recommendations to the City Council once it has a more complete understanding of the proposals.

Centralized Services and Citywide Priorities

Several ongoing points of discussion with the PUB and the bureaus concern centralized services and citywide priorities. Centralized provision and citywide goals provide the opportunity for standardization and can result in efficiencies. There is also potential for duplication and fragmented implementation. For example, the PUB has heard from both bureaus that recruitment, hiring, and procurement services negatively impact bureau operations. The proposed bureau budgets include requests for staff to supplement or facilitate some of these services. Generally, the board believes the bureaus should refrain from building internal capacity for services that should be provided by other City agencies. PUB members encourage the bureaus to continue to work with other city bureaus to identify and implement improvements to the provision of central services.

The PUB would like consideration of the budget and staffing impacts as citywide policies are identified and evaluated. In particular, the PUB continues to encourage the Mayor and City Council to engage in a Citywide conversation about how the City is managing human resources

invested in equity work across the city. The City should work to ensure that bureau-level investments are incorporated into a well-framed and measurable citywide strategies.

Strategic Planning

The PUB enthusiastically supports the roadmap laid out in the BES' new 10-year strategic plan and commends the bureau's staff and leadership for their work over the past two years to identify six core goals that will guide the bureau's work over the next decade. The PUB looks forward to working in partnership with BES to prioritize the strategic initiatives through the city's budget process. The Portland Water Bureau has begun work on its Strategic Business Plan and the PUB looks forward to working with the bureau to provide input on that plan. PUB members appreciate the work that BES did to link their packages to their strategic plan. They look forward to seeing that connection be refined to a more granular level in coming years. PUB members encourage both bureaus to continue to refine their budget requests to have similar formats and align with their strategic plans.

The PUB encourages both bureaus to continue their strategic work and to craft metrics for measuring their progress towards achieving the outcomes identified in those plans. In addition, the PUB expects that the bureaus will include performance metrics for accountability when proposing new programs or significant changes to existing ones.

Regulatory Compliance

Both BES and the Water Bureau are heavily regulated by state and federal entities which limits the discretionary components of their respective budgets. However, the bureaus do have flexibility to decide how and in some instances when regulatory requirements are met. Going forward, PUB members ask the bureaus to clearly present in their budget requests those items that are regulatory requirements at this time, those that can be implemented over time, and those that are related to or complement regulatory requirements but would not jeopardize compliance.

Communications and Transparency

In several past recommendations to City Council, the PUB highlighted that 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. PUB members commend the bureaus for the work they did early in the budget process to provide information in similar formats. Easily understood and publicly assessable budget information is one way to strengthen and maintain the public trust and PUB members encourage the bureaus to continue that work.

PUB members also encourage the bureaus to explore a combined communication strategy with consistent outreach and messages to the public.

Comments on specific budget proposals

The PUB views this opportunity to comment on the bureaus' budget submissions as the first of several touch points with City Council throughout the annual budget and planning processes. PUB members will review the analysis and recommendations of the City Budget Office, consider further input from the bureaus, and weigh the requests through the lenses of its stated values, cost, impact on service delivery, connection to strategic plan, and expected outcomes. We look forward to providing you further input as the budget process continues through the spring.

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