Reserve Funds
Types of Reserves

- **Cash**
  - Current Fund
    - Unrestricted
    
  - Rate Stabilization Fund (RSF)
    - Unrestricted
    - Purpose: reduce rate volatility
    - Transfer of revenue into the RSF defers those revenues
    - Transfer of revenue out of the RSF will recognize the revenue in the transfer year

- **Revenue**
  - Bond-Related Funds
    - Restricted
    - Isolated Bond proceeds used to pay capital spending
    - Bond debt service reserves set aside (if required)
    - Accumulate monthly debt service accruals to pay principal and interest

- **Cash**
  - Tacoma Power Operating Fund
    - Unrestricted
The Flow of Unrestricted Reserves

The Current Fund
- is operating cash;
- is increased or reduced by Net Revenue each period;
- only impacts our Days of Liquidity metric.

The Rate Stabilization Fund
- is revenue that can be applied in the future;
- is considered revenue AND liquidity;
- impacts both our Days of Liquidity and Debt Service Coverage Ratio.

Expenses

Revenues

Net Revenue

Current Fund

Total Liquidity
Liquidity - the amount of immediate reserves available to cover necessary expenses.

Cash + Revenue = Total Liquidity

- Liquidity
- immediate reserves available to cover necessary expenses

Rate Stabilization Fund (RSF)
Reserves Impact System Rates through Financial Metrics

Rate Stabilization Fund provides flexibility to meet our financial metrics requirements

Accounting rules require revenues and expenses be recognized in the year that they are earned.

• extra revenue this year cannot be applied to future years

Exception – revenues can be applied in future years if transferred into the Rate Stabilization Fund.

Rate Stabilization Fund (RSF) can improve the Debt Service Coverage Ratio

• Debt Service Coverage Ratio
  Net Revenue / Debt Service Expenses:
  Minimum: 1.25x
  Target: 2.0x

• Days of Liquidity
  Annual Liquidity / Operating Expenses:
  Minimum: 150 Days
  Target: 180 Days
Use of the Rate Stabilization Fund Helps us Maintain our Rating and Avoid Rates Shocks

2019 after the near-critical water year:
• Used $10 million of RSF to meet minimum ratio and avoid default on outstanding Bond Covenants & a 4% rate increase

2021 after high wholesale prices:
• Deferred $25 million of wholesale revenue to apply to future years
Forecasts use the Rate Stabilization Fund to Smooth Rates

Maintaining adequate reserves will help mitigate rate and financial risks

| RATE STABILIZATION FUND BALANCES (YEAR-END) |
|-----------------|-----|-----|-------|-----|-----|-----|-----------------|
| ADDITION / - WITHDRAWAL | $10 M | +$26 M | +$12 M | $0 | -$10 M | $25 M | $95 M | ~$90 M (TOTAL) |
| BALANCE         | $10 M | $36 M | $48 M | $48 M | $38 M | $63 M | $158 M | $68 M |
Current Core Rate Stabilization Fund Balance is Less Than Recommended

2024 Tacoma Power Bond Issuance Request for Information Underwriter Bank Responses

11 Underwriter Bank Responses:
4 respondents provided to Tacoma Power a core balance recommendation to address revenue volatility:
• 3 recommend a core balance of $100 - $120 million to address hydro and market price volatility
• 1 recommends a core balance of $60 million to address hydro volatility

Respondents further recommend additional funds in the RSF be reserved and allocated toward debt service, significant future expenses, or capital projects.

Once the RSF is used as planned in future high expense years, Tacoma Power’s RSF core balance will be $68 million

*Includes $31.4 million in a separate Hydro Stabilization Fund

Comparative Analysis of WA Public Power Issuers (FY 2022)

<table>
<thead>
<tr>
<th>Utility</th>
<th>Planned Use $000</th>
<th>RSF Balance $000</th>
<th>RSF % of Operating Revenue</th>
<th>Wholesale Revenue % of Operating Revenue</th>
<th>Replenish Mechanism</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tacoma</td>
<td>- $90,000</td>
<td>$158,000</td>
<td>12% (core)</td>
<td>27%</td>
<td>Annual evaluation</td>
</tr>
<tr>
<td>Clark</td>
<td>$64,000</td>
<td>$12%</td>
<td>11%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Snohomish</td>
<td>$115,000</td>
<td>15%</td>
<td>10%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Grant</td>
<td>$98,182</td>
<td>24%</td>
<td>24%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Seattle</td>
<td>$100,000</td>
<td>8%</td>
<td>14%</td>
<td></td>
<td>Automatic rate increase if &lt; $75M</td>
</tr>
<tr>
<td>Sacramento PUD *</td>
<td>$190,000</td>
<td>9%</td>
<td>19%</td>
<td></td>
<td>Hydro rate surcharge or rebate</td>
</tr>
</tbody>
</table>

*Includes $31.4 million in a separate Hydro Stabilization Fund
Future expenses
• Debt Service spikes
• Hydro relicensing of 3 dams
• Dam Safety Program
• Grid modernization projects

The totality of these expenses expected to be > $500 million over the next ten years

Future risks & emerging issues
Post 2028 BPA Contract
• likely not as effective in meeting resource needs so we will need to procure more power supply

Wildfire liability risk
• 2 largest Oregon utilities requesting $185 million investments in wildfire projects

Increasing market volatility
• SCL burns through cash reserves
• Clark PUD uses RSF to address $17.7M shortfall
## Peer Utility Rate Increases

<table>
<thead>
<tr>
<th>Utility</th>
<th>Rate Increase</th>
</tr>
</thead>
<tbody>
<tr>
<td>Seattle City Light</td>
<td>Seattle City Light: 9.5% 2024</td>
</tr>
<tr>
<td>Snohomish PUD</td>
<td>SnoPUD: 5.8% 2024</td>
</tr>
<tr>
<td>Puget Sound Energy</td>
<td>PSE: 8.7% 2023, 1.7% 2024</td>
</tr>
<tr>
<td></td>
<td>PSE: 17%* 2025 &amp; 2026</td>
</tr>
<tr>
<td>Grant PUD</td>
<td>Grant PUD: 3.5% 2024</td>
</tr>
<tr>
<td>Chelan PUD</td>
<td>Chelan PUD: 3% 2020-2024</td>
</tr>
<tr>
<td>Clark PUD</td>
<td>Clark PUD: 14% 2024</td>
</tr>
<tr>
<td>Pacific Power</td>
<td>Pacific Power: 12.9% 2024</td>
</tr>
<tr>
<td></td>
<td>Pacific Power: 16.9%* 2025</td>
</tr>
<tr>
<td>Portland General</td>
<td></td>
</tr>
<tr>
<td>Electric</td>
<td>PGE: 17% 2024, 7.4%* 2025</td>
</tr>
<tr>
<td>Avista</td>
<td>Avista: 12.6%* 2024, 7.8%* 2025</td>
</tr>
</tbody>
</table>

* Proposed

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**Weather challenges, demand increases, and rising costs result in changes to customer electricity rates**

City Light rates in Seattle to increase by nearly 10% next year

Puget Sound Energy proposes hefty rate hikes to pay for hydro and wind power

Chelan PUD customers face five years of 3% rate increases

Clark Public Utilities rates will jump 14.5 percent as of March 1

Pacific Power Increases Rates, Citing Rising Costs And Wildfire Mitigation

After raising rates by 17% in 2024, PGE requests further hikes for 2025

Avista Utilities set to raise Washington electricity rates
Board Guiding Principle #2: Financial Sustainability
• Directs for planning methods that incorporate conservatism and gradualism … to ensure long-term financial stability and anticipate unexpected future events with adequate cash reserves and insurance.

Board Guiding Principle #3: Rates
• Directs for planned gradual and consistent utility rate changes to mitigate large customer rate increases

Maintaining Low and Stable Rates Requires a Robust Rate Stabilization Fund to Mitigate:
• Hydro and Price volatility
• Future operational risks
• Expense spikes
• Emerging issues
• General cost pressures

Rate Stabilization Fund Recommendations:
• Maintain a core balance of $100 million to address hydro and market price volatility
  • Current planned use of $90 million in the next ten years will reduce core balance down to $68 million
  • Allocate additional funds in the RSF toward significant future expenses and emerging issues

Several peer utilities without a sufficient Rate Stabilization Fund are increasing rates significantly
Questions?

Appendix
When using the RSF, total liquidity does not change because the revenue transfers from one liquidity account to the other.

2019 after the near-critical water year:
- Reduced the RSF balance by $10 million
- Increased revenue by $10 million
- Increased current operating fund by $10 million

2021 after high wholesale prices:
- Reduced Wholesale Revenue by $25 million
- Reduced Current Operating Fund by $25 million
- Increased Rate Stabilization Fund by $25 million
Variance in Wholesale Revenue is a Result of Hydro and Market Price Volatility

Over the last 15 years, Wholesale revenue has contributed between 8% and 26% of Total Revenue for Tacoma Power.

<table>
<thead>
<tr>
<th>Year</th>
<th>Wholesale Revenue %</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008</td>
<td>24%</td>
</tr>
<tr>
<td>2009</td>
<td>19%</td>
</tr>
<tr>
<td>2010</td>
<td>19%</td>
</tr>
<tr>
<td>2011</td>
<td>20%</td>
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<td>2012</td>
<td>17%</td>
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<td>2014</td>
<td>19%</td>
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<tr>
<td>2015</td>
<td>12%</td>
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<td>2016</td>
<td>13%</td>
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<td>2017</td>
<td>13%</td>
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<tr>
<td>2018</td>
<td>12%</td>
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<tr>
<td>2019</td>
<td>8%</td>
</tr>
<tr>
<td>2020</td>
<td>12%</td>
</tr>
<tr>
<td>2021</td>
<td>17%</td>
</tr>
<tr>
<td>2022</td>
<td>26%</td>
</tr>
</tbody>
</table>
2024 Tacoma Water Reserves Overview

Presented by Jodi Collins for the Public Utility Board on March 27, 2024
Tacoma Water currently maintains 32 funds in order to properly classify and account for financial activities.
Gradual approach sets rates as low as is responsible and ensures that we meet policy financial metrics

The debt service coverage ratio shows how many times we can pay outstanding debt service with the cash we have available in a given year. It measures compliance with debt covenants and provides financial flexibility.

- **Senior**: Net Revenue/Debt Service after transfers from RSA and without gross earnings tax or subordinate debt
- **All-In**: Net Revenue/Debt Service does not include transfers from RSA and does include gross earnings transfer and subordinate debt

Liquidity helps manage risk, meet working capital needs, and support stable rate adjustments. Days Liquidity shows how many days of operating expenses we could fund from reserves.

- **Days on Hand**: (Operating Fund balances + Capital Reserve and SDC Fund balances * 365 days)/annual budgeted operating expenses
## Location and size of the utility
- Smaller utilities may be more susceptible to revenue/expense volatility
- Drought restrictions common in some locations
- Reserves, rate stabilization funds, rate structure decisions

Tacoma Water
- We are not a small utility and drought restrictions are relatively uncommon in the Pacific Northwest
- We have established operating and capital reserves to address fluctuations
- Our current rate design provides revenue stability

## Seasonality and weather fluctuations
- Operating reserve to manage risk, revenue and expense fluctuations, and meet working capital needs, rate stabilization funds

Tacoma Water
- We have seasonal fluctuations and are able to forecast relatively accurately (generally with less than 10% variance), with minimal volatility in water demand/usage
- 60 days of budgeted operating expenses supports cash fluctuations
- Water’s Rate Stabilization Account (RSA) in the SDC Fund was created in 2009 using wholesale connection charges that were already deferred and must be used for capital expenditures
- As of 2013, the balance was about $35 million and has not been used to boost coverage since 2012, cash in the RSA is included as liquidity

## Age and type of infrastructure
- Capital reserves, consider inter-generational equity

Tacoma Water
- We have over $1.3 billion original cost plant in service to care for
- We do see some volatility in our capital planning (large projects or programs, regulatory requirements, future risks)
- Capital reserves are set to fund 1% of that original cost to help mitigate renewal and replacement

## Legal covenants and debt burden
- Bond covenants require adequate debt service coverage ratios that helps manage debt

Tacoma Water
- Our bond covenants require 1.25X coverage
- Our policy requires Senior coverage (as defined in bond covenants) above 1.50X and All-In coverage at 1.25X (or 1.00X during times of reserve spend-down)

*AWWA Rates & Charges Committee Project: Cash Reserve Policy Guidelines (2018)*
Questions?

Contact Jodi Collins (jlcollins@cityoftacoma.org) or Lyna Vo (lvo@cityoftacoma.org)
Volume Investment Reserve Fund

2024
• Established from the 2023 Rail Rate Policy
  • Section B.1.
    • Rates will be based on best estimates of rail volume. Operating revenue surpluses due to unanticipated rail volume growth may be applied to the Volume Investment Fund, a sub-fund of Tacoma Rail’s enterprise fund. To establish a balance to the fund, an initial $500,000 will be transferred to the sub-fund when created.
  • Section C.4.
    • Tacoma Rail maintains a Volume Investment Fund, a sub-fund of Tacoma Rail’s enterprise fund, that provides revenue requirement flexibility during times of unanticipated economic downturns or capital spending that may be used to offset the necessity of rate increases. Use of the fund will be limited to:
      a. Workforce stability to ensure staffing retention for service reliability and resiliency when rail volumes rebound after a downturn.
      b. Locomotive upgrades to sustain Tacoma Rail’s environmental leadership goals.
      c. Timely acquisition, replacement and upgrade of infrastructure and capital assets.
      d. Grant or debt matching opportunities.

• Current balance: $500K
Questions?

Contact Dan McCabe (dmccabe@cityoftacoma.org)