San Francisco Water Power Sewer
Services of the San Francisco Public Utilities Commission

# FUND BALANCE RESERVE POLICY

The San Francisco Charter Section 8B.125 requires the SFPUC to be a financial steward by establishing "rates, fees and charges at levels sufficient to improve or maintain financial condition and bond ratings at or above levels equivalent to highly rated utilities of each enterprise under its jurisdiction, meet requirements and covenants under all bond resolutions and indentures… and provide sufficient resources for the continued financial health (including appropriate reserves), operation, maintenance and repair of each enterprise, consistent with good utility practice." To most effectively meet this requirement, the SFPUC will utilize financial policies that foster financial stability, support fiscal discipline, and maintain credit ratings at or above levels equivalent to highly rated utilities. Institutionalized policies signal to rating agencies and the capital markets that an entity is well managed and committed to prudent financial practices.

The SFPUC faces a number of risks to revenue stability, including multi-year rate packages, drought and weather variability, and highly volumetric rates. To manage these risks and reduce susceptibility to emergency rate increases, the SFPUC will ensure adequate ratepayer protection in the form of a Fund Balance Reserve. For each enterprise, the SFPUC will adopt budgets and establish rates to maintain undesignated fund balances that provide sufficient capacity to bridge shortfalls in cash flow and cover unanticipated expenditures, while also considering ratepayer impact and fairness in compliance with the San Francisco Charter.

Specifically, for the time period covered in the SFPUC's Charter-mandated 10-Year Financial Plan, operating and capital budgets and rates will be proposed for adoption such that the Fund Balance Reserve totals **a minimum of 90 days or 25% of Operations & Maintenance Expenses** (including programmatic projects, and excluding debt service and revenue-funded capital) throughout the forecast period. Amounts in excess of the minimum will be considered for contingencies and rate stabilization.

In the event that Fund Balance Reserve exceeds 250 days or 68% of Operations & Maintenance Expenses, this fact will be brought to the Commission during the subsequent biannual budget process for consideration for uses, including:

- The reduction of future customer rate increases,
- Management of unanticipated one-time events (such as an earthquake or disaster), or any ongoing impairment to revenues (such as a drought or economic downturn), or
- Revenue-funded capital projects, which will reduce projected future debt issuance.

To monitor compliance with this policy, SFPUC Finance staff will present this metric to the Commission as part of the annual 10-Year Financial Plan and Quarterly Budget Status Report.

## CLEANPOWERSF FUND BALANCE RESERVE

While CleanPowerSF operates under much of the same legal and policy framework as the SFPUC's other utility services, the program is also uniquely reliant on a volatile power supply market, and faces competitive pressures that reduce its flexibility for rate increases. Moreover, CleanPowerSF's credit impacts not only lending terms, but also third-party power supply contracts, a key tool to mitigate market exposure. In the case of CleanPowerSF, the reserves need to be higher than in other Enterprises to account for the increased financial pressures and need for rate stabilization faced by power supply market volatility impacting open positions.

Consistent with this policy and with the San Francisco Charter, the SFPUC will adopt budgets and establish rates for CleanPowerSF that provide for adequate ratepayer protection in the form of a Fund Balance Reserve.

This Fund Balance Reserve for CleanPowerSF will be established at the following funding levels to mitigate short-term, unanticipated loss of revenues or increase in expenses; stabilize rates; and support the growth of the program:

- Operating Reserve Fund Minimum: equal to 150 days cash on hand (or 41%) of annual operating expenditures; and
- Operating Reserve Fund Target: equal to 180 days cash on hand (or 49%) of annual operating expenditures.

"Operating expenditures" are defined as all expenses in annual funds, including both operations and maintenance and personnel costs, as well as power supply costs and related expenditures, but excluding contributions to the reserve fund. The Fund Balance Reserve will be evaluated at least quarterly; the days cash on hand for Fund Balance Reserve minimum and target will be calculated using an annual basis of the twelve months operating expenditures in the fiscal year.

To allow for rate stabilization, budgets and rates may be set to draw down the Fund Balance Reserve to a minimum of 150 days cash on hand; further reductions should only occur due to unanticipated expenditure or revenue changes during the fiscal year. If the Fund Balance Reserve ends the fiscal year below the target of 180 days cash on hand, budgets and rates must be set to build back up to the target within three fiscal years.