

2018 Budget



MEMORANDUM

December 12, 2017

TO: Scott Hautala, General Manager
FROM: Jean M. Lane, Director of Finance
RE: 2018 Proposed Operations and Capital Budget

Background

The Director have had several meetings with myself and at a group to discuss the 2018 operations (revenue and expense) and 2018 capital budget.

The proposed budget has been presented to the Commission previously both a work session and regular meeting. Key elements have been discussed: including; impact of Xcel Energy termination with LEA, increasing revenues through increased rates in each of the four utilities (gas, steam, water, and electric), the allocation of expenses based on historical allocation methods and reviewing possible changes for the future, reduction of the workforce due to the impact of the Xcel Energy termination with LEA and also to right-size the utilities for the future. There are still many items which have not reached a conclusion and impact the operations and capital budgets of the HPU. As such the Commission has requested the 2018 operations and capital budget be flexible.

Attached please find the following documents:

- A cover worksheet by department with proposed revenue, expenses, net income (loss) along with additional one time revenue and expenses noted.
- Description of the rate increases
- Two impact worksheets detailing the proposed rate increases and impact to residential and commercial customers.
- 2018 proposed capital projects.
- Draft rate increases per type of services in policy form.
- A 10-year historical actual revenues and expenses with a detail of the 2018 proposed budget.

Items to note from the previous Commission presentation is (1) an addition of \$50,000 in the steam department for distribution repairs to steam heat lines and main holes; (2) increase in the transition costs for 2018 by \$150,000; (3) increase in the proposed capital to \$1,742,000 with priority given to safety, continuous operations, and efficiency. There is still a proposed loss of over (\$4.8 million) even with the LEA wind-down (RDF and Xcel payments) of \$5 million, rates increases and transitioning to a reduced workforce by the end of 2018. Even though there is an attached listing of 2018 proposed capital, I am not asking the Commission to approve the actual projects. It is my understanding each project will need to be approved separately by the Commission during the year and the amount of money is the suggested amount of capital which is needed in 2018 for safety, to keep operations in services, and for efficiency.

Recommendation

I recommend the Commission consider adopting an operating budget with a proposed net loss of (\$4,834,292) which includes proposed rate increases, LEA revenue from wind-down, one-time transition costs, and money allocated for capital projects.

JML/pil

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HIBBING PUBLIC UTILITIES
PROPOSED 2018 OPERATIONS AND CAPITAL BUDGET

DEPARTMENTS	ALLOCATED			2018 Proposed Expenses
	2018 Proposed Revenue	2018 Proposed Expenses	2018 Proposed Gain/(Loss)	
Electric	\$ 13,913,902	\$ 19,503,260	\$ (5,589,358)	\$11,716,374
Steam	\$ 3,063,173	\$ 5,651,496	\$ (2,588,323)	1,322,398
Plant	-	-		9,771,110
Gas	\$ 5,953,501	\$ 5,130,352	\$ 823,149	4,373,652
Water	\$ 2,467,605	\$ 2,102,865	\$ 364,740	1,760,805
Administration		\$ -		975,757
Warehouse		\$ -		218,986
Service Center		\$ -		95,554
Meter Maintenance		\$ -		198,520
Meter Reading		\$ -		250,066
Customer Service		\$ -		523,936
Transportation		\$ -		556,820
Engineering		\$ -		106,993
Safety/Environment		\$ -		429,502
Nonoperating	\$ 300,000	\$ -		87,500
Interest Expense	-	\$ 152,500		152,500
			\$ -	
Subtotal	\$ 25,698,181	\$ 32,540,473	\$ (6,842,292)	32,540,473
RDF/Xcel - May-18			\$ 5,000,000	
LEA Wind-down				
Subtotal Net Income (Net Loss)			\$ (1,842,292)	
Transition Costs			\$ (1,250,000)	
TOTAL NET INCOME/(NET LOSS)			\$ (3,092,292)	
Capital			\$ 1,742,000	

**HIBBING PUBLIC UTILITIES
2018 PROPOSED CAPITAL EXPENSES**

PRIORITIES:

#1 A - SAFETY ISSUES

#1 B - KEEP SYSTEMS OPERATIONS

#2 - INCREASED EFFICIENCIES

WIP-work in progress

	2018 PROPOSED BUDGET	PRIORITY RANK	2018 REVISED BUDGET	2018 ACTUAL EXPENSES	REMAINTING BALANCE	Project Number	GL ACCT Number
POWER PLANT							
Continuous Emission Monitoring	75,000	1A & B			-	18-201	1-1918-201
Power Plant Fire Protection	105,000	1A			-	18-202	1-1918-202
Vacuum Breaker Replacement 22.9K	70,000	1A & B			-	18-203	1-1918-203
Breaker Replacement 13.8kVA	55,000	1B			-	18-204	1-1918-204
Consolidated Control Room FEED Study	640,000	2			-	18-205	1-1918-205
Power Plant Projects	-	-			-		
Subtotal	945,000		-	-	-		
STEAM DISTRIBUTION							
Abatement & Installation of 25th Street 66C	120,000	1B & 2			-	18-401	1-1918-401
Steam Distribution Department Projects	-	-			-		
Subtotal	120,000		-	-	-		
ELECTRICAL DISTRIBUTION							
North Howard Alley Line Extension	60,000	1 B			-	18-301	1-1918-301
Rebuild 5th & 6th Ave East Alley	83,000	1 B			-	18-303	1-1918-303
Rebuild 7500 kVA Interconnect Sub X	17,000	1 B			-	18-304	1-1918-304
Rebuild 7500 kVA Beltline Substation	17,000	1 B			-	18-305	1-1918-305
Replace 22kV Breaker MP Hibbing Substation	85,000	1 B			-	18-306	1-1918-306
Electric Department Projects	-	-			-		
Subtotal	262,000		-	-	-		
WATER							
Water Treatment Plant Chemical Feed Auto	130,000	1 B			-	18-503	1-1918-503
Well 8 Rehabilitation	50,000	1 B			-	18-501	1-1918-501
Pressure filter Outer Skin Rehabilitation	50,000	1 B			-	18-502	1-1918-502
Water Department Projects	-	-			-		
Subtotal	230,000		-	-	-		
GAS							
Gas Mains & Extensions	20,000	1 B			-	18-601	1-1918-601
Travel Vac	18,500	1 B			-	18-701	1-1918-701
Gas Department Projects	-	-			-		
Subtotal	38,500		-	-	-		
TRANSPORTATION							
Trenching Track Propelled Machine	55,000	1 B			-	18-706	1-1918-706
Subtotal	55,000		-	-	-		
OFFICE							

10 new workstations (computers)	10,000	2	-	18-802	1-1918-802
ARMER Radio System	60,000	1 A & B		18-801	1-1918-801
Clarity Software upgrade	21,500	2		18-803	1-1918-803
Administration Department Projects	-	2	-		
Subtotal	91,500		-		

GRAND TOTAL \$ 1,742,000 \$ - \$ - \$ -

2018 Financial Overview

2018 Operations Plan is expected to result in a significant change in the Power Plant operations, no longer producing electricity for major customer Xcel Energy. Xcel Energy initiated the contract termination process. The first year termination payments from Xcel Energy will be used to pay off outstanding debt and remaining five year's payments to be used to improve the infrastructure of the utilities, per Commission directions.

Cost Reduction

HPU's largest cost items are electricity, power plant fuels (coal, wood, and gas), natural gas for the gas distribution utility, and personnel. Operational spending will have continual review for reductions. All employees - union and nonunion - will looking for new solutions to maximize the use of the workforce and minimize costs for the HPU customers. We take our mission to provide reasonable rates to our HPU customers seriously.

Increase in Rates for 2018

Even with cost reductions the HPU had a significant operating loss projected for 2018. The Commission deliberated and approved the below 2018 rates/base residential and commercial charge increases:

Electricity usage and base charge +5%

Steam usage and base charge +9%

Water usage and base charge +4%

Gas usage and base charge +2%

Based on research residential customers have been paying for more than their "fair share" for overall cost of utility services. Starting January 2018, commercial accounts will have an electrical base charge, an increased electric conservation improvement charge, and a water base charge calculated on meter size.

Due to the high steam distribution inefficiencies during the summer, summer steam usage will have a separate rate which is 20% higher than non-summer.

Each utility individually does not show a positive result even with the rate increases above. A reason why the rate increases are different are to close the gap for each utility. The Commission has discussed and will continue to discuss each utility's financial performance.

While there is no average residential customer that can be used for all scenarios, the estimated 2018 impact of these rate increases is \$8 to \$25/per average month. Due to the large difference in commercial customer's utilities, each commercial customer's monthly bill increase is specific to the customer.

It will be a challenging year of transition and exciting to develop a long-term plan for the customers and employees to achieve sustainable Hibbing Public Utilities success.