Memorandum

To: Philip A. Zavadil
City of Saint Paul, Alaska

Date: January 28, 2025

From: William Wilks, President
Wilks Consulting Services Inc.

RE: **Bulk Fuel Utility Rate Study**

Executive Summary

The City of Saint Paul ("City") engaged our firm to conduct a revenue requirement (rate study) for its Bulk Fuel Utility ("BFU"). The revenue requirement rate study method used herein is a forward-looking review of BFU's operating and capital cost (2025 thru 2030) to determine if the utility is operating at a surplus or deficiency and the percent adjustment to the throughput rate **"applied on an across-the-board"** basis, upward or downward, to achieve the utility's revenue requirement.

Our study concluded that based on 2025 approved budgeted operating and capital costs BFU is forecasted to operate by the end of 2025 at a revenue deficiency and a policy decision to leave rates at current levels throughout the forecast period may likely result in a negative unrestricted fund balance for the utility of $5.6 million, effectively using up more than all available unrestricted fund balance for the entire city.

In this revenue requirement rate study, we developed four rate scenario adjustments to the throughput rate to provide the city with a review of the BFU's financial health under each scenario. These scenarios are more fully explained in this technical memorandum but in summary these scenarios are:

1. **Do Nothing Scenario but Decrease Throughput Rate 10%:** This scenario effectively reduces the throughput rate currently in effect by 10% per year over the forecast period.
2. **Do Nothing Scenario:** This scenario effectively maintains the throughput rate at current levels throughout the forecast period.
3. **Just Cover Revenue Requirement Scenario:** This scenario effectively adjusts rates sufficient to cover just operating and capital costs of BFU but not enough to establish operating, capital and debt service reserves at levels used by financially healthy utilities that use a "Best Practices" rate approach.
4. **Best Practices Scenario: This** scenario effectively adjusts rates to not only cover operating and capital cost but to also build an operating reserve equivalent to a minimum and maximum of 30 to 45 days to cover cash operating expenses of the utility, and a capital reserve equal to 4% of the utility's plant in service. Lastly, this scenario proposes a debt service reserve sufficient to cover one year's bond principal and interest payments to lenders.

In this Executive Summary we provide a table for each of the above scenarios showing whether the three significant factors to a healthy utility are present. These factors are: one, that

proposed rates achieve the revenue requirement; two, that operating and capital reserves meet Best Practices; and three, that bond reserves are sufficient to cover the current year's bond principal and interest payment to lenders and that the bond coverage ratio typically found in bond covenants are at or above minimum required levels.

Summary of Do-Nothing but Decrease Throughput Rate 10%:

Chart Data	2025	2026	2027	2028	2029	2030
Throughput Diesel	$ 1.36	$ 1.22	$ 1.10	$ 0.99	$ 0.89	$ 0.80
Throughput Gasoline	$ 1.86	$ 1.67	$ 1.50	$ 1.35	$ 1.22	$ 1.10
Revenue Under Existing Rates	$ 3,538,589	$ 3,538,605	$ 3,538,622	$ 3,538,640	$ 3,538,658	$ 3,538,678
Revenue with Proposed Increase	$ 3,538,589	$ 3,462,845	$ 3,394,678	$ 3,333,331	$ 3,278,121	$ 3,228,434
Annual Expenditures	$ 3,661,480	$ 3,847,626	$ 4,050,935	$ 4,272,072	$ 4,565,109	$ 4,854,295
Net Cash Flow	$ (122,891)	$ (384,780)	$ (656,256)	$ (938,741)	$ (1,286,988)	$ (1,625,861)
Fund Balances						
Operating Fund	$ (2,713,710)	$ (2,148,491)	$ (2,799,847)	$ (3,719,791)	$ (5,006,780)	$ (6,632,641)
Capital Fund	$ 40,047	$ 80,495	$ -	$ -	$ 20,301	$ 39,915
Debt Reserve	$ 86,135	$ 86,135	$ 86,135	$ 91,036	$ 91,036	$ 91,036
Target Balance	$ 791,713	$ 829,289	$ 873,185	$ 1,007,623	$ 1,061,668	$ 1,152,150
Days of O&M	(280)	(211)	(261)	(329)	(421)	(530)
Target Range	30	30	30	30	30	30
	45	45	45	45	45	45
Rate Increases						
Annual Rate Increase	0.00%	-10.00%	-10.00%	-10.00%	-10.00%	-10.00%
Cumulative Rate Increase	0.00%	-10.00%	-19.00%	-27.10%	-34.39%	-40.95%
System Reinvestment	100%	100%	100%	100%	100%	100%
1	$ -	$ -	$ -	$ -	$ -	$ -

As mentioned earlier, this scenario simply decreases the throughput rate currently in effect by 10% each year over the forecast period. This scenario is the most egregious of the four scenarios reviewed because it does not meet any of the three criteria for a financially healthy utility (meet revenue requirement, achieve operating and capital reserves and achieve a minimum bond coverage ratio). In fact, net cash flow grows from a negative $122,891 in 2025 to a negative $1,625,861 by 2030 because of decreases in throughput rates and assuming a historical demand for fuel and applying reasonable inflationary factors to operating and capital costs. As shown above, throughput rates for diesel and gasoline in 2025 are $1.36 and $1.86 respectively and by the end of the forecast period are $0.80 for diesel and $1.10 for gasoline. Furthermore, this scenario may likely deplete unrestricted fund balance for not only the utility but for the entire city as shown in 2030 of a negative operating reserve of $6,632,64.

Summary of Do-Nothing Scenario:

Chart Data	2025	2026	2027	2028	2029	2030
Throughput Diesel	$ 1.36	$ 1.36	$ 1.36	$ 1.36	$ 1.36	$ 1.36
Throughput Gasoline	$ 1.86	$ 1.86	$ 1.86	$ 1.86	$ 1.86	$ 1.86
Revenue Under Existing Rates	$ 3,538,589	$ 3,538,605	$ 3,538,622	$ 3,538,640	$ 3,538,658	$ 3,538,678
Revenue with Proposed Increase	$ 3,538,589	$ 3,538,605	$ 3,538,622	$ 3,538,640	$ 3,538,658	$ 3,538,678
Annual Expenditures	$ 3,661,480	$ 3,847,626	$ 4,050,935	$ 4,272,072	$ 4,565,109	$ 4,854,295
Net Cash Flow	$ (122,891)	$ (309,021)	$ (512,313)	$ (733,432)	$ (1,026,451)	$ (1,315,617)
Fund Balances						
Operating Fund	$ (2,713,710)	$ (2,072,731)	$ (2,580,143)	$ (3,294,779)	$ (4,321,230)	$ (5,636,848)
Capital Fund	$ 40,047	$ 80,495	$ -	$ -	$ 20,301	$ 39,915
Debt Reserve	$ 86,135	$ 86,135	$ 86,135	$ 91,036	$ 91,036	$ 91,036
Target Balance	$ 791,713	$ 829,289	$ 873,185	$ 1,007,623	$ 1,061,668	$ 1,152,150
Days of O&M	(280)	(203)	(240)	(292)	(363)	(450)
Target Range	30	30	30	30	30	30
	45	45	45	45	45	45
Rate Increases						
Annual Rate Increase	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Cumulative Rate Increase	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
System Reinvestment	100%	100%	100%	100%	100%	100%
1	$ -	$ -	$ -	$ -	$ -	$ -

This scenario maintains the throughput rate at the current level with no increases over the forecast period. This scenario also does not meet any of the three criteria for a financially healthy utility (meet revenue requirement, achieve operating and capital reserves and achieve a minimum bond coverage ratio). In fact, net cash flow grows from a negative $122,891 in 2025 to a negative $1,315,617 by 2030 because of no rate increases, a historical demand for fuel and applying reasonable inflationary factors to operating and capital costs. Furthermore, a Do-Nothing scenario may also deplete unrestricted fund balance for not only the utility but for the entire city as shown in 2030 of a negative operating reserve of $5,638,848.

Summary of Cover the Revenue Requirement Scenario:

Chart Data	2025	2026	2027	2028	2029	2030
Throughput Diesel	$ 1.36	$ 1.91	$ 2.27	$ 2.67	$ 3.19	$ 3.71
Throughput Gasoline	$ 1.86	$ 2.61	$ 3.11	$ 3.65	$ 4.37	$ 5.08
Revenue Under Existing Rates	$ 3,538,589	$ 3,538,605	$ 3,538,622	$ 3,538,640	$ 3,538,658	$ 3,538,678
Revenue with Proposed Increase	$ 3,538,589	$ 3,847,629	$ 4,050,944	$ 4,272,054	$ 4,565,057	$ 4,854,262
Annual Expenditures	$ 3,661,480	$ 3,847,626	$ 4,050,935	$ 4,272,072	$ 4,565,109	$ 4,854,295
Net Cash Flow	$ (122,891)	$ 3	$ 9	$ (17)	$ (52)	$ (33)
Fund Balances						
Operating Fund	$ (2,713,710)	$ (1,763,707)	$ (1,758,798)	$ (1,740,019)	$ (1,740,071)	$ (1,740,105)
Capital Fund	$ 40,047	$ 80,495	$ -	$ -	$ 20,301	$ 39,915
Debt Reserve	$ 86,135	$ 86,135	$ 86,135	$ 91,036	$ 91,036	$ 91,036
Target Balance	$ 791,713	$ 829,289	$ 873,185	$ 1,007,623	$ 1,061,668	$ 1,152,150
Days of O&M	(280)	(173)	(164)	(154)	(146)	(139)
Target Range	30	30	30	30	30	30
	45	45	45	45	45	45
Rate Increases						
Annual Rate Increase	0.00%	40.79%	19.06%	17.41%	19.65%	16.21%
Cumulative Rate Increase	0.00%	40.79%	67.62%	96.81%	135.48%	173.65%
System Reinvestment	100%	100%	100%	100%	100%	100%
1	$ -	$ -	$ -	$ -	$ -	$ -

This scenario meets two of three factors needed to achieve a financially healthy utility as shown under Net Cash Flow in the table above just being barely sufficient to cover operating and

capital reserves, and the debt service reserve and ratio to cover typical lender requirements on bond instruments. The missing factor being virtually no operating reserve is never achieved, and further, capital reserve is likely not sufficient to meet its intended purpose. The operating reserve should be equivalent to a minimum of 30 to a maximum 45 days of cash operating expense to cover cash working capital requirements. The table above shows the number of days of coverage in 2025 at a negative 280 days and by the end of the forecast period slightly improves to a negative 139 days. This scenario shows the required rate increases year-over-year to achieve two of the three required factors for a financially healthy utility beginning in 2025 at a 40.79% increase in the throughput rate with cumulative rate increases by 2030 of 173.65%.

Summary of "Best Practices" Scenario:

Chart Data	2025	2026	2027	2028	2029	2030
Throughput Diesel	$ 1.36	$ 1.90	$ 2.66	$ 3.67	$ 5.06	$ 5.31
Throughput Gasoline	$ 1.86	$ 2.60	$ 3.64	$ 5.02	$ 6.93	$ 7.27
Revenue Under Existing Rates	$ 3,538,589	$ 3,538,605	$ 3,538,622	$ 3,538,640	$ 3,538,658	$ 3,540,297
Revenue with Proposed Increase	$ 3,538,589	$ 3,841,644	$ 4,265,915	$ 4,830,191	$ 5,608,886	$ 5,751,916
Annual Expenditures	$ 3,661,480	$ 3,847,626	$ 4,050,935	$ 4,272,072	$ 4,565,109	$ 4,854,295
Net Cash Flow	$ (122,891)	$ (5,982)	$ 214,980	$ 558,120	$ 1,043,777	$ 897,621
Fund Balances						
Operating Fund	$ (2,713,710)	$ (1,769,692)	$ (1,549,811)	$ (972,896)	$ 70,881	$ 563,412
Capital Fund	$ 40,047	$ 80,495	$ -	$ -	$ 20,301	$ 445,005
Debt Reserve	$ 86,135	$ 86,135	$ 86,135	$ 91,036	$ 91,036	$ 91,036
Target Balance	$ 791,713	$ 829,289	$ 873,185	$ 1,007,623	$ 1,061,668	$ 1,152,150
Days of O&M	(280)	(174)	(144)	(86)	6	45
Target Range	30	30	30	30	30	30
	45	45	45	45	45	45
Rate Increases						
Annual Rate Increase	0.00%	40.00%	40.00%	38.00%	38.00%	5.00%
Cumulative Rate Increase	0.00%	40.00%	96.00%	170.48%	273.26%	291.93%
System Reinvestment	100%	100%	100%	100%	100%	100%
1	$ -	$ -	$ -	$ -	$ -	$ -

This scenario at the proposed rate increases achieves all three factors for a financially healthy utility. Notice that net cash flow becomes positive by 2017 of $214,980 and the operating reserve goes positive in 2029 after eliminating the large negative beginning fund balance in 2025 of $2,713,710. By 2030 the days of O&M reach a healthy level of 45 days of cash operating expense on hand, and further, the capital reserve, bond debt service coverage and bond coverage ratio are all at ideal levels under this scenario.

As stated in the introduction section of the Executive Summary, we noted that this rate study (revenue requirement) approach applied rate increases on an across-the-board basis for fuel throughput to all customer classes. This rate study is the foundational study used by two other rate studies that look to rate adjustments on other than on an across-the-board basis. These studies are a cost-of-service and rate design study. While the cost-of-service study analyzes the service cost to each customer class (i.e. residential verses commercial customers) to determine rate equity by customer class as a basis to adjust rates, the rate design study is based on adjustment to rates by customer class based on policy directives to achieve desired results, For example many telecommunication companies offer residential landline and cell phone service to "at need customers" significantly below a typical residential phone rate to ensure this class of customers have phone service for public safety needs. These additional studies may offer the city a panacea to adjusting rates on an across-the-board basis when using only a revenue requirement approach.

End of Executive Summary

Technical Memorandum

This memorandum documents the objectives, assumptions, findings, and recommendations for the BFU rate study for the City of Saint Paul, Alaska ("City"). Major study elements include:

- Evaluation of Financial Policies
- Development of Capital Financing Strategies
- Assessment of Revenue Needs
- Forecast of Rate Adjustments

As noted above the BFU rate study model is based on assumptions and in some cases placeholders where management can further evaluate and modify inputs if desired. The rate study models allow for adjustments to be made to the financial assumptions and when made immediately provide impact on utility rates and financial position for each year of the forecast period for the BFU.

Further details can be found in the following notebook appendices:

- Appendix A – Bulk Fuel Utility Model Scenarios

A. FINANCIAL POLICIES

To establish adequate utility rates, a utility must define its benchmark(s) for financial performance. Typically, several different standards are necessary to satisfy all financial objectives. Like any business, a municipal utility requires certain minimum levels of cash reserves to operate; these reserves address variability and timing of expenditures and receipts, as well as occasional disruptions in activities, costs or revenues. In addition, as a public service provider, a municipal utility has a commitment to provide an essential service at a certain standard. Therefore, protection against financial disruption is very important.

This section recommends best practice financial policies that the City might consider in the context of this mission. These policies form the foundation of utility management and, with routine application, can act as overarching guidelines for consistent decision making. The following policies are evaluated:

- Self-Supporting Enterprise Fund
- Cash Reserves
- System Reinvestment Funding

1. SELF SUPPORTING ENTERPRISE FUND

A fund is an accountability unit used to maintain control over resources segregated for specific activities or objectives. Proprietary, or enterprise, funds report services for which a utility charges customers a fee. These funds are generally self-supporting, receiving revenues for payment of services on a user fee basis as opposed to property taxes or other general fund revenue sources.

Conceptually, and by accounting convention, each utility is divided into two primary activity centers: operating and capital. For financial forecasting purposes, operating costs tend to be ongoing and predictable, while capital costs are highly variable in comparison. In addition, each of these has specific funding sources and mechanisms available to them.

When determining the amount of rate revenue required, we necessarily separate these cost centers to reflect these differences. Note, however, that there is some interaction between the two centers – for example, capital projects may be funded through a policy of system reinvestment funding from rates, direct rate funding, or through debt issuance. In each case, rates are paying for capital projects. These demands on operational resources (primarily rates) thus become expenditures from that perspective.

This ideal separation is illustrated in the exhibit below.

Capital Account	Operating Account
Sources of Funding	**Sources of Funding**
Debt Proceeds	User Rates
Transfers from Operations	Interest Earnings
Interest Earnings	Miscellaneous Service Fees
Grants	
Miscellaneous Proceeds	**Uses**
	Operating & Maintenance Expenses
Uses	Administrative Expenses
Capital Project Funding	Rate-Funded Capital
	System Reinvestment (R&R) Funding
	Debt Service
	Addition to Operating Reserves

Though virtually all utilities maintain reserves in some form, the segregation of those reserves can vary greatly between utilities. While a complete delineation of the functions of reserves is not always documented, the underlying purposes remain valid components of reserve management. Further, as reserve objectives are identified, the mechanisms for managing, using and replenishing those reserves become important elements of financial management.

When evaluating reserve levels and objectives, it is vital to recognize that the value of reserves lies in their use. It goes without saying that a strategy that deliberately avoids the use of reserves negates their purpose. Fluctuations of reserve levels merely indicate that the system is working, while lack of variation strongly suggests that the reserves are, in fact, unnecessary.

The City maintains a single enterprise fund for its BFU in which operating, and capital-related cash deposits and withdrawals are made. No specific policy is in place to establish the desired level of cash balances. That said, the rate strategy developed for this study presume that the BFU will operate as a self-supporting enterprise fund, with minimum operating cash balances established for the utility (discussed further below).

2. OPERATING (WORKING CAPITAL) RESERVES

An operating reserve is essentially a minimum unrestricted fund balance used to accommodate the short-term cycles of revenues and expenses. For rate modeling, it would be a

minimum balance that is maintained through rate increases as necessary; for budgeting, it would be a minimum ending balance for the utility operating fund; and for accounting, the balance would simply appear as part of unrestricted cash and investments.

Operating or working capital reserves provide a "cushion" that can be used to cover cash balance fluctuations. These reserves are intended to address both anticipated and unanticipated changes in revenues and expenses. Examples of the former include billing and receipt cycles, payroll cycles, and other payables; examples of the latter include droughts, economic cycles, and other periods of low demand.

Target funding levels are often characterized in terms of a recommended number of days of cash operating and maintenance expenses (O&M), with the minimum number of days varying with the expected risk of unanticipated needs – these are likely to vary based on the relative volatility of revenues and expenses.

Industry practice ranges from 30 days to 120 days of O&M, with the lower end more appropriate for utilities with very stable revenue streams and the higher end more appropriate for utilities with significant seasonal variations. This study incorporates a minimum and maximum balance in the operating account equal to 30 and 45 days respectively of annual operating & maintenance (O&M) expense sustained from rate revenue for the BFU. These target levels are consistent with industry practices.

The target balance should be evaluated as of June 30 of each fiscal year, with the balance expected to vary during the course of a year. In any year where the cash balance exceeds the target, we recommend transferring the excess to the capital account to help pay for capital projects.

3. CAPITAL CONTINGENCY

In addition to protecting against variations in operating costs and revenues, it is prudent to establish and maintain a capital contingency reserve to meet unexpected emergency capital outlays. While it would be impractical to reserve against major system-wide failures such as earthquake or other catastrophic events, it is reasonable and prudent to identify and quantify possible failures of individual system components. There are several methods used in the industry to set the level of these types of reserves, including:

- Percentage of Utility Plant: As a rule of thumb, a utility may elect to hold a contingency reserve equal to a percentage of the total costs of its fixed assets, usually 1% to 4% of asset original cost depending on the remaining life of the utility's assets.
- Most Costly Piece of Equipment: A utility may predict the cost of replacing the most expensive piece of equipment or facility that each utility relies on, such as its largest or most powerful pump, and reserve an amount equal to the cost of a major repair of that facility.
- Average Annual Cost of Capital Program: Alternatively, a utility may use a percentage of its 5- or 10-year capital program or set the reserve equal to the average annual costs of it capital program.
- Use of Replacement Reserves: Essentially, the contingency reserve becomes a minimum balance in the utility capital fund. If a system reinvestment funding policy has been established, those cash resources can also be relied on for this purpose (nesting system reinvestment funding monies within the contingency reserve). Again, this would avoid the need for multiple reserve policies when they can serve overlapping purposes.

- Reliance on Other Reserve Resources: Many cities maintain "rainy day" funds as hedges against emergencies or unusual circumstances. In such cases, extending the applicability of these funds to utility emergency repairs could preclude the need for a separate utility contingency.

While the rate strategy for these studies does not force funding of a capital contingency, varying levels of cash reserves are generated for each utility based on interest earnings of excess operating reserves. We suggest the City evaluate its capital funding resources on a regular basis and consider implementing this policy in conjunction with system reinvestment funding over time.

4. SYSTEM REINVESTMENT FUNDING

System reinvestment funding from rates provides for: (1) ongoing system integrity through reinvestment in the system – replacing physical assets with cash assets; (2) rate stability through regular accumulation of cash toward funding future replacement costs; and (3) charging customers commensurate with their consumption of system facilities.

Each year, system assets lose value, and as they lose value, they are moving toward eventual replacement. That accumulating loss in value and future liability is measured for financial purposes as annual depreciation expense, which is based on the original cost of the asset over its anticipated useful life. While this expense reflects the consumption of the existing asset at its original investment, the replacement of that asset will likely cost much more, factoring in inflation and construction conditions. Therefore, the added annual replacement liability is even greater than the recorded annual depreciation. Given the integrated nature of system assets, it is likely that multiple assets will have to be replaced concurrently. This further exacerbates the issue of capital investment "spikes". It is prudent to develop a long-term replacement funding strategy for each system to mitigate the impacts to ratepayers during these periods of substantial system investment.

System reinvestment funding specifically addresses the concept of funding repair and replacements (R&R) through a regular and predictable rate provision. By establishing a steady funding mechanism, a system reinvestment funding program can then be structured, which takes into account the defined funding source, accumulation of funds when funding exceeds near term needs, and augmentation of funds (for example through debt) when R&R needs exceed available cash resources. A common approach of municipal utilities is to establish a policy of system reinvestment funding through rates using depreciation expense as the benchmark for the appropriate level of funding. Depreciation is a commonly used accounting measure of the decline in asset value attributable to the wear and tear associated with routine use. Depreciation expense is recorded as a system expense for purposes of financial reporting. However, because depreciation expense is a non-cash expense, it generally does not appear in cash-based budgets, thus potentially disguising a very real and accumulating cost of the systems.

Collecting the amount of annual depreciation expense through rates provides a stable funding source for capital expenditures, especially those related to repair and replacement of existing system plant. It is important to note that depreciation is not equal to the future replacement cost of the utility systems but serves simply as a starting point for addressing long-term replacement needs. As noted previously, actual system replacement costs will be significantly higher than the cost originally incurred to build the systems.

The City's historical practice has been to fund capital needs through a combination of grants, loans, and "pay-as-you-go" funding from rates. Rates have not been set at a level sufficient to fund depreciation. With these updated rate studies, we proposed setting rates for the BFU to fully fund

depreciation. We suggest the City evaluate its capital funding resources on a regular basis and consider phasing in this policy over time. It is worth noting that as state grant and low-cost loans are becoming more and more competitive, eligibility criterion are expanding to include review of best management practices such as system reinvestment funding policies.

5. CUMULATIVE IMPACT OF FISCAL POICIES

Satisfying all these policy objectives might seem daunting at first, but the outcome is that multiple benchmarks overlap, resulting in the simultaneous achievement of multiple objectives within the same level of rates. For example, the policy for system reinvestment funding through rates serves several beneficial purposes: it provides a cash resource to the capital accounts that helps build capital contingency reserves; it contributes to the cash funding of capital, helping to maintain healthy debt-to-equity ratios; and it helps to avoid rate spikes during periods of significant replacement needs.

Each criterion provides a different perspective on how much revenue is appropriate and satisfying them all generally results in higher rates than if only a single standard is considered. However, this approach reduces financial risk and increases financial stability – any near-term increases that result will help to promote more stable, and lower, long-term rates.

In summary, utility reserves are intended to absorb fluctuation in revenues or expenditures without abrupt rate impacts. As reserve levels vary, a policy structure can define the mechanisms for regulating those levels and returning them to intended targets. The general objectives of these and other policy elements are stable and predictable rates and funding sources, along with equitable recovery of costs from customers as they are being incurred.

B. STUDY ASSUMPTIONS

In addition to the financial policies summarized above, the following major assumptions were used in preparing this analysis:

- Study period includes fiscal years (FY) 2025 budget through FY 2030.
- Revenue under existing rates is assumed to remain flat over the study period.
- FY 2025 beginning cash balances as reported in the City's FY 2023 CAFR for the operating and capital accounts. Interest earnings rate on available cash balances are estimated at 1.0% per year.
- Operating and maintenance (O&M) expenditures are based on the FY 2025 operating budget, escalated by 5.33% annual inflation, except for employee labor and benefits, which are escalated at 3.22% and 5.68% respectively.
- The BFU has an outstanding debt of $86,135 per year consisting of principal and interest payments for at least the remainder of the forecast period.
- Capital programs were provided by City staff in the current day dollars and escalated at 3.00% per year to the date of anticipated construction for each project.
- Future years' debt service incorporates the impact of the proposed capital financing plan. State loans assume an interest rate of 1.5% and a 20-year repayment term and are assumed to fund capital needs in excess of grant and cash funding.

C. REVENUE REQUIREMENT ANALYSIS

The revenue requirement analysis determines the total amount of revenue needed each year of the study period to pay operating & maintenance costs, capital-related costs, and impacts of financial policies. A capital funding analysis, revenue needs assessment, rate forecast, and reserves analysis was prepared for BFU. Forecasted total financial requirements were compared against forecasted total rate revenue under existing rates to determine annual and cumulative rate adjustments needed to ensure financial sustainability over time. Results are summarized below for BFU.

a) Capital Financing Strategy

The city has identified approximately $3.64 million (escalated) in capital improvement for the replacement projects planned for construction FY 2026 through FY 2030 for the BFU. Capital spending levels vary from year to year, with the largest project (Bulk Fuel Facility/Dispensing Tankage system - $1.39 million) occurring in FY 2028. The capital funding plan assumes the exclusive use of capital fund balance. Exhibit 1 summarizes the BFU capital funding analysis.

Exhibit 1: Capital Financing Plan – BFU

Capital Funding	2025	2026	2027	2028	2029	2030
Total Capital Projects	**$ -**	**$ 365,650**	**$ 493,319**	**$ 2,602,346**	**$ 88,973**	**$ 91,642**
Grants & Developer Donations	-	365,650	291,748	2,192,573	-	-
Use of Capital Fund Balance	-	-	128,660	57,227	88,973	91,642
ADEC & Other Loans	-	-	72,911	352,546	-	-
Direct Rate Funding	-	-	-	-	-	-
Total Funding Sources	**$ -**	**$ 365,650**	**$ 493,319**	**$ 2,602,346**	**$ 88,973**	**$ 91,642**

b) Revenue Needs Assessment

BFU's revenue requirement (summarized in Exhibit 2) reflect the assumptions and utility information described herein. As shown, forecasted **revenues under existing rates** are not sufficient to meet the needs of the utility over the study period.

Exhibit 2: Revenue Needs Assessment – BFU "No Rate Increase Scenario"

Revenue Requirements	2025	2026	2027	2028	2029	2030
Revenues						
Rate Revenues Under Existing Rates	$ 757,597	$ 757,597	$ 757,597	$ 757,597	$ 757,597	$ 757,597
Non-Rate Revenues	2,780,992	2,781,008	2,781,025	2,781,042	2,781,061	2,781,081
Total Revenues	**$ 3,538,589**	**$ 3,538,605**	**$ 3,538,622**	**$ 3,538,640**	**$ 3,538,658**	**$ 3,538,678**
Expenses						
Cash Operating Expenses	$ 3,535,298	$ 3,721,443	$ 3,917,440	$ 4,123,809	$ 4,341,103	$ 4,569,901
Existing Debt Service	86,135	86,135	86,135	86,135	86,135	86,135
New Debt Service	-	-	-	4,901	28,597	87,206
Rate-Funded CIP	-	-	-	-	-	-
Additions to Operating Reserve	-	-	-	-	-	-
Total Expenses	**$ 3,661,480**	**$ 3,847,626**	**$ 4,050,935**	**$ 4,272,072**	**$ 4,565,109**	**$ 4,854,295**
Maximum Net (Cash or Coverage)	**$ (122,891)**	**$ (309,021)**	**$ (512,313)**	**$ (733,432)**	**$ (1,026,451)**	**$ (1,315,617)**
Annual Rate Adjustment	**0.00%**	**0.00%**	**0.00%**	**0.00%**	**0.00%**	**0.00%**
Cumulative Rate Increase	**0.00%**	**0.00%**	**0.00%**	**0.00%**	**0.00%**	**0.00%**
Sample Throughput Rate	$1.36	$1.36	$1.36	$1.36	$1.36	$1.36
Rate Revenues After Rate Increase	$ 757,597	$ 757,597	$ 757,597	$ 757,597	$ 757,597	$ 757,597
Net Cash Flow After Rate Increase	(122,891)	(309,021)	(512,313)	(733,432)	(1,026,451)	(1,315,617)
Coverage After Rate Increases	0.04	(2.12)	(4.39)	(6.79)	(9.32)	(11.97)

Without any rate increase the BFU is expected to have a revenue deficiency in 2025 of $122,891 and a .04 debt service coverage ratio. Typically, debt service coverage ratios need to be at least 1.25 for utilities to meet bond covenants typically contained in revenue bond lending instruments, thereby making a "No Rate Adjustment" scenario an unlikely option for the city given its existing and proposed future bonding requirements for the BFU.

c) Rate Adjustment Options and Recommendations

Exhibit 3a presents the calculated rate increase to generate the required revenue that will allow the BFU to maintain its debt service cover ratio and to cover operating and maintenance cost. Exhibit 3b presents the calculated rate increases to allow the utility to cover its debt service ratio, have a positive cash flow and meet all of its revenue requirement (i.e. operating, capital and debt service reserves) by the end of the forecast period.

Exhibit 3a: Rate Adjustment Recommendation Option 1 – Debt Service Coverage Ratio Necessity

Revenue Requirements	2025	2026	2027	2028	2029	2030
Revenues						
Rate Revenues Under Existing Rates	$ 757,597	$ 757,597	$ 757,597	$ 757,597	$ 757,597	$ 757,597
Non-Rate Revenues	2,780,992	2,781,008	2,781,025	2,781,042	2,781,061	2,781,081
Total Revenues	**$ 3,538,589**	**$ 3,538,605**	**$ 3,538,622**	**$ 3,538,640**	**$ 3,538,658**	**$ 3,538,678**
Expenses						
Cash Operating Expenses	$ 3,535,298	$ 3,721,443	$ 3,917,440	$ 4,123,809	$ 4,341,103	$ 4,569,901
Existing Debt Service	86,135	86,135	86,135	86,135	86,135	86,135
New Debt Service	-	-	-	4,901	28,597	87,206
Rate-Funded CIP	-	-	-	-	-	-
Additions to Operating Reserve	-	-	-	-	-	-
Total Expenses	**$ 3,661,480**	**$ 3,847,626**	**$ 4,050,935**	**$ 4,272,072**	**$ 4,565,109**	**$ 4,854,295**
Maximum Net (Cash or Coverage)	**$ (122,891)**	**$ (309,021)**	**$ (512,313)**	**$ (733,432)**	**$ (1,026,451)**	**$ (1,315,617)**
Annual Rate Adjustment	**0.00%**	**40.79%**	**19.06%**	**17.41%**	**19.65%**	**16.21%**
Cumulative Rate Increase	**0.00%**	**40.79%**	**67.62%**	**96.81%**	**135.48%**	**173.65%**
Sample Throughput Rate		$0.00	$0.00	$0.00	$0.00	$0.00
Rate Revenues After Rate Increase	$ 757,597	$ 1,066,621	$ 1,269,919	$ 1,491,012	$ 1,783,996	$ 2,073,181
Net Cash Flow After Rate Increase	(122,891)	3	9	(17)	(52)	(33)
Coverage After Rate Increases	0.04	1.47	1.56	1.72	2.60	3.30

Fund Balances - Projected Y-E	2025	2026	2027	2028	2029	2030
Operating Reserves	$ (2,713,710)	$ (1,763,707)	$ (1,758,798)	$ (1,740,019)	$ (1,740,071)	$ (1,740,105)
Capital Reserves	40,047	80,495	-	-	20,301	39,915
Debt Reserves	86,135	86,135	86,135	91,036	91,036	91,036
Total	**$ (2,587,528)**	**$ (1,597,077)**	**$ (1,672,663)**	**$ (1,648,983)**	**$ (1,628,735)**	**$ (1,609,154)**
Combined Minimum Target Balance	*$ 646,427*	*$ 676,353*	*$ 712,195*	*$ 838,151*	*$ 883,266*	*$ 964,346*

As shown in Exhibit 3a above utility cash flow is negative after an initial rate increase in 2026 and bond coverage ratio is 1.47 which is above the typical minimum coverage ratio of 1.25. We believe Option 3.a. represents the barebones minimum rate adjustments the city should consider in order to maintain its debt service coverage for future revenue bond considerations for capital projects.

Exhibit 3b: Rate Adjustment Recommendation Option 2 – Debt Service Coverage Ratio and Positive Cash Flow scenario

Revenue Requirements	2025	2026	2027	2028	2029	2030
Revenues						
Rate Revenues Under Existing Rates	$ 757,597	$ 757,597	$ 757,597	$ 757,597	$ 757,597	$ 757,597
Non-Rate Revenues	2,780,992	2,781,008	2,781,025	2,781,042	2,781,061	2,782,700
Total Revenues	**$ 3,538,589**	**$ 3,538,605**	**$ 3,538,622**	**$ 3,538,640**	**$ 3,538,658**	**$ 3,540,297**
Expenses						
Cash Operating Expenses	$ 3,535,298	$ 3,721,443	$ 3,917,440	$ 4,123,809	$ 4,341,103	$ 4,569,901
Existing Debt Service	86,135	86,135	86,135	86,135	86,135	86,135
New Debt Service	-	-	-	4,901	28,597	87,206
Rate-Funded CIP	-	-	-	-	-	-
Additions to Operating Reserve	-	-	-	-	-	-
Total Expenses	**$ 3,661,480**	**$ 3,847,626**	**$ 4,050,935**	**$ 4,272,072**	**$ 4,565,109**	**$ 4,854,295**
Maximum Net (Cash or Coverage)	**$ (122,891)**	**$ (309,021)**	**$ (512,313)**	**$ (733,432)**	**$ (1,026,451)**	**$ (1,313,998)**
Annual Rate Adjustment	**0.00%**	**40.00%**	**40.00%**	**38.00%**	**38.00%**	**5.00%**
Cumulative Rate Increase	**0.00%**	**40.00%**	**96.00%**	**170.48%**	**273.26%**	**291.93%**
Sample Throughput Rate	$1.36	$1.90	$2.66	$3.67	$5.06	$5.31
Rate Revenues After Rate Increase	$ 757,597	$ 1,060,636	$ 1,484,890	$ 2,049,149	$ 2,827,825	$ 2,969,216
Net Cash Flow After Rate Increase	(122,891)	(5,982)	214,980	558,120	1,043,777	897,621
Coverage After Rate Increases	0.04	1.40	4.06	8.20	14.72	13.73

Fund Balances - Projected Y-E	2025	2026	2027	2028	2029	2030
Operating Reserves	$ (2,713,710)	$ (1,769,692)	$ (1,549,811)	$ (972,896)	$ 70,881	$ 563,412
Capital Reserves	40,047	80,495	-	-	20,301	445,005
Debt Reserves	86,135	86,135	86,135	91,036	91,036	91,036
Total	**$ (2,587,528)**	**$ (1,603,062)**	**$ (1,463,676)**	**$ (881,860)**	**$ 182,218**	**$ 1,099,453**
Combined Minimum Target Balance	*$ 646,427*	*$ 676,353*	*$ 712,195*	*$ 838,151*	*$ 883,266*	*$ 964,346*

As shown in Exhibit 3b his scenario at the proposed rate increases achieves all three factors for a financially healthy utility. Notice that net cash flow after rate increases becomes positive by 2027 of $214.980 and the operating reserve goes positive in 2029 after eliminating the large negative beginning fund balance in 2025 of $2,713,710. By 2030 the days of O&M reach a healthy level of 45 days of cash operating expense and hand, and further, the capital reserve, bond debt service coverage and bond coverage ratio are all at ideal levels under this scenario.

As noted earlier we believe, at a minimum, that the city give consideration to rate increases as shown in Exhibit 3a above in order to maintain debt service coverage. Ideally, the city should strive to set rates as shown in exhibit 3.b. above to achieve all three factors necessary to have a

financially health utility. Failure to meet debt service coverage requirements places current revenue bonds at risk and subject to being required to be paid back

SUMMARY

In developing the rate model and associated scenarios for your BFU we have discussed herein the underlying financial assumptions and the impact those assumptions have on revenue needs and rate adjustments. We understand that adjusting bulk fuel rates at these levels may impose rate shock for customers, that is why we are proposing a five-year phase in approach to mitigate customer impact while at the same time moving forward to achieve a healthy utility by 2030. Not taking action to adjust rates now may likely result in even higher rates in the future, or no action on rates at all may likely compromise the financial health of the entire city.

We have also addressed herein alternative rate studies (Cost-of-Service and Rate Design Studies) to adjust rates on other than on an across-the-board basis when using a Revenue Requirement rate study to adjust rates. Further, the Revenue Requirement study is foundational to building these alternative rate adjustment models so that rates based on either cost-of-service or rate design ultimately achieve the utility's revenue requirement. Consideration to develop these alternative studies gives the city an opportunity to adjust rates on either service cost or alternatively on public policy considerations.

Finally, Wilks Consulting Services Inc. recommends regular review of all underlying assumptions and an update of the rate analysis as necessary to meet the financial obligations of the utility and the city.