



# City of San Antonio

## Agenda Memorandum

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**Agenda Item Number:** 3

**Agenda Date:** October 18, 2023

**In Control:** Governance Committee Meeting

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**DEPARTMENT:** Office of the City Manager

**DEPARTMENT HEAD:** Ben Gorzell Jr., Chief Financial Officer

**COUNCIL DISTRICTS IMPACTED:** Citywide

**SUBJECT:** Council Consideration Request by Councilmember Melissa Cabello Havrda (District 6) on CPS Energy.

**SUMMARY:**

On September 12, 2023, Councilmember Melissa Cabello Havrda issued a City Council Consideration Request (CCR) requesting to return 2% to 3% of the City's 14% of gross revenues payment from CPS Energy back to CPS Energy in order to improve CPS Energy's resiliency and reliability. Additionally, the CCR states that the conversation should focus on staving off rate increases for a minimum of five years.

**BACKGROUND INFORMATION:**

The City of San Antonio has owned CPS Energy since 1942. Under our ownership model, the San Antonio community has benefited tremendously with an electric and gas utility with strong reliability and competitive rates coupled with a return to the City via a General Fund transfer that supports basic services for the citizens of San Antonio and benefits for the greater San Antonio area.

Under the CPS Energy bond indenture, the City receives a payment of up to 14% of Gross Revenues as the owner of CPS Energy. This payment from CPS Energy is comparable to a private utility from the perspective that it represents compensation for use of the public right-of-way, a payment in-lieu-of property taxes and a return to its shareholders. In the case of CPS Energy, the shareholders are the citizens of San Antonio who benefit from paying competitive rates to CPS Energy but rather than profits being generated to private investors, the return is paid to San Antonio via the General Fund transfer and used to fund basic services for the owners of the utility, the citizens of San Antonio. These basic city services include police, fire, emergency medical services, animal care, libraries, parks, street maintenance, code compliance, and many more.

The CCR proposes to reduce the City Payment rate to 12% or 11% of Gross Revenues from the current 14% rate. Based on the FY 2024 Adopted Budget, a reduction in the City Payment rate of 2% or 3% equates to approximately \$60 million or \$90 million, respectively, in recurring General Fund revenue. If such a reduction in the rate of City Payment were adopted, a reduction in recurring General Fund expenses (services) would be required in the same amount to correspond to the reduction in General Fund revenues. To implement such a substantial reduction, City staff would request feedback in a B-Session from City Council on areas for elimination or substantial reduction within the General Fund.

With respect to CPS Energy rates, the Board of Trustees formally forwards recommendations for adjustments in electric and gas rates to the City Council who has final authority. The City has a Supervisor of Public Utilities position with the responsibility to review and make recommendations to the City Manager and Mayor & City Council on requests to adjust rates. The position of Supervisor of Public Utilities is combined with that of the City's Chief Financial Officer and is supported by staff within the Public Utilities Division of the Finance Department. The comprehensive review led by the Public Utilities Supervisor focuses on the business case justification to support a rate adjustment with a focus on objectives such as supporting the service reliability, competitiveness of rates, and financial health of CPS Energy.

A business case justifying a rate increase is seeking recurring additional revenue to support the business needs of the CPS Energy system. The business case outlines the justification for the rate case which can be driven by many factors such as operational costs, capital investment levels, system improvements, inflationary pressures, financial metrics, and many other factors.

In January 2022, City Council approved the last rate adjustment for CPS Energy which included the following: 3.85% base rate increase; and recovery through the fuel adjustment of approximately 0.8% for Winter Storm Uri costs. At that time, a forecast was provided which included projected rate increases of 5.5% in CPS Energy's Fiscal Year 2025 and 2027, respectively. Each rate increase of 5.5% would generate approximately \$110 million in additional revenues for CPS Energy. As noted above, a reduction in the rate of City Payment of 3% is equivalent to approximately \$90 million. As such, based on a 5.5% rate increase, this reduction in City Payment would not fully offset a 5.5% rate increase in 2025 nor address at all the proposed rate increase in FY 2027. Additionally, such a reduction in the rate of City Payment would also have to be coupled with a corresponding reduction in the General Fund expenses.

#### Alternative Approach

The intent of the CCR focused on several objectives: supporting the business requirements of CPS Energy to include resiliency and reliability projects; re-investing a portion of the City's payment from CPS Energy into key projects at CPS Energy while not significantly impacting city services; and lowering the amount of future rate increases. In collaboration with Councilwoman Cabello Havrda, City staff explored alternatives focusing on the objectives of the CCR. The following is a recommended alternative.

In FY 2023, the City's financial policies were updated to include the following related to City's Payment from CPS Energy: "Annually assess the City's payment from CPS Energy to determine the portion, if any, deemed to be unusual, out of the ordinary, and one-time in nature, and make recommendations for that amount taking into consideration factors such as the City's overall financial position, impact on service delivery, benefit to the community, and responsible ownership." In practice, if the estimated City Payment from CPS Energy exceeds 10% of the Adopted Budget for the fiscal year, the amount of funds above the 10% were to be set aside for input from the City Council before a recommendation from City Staff was made.

The proposed alternative would amend this financial policy and its application to distribute the amount of City Payment above 10% of the Adopted Budget to CPS Energy for resiliency and reliability projects and to the City's Resiliency, Energy Efficiency, and Sustainability (REES) Fund. The allocation would be as follows: 80% to CPS Energy resiliency and reliability projects and 20% to the City's REES Fund. The methodology for the development of the Adopted Budget for City Payment each year would continue to be based on a moderately conservative approach given the City's reserve levels and overall financial policies. Lastly, had this financial policy been in place over the past twenty fiscal years, a total of \$137.6 million would have been distributed back for these projects and of that total, \$61.1 million would have been from the last two fiscal years.

This proposed alternative would allow a portion of City Payment to be used to reinvest in CPS Energy resiliency and reliability projects and the City's REES Fund while not significantly impacting the City's General Fund budget and the services provided. Any reinvestment of City Payment towards CPS Energy resiliency and reliability projects could also assist in lowering the level of potential future CPS Energy rate increases.

#### **ISSUE:**

The City would amend its financial policy related to City Payment and its application to distribute the amount of City Payment above 10% of the Adopted Budget to CPS Energy for resiliency and reliability projects and to the City's REES Fund. This approach would allow a portion of City Payment to be used to reinvest in resiliency and reliability projects while not significantly impacting the City's General Fund budget and the services provided. Any reinvestment of City Payment towards CPS Energy resiliency and reliability projects could also assist in lowering the level of potential future CPS Energy rate increases.

#### **FISCAL IMPACT:**

This item is for briefing purposes only.

**ALTERNATIVES:**

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**RECOMMENDATION:**

City staff recommends the City's financial policy related to City Payment and its application be amended to distribute the amount of City Payment above 10% of the Adopted Budget to CPS Energy resiliency and reliability projects and the City's REES Fund. The allocation would be as follows: 80% to CPS Energy resiliency and reliability projects and 20% to the City's REES Fund.