

PROPOSED 2009 KPU ANNUAL BUDGET

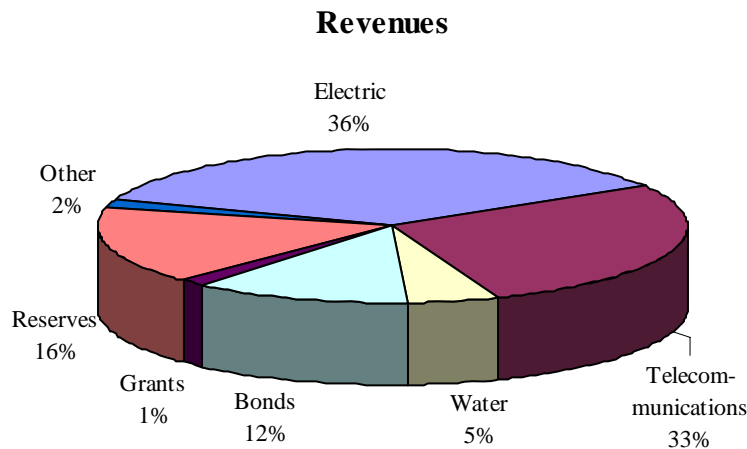
The mission of Ketchikan Public Utilities is to provide quality utility services as efficiently and effectively as possible within guidelines established by federal and state law; the Charter of the City of Ketchikan; the Ketchikan Municipal Code and the ratepayers of the Utility as represented by the City Council. The proposed 2009 KPU Annual Budget, which was submitted to the City Council on November 6, 2008, is the spending plan developed to ensure that these goals and objectives will be met in 2009.

How the Budget is Developed

- The divisions of the Utility developed the programs and services contained within the proposed spending plan for 2009.
- The proposed spending plan was reviewed and modified as necessary by the Office of the General Manager and the Finance Director to ensure compliance with the Utility mission statement and direction from the City Council
- Additional direction from the City Council and input from the general public will be considered prior to finalization of the proposed spending plan.

Where the Money Comes From

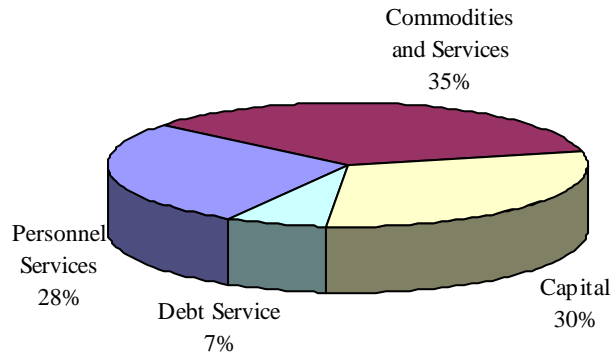
The proposed 2009 KPU Annual Budget is projecting revenues of \$37.4 million and requesting \$44.8 million in appropriations net of reserves. The money to finance the proposed 2009 KPU Annual Budget comes from six major revenue categories plus reserves. The pie chart below identifies each category and their contribution to the proposed 2009 KPU Annual Budget.



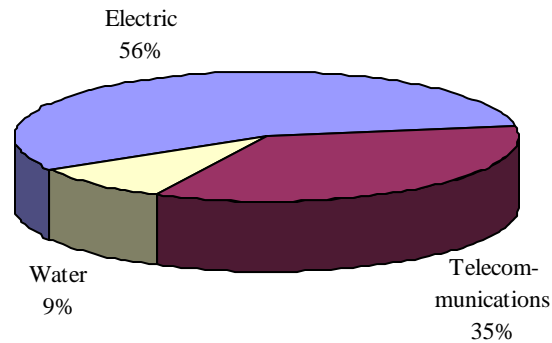
Where the Money Goes

The money will be spent under the proposed 2009 KPU Annual Budget can be categorized by utility and function. The pie charts below identify each utility and the four major expense functions.

Expenses by Cost Category



Expenses by Utility



Financial Highlights for 2009

- Operating revenues of \$30.8 million have been projected, with the electric utility accounting for 52 percent of the total. The telecommunications and water utilities account for 40 percent and 8 percent, respectively, of the total.
- Operating expenses of \$28.24 million net of debt service have been projected. Purchased power and leased telecommunications equipment and lines account for nearly 25 percent of total operating expenses.
- KPU will incur \$3.08 million in debt service on its outstanding revenue bonds. KPU will begin paying debt service on its \$2.1 million ADEC Drinking Water Loan. KPU will issue bonds totaling \$5.3 million for electric utility capital improvements.

- Capital spending totaling \$13.45 million has been programmed. Bonds and grants will finance about six million dollars of the proposed capital budget and most of the remaining balance will be financed from reserves. Approximately 62 percent of the capital budget has been designated for the electric utility. The telecommunications and water utilities will receive 27 percent and 7 percent, respectively.
- KPU will employ 116 employees, a reduction of 2 employees from 2008. Thirty-nine percent of KPU's employees will work for the telecommunications utility. The electric and water utilities employ 36 percent and 6 percent, respectively. Administration, engineering and customer service employ 19 percent. Total gross payroll is estimated at \$8.25 million.
- Water utility rates have been programmed to increase by 15 percent.
- Approximately \$7.34 million in reserves will be needed to balance the overall budget.
- KPU reserves will decrease from \$12.6 million to \$5.3 million.

Important Budget Issues for 2009

- Water - There continues to be **concerns about the adequacy of water utility rates** to finance the water utility's cost of operations, the capital cost of replacing or maintaining its utility systems, and the cost of complying with unfunded mandates being imposed upon the utility by federal and state regulatory bodies. The utility has been incurring net losses in excess of \$1 million annually for the past five years. A 15 percent water rate increase has been proposed as a short-term fix. A long-term strategy is needed to correct this deficiency.
- Electric - The community's demand for energy continues to increase to levels that are stretching KPU's low cost energy resources and forcing the Utility to use more expensive diesel generation to meet the demand. **Developing and constructing additional generation resources remains one of KPU's highest priorities.** Cheap, reliable power is necessary to promote and sustain economic growth. Recognizing the urgency to bring these resources on line as soon as possible, KPU has elected to undertake the following projects in its efforts to meet the current and future demand for energy: (1) Swan Lake-Lake Tye Intertie; (2) Whitman Lake Hydroelectric Project; (3) Metlakatla Intertie/Triangle Lake Hydroelectric Project; and (4) Mahoney Lake Hydroelectric Project. The Intertie is nearing completion and KPU needs to continue its plans to aggressively pursue the development of the \$18 million Whitman Lake Hydroelectric Project. A \$1.13 million request has been programmed to continue the licensing and design process.

- Telecommunications - The City needs to **weigh the benefits of continuing ownership of the telecommunications utility against the cost of continuing ownership** and make a decision that brings about the best results for the citizens of the City. The City recently engaged the services of a consultant to review the feasibility of the City continuing ownership of its telecommunications utility. The firm issued its report with a strong recommendation that the City consider selling the utility. The firm noted that the telecommunications industry is becoming increasingly competitive and technologically complex, and that the City would be required to make a substantial investment in order to stay in the business. The firm concluded that the telecommunications utility would most likely not be well positioned financially to remain competitive and was at risk of experiencing deterioration in the current value of its assets the longer it remained a part of KPU.
- Historically, KPU has employed a balanced approach to finance its capital improvement programs by using a mix of revenues from operations, grants, reserves and debt. Unfortunately, competition and operating costs are beginning to consume a larger share of operating revenues leaving very little remaining for capital spending. If this trend continues, KPU will be required to rely solely on grants, reserves and debt to finance its capital improvement programs. **One possible solution is to require each utility to stand on its own financially and set rates accordingly.** This means that rates would be set to recover the cost of service. While this is a change in KPU's current rate setting philosophy, it will strengthen the Utility financially. If the City decides to retain the telecommunications utility, this approach would free up telecommunication resources that are being used to subsidize the other utilities.

The City Council will begin deliberations on the proposed 2009 KPU Annual Budget in November 2008. The budget is scheduled for adoption on December 18, 2008. Budget deliberations are open to the public and the public is invited to attend. If you have questions or would like to submit comments, please contact the General Manager's Office at 228-5603 or karla@city.ketchikan.ak.us.