Item 2
PRESENTATION

# FY 22-23 Budget Preview

Amrit Singh
Finance and Administration Committee
August 1, 2022

SILICON VALLEY
CLEAN ENERGY

# Purpose

1. Review: Proposed fiscal year 2022-2023 (FY 23) budget
2. Action: Recommend approval to the Board, with any suggested changes:
   a) The proposed budget
   b) Revised reserves policy with new reserve targets

# Main Areas of Discussion

1. Summary of the Proposed Budget
2. Revenue Modeling
   - PCIA and PG&E Gen Rate Uncertainty
3. Reserve Targets
4. Customer Discount Rate and Funding for Programs
5. Power Supply Costs
6. Other Cost Drivers
   - Personnel, BPO, Legal, Cybersecurity

# FY22-23 Budget will be ready for Discussion in August

**June 24**

Budget Framework at Exec Comm

**August 1**

Present Draft Budget to Finance & Admin Comm

**August 8**

Present Draft Budget to BOD

**Late August**

Incorporate Changes based on BOD feedback

**Sept. 14**

Present Recommended Budget to BOD. Adopt updated Strategic Plan

**March 2023**

Mid-Year Budget Review / Adjustment

# 1. Proposed FY 23 vs FY 22 Mid-Year Adjusted Budget

## Revenue increase, due to higher margins, outpaces rising energy costs

**SILICON VALLEY CLEAN ENERGY**
**FY 2022-23 OPERATING BUDGET**
**($ in thousands)**

| | FY 2021-22 ADJUSTED BUDGET | FY 2022-23 PROPOSED BUDGET | VARIANCE $ | VARIANCE % |
|---|---|---|---|---|
| **Energy Revenues** | 385,502 | 483,860 | 98,358 | 25.5% |
| **Power Supply Expense** | 274,979 | 325,296 | 50,317 | 18.3% |
| **Operating Margin** | **110,523** | **158,564** | **48,041** | **43.5%** |
| **Operating Expenses** | 21,693 | 28,204 | 6,512 | 30.0% |
| **Non-Operating Revenues/(Expenses)** | 310 | 639 | 329 | 106.1% |
| **Transfers and Other Expenses** | $27,531 | $15,465 | $12,066 | -43.8% |
| **BALANCE AVAILABLE FOR RESERVES** | **$61,609** | **$115,534** | **$53,924** | **87.5%** |

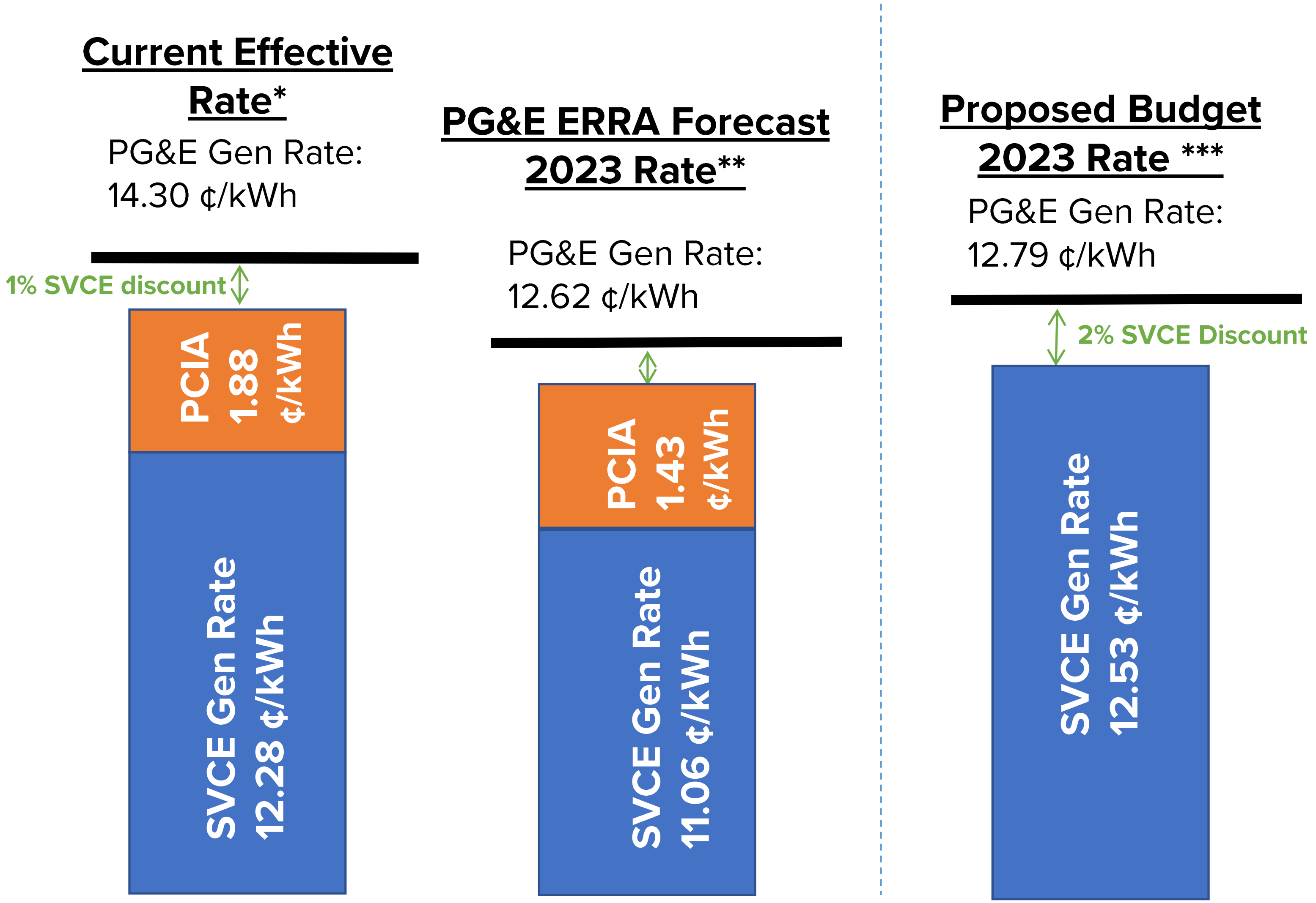
# 2. Revenues

**Strategic Focus Areas: Impacts all five strategic focus areas**

| | Issue | Proposed Budget | Implications/Reasons |
|---|---|---|---|
| 1. Revenues | • PG&E's preliminary 2023 rate forecast, issued in May, is based on outdated market prices. Results in lower SVCE revenues than likely the case.<br><br>• Attempt to calibrate NewGen Model to likely prices used by PG&E overstates SVCE Margins by ~10%*.<br><br>**Using latest version 3.1 – version 2.5 used for Executive Committee presentation.* | • Uses latest market data in NewGen model and discounts results (reduce SVCE Margins) by 10% for modeling error. | • Likely aligns revenues closer to rates that PG&E will update in October.<br><br>• Better aligns revenues with power supply costs<br><br>• Primarily for budget setting purposes.<br><br>• Additional expenditures based on headroom projections will be made by the Board likely in December when actual PG&E and PCIA rates are known. |

# Healthy SVCE Margins Remain

- PG&E filed it's forecast of 2023 Rates in May
  - PG&E Gen Rate down ~12%
  - PCIA Down ~24%
  - SVCE Margin Down ~10%
- PG&E Used 3/28 Forward Prices
- Prices since have increased ~20%
- PG&E will update this forecast in the Fall ; CPUC will rule in December
- Relative to PG&E Forecast NewGen Model shows (using 3/28 prices) ~10% higher SVCE Margin.
- Proposed budget uses the latest NewGen Model results
  - Reduces model's PG&E GenRate by 10% for modeling error
  - Sets PCIA to Zero per PG&E Tariff since it's forecast to be slightly negative




* Source: PG&E June 2022 Updated Rates
** Source: PG&E 2022 ERRA Forecast (Weighted for SVCE Portfolio Load)
*** Using NewGen Model with 7/16/2022 Forward Curves and 10% haircut
*Above margin analyses ignores minor reductions for franchise fees (0.09 ¢/kWh)*

# 3. Reserve Targets

**Strategic Focus Areas: Impacts all five strategic focus areas**

| | Issue | Proposed Budget | Implications/Reasons |
|---|---|---|---|
| 2. Reserve Targets | • Ensure SVCE maintains sufficient reserves to manage risks such as those modeled under Stress Test Scenario Two.<br>    • Prices collapse reducing revenues and there's additional draw on reserves from increase in financial posting requirements to the Provider of Last Resort (PG&E).<br><br>• Use stress test 2 scenario assumptions and update for Fiscal Year period (Oct 2022 to Sep 2023) and latest market data | Targets to keep reserves above 120 Days Cash On Hand (DCOH) for FY 2022-2023 and FY 2023-2024 (under stress test scenario 2 assumptions)<br><br>Resets Upper Reserve Target such that over the next 5 fiscal years reserves do not fall below 90 DCOH | • FY 23 margins not guaranteed given true-up in 2024 for PCIA and PG&E Gen rate<br><br>• If adverse conditions materialize, need 120 days to reshape strategy and secure additional liquidity<br><br>• Increase upper reserve target to take advantage of good margin years to manage risks over 5-year period |

# New Reserve Targets

| Reserve Targets (DCOH) | Current | New Targets |
|---|---|---|
| Minimum | 120 | 120 |
| Goal (Target) | 230 | 285 |
| Maximum (Upper Target) | 320 | 490 |

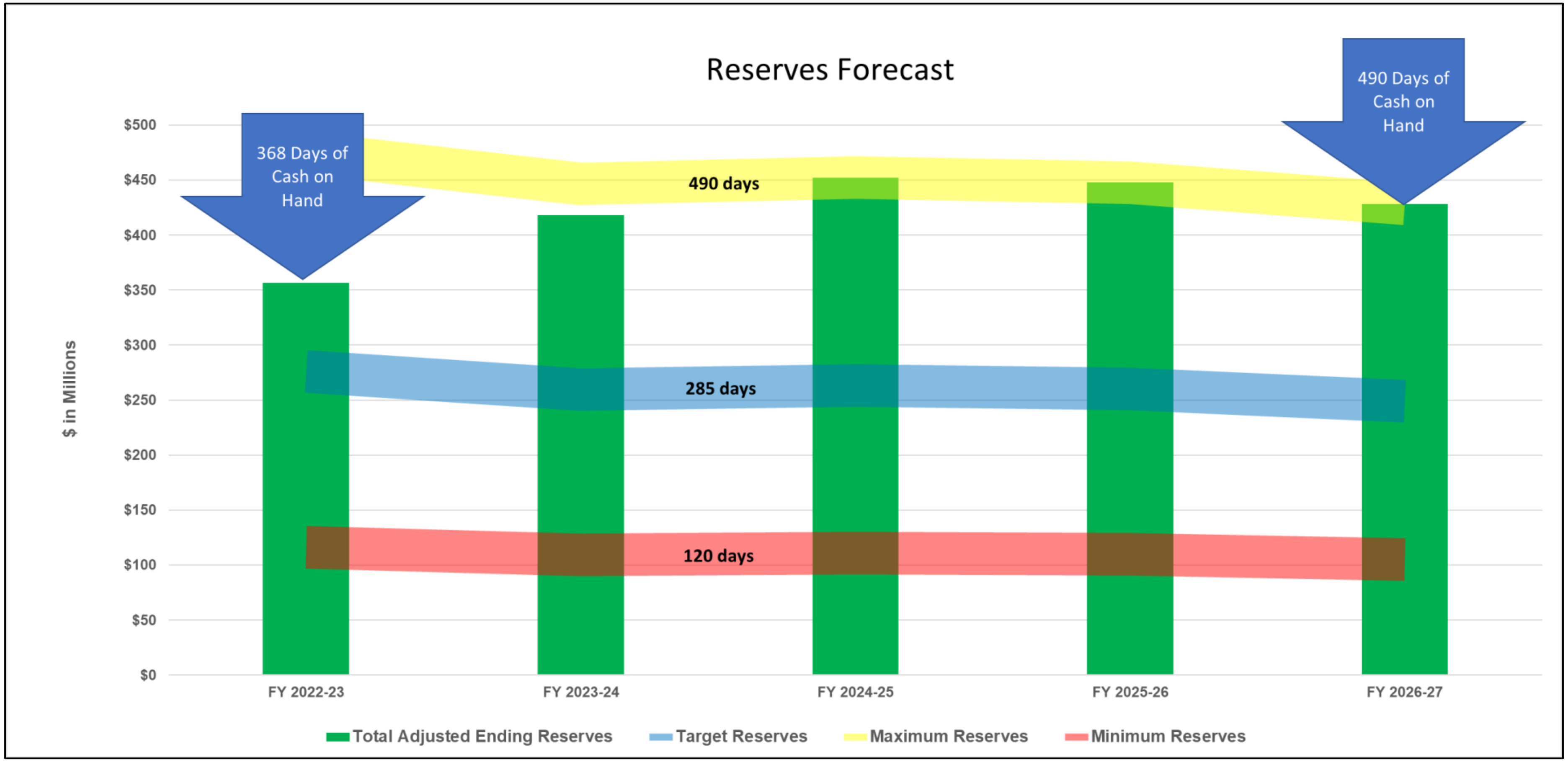
Derived using stress test scenario 2*:

- Draw on reserves in FY 2024 would be ~$186 million
- To end up with 120 DCOH in FY 2024, need to end 2023 with ~$288 million in reserves
- $288 million is equivalent to holding 285 DCOH (@ $1.01 million a day burn rate)

* Updated with budget assumptions and modeled over fiscal year as opposed to calendar year

# 9. Reserve Projection (Move to Appendix?)

Projections include unspent program dollars




*Source: FY2022-23 Proposed Budget*

# 4. Add’l Expenditure – Discount Rate & Programs Funding

**Strategic Focus Areas: Supplier of Choice; Work Electrification into SVCE’s Value Prop. to Customers**

| | Issue | Proposed Budget | Implications/Reasons |
|---|---|---|---|
| 3. Additional Expenditure<br><br>1% discount over 12 months ~$5 million<br><br>1% discount over 9 months (Jan – Sep) ~$3.6 million<br><br>Monthly Average Bill Savings of 1% Discount:<br>• Residential - ~$0.66<br>• Small Commercial - ~$2.39<br>• Medium Commercial - ~$26.89 | • Continue to provide competitively-priced and high-valued services to SVCE customers<br><br>• Funds not needed to cover cost-of-service flow to customers via lower SVCE rates (discount to comparable PG&E rates)<br><br>• Cost-of-service includes funds needed to cover operations, meet reserve targets, and fund decarbonization programs | • Target discount at 3%<br>  • 2% for all customers<br>  • Additional 1% converted to $ bill credits to CARE & FERA customers<br><br>• Board can change the budgeted discount rate, once actual PG&E rates are known, which is expected to occur in late Dec 2022. Until then current 1% discount rate continues.<br><br>• Revisit additional funding for programs during mid-year budget update in March given time needed to ramp up new initiatives to utilize existing authorized funds | • Reaching new target reserve levels ensures SVCE can withstand adverse risk scenarios<br><br>• Keeping the discount rate to a reasonable level<br>  • Enables additional funding for valued customer programs such as decarbonization efforts<br>  • Ensures there’s more organizational resiliency to respond to risks over the 5-yr planning horizon<br><br>• Time SVCE rate change with PG&E rate change when Board will have more certainty on PG&E Gen and PCIA rates |

# 5. Power Supply Expenses

## Strategic Focus Areas: Supplier of Choice, 24x7 Clean Energy Delivery

| | Issue | Proposed Budget | Implications/Reasons |
|---|---|---|---|
| 4. Power Supply<br><br>>90% of Expenses | • Power prices are near record high levels and market is very volatile<br>• In addition to PG&E Gen Rate and PCIA uncertainty, power price volatility makes budget projections more uncertain<br>  ◦ Currently hedged ~79% for FY 2023<br>  ◦ Remaining 21% exposed to volatile market prices<br>• Load Projection for FY2023 is ~3.9 Twh, slightly higher than Mid-Year Budget<br>  ◦ Commercial load is to yet to recover pre-Covid levels (-)<br>  ◦ Offset by increase in number of meters served by SVCE (+)<br>• Contract delays/negotiations further add uncertainty<br>• Cost of carbon-free energy is high due to low hydro conditions. PG&E allocations help<br>• Resource Adequacy requirements are changing, and costs are high | • Continue hedging to current ERM (Energy Risk Management) targets<br>  ◦ Staff conducting additional analyses of hedging targets based on stress test findings. Recommendations to be developed later.<br>• Continue with SVCE 100% clean policy<br>  ◦ Purchasing remaining carbon free allocations expected to cost about $1.2 million to $6 million depending on PG&E allocations. | • High hedge targets increase risk to price collapse; does not account for correlation of prices to PCIA and PG&E Gen rate<br>  ◦ Need further analysis before changing policy given challenges of uncertainty in modeling PCIA and PG&E Gen Rates<br>• Maintain high customer value proposition with 100% clean energy and serve SVCE mission<br>• Furthers SVCE focus toward 24x7 clean energy goal |

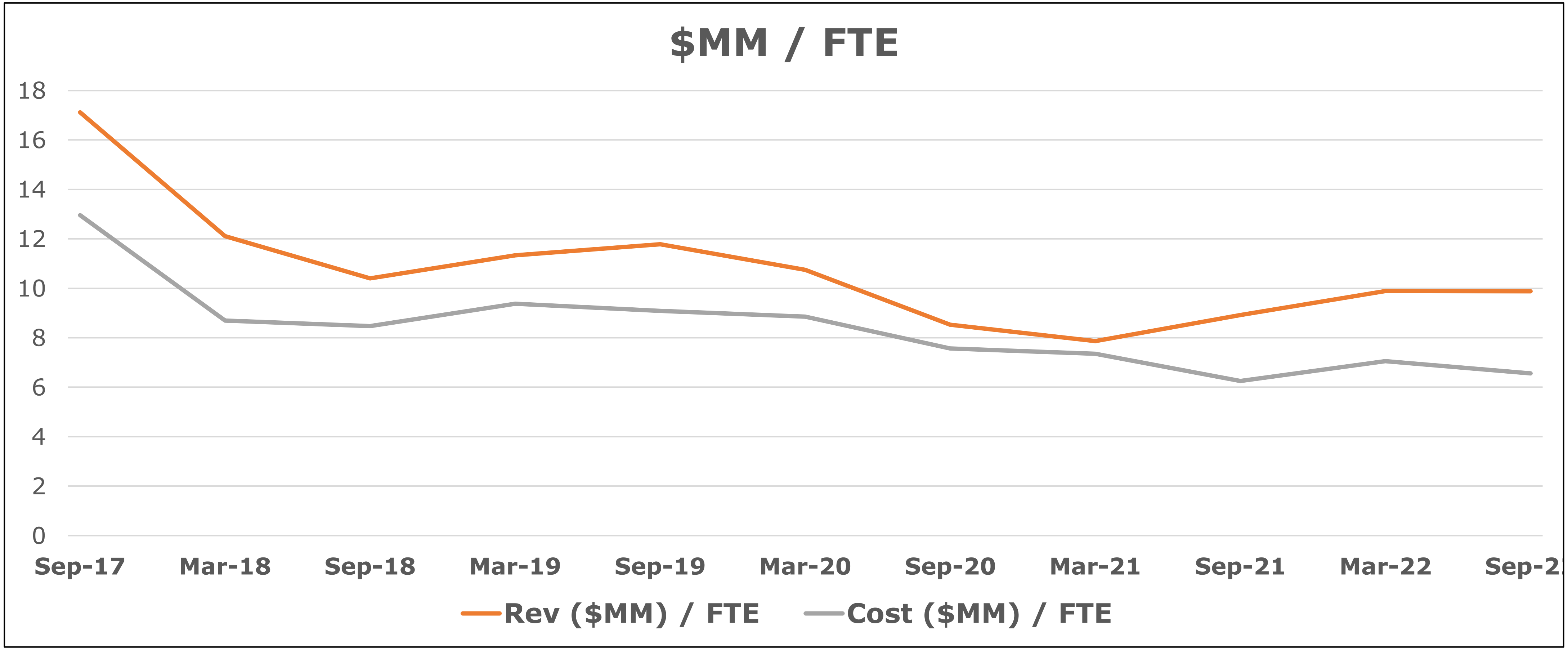
# 6. Other Major Additional Costs

**Strategic Focus Area: Employer of Choice; Leverage Balance Sheet for Structured Financing**

| | Issue | Proposed Budget | Implications/Reasons |
|---|---|---|---|
| 4. Additional Costs | • Growth in all areas of the organization requires additional staffing<br>• Decarb Programs effort increasing from ~$2M/year to ~$20/year for the next 3 years<br>  • Going from hundreds of rebates to thousands<br>  • Increased engagement with local agencies<br>• Increase employee salaries for cost-of-adjustment and merit/promotions<br>• Enhance employee benefits to remain competitive with peer CCAs<br>• Budget for BPO, legal costs, consulting for structed financing, and cybersecurity enhancements | • Add 10 full time staff positions to the current headcount of 39, bringing new headcount level to 49 (Details in next slide)<br>• 5.3% adjustment for COLA<br>  • Based on 6-month rolling average of SF Bay Area CPI (Dec-21 to June-22)<br>  • CEO discretion applied depending on employee pay relative to market range, performance, and date of hire<br>  • ~$350k annual cost increase @ 39 FTE<br>• Any additional increases for merit and promotions based on CEO discretion<br>  • ~$330k annual cost increase @ 39 FTE<br>• Employee benefit enhancements (see detailed slide) - ~$370k annual cost increase<br>• Other Additional Costs:<br>  • BPO - $1.375 million<br>  • Legal - $1.5 million<br>  • Structured Finance: $150k<br>  • Cybersecurity improvements: $250k | • Additional staff needed to:<br>  • Scale up programs team for double down effort (more details in appendix)<br>  • Reduce high level of existing employee workload<br>  • Advance strategic focus area goals<br>  • Create organization depth for business continuity<br>• Adjustments to employee compensation and benefits needed to retain and attract talent<br>• BPO, a key FY 21-22 strategic focus area to mature operations to industry standards and reduce operational risks<br>• Sustained investments in cybersecurity preparedness; FY22-23 efforts include virtual CISO; Incident Response Tabletop exercises; and a combined IT audit / security assessment, along with continued monitoring and security tools. |

# Revenues/FTE; Energy/FTE

Revenue and Energy Costs / FTE have remained fairly flat over time.



# Staffing – Propose 10 Additional Full-time Positions

**Current Staffing**

- 39 full-time employee
  - 6 vacancies; 1 on Maternity Leave
- 5 intern positions
  - 1 currently filled
- 4 part-time employees
  - Don Bray transitioned to part-time as Director of Strategic Development
- 2 Climate Corps Fellows
- 2 long-term independent consultants

**Personnel Authority**

- CEO can approve job titles, salary ranges, and org chart positions
- Positions can be swapped / changed and added within Board-approved budget
- Additions will not exceed 10% of authorized number shown in budget
- Changes / hires communicated in next CEO report to Board

***Per CEO personnel authority, these and existing positions may change to address evolving business needs.***

**Decarbonization Programs and Policy:**

- Senior Programs Specialist – Community Programs – to design and implement decarbonization programs
- Programs Specialist – Policy – to support state and local policy and government initiatives
- Program Implementation Manager – to oversee program delivery and effectiveness
- Additional Staff – Will need additional staff over coming 12 months as programs scale up and more clarity is gained on types of resources needed

**4PRO**

- Regulatory Analyst – to support engagement at CPUC, CAISO, CEC
- Power Data / Markets Analyst (2) – to support increased data analysis from operational PPAs and Load Forecasting

**ESCR**

- Energy Services Specialists (2) – to support rate implementations and commercial / industrial offerings
- Outreach Specialist – to support outreach directly to member agencies and community groups

**Finance & Admin**

- Risk Control Analyst– to support middle office functions and administration of internal controls including implementation of BPO

# Proposed Benefit Improvements

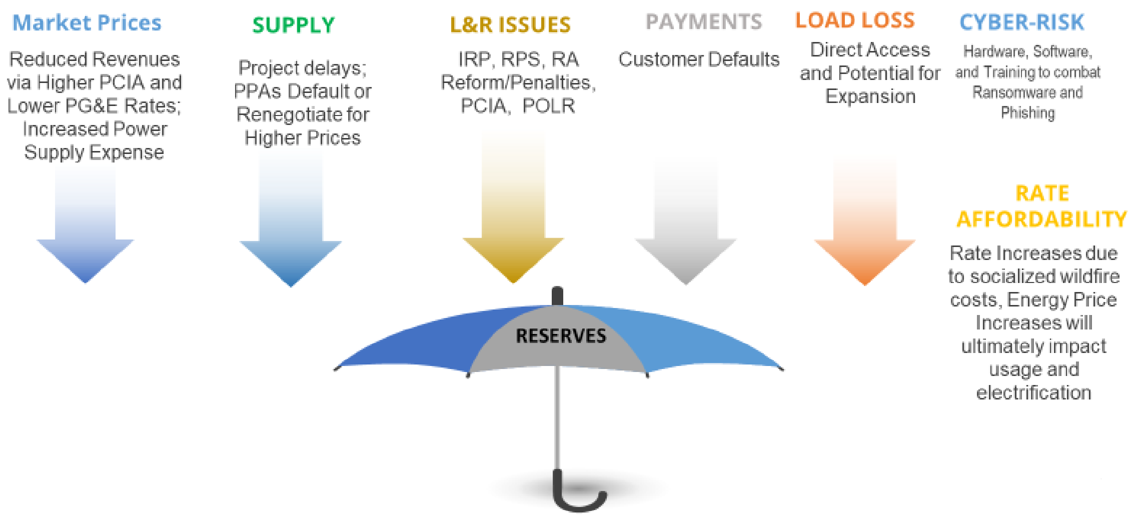
## SVCE is proposing benefit increases to remain competitive with peer CCAs

| Benefit | Current | Proposed | Supporting Detail |
|---|---|---|---|
| **Health Reimbursement Account (HRA) Cap** | $6000 / year | Cap @ $18k (3x annual) | SVCE leading (3CE offers $3600 / year), but balances growing beyond useful limits. |
| **Cash In Lieu of Health Benefits** | $250 / mo | $600 / mo | CCA range ($250 - $750) |
| **Monthly Premium Contribution** | $1200 / mo | $1500 / mo | CCA range ($1200 - $1891) |
| **Phone / Internet Allowance** | $50 / mo (phone only) | $120 / mo | CCA range ($50 - $150) – combine into a single "remote technology" allowance |
| **Paid Parental Leave (bonding)** | none | 120 hours during 1st year after birth | Offered by MCE and PCE |
| **Employee Participation in Program Incentives** | none | $2500 / FTE | Recommend setting up a budget amount for staff to benefit from similar decarbonization incentives as customers, but separated to avoid issues of unfair access. Estimating 50% utilization |

# Summary - Despite ongoing uncertainty, the overall financial picture looks good for FY22-23

- Biggest risks include late-year adjustments to PCIA / PG&E Gen Rate and significant volatility in power prices
- Reserve targets increase to account for risks as modeled in the stress test analyses
- Keep 1% customer discount rate and revisit once PG&E and PCIA rates are known
- Power supply costs will increase, but margins showing favorable improvement
- Budget increases for operating expenses other than power supply needed to advance strategic focus areas including retaining and attracting employees, reducing operational risks, and enhancing operational efficiency.

## Many Risks can Deplete Reserves




# Next Steps

**June 24**
Budget Framework at Exec Comm

**August 1**
Present Draft Budget to Finance & Admin Comm

**August 8**
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**Late August**
Incorporate Changes based on BOD feedback

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Mid-Year Budget Review / Adjustment

# Recommendations to the Board

- Approve the Proposed FY 2022-23 Operating Budget
- Approve the Updated Reserves Policy

# Thank you! / Questions?

# 5-year forecast

| ($ in Thousands) | | | | | | |
|---|---|---|---|---|---|---|
| | 2022 | 2023 | 2024 | 2025 | 2026 | 2027 |
| **Operating Revenue** | (Budget) | (Budget) | (Forecast) | (Forecast) | (Forecast) | (Forecast) |
| GWh Sales | 3,914 | 3,907 | 3,782 | 3,746 | 3,766 | 3,767 |
| Electricity Sales, Net | $ 384,498 | $ 482,930 | $ 410,965 | $ 394,285 | $ 361,155 | $ 338,749 |
| Available for PCIA/Gen Rate/Power Supply Cost Changes | - | - | - | (13,000) | (27,000) | (35,000) |
| GreenPrime Electricity Premium | 1,005 | 931 | 899 | 873 | 872 | 875 |
| **Total Operating Revenues** | **385,502** | **483,860** | **411,864** | **382,158** | **335,028** | **304,624** |
| **Operating Expense** | | | | | | |
| Power Supply | $ 274,979 | $ 325,296 | $ 302,663 | $ 305,570 | $ 300,691 | $ 285,026 |
| **Operating Margin** | **110,523** | **158,564** | **109,201** | **76,587** | **34,337** | **19,598** |
| Data Management | 3,249 | 3,413 | 3,413 | 3,583 | 3,762 | 3,950 |
| PG&E Service Fees | 1,450 | 1,470 | 1,544 | 1,621 | 1,702 | 1,787 |
| Staff Compensation | 8,535 | 12,024 | 13,263 | 13,694 | 14,139 | 14,599 |
| Consultants and other Professional Fees | 5,669 | 7,922 | 8,318 | 8,734 | 9,170 | 9,629 |
| Communications and Noticing | 1,040 | 993 | 1,043 | 1,095 | 1,150 | 1,207 |
| General and Administration | 1,750 | 2,382 | 2,501 | 2,626 | 2,758 | 2,895 |
| Programs | 27,381 | 15,265 | 8,237 | 7,903 | 7,241 | 6,792 |
| **Total Operating Expenses** | **324,053** | **368,766** | **340,981** | **344,826** | **340,613** | **325,886** |
| **Operating Income** | **61,449** | **115,095** | **70,883** | **37,331** | **(5,585)** | **(21,262)** |
| **Nonoperating Revenue (Expense)** | | | | | | |
| Other Income | 50 | 50 | 51 | 51 | 52 | 52 |
| Investment Income | 300 | 592 | 713 | 836 | 904 | 895 |
| Capital Outlay & Financing Costs | (190) | (203) | (53) | (53) | (53) | (53) |
| Grant Income | - | - | - | - | - | - |
| **Total Non-Operating Revenue (Expense)** | **160** | **439** | **711** | **834** | **903** | **894** |
| | | | | | | |
| **Change in Net Position/Available for Reserves** | **61,609** | **115,534** | **71,593** | **38,166** | **(4,682)** | **(20,368)** |

# Goals Spotlight – Five Focus Areas

- All are important
- Shining a spotlight on incremental areas
- Workplan will include the details on how we will address these and other areas/goals (internal document)

1. Employer of Choice

2. Supplier of Choice (electrification, rates, DA customers, 24x7 CFE… )

3. Leverage Balance Sheet for Structured Financing

4. Efficient and Effective Internal Operations

5. 24x7 clean energy delivery

6. Operationalize resources and portfolio/asset management in the wholesale market to achieve objectives

7. Ensure state and federal policy landscape preserve CCA autonomy + program policies

8. Work electrification into SVCE's value proposition to customers

9. Expand focus on C&I decarb/industrial load

10. Expand/scale digital and in-person electrification awareness and education

11. Execute on planned programs to demonstrate impacts and influence policy

12. Operationalize equity into programs

# NewGen Projection vs PGE ERRA Forecast

## Comparing 2023 PCIA / Gen Rates using 3/28 curves

| | Proposed PGE ERRA Rate (3/28) | NewGen Projection (3/28)* | Variance |
|---|---|---|---|
| Gen Rate (₵/KWH) | 12.62 | 13.05 | 0.43 |
| PCIA (₵/KWH) | 1.43 | 0.93 | -0.50 |
| Headroom (₵/KWH) | 11.19 | 12.12 | 0.93 |

* *Source: NewGen 3.1*

# Stress Test Scenarios

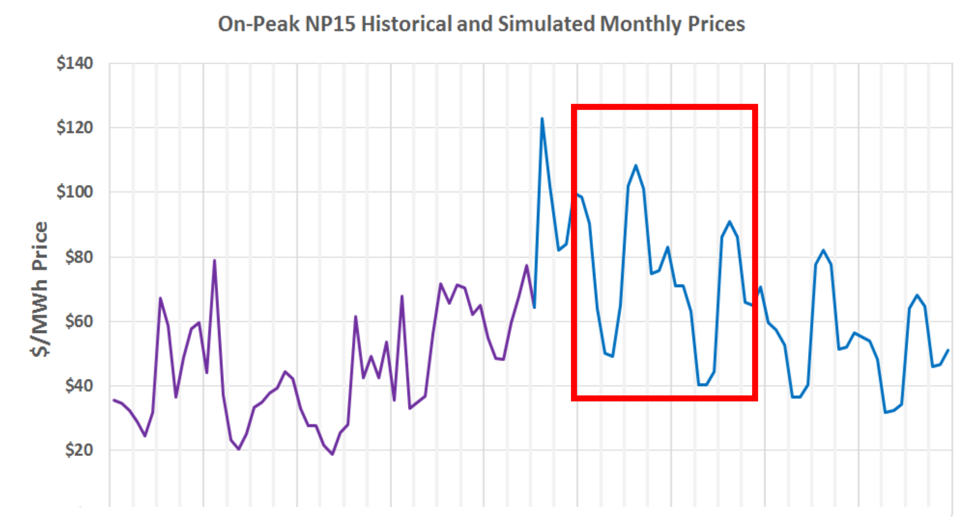
*Extreme but plausible scenarios that can deplete reserves and make SVCE uncompetitive.*

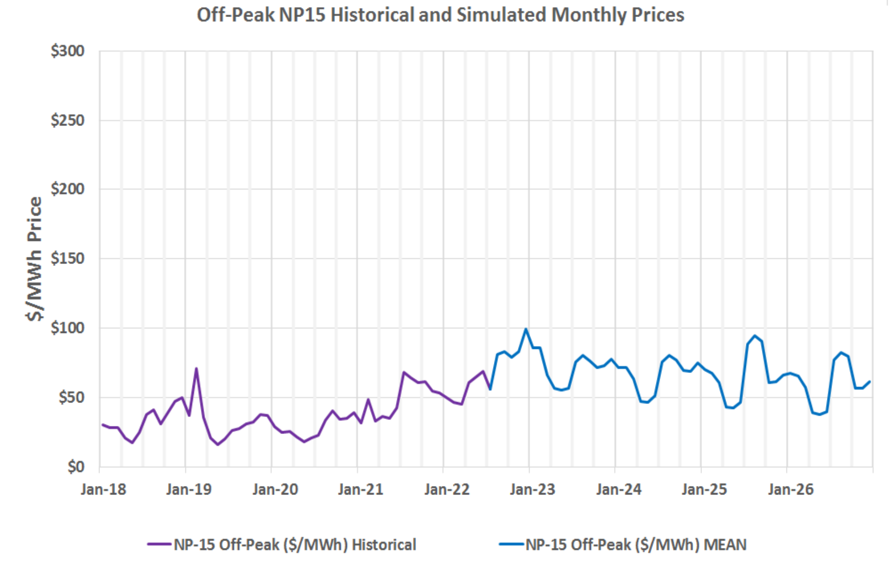
- Ensure adequacy of reserves and organizational resiliency
- Guide development of strategic plan
- Shape FY 22-23 budget and reserve targets
- Price uncertainty Drives the first 4 scenarios

Stress Scenarios for CY 2023 to CY2027 (five-year horizon):

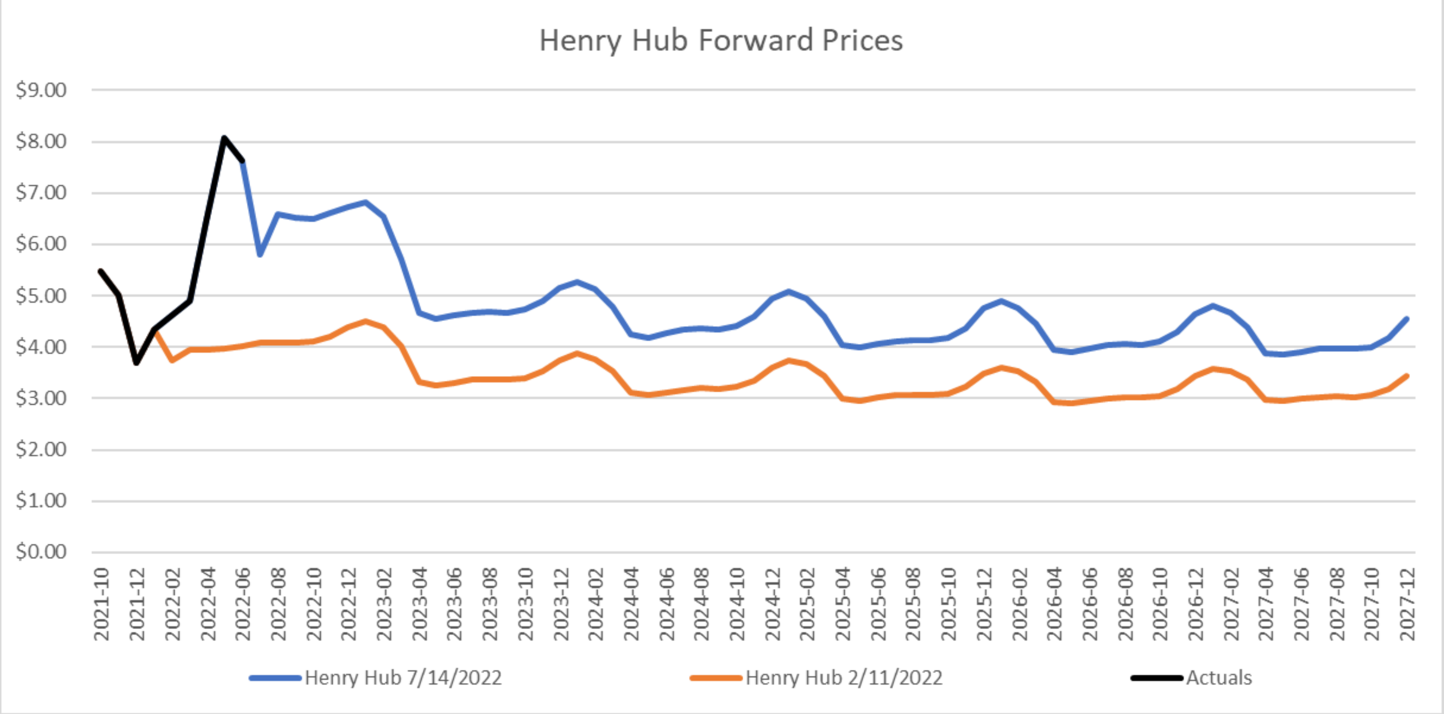
1. Significant drop in energy prices including REC
   - Higher PCIA and lower PG&E Gen Rate
2. Insufficient financial liquidity
   - Price collapse triggers credit downgrade
   - Collateral calls from counterparties and CAISO
   - Increase in POLR (Provider of Last Resort) funding (called FSR – Financial Security Requirement)
3. PPAs default, renegotiate for higher prices, and/or delay start
   - RPS non-compliance penalty
   - Replacement at higher prices
4. Load loss due to direct access and distributed load
5. Threat to Public Services or Facilities

# Power Market Price Volatility



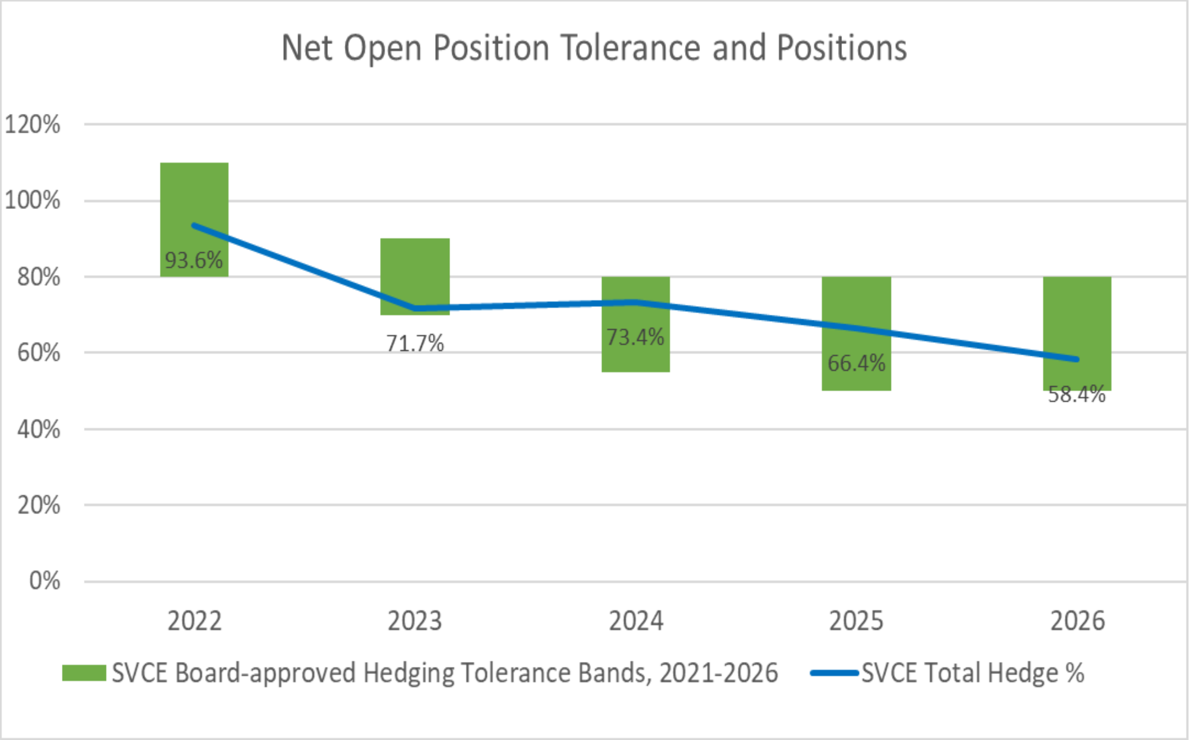

## Forward Price Levels elevated compared to history, driven by gas prices recently due to Ukraine Crisis



# Energy Risk Management Min/Max Bands

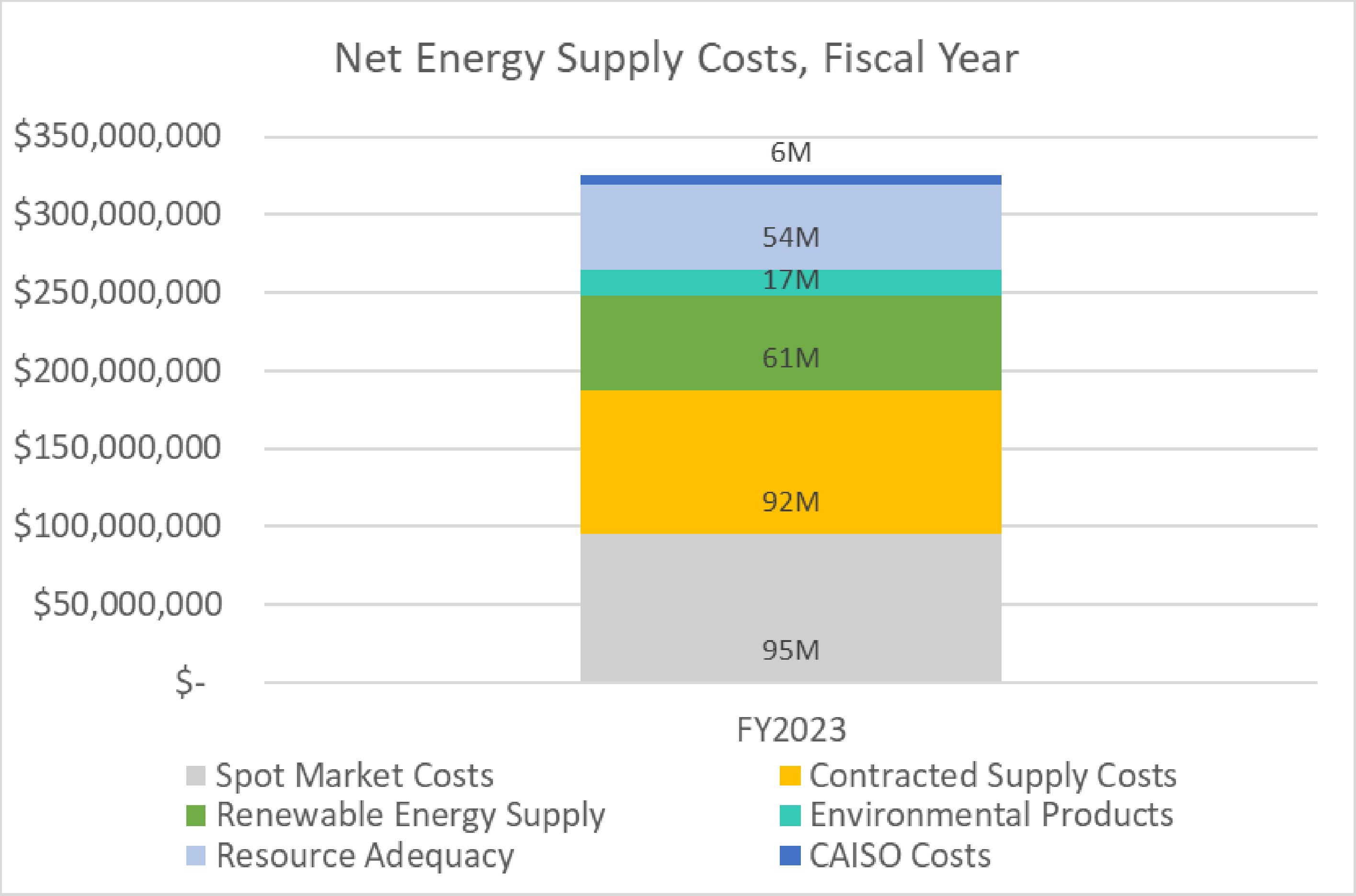
We hedge to manage market price risk. 79% of FY 23 load is hedged. However only 72% of CY 23 is hedged.

| Period | Year | ERM Min Tolerance – LRB % | ERM Max Tolerance LRB % | SVCE Total Hedge % |
|---|---|---|---|---|
| Balance of Year | 2022 | 80% | 110% | 94% |
| Year 2 - 2023 | 2023 | 70% | 90% | 72% |
| Year 3 - 2024 | 2024 | 55% | 80% | 73% |
| Year 4 - 2025 | 2025 | 50% | 80% | 66% |
| Year 5 - 2026 | 2026 | 50% | 80% | 58% |



# Power Supply Costs

FY 23 costs are estimated to be higher than FY 22 at the Mid-Year Budget.




FY 23 Power Supply Cost ~$325.7M:

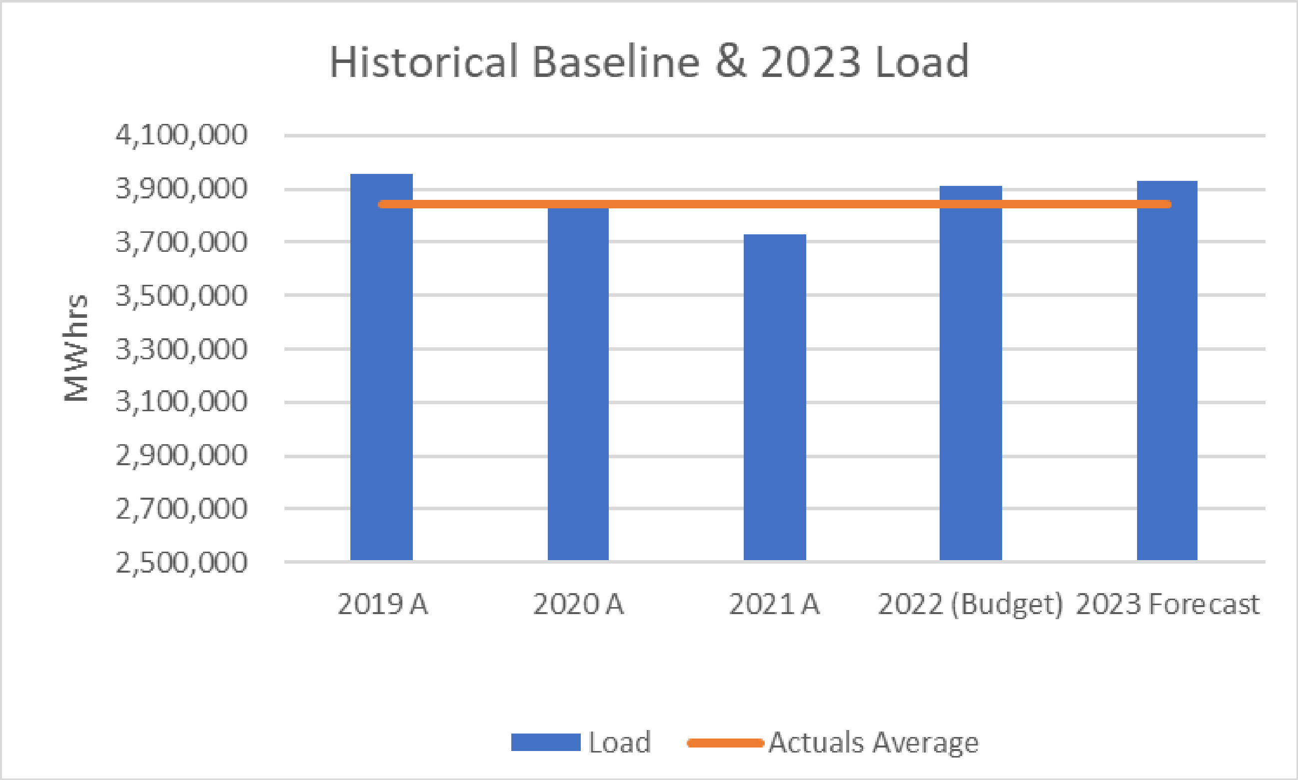
- Load Cost - CAISO energy **(+)**
- Energy hedges (net of CAISO revenues) **(+)**
- Renewable Energy Supply (PPAs) **(-)**
- Clean Environmental Products – short-term index + RECs and carbon-free resources **(+)**
- Resource Adequacy **(+)**
- CAISO non-energy costs **(+)**

*Source: FY2022-23 Early Draft numbers*

# Load Projection

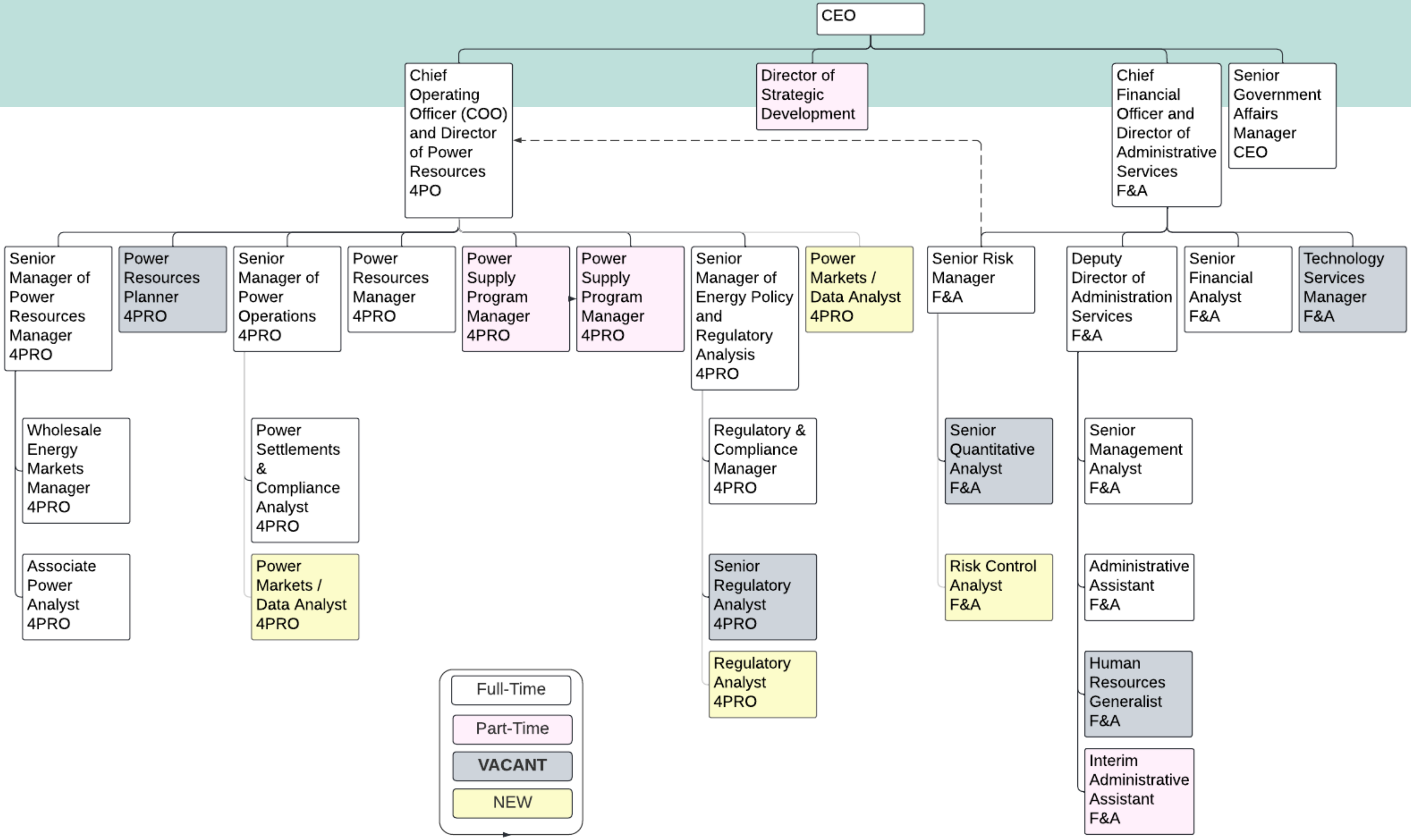
Load Recovery is assumed to be about 50%* offset by increase in new load moving into SVCE portfolio

- Load is yet to recover to Pre-COVID levels.
  - C&I Load is yet to recover
  - Shelter in place residential load increase has tapered off due to return to office and milder temperatures
- This Load loss is offset by some growth with new meters.

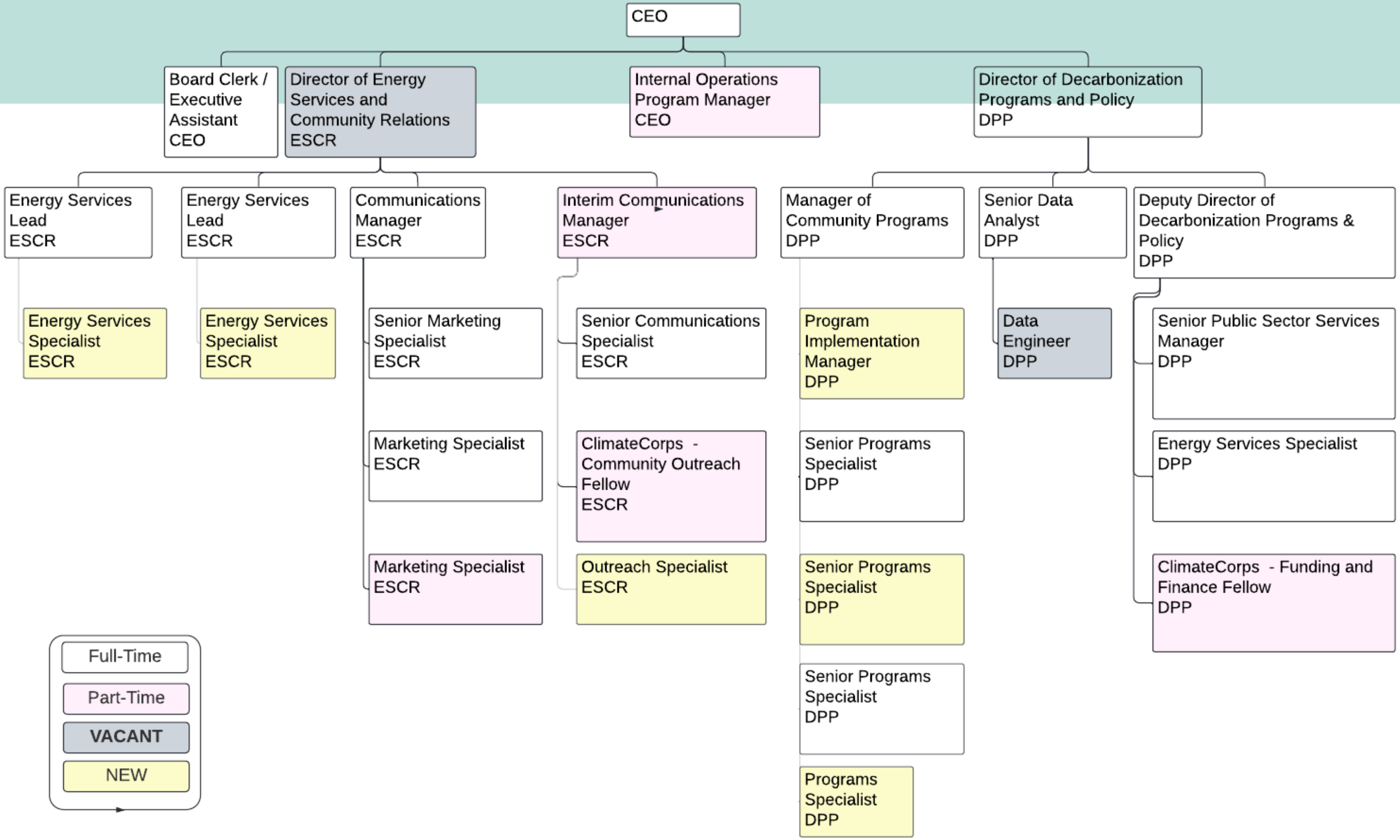



*Prior forecast had assumed 100% recovery by 2022.

# Organization Chart (4PRO / F&A)



# Organization Chart (ESCR / DPP)



# Decarb Programs and Policy Staffing - today

## Current Staff

- Director
- Programs-focused team (3 staff)
- Policy and government support team (3 staff)
- Data team (1 staff, hiring another now)

## Recent Re-org

- Consolidated staff working to design and manage programs
- Emphasized tie-in for programs to support local government initiatives and policy

## Double Down

- Direction from Board to increase efforts 2X over next few years
- Major scale-up in program scope and local policy support
- On top of ongoing and planned current efforts

# Decarb Programs and Policy Staffing - future

## Significant Increase in Efforts

- Need to go from ~$2M/year to ~20M/year for next three years
- Need to go from hundreds of rebates to thousands
- Need to meet more with local agencies to explore options and provide support

## More Staff Required

- Build capacity for managing additional, larger programs
- Ensure time available for analysis, review and optimizing efforts
- Developing relationships is labor intensive

## Tools Required

- Simplify and streamline budgeting, tracking and reporting
- Facilitate increased volume of applications

# Decarb Programs and Policy Staffing - needs

## Known

- Data analysis support – further inform program approaches and respond to policy questions from cities *(hiring Data Engineer now)*
- Program roll-out capacity – move planned but de-prioritized projects forward, add ability to handle new projects that arise, and increase ability to dig deeper into program details to improve the offerings we have *(requesting Sr Programs Specialist)*
- Government and policy support – allow for more concurrent analysis of requests from different cities, ramp up conversations sooner, and deeply participate in key state-level proceedings impacting decarbonization *(requesting Programs Specialist)*

## Currently Unknown – will evolve over coming 12 months

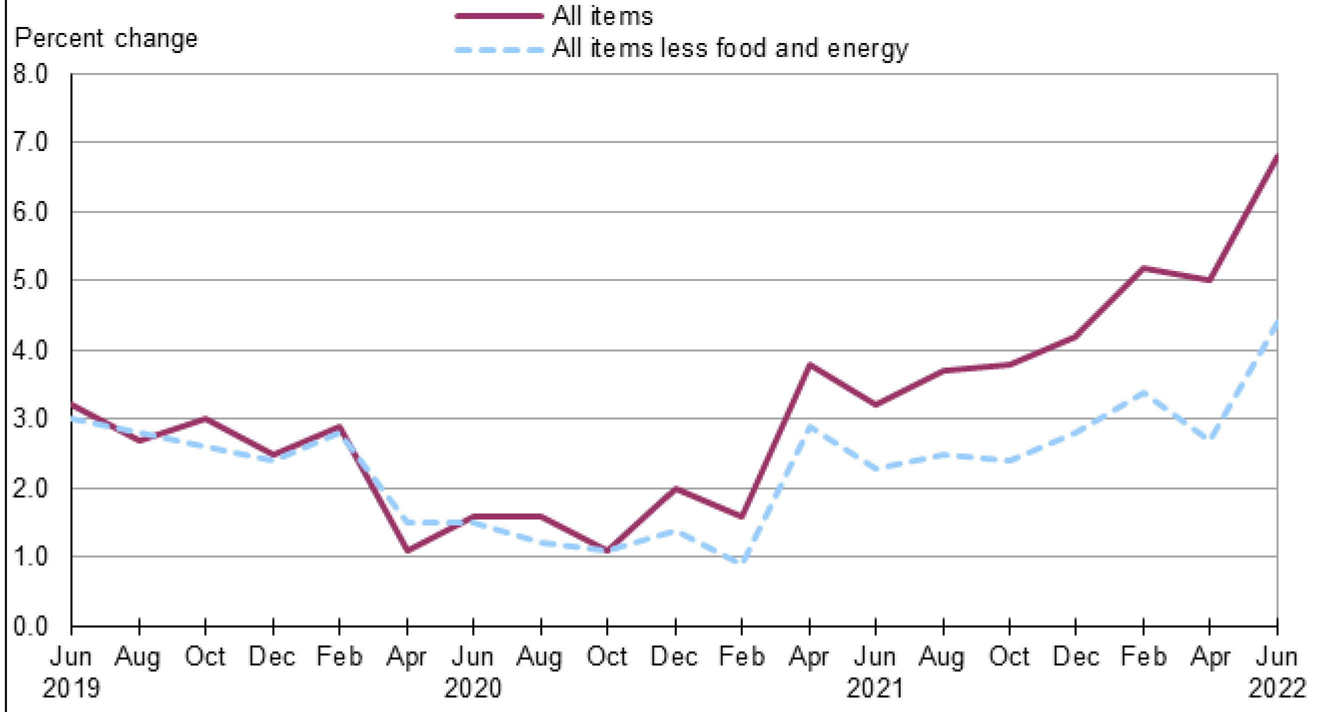
- To reach necessary scale of programs, do we need more staff? Consultants?
- What is the level of uptake from our cities in policy experimentation and exploration?
- How much effort is required to implement new tools? Once in place, how much time do they free up?

# Cost-of-Living & Adjustment (COLA) & Merit Increase Proposals

Proposed 5.3% COLA based on SF Bay Area CPI; smoothed over trailing months

Add'l Merit/promotional increases at CEO discretion

**Chart 1. Over-the-year percent change in CPI-U, San Francisco-Oakland-Hayward, CA, June 2019–June 2022**




Source: U.S. Bureau of Labor Statistics.

| Year | COLA |
|---|---|
| FY17-18 | 3% |
| FY18-19 | 4% |
| FY19-20 | 4% |
| FY20-21 | 0% |
| FY21-22 | 5% |
| FY22-23 (6 mo trailing CPI) - proposed | 5.3% |

[Consumer Price Index, San Francisco Area — U.S. Bureau of Labor Statistics (bls.gov)]

# Budget Impact of COLA & Merit Increase Proposals

Proposed 5.3% COLA to be based on SF Bay Area CPI; smoothed over trailing 6 months

Merit increases at CEO discretion

| Headcount | Base Salary Cost* | COLA (5.3%) | Merit (5% avg) | Total Annual Salary Cost* |
|---|---|---|---|---|
| 39 | $6,582,670 | $348,882 | $329,134 | $7,260,685 |

*Salary, not including benefits or contingency

# Proposed Benefit Improvements – Cost Breakdown

SVCE is proposing benefit increases to remain competitive with peer CCAs

| Benefit | Current | Proposed | Total Added Annual Cost | % of Personnel Budget | Supporting Detail |
|---|---|---|---|---|---|
| **Health Reimbursement Account (HRA) Cap** | $6000 / year | Cap @ $18k (3x annual) | $0 | 0% | SVCE leading (3CE offers $3600 / year), but balances growing beyond useful limits. |
| **Cash In Lieu of Health Benefits** | $250 / mo | $600 / mo | $37,800 | 0.31% | CCA range ($250 - $750) |
| **Monthly Premium Contribution** | $1200 / mo | $1500 / mo | $144,000 | 1.20% | CCA range ($1200 - $1891) |
| **Phone / Internet Allowance** | $50 / mo (phone only) | $120 / mo | $41,160 | 0.34% | CCA range ($50 - $150) – combine into a single "remote technology" allowance |
| **Paid Parental Leave (bonding)** | none | 120 hours during 1st year after birth | $84,000 | 0.70% | Offered by MCE and PCE |
| **Employee Participation in Program Incentives** | none | $2500 / FTE | $61,250 | 0.51% | Recommend setting up a budget amount for staff to benefit from similar decarbonization incentives as customers, but separated to avoid issues of unfair access. Assumes 50% utilization. |
| | | **TOTAL** | **$368,210** | **3.06%** | |

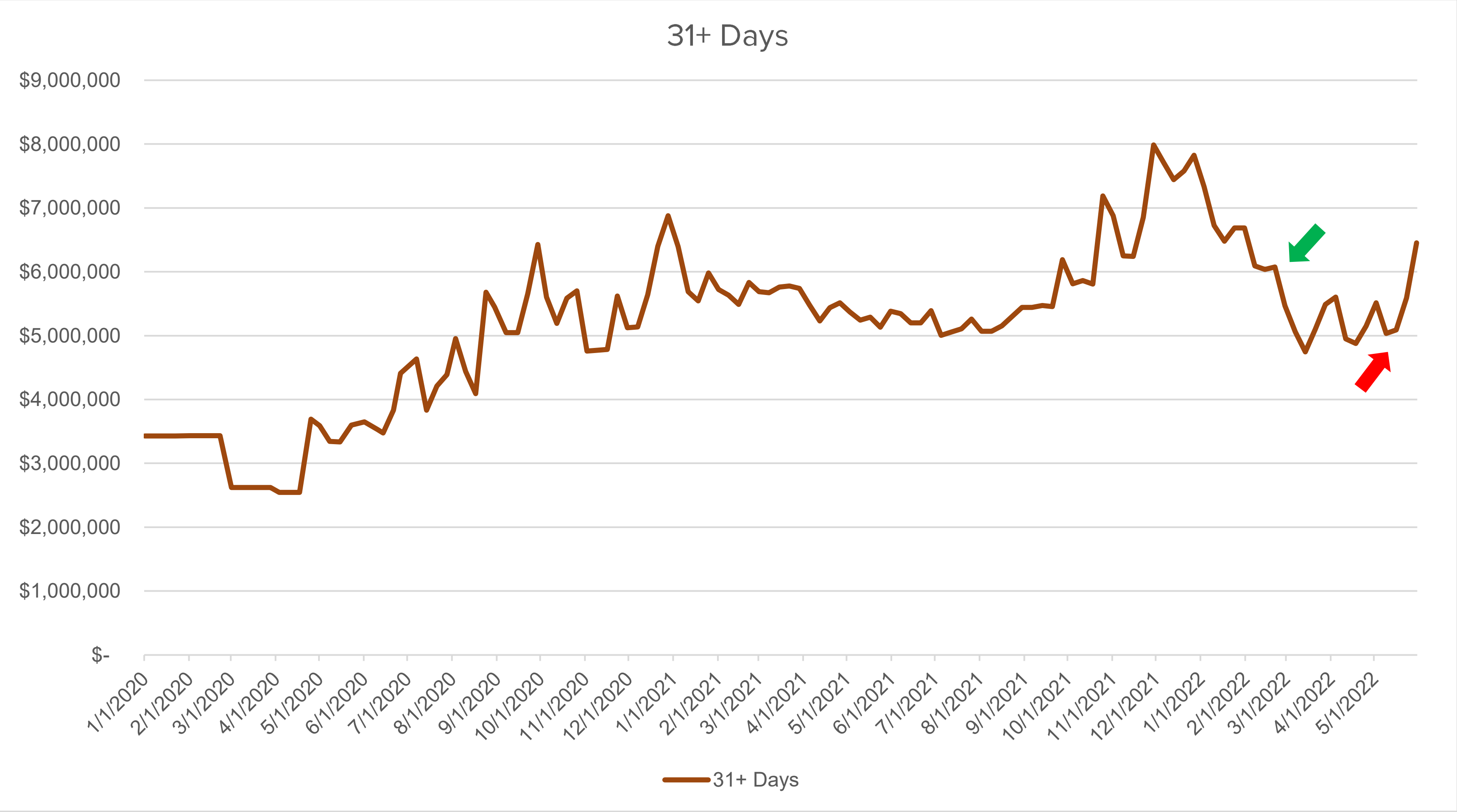
# Staffing / Benefits – Fiscal Impacts

## HRA Levels by # of FTEs

| HRA Balance | # of FTEs |
|---|---|
| Above $18k | 6 |
| $10k - $18k | 5 |
| $5k - $10k | 10 |
| Under $5k | 4 |

# Since March 2020, the overall arrearage amounts have grown roughly 2.5x.

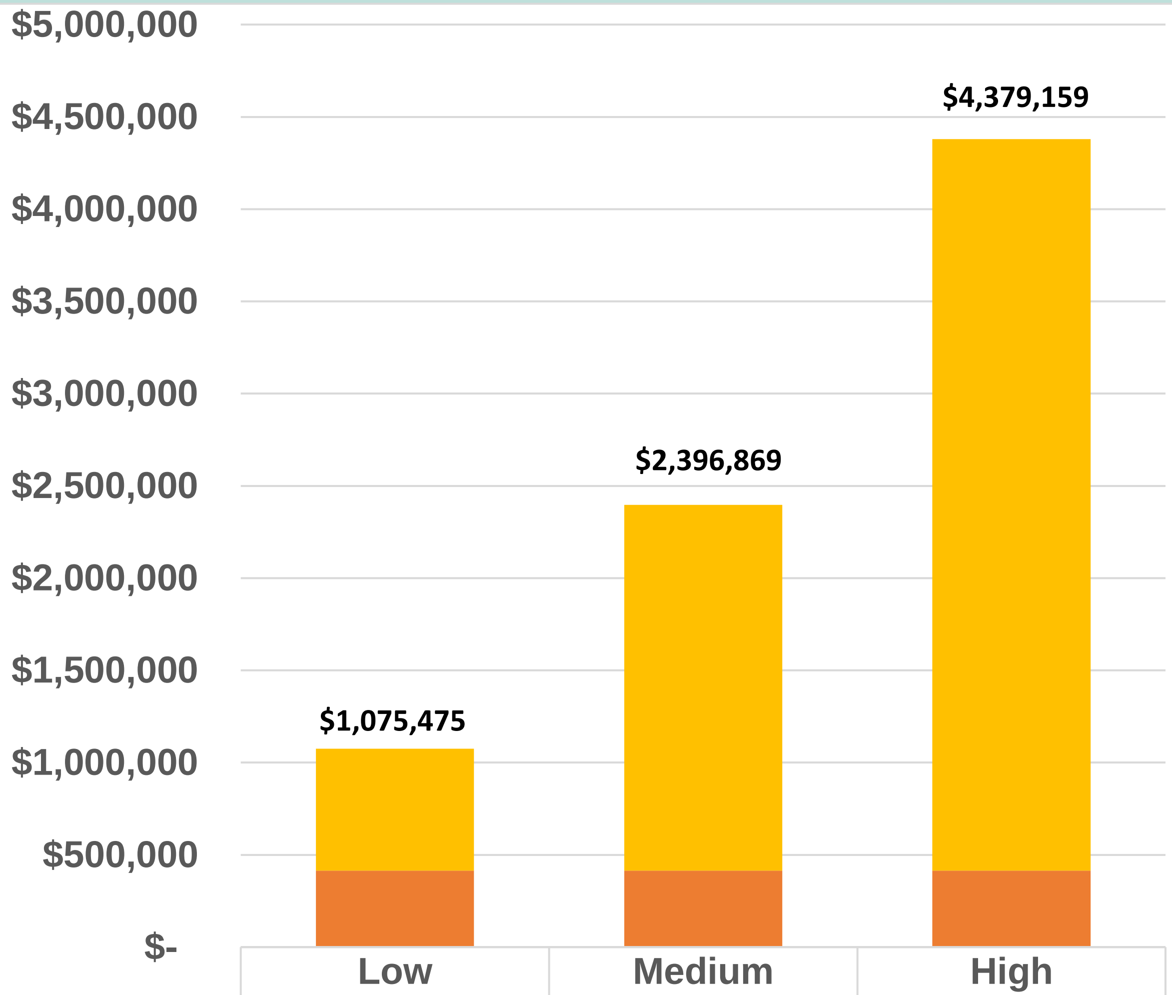
## SVCEs Arrearage Total for customers 31+ days late




| | Date | Amount |
|---|---|---|
| High | 11/29/2021 | $7.99M |
| Low | 4/17/2020 | $2.54M |
| **Current** | **5/30/2022** | **$6.45M** |

- Green arrow indicates receipt of $1.3M in Federal CAPP funds
- A second round of CAPP funding is expected for late summer/fall 2022
- Growth at red arrow indicates short-term growth in 31-60 day aging bucket only - will likely decrease

# SVCE 2022 Customer Debt Write-off Bookends




| | Low | Medium | High |
|---|---|---|---|
| 2022 Additional | $660,895 | $1,982,290 | $3,964,579 |
| 2019 Ordinary Loss | $414,580 | $414,580 | $414,580 |

- 2019 Average 31+ Day Arrearage of $2.5M yielded $415k in Write-offs (16.7% of total)
- 2022 Arrearage is $3.9M higher than 2019 after receiving $1.3M in CAPP payments in March 2022
- Remaining $3.9M used as basis for the following write-off scenarios:

| Scenario | Assumptions |
|---|---|
| Low | 16.7% of $2.5M **PLUS 16.7%** of $3.9M- same as ‘normal’ year |
| Medium | 16.7% of $2.5M **PLUS 50%** of $3.9M |
| High | 16.7% of $2.5M **PLUS 100%** of $3.9M |

*Data Current 5/30/2022*

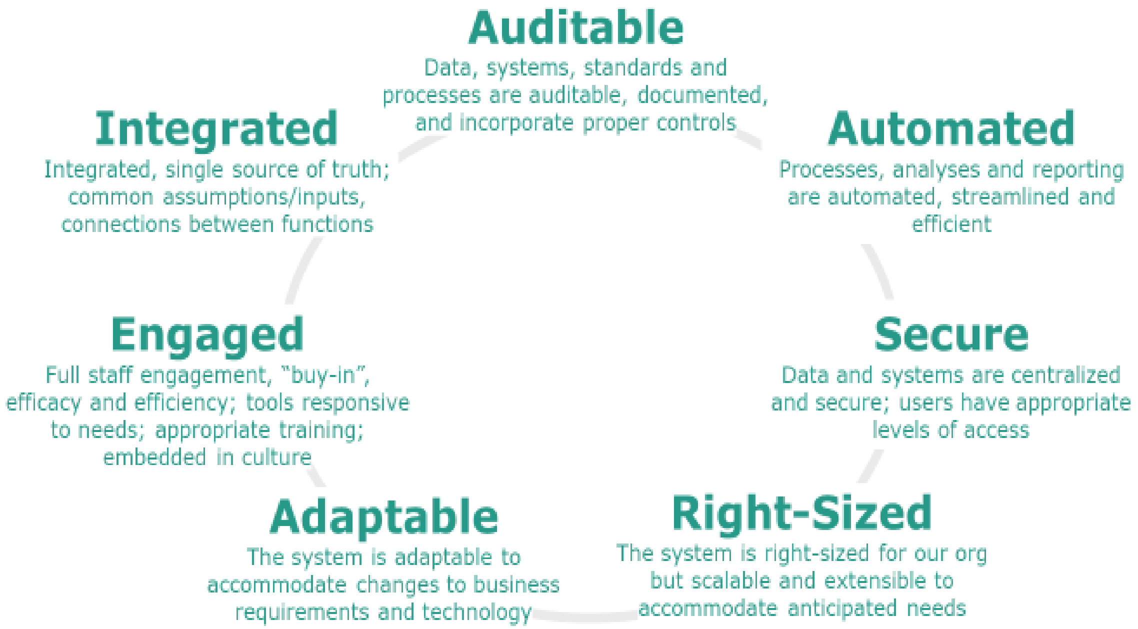
# BPO Overview

*BPO is a key initiative under the strategic focus area: Internal Operations & Cyber Risk Management*

**CURRENT STATE**

1. Small group of people managing multiple large transactions (~$275MM annually)
2. Leveraging many consultants & outside experts
3. Adapting to new regulations continuously
4. Manual and labor-intensive processes create operational and business continuity risks
5. Non-integrated data impedes ability to efficiently and effectively make insightful data-driven decisions

Future

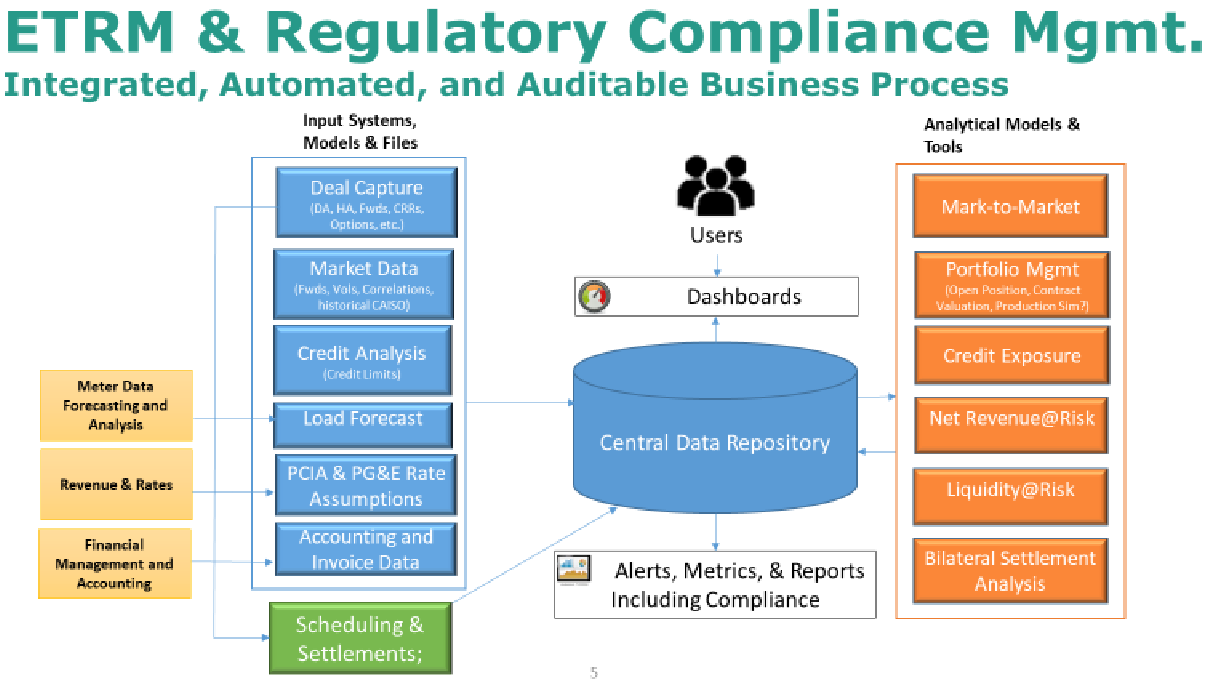


# BPO - Phased Implementation of a Detailed Roadmap

- Current: Phase 1 of the project focuses on Deal Capture and Settlements
    - $500k year 1 license
    - $600k implementation
    - $275k contingency

- Phase 2 will focus on portfolio and risk management integrations

- Phase 3 will be defined later but could include:
    - Customer Relationship Management Including Program Design and Implementation
    - Meter Data Forecasting and Analysis
    - Financial Management and Modeling



# BPO - Next Steps for Deal Capture and Settlements System

| | |
|---|---|
| June/July 2022 | • Contract negotiation |
| August 2022 | • Seek BOD approval |
| Aug. & Sep. 2022 | • Work commences |
| Balance of FY22 & 23 | • Project timeline<br>• Vendor proposals indicate a 6–12-month implementation plan |
| Late FY23 & early FY24 | • Implementation complete |

# Value of Deal Capture and Settlements

## Scale of SVCE's Wholesale Portfolio

- SVCE's wholesale portfolio is scheduled and settled at an hourly and sub-hourly basis
- Monthly settlements with suppliers are payables of over **$25M per month** and based on over **348K rows of data**
- CAISO settlements have approximately 20 highly relevant charge codes applicable to SVCE's portfolio and CAISO settles each trading day 5 times resulting in nearly **35M rows of data** per month and over **$50M in total costs and revenues**
- Sheer magnitude of portfolio requires a Deal Capture and Settlements system
  - Not manageable with spreadsheets (Excel limit is ~1M rows)
  - Significant operational risk if SVCE operates without a scalable system
  - System is basis for confidence in accuracy of SVCE's portfolio costs and revenues

| | Bilateral Settlements |
|---|---|
| # of PPAs | 13 |
| # of Data Points (Price, Quantity, Amount) | 3 |
| # of Intervals per Hour | 12 |
| # of Hours per Day | 24 |
| # of Days per Month | 31 |
| Total Intervals of Data | 348,192 |

| | CAISO Settlements |
|---|---|
| # of Relevant CAISO Charge Codes | 20 |
| # of Settlement Versions | 5 |
| Total Intervals of CAISO Data | 34,819,200 |

| | |
|---|---|
| Contract Costs Paid to Suppliers | $25,000,000 |
| Absolute Value of CAISO Settlements per Month | $50,000,000 |
| Total Dollars Settled per Month | $75,000,000 |

# 2022-2023 Operating Budget

**SILICON VALLEY CLEAN ENERGY**
**FY 2022-23 OPERATING BUDGET**
**($ in thousands)**

| DESCRIPTION | FY 2022-23 PROPOSED BUDGET |
|---|---|
| **ENERGY REVENUES** | |
| Energy Sales | 482,930 |
| Green Prime | 931 |
| **TOTAL ENERGY REVENUES** | **483,860** |
| **ENERGY EXPENSES** | |
| Power Supply | 325,296 |
| **OPERATING MARGIN** | **158,564** |
| **OPERATING EXPENSES** | |
| Data Management | 3,413 |
| PG&E Fees | 1,470 |
| Salaries and Retirement | 12,024 |
| Professional Services | 7,922 |
| Marketing & Promotions | 862 |
| Notifications | 131 |
| Lease | 525 |
| General & Administrative | 1,857 |
| **TOTAL OPERATING EXPENSES** | **28,204** |
| **OPERATING INCOME (LOSS)** | **130,360** |
| **NON-OPERATING REVENUES** | |
| Other Income | 50 |
| Interest Income | 592 |
| Grant Income | 0 |
| **TOTAL NON-OPERATING REVENUES** | **642** |
| **NON-OPERATING EXPENSES** | |
| Financing | 3 |
| Interest | 0 |
| **TOTAL NON-OPERATING EXPENSES** | **3** |
| **TOTAL NON-OPERATING INCOME (EXPENSES)** | **639** |
| **CHANGE IN NET POSITION** | **130,999** |
| **CAPITAL EXPENDITURES, INTERFUND TRANSFERS & OTHER** | |
| Capital Outlay | 200 |
| Transfer to CRCR Fund | 0 |
| Transfer to Program Fund | 9,765 |
| Nuclear Allocation | 1,900 |
| Add'l Programs Allocation | 0 |
| Add'l Customer Bill Relief | 3,600 |
| Other | 0 |
| **TOTAL CAPITAL EXPENDITURES, INTERFUND TRANSFERS & OTHER** | **$15,465** |
| **BALANCE AVAILABLE FOR RESERVES** | **$115,534** |

Item 3
PRESENTATION

pfm asset management

# Silicon Valley Clean Energy

## Investment Program Update

August 1, 2022

**Monique Spyke**
*Managing Director*

| pfmam.com

*PFM Asset Management LLC*

***NOT FDIC INSURED : NO BANK GUARANTEE : MAY LOSE VALUE***

# Update

- Meetings held with staff, consultant, and PFMAM to further discuss investment policy recommendations and portfolio strategy and benchmarks.

| Meeting Topic | Outcome |
|---|---|
| June 1: Cashflow Discussion | Ongoing – SVCE performing internal analysis to determine allocation between cash and investments |
| June 14 and July 13: Investment Policy Discussions | Recommend expanding SVCE's list of permitted investments |
| July 20: Investment Strategy Discussion | Discussed maturity structure and benchmark for SVCE |

# Investment Policy and Permitted Investments

# Investment Universe vs. California Government Code

<table>
<tr><th></th><th></th><th>1 Day</th><th>180 Days</th><th>270 Days</th><th>1 Year</th><th>5 Years</th><th>Over 5 Years</th></tr>
<tr><td rowspan="13">Conventional Fixed Income</td><td>U.S. Treasuries</td><td colspan="5">Permitted</td><td>Requires Approval</td></tr>
<tr><td>Federal Agencies</td><td colspan="5">Permitted</td><td>Requires Approval</td></tr>
<tr><td>Municipal Securities</td><td colspan="5">Permitted</td><td>Requires Approval</td></tr>
<tr><td>Negotiable Certificates of Deposit</td><td colspan="5">Permitted</td><td>Requires Approval</td></tr>
<tr><td>Commercial Paper</td><td colspan="3">Permitted</td><td colspan="3">Prohibited</td></tr>
<tr><td>Bankers’ Acceptances</td><td colspan="2">Permitted</td><td colspan="4">Prohibited</td></tr>
<tr><td>Medium-Term Corporate Notes</td><td colspan="5">Permitted</td><td>Prohibited</td></tr>
<tr><td>Asset-Backed Securities (ABS)</td><td colspan="5">Permitted</td><td>Prohibited</td></tr>
<tr><td>Supranationals</td><td colspan="5">Permitted</td><td>Prohibited</td></tr>
<tr><td>Public Bank Debt</td><td colspan="5">Permitted</td><td>Requires Approval</td></tr>
<tr><td>Repurchase Agreements</td><td colspan="4">Permitted</td><td colspan="2">Prohibited</td></tr>
<tr><td>Money Market Funds/Bond Mutual Funds</td><td>Permitted</td><td colspan="5">Prohibited</td></tr>
<tr><td>Local Government Investment Pools</td><td>Permitted</td><td colspan="5">Prohibited</td></tr>
<tr><td rowspan="8">Broader Fixed Income</td><td>Foreign Sovereign</td><td colspan="6">Prohibited</td></tr>
<tr><td>Fixed-Income ETFs</td><td colspan="6">Prohibited</td></tr>
<tr><td>High-Yield Bonds</td><td colspan="6">Prohibited</td></tr>
<tr><td>Private Placements</td><td colspan="6">Prohibited</td></tr>
<tr><td>Convertibles</td><td colspan="6">Prohibited</td></tr>
<tr><td>Non-U.S. Dollar Investment Grade</td><td colspan="6">Prohibited</td></tr>
<tr><td>Emerging Markets Debt</td><td colspan="6">Prohibited</td></tr>
<tr><td>Bank Loans</td><td colspan="6">Prohibited</td></tr>
<tr><td rowspan="5">Equities</td><td>Domestic Equities (Large-, Mid-, Small Cap)</td><td colspan="6">Prohibited</td></tr>
<tr><td>International Equities (Large-, Mid-, Small Cap)</td><td colspan="6">Prohibited</td></tr>
<tr><td>Emerging Markets</td><td colspan="6">Prohibited</td></tr>
<tr><td>Preferred Stock</td><td colspan="6">Prohibited</td></tr>
<tr><td>Equity Mutual Funds and ETFs</td><td colspan="6">Prohibited</td></tr>
<tr><td rowspan="7">Alternatives</td><td>Commodities</td><td colspan="6">Prohibited</td></tr>
<tr><td>Real Estate</td><td colspan="6">Prohibited</td></tr>
<tr><td>Hedge Funds</td><td colspan="6">Prohibited</td></tr>
<tr><td>Private Equity</td><td colspan="6">Prohibited</td></tr>
<tr><td>Venture Capital</td><td colspan="6">Prohibited</td></tr>
<tr><td>Tangible Assets</td><td colspan="6">Prohibited</td></tr>
<tr><td>Complex Derivatives, Futures, and Options</td><td colspan="6">Prohibited</td></tr>
</table>

*Source: California Government Code Section 53601.*

# Expand List of Authorized Investments

- The table below summarizes the investment types we recommend SVCE add to its list of authorized investments. We are recommending most of the investment types allowed by Code.
  - SVCE's current Policy's list of authorized investments includes deposits at banks and LAIF.

| | California Code Allowed Investments | SVCE Approved 2017 Policy | 2022 PFMAM Recommendations |
|---|---|---|---|
| Overnight | Money Market Funds | Not permitted | Allow |
| | Local Government Investment Pools | Not permitted | Allow |
| Government | U.S. Treasuries | Not permitted | Allow |
| | Federal Agencies | Not permitted | Allow |
| | Municipal Obligations | Not permitted | **5% per issuer** |
| | Supranational Obligations | Not permitted | 5 years, "AA" rated,<br>30% of portfolio, **5% per issuer** |
| Credit | Commercial Paper | Not permitted | 270 days, A-1 rated,<br>40% of portfolio, **5% per issuer** |
| | Negotiable Certificates of Deposit | Not permitted | 30% of portfolio, **5% per issuer** |
| | Asset-Backed Securities | Not permitted | 5 years, "AA" rated,<br>20% of portfolio, **5% per issuer** |
| | Medium Term Notes | Not permitted | 5 years, "A" rated,<br>30% of portfolio, **5% per issuer** |

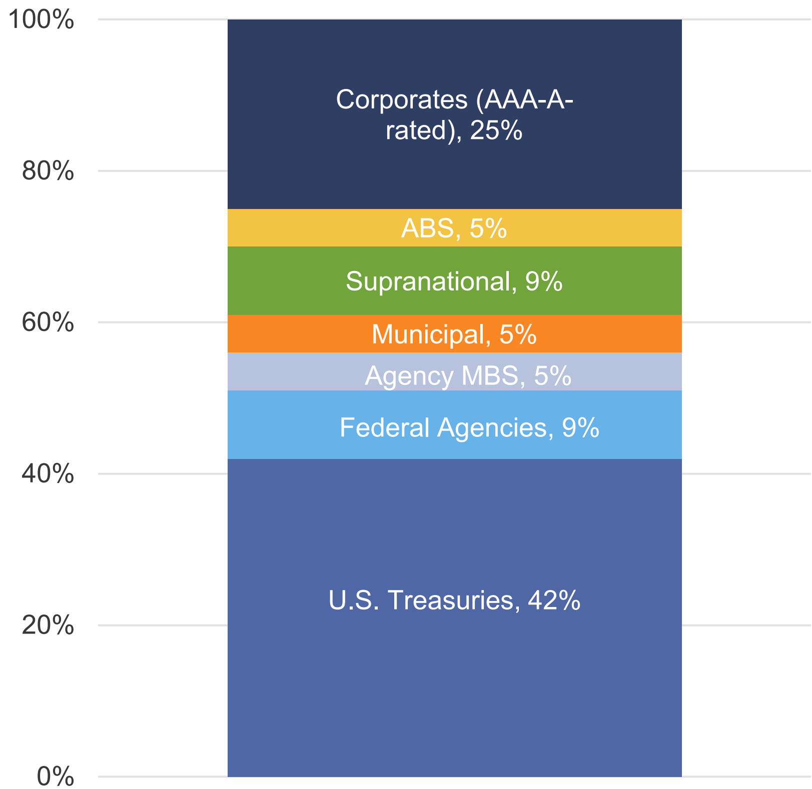
*California Government Code 53601. Other restrictions and requirements may be included in Code. Credit ratings apply to equivalent ratings and represent the rating category.*

# Allowing Broad Range of Investments Would Allow for a Diversified Portfolio



- A diversified portfolio enhances return potential and reduces volatility.

**Sample Portfolio Recommendation for SVCE**




**Average credit quality: AA**

**Maturity range: 1-3 years**

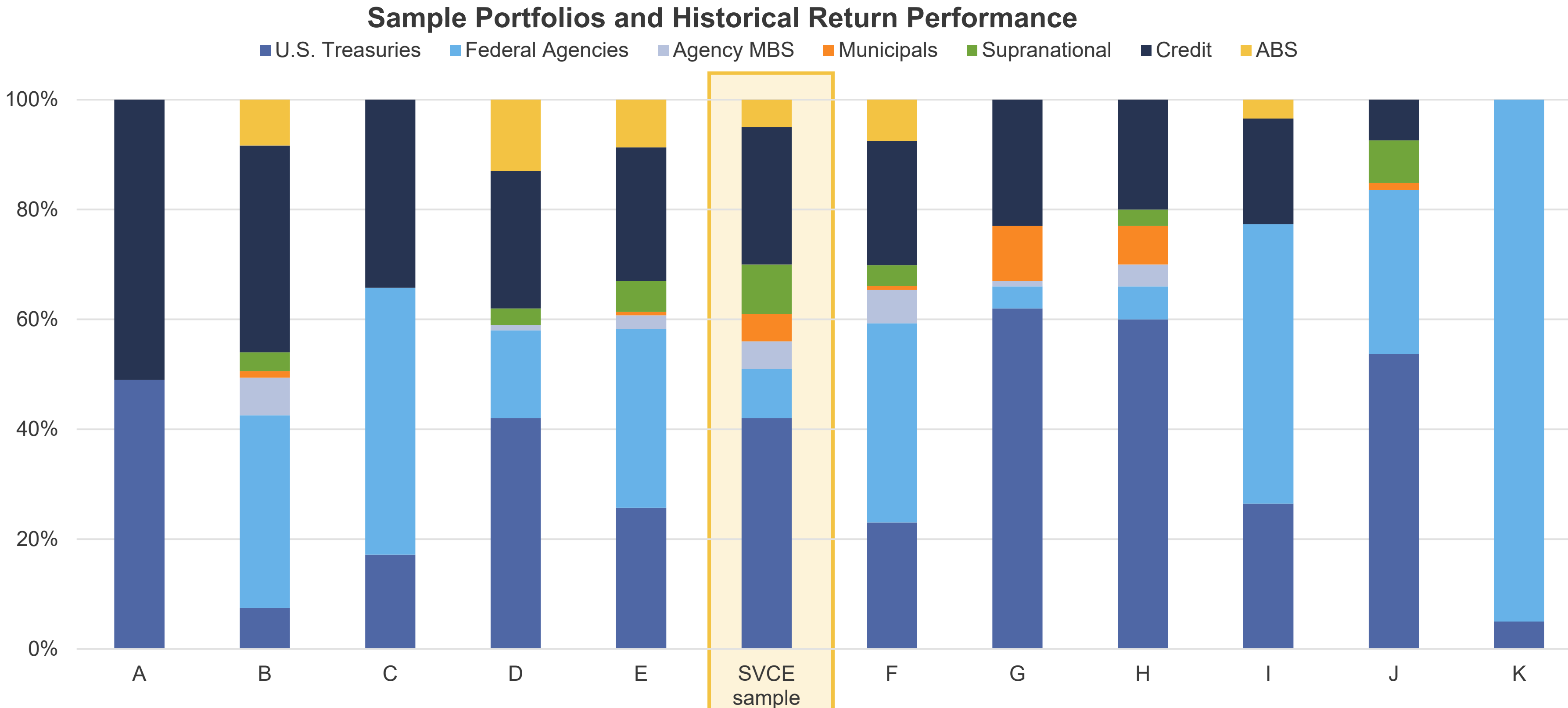
**Past 10-year average annual total return: 1.04%**

**Maturity range: 1-5 years**

**Past 10-year average annual total return: 1.20%**

*Portfolio recommended to SVCE as of July 13, 2022, and subject to change based on amount of funds that are invested, SVCE's permitted investments, the benchmark selected, and the interest rate environment at time of purchase. Total returns are based on ICE BofAMerrill Lynch 1-3 year or 0-3 year and 1-5 year or 0-5 year indices, for 10-years ended June 30, 2022. Assumes static sector allocation over time period.*

# Sample Portfolios and Historical Returns




| | A | B | C | D | E | SVCE sample | F | G | H | I | J | K |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Past 10-year average annual total return | 1.20% | 1.15% | 1.08% | 1.05% | 1.05% | 1.04% | 1.03% | 0.99% | 0.97% | 0.98% | 0.88% | 0.83% |
| Estimated Total Earnings (in millions) on $100 million | $12.61 | $12.15 | $11.38 | $11.03 | $10.96 | $10.91 | $10.78 | $10.30 | $10.11 | $10.21 | $9.13 | $8.61 |

*Total return based on ICE BofAMerrill Lynch 1-3 year or 0-3 year indices, for 10-years ended June 30, 2022. Total return calculation assumes static sector allocation over time period. Credit allocation may include corporate notes, commercial paper, and negotiable CDs.*

# Benchmark Discussion

# Benchmark Selection

- Purpose of a Benchmark:
  - Measures and evaluates relative investment performance;
  - Defines Provides for comparison of risk and return;
  - and evaluates a long-term investment strategy
- A Benchmark Should:
  - Be an independent representation;
  - Reflect asset mix, credit quality, and average maturity or duration of the portfolio; and/or
  - Be a baseline, such as a U.S. Treasury Index

# Historical Risk/Return Analysis

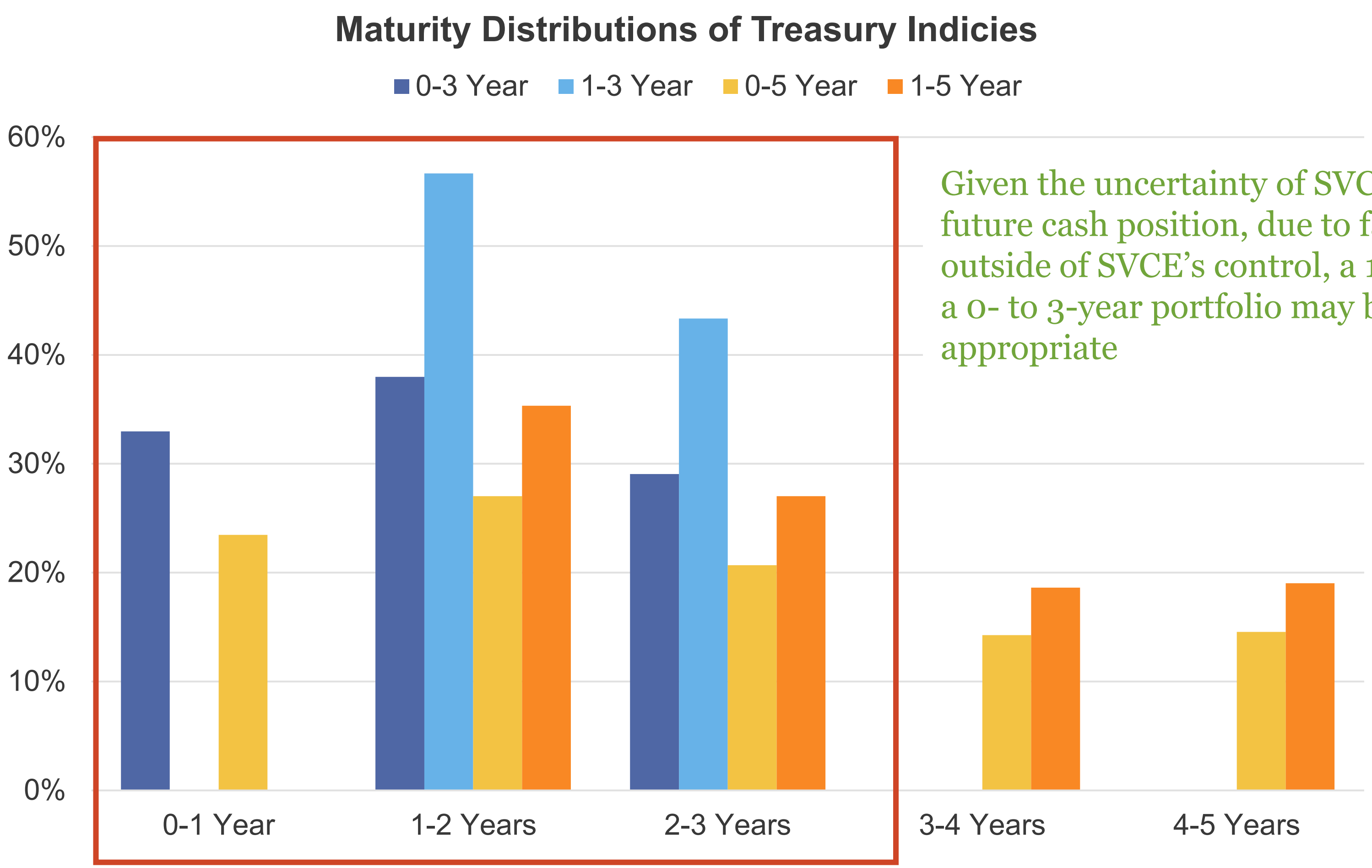
| Risk/Return of Various Investment Strategies<br>10 Years Ended June 30, 2022 | | | | |
|---|---|---|---|---|
| **Strategy** | **Duration** | **10-Year Average Annual Total Return** | **Cumulative Earnings on $100 Million** | **Quarters With Negative Return** |
| 0-3 Year U.S. Treasury Index | 1.41 | 0.77% | $107,965,034 | 10 out of 40 |
| 1-3 Year U.S. Treasury Index | 1.85 | 0.78% | $108,136,212 | 11 out of 40 |
| 0-5 Year U.S. Treasury Index | 2.10 | 0.86% | $108,971,116 | 12 out of 40 |
| 1-5 Year U.S. Treasury Index | 2.58 | 0.89% | $109,314,020 | 13 out of 40 |

Historically, longer-duration strategies have outperformed shorter strategies over the long term.

But with increased volatility.

*ICE BofA Merrill Lynch (BAML) Indices provided by Bloomberg Financial Markets. Direct investment in these indices is not possible.*

# Maturity Structure of Different Strategies




Given the uncertainty of SVCE's future cash position, due to factors outside of SVCE's control, a 1- to 3- or a 0- to 3-year portfolio may be most appropriate

*Source: As of June 30, 2022. ICE BofA Merrill Lynch (BAML) Indices.*

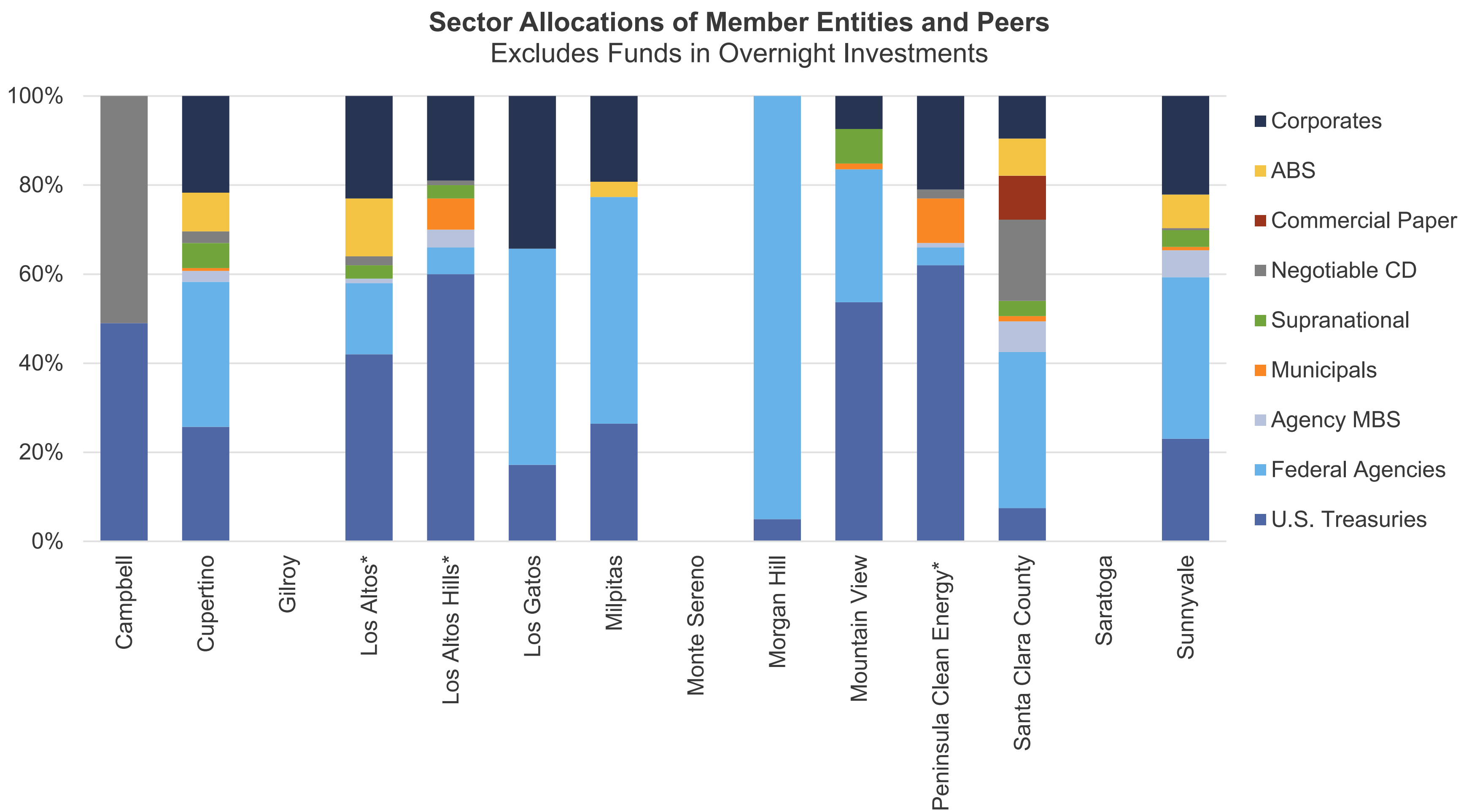
# Next Steps

- Approve Investment Policy
- Complete cash flow analysis to determine appropriate allocation between liquidity and core portfolios
- Determine benchmark/duration strategy

# Appendix

# Portfolio Composition of Member Entities and Peers






*Source: Financial reports from entity websites or PFMAM. Data as of June 30, 2021, or more current.*
** PFMAM fixed-income clients*

# Glossary of Terms

# Glossary

**ACCRUED INTEREST:** Coupon interest accumulated on a bond or note since the last interest payment or, for a new issue, from the dated date to the date of delivery.

**ANNUAL COMPREHENSIVE FINANCIAL REPORT (ACFR):** The official annual report of the *(entity).* It includes five combined statements for each individual fund and account group prepared in conformity with GAAP. It also includes supporting schedules necessary to demonstrate compliance with finance-related legal and contractual provisions, extensive introductory material, and a detailed Statistical Section.

**ASSET-BACKED SECURITIES**: Securities that are supported by pools of assets, such as installment loans or leases, or by pools of revolving lines of credits. Asset-backed securities are structured as trusts in order to perfect a security interest in the underlying assets.

**ASKED**: The price at which securities are offered.

**BANKERS' ACCEPTANCE (BA):** A draft or bill or exchange accepted by a bank or trust company. The accepting institution guarantees payment of the bill, as well as the issuer.

**BASIS POINTS**: Refers to the yield on bonds. Each percentage point of yield in bonds equals 100 basis points (1/100% or 0.01%). If a bond yield changes from 2.25% to 2.39%, that is a rate of 14 basis points.

**BENCHMARK**: A comparative base for measuring the performance or risk tolerance of the investment portfolio. A benchmark should represent a close correlation to the level of risk and the average duration of the portfolio's investments.

**BID**: The price offered by a buyer of securities. (When you are selling securities, you ask for a bid.) See Offer.

**BOOK RETURN**: Book return includes interest, amortization/accretion of premiums/discounts, realized gains and losses, over a given period of time.

**BOOK VALUE**: The value at which an asset is carried on a balance sheet.

**BROKER**: A broker brings buyers and sellers together for a commission.

**CALLABLE SECURITIES**: An investment security that contains an option allowing the issuer to retire the security prior to its final maturity date.

# Glossary

**CERTIFICATE OF DEPOSIT:** A short-term, secured deposit in a financial institution that usually returns principal and interest to the lender at the end of the loan period. Certificates of Deposit (CDs) differ in terms of collateralization and marketability. Those appropriate to public agency investing include:

*Negotiable Certificates of Deposit*

Generally, short-term debt instrument that usually pays interest and is issued by a bank, savings or federal association, state or federal credit union, or state-licensed branch of a foreign bank. The majority of negotiable CDs mature within six months while the average maturity is two weeks. Negotiable CDs are traded in a secondary market and are payable upon order to the bearer or initial depositor (investor). Negotiable CDs are insured by FDIC up to $250,000, but they are not collateralized beyond that amount.

*Non-Negotiable Certificates of Deposit*

CDs that carry a penalty if redeemed prior to maturity. A secondary market does exist for non-negotiable CDs, but redemption includes a transaction cost that reduces returns to the investor. Non-negotiable CDs issued by banks and savings and loans are insured by the Federal Deposit Insurance Corporation up to the amount of $250,000, including principal and interest. Amounts deposited above this amount may be secured with other forms of collateral through an agreement between the investor and the issuer. Collateral may include other securities including Treasuries or agency securities such as those issued by the Federal National Mortgage Association.

**COLLATERAL**: Securities, evidence of deposit or other property, which a borrower pledges to secure repayment of a loan. Also refers to securities pledged by a bank to secure deposits of public monies.

**COMMERCIAL PAPER**: An unsecured short-term promissory note issued by corporations or municipalities, with maturities ranging from 2 to 270 days.

**COUPON**: (a) The annual rate of interest that a bond's issuer promises to pay the bondholder on the bond's face value. (b) A certificate attached to a bond evidencing interest due on a payment date.

**CREDIT RISK**: The chance that an issuer will be unable to make scheduled payments of interest and principal on an outstanding obligation. Another concern for investors is that the market's perception of an issuer/borrower's credit will cause the market value of a security to fall, even if default is not expected.

# Glossary

**DEALER**: A dealer, as opposed to a broker, acts as a principal in all transactions, buying and selling for his own account.

**DEBENTURE**: A bond secured only by the general credit of the issuer.

**DELIVERY VERSUS PAYMENT**: There are two methods of delivery of securities: delivery versus payment and delivery versus receipt. Delivery versus payment is delivery of securities with an exchange of money for the securities. Delivery versus receipt is delivery of securities with an exchange of a signed receipt for the securities.

**DERIVATIVES**: (1) Financial instruments whose return profile is linked to, or derived from, the movement of one or more underlying index or security, and may include a leveraging factor, or (2) financial contracts based upon notional amounts whose value is derived from an underlying index or security (interest rates, foreign exchange rates, equities or commodities).

**DISCOUNT**: The difference between the cost price of a security and its maturity when quoted at lower than face value. A security selling below original offering price shortly after sale also is considered to be at a discount.

**DISCOUNT SECURITIES**: Noninterest-bearing money market instruments that are issued a discount and redeemed at maturity for full face value *(e.g., U.S. Treasury Bills.)*

**DIVERSIFICATION**: The allocation of different types of assets in a portfolio to mitigate risks and improve overall portfolio performance.

**DURATION**: A measure of the sensitivity of the price (the value of principal) of a fixed-income investment to a change in interest rates. Duration is expressed as a number of years. Rising interest rates mean falling bond prices, while declining interest rates mean rising bond prices.

**EFFECTIVE DURATION**: Duration measures the weighted average of the present value of the cash flows of a fixed-income investment. Effective duration measures the price sensitivity of fixed-income investments, especially for those with embedded option features such as call options. As yields rise, the effective duration of a callable investment rises to reflect the fact that it has become less likely to be called. The more rates rise, the longer the effective duration will become, approaching the duration to maturity. The converse is true in a declining interest rate environment (that is, the more rates fall, the shorter the effective duration will become, approaching the duration to call). For securities without an embedded option, the duration to call, maturity, and effective duration are all the same. The calculation for effective duration is complicated and involves averaging the duration under a simulation of many possible interest rate scenarios in the future.

**FEDERAL DEPOSIT INSURANCE CORPORATION (FDIC):** A federal agency that insures bank deposits, currently up to $250,000 per entity.

# Glossary

**FEDERAL FUNDS RATE**: The rate of interest at which Fed funds are traded. This rate is currently pegged by the Federal Reserve through open-market operations.

**GOVERNMENT ACCOUNTING STANDARDS BOARD (GASB)**: A standard-setting body, associated with the Financial Accounting Foundation, which prescribes standard accounting practices for governmental units.

**GOVERNMENT SPONSORED ENTERPRISES (GSE):** Privately held corporations with public purposes created by the U.S. Congress to reduce the cost of capital for certain borrowing sectors of the economy. Securities issued by GSEs carry the implicit backing of the U.S. Government, but they are not direct obligations of the U.S. Government. For this reason, these securities will offer a yield premium over Treasuries.

**INTEREST**: The amount a borrower pays to a lender for the use of his or her money.

**INTEREST RATE RISK**: Interest rate risk is the risk that an investment's value will change due to a change in the absolute level of interest rates, spread between two rates, shape of the yield curve, or any other interest rate relationship.

**LIQUIDITY:** A liquid asset is one that can be converted easily and rapidly into cash without a substantial loss of value. In the money market, a security is said to be liquid if the spread between bid and asked prices is narrow and reasonable size can be done at those quotes.

**LOCAL AGENCY INVESTMENT FUND**: A voluntary investment fund open to government entities and certain non-profit organizations in California that is managed by the State Treasurer’s Office.

**LOCAL GOVERNMENT INVESTMENT POOL (LGIP)**: The aggregate of all funds from political subdivisions that are placed in the custody of the State Treasurer for investment and reinvestment.

**MARKET RISK:** The chance that the value of a security will decline as interest rates rise. In general, as interest rates fall, prices of fixed income securities rise. Similarly, as interest rates rise, prices fall. Market risk also is referred to as systematic risk or risk that affects all securities within an asset class similarly.

**MARKET VALUE**: The price at which a security is trading and could presumably be purchased or sold.

# Glossary

**MASTER REPURCHASE AGREEMENT**: A written contract covering all future transactions between the parties to repurchase—reverse repurchase agreements that establishes each party's rights in the transactions. A master agreement will often specify, among other things, the right of the buyer-lender to liquidate the underlying securities in the event of default by the seller borrower.

**MATURITY**: The date upon which the principal or stated value of an investment becomes due and payable.

**MEDIUM TERM NOTES:** Corporate and depository institution debt securities with a maximum remaining maturity of five years or less, issued by corporations organized and operating within the United States or by depository institutions licensed by the United States or any state and operating within the United States.

**MONEY MARKET:** The market in which short-term debt instruments (bills, commercial paper, bankers' acceptances, etc.) are issued and traded.

**MONEY MARKET MUTUAL FUNDS**: MMF's are mutual funds that invest exclusively in short-term money market instruments. MMF's seek the preservation of capital as a primary goal while maintaining a high degree of liquidity and providing income representative of the market for short-term investments.

**MORTGAGE BACKED SECURITIES:** Mortgage-backed securities (MBS) are created when a mortgagee or a purchaser of residential real estate mortgages creates a pool of mortgages and markets undivided interests or participations in the pool. MBS owners receive a prorata share of the interest and principal cash flows (net of fees) that are "passed through" from the pool of mortgages. MBS are complex securities whose cash flow is determined by the characteristics of the mortgages that are pooled together. Investors in MBS face prepayment risk associated with the option of the underlying mortgagors to pre-pay or payoff their mortgage. Most MBS are issued and/or guaranteed by federal agencies and instrumentalities (e.g., Government National Mortgage Association (GNMA), Federal National Mortgage Association (FNMA), and Federal Home Loan Mortgage Corporation (FHLMC)).

**MORTGAGE PASS-THROUGH OBLIGATIONS:** Securities that are created when residential mortgages (or other mortgages) are pooled together and undivided interests or participations in the stream of revenues associated with the mortgages are sold.

**MUNICIPAL NOTES, BONDS, AND OTHER OBLIGATIONS**: Obligations issued by state and local governments to finance capital and operating expenses.

# Glossary

**NET ASSET VALUE**: Net asset value (NAV) is a term used in the mutual fund industry to determine the average price per share of a pool or mutual fund. How this measure varies over time provides information on whether the pool is stable or variable. NAV is the market value of all securities in a mutual fund, less the value of the fund's liabilities, divided by the number of shares in the fund outstanding. Shares of mutual funds are purchased at the fund's offered NAV.

**OFFER**: The price asked by a seller of securities. (When you are buying securities, you ask for an offer.) See Asked and Bid.

**PAR AMOUNT OR PAR VALUE**: The principal amount of a note or bond which must be paid at maturity. Par, also referred to as the "face amount" of a security, is the principal value stated on the face of the security. A par bond is one sold at a price of 100 percent of its principal amount.

**PORTFOLIO**: Combined holding of more than one stock, bond, commodity, real estate investment, cash equivalent, or other asset. The purpose of a portfolio is to reduce risk by diversification.

**PRIMARY DEALER**: A group of government securities dealers who submit daily reports of market activity and positions and monthly financial statements to the Federal Reserve Bank of New York and are subject to its informal oversight. Primary dealers include Securities and Exchange Commission (SEC)-registered securities broker-dealers, banks, and a few unregulated firms.

**PRUDENT INVESTOR STANDARD:** A standard of conduct where a person acts with care, skill, prudence, and diligence when investing, re-investing, purchasing, acquiring, exchanging, selling, and managing funds. The test of whether the standard is being met is if a prudent person acting in such a situation would engage in similar conduct to ensure that investments safeguard principal and maintain liquidity.

**PUBLIC BANK**: A corporation, organized as either a nonprofit mutual benefit corporation or a nonprofit public benefit corporation for the purpose of engaging in the commercial banking business or industrial banking business, that is wholly owned by a local agency, as specified, local agencies, or a joint powers authority.

**QUALIFIED INSTITUTIONAL BUYER**: Federal regulations define qualified institutional buyer (QIB) as any of the following entities, acting for its own account or the accounts of other QIBs, that in the aggregate owns and invests on a discretionary basis at least $100 million in securities of issuers that are not affiliated with the entity: insurance company, investment company, small business investment company, a Rural Business Investment Company, a plan (established and maintained by a public agency) for the benefit of its employees, employee benefit plan, trust fund (bank or trust company), business development company, 501(c)(3), investment adviser, and dealer, an institution that qualifies as an accredited investor. 17 CFR § 230.144A and 230.145

# Glossary

**RATE OF RETURN**: The yield obtainable on a security based on its purchase price or its current market price. This may be the amortized yield to maturity on a bond the current income return.

**REINVESTMENT RISK**: The risk that interest rates may be lower than the yield on a fixed income security when the investor seeks to reinvest interest income or repaid principal from the security.

**REPURCHASE AGREEMENT (REPO):** A holder of securities sells these securities to an investor with an agreement to repurchase them at a fixed price on a fixed date. The security "buyer" in effect lends the "seller" money for the period of the agreement, and the terms of the agreement are structured to compensate them for this.

**REVERSE REPURCHASE AGREEMENT (REVERSE REPO)**: A reverse-repurchase agreement (reverse repo) involves an investor borrowing cash from a financial institution in exchange for securities. The investor agrees to repurchase the securities at a specified date for the same cash value plus an agreed upon interest rate. Although the transaction is similar to a repo, the purpose of entering into a reverse repo is quite different. While a repo is a straightforward investment of public funds, the reverse repo is a borrowing.

**SAFEKEEPING**: A service to customers rendered by banks for a fee whereby securities and valuables of all types and descriptions are held in the bank's vaults for protection.

**SECONDARY MARKET**: A market made for the purchase and sale of outstanding issues following the initial distribution.

**SECURITIES & EXCHANGE COMMISSION**: Agency created by Congress to protect investors in securities transactions by administering securities legislation.

**SEC RULE 15C3-1:** See Uniform Net Capital Rule.

**STRUCTURED NOTES**: Notes issued by Government Sponsored Enterprises (FHLB, FNMA, FHLMC, etc.) and Corporations, which have imbedded options (e.g., call features, step-up coupons, floating rate coupons, derivative-based returns) into their debt structure. Their market performance is impacted by the fluctuation of interest rates, the volatility of the imbedded options and shifts in the shape of the yield curve.

**SUPRANATIONAL INSTITUTIONS:** International institutions formed by two or more governments that transcend boundaries to pursue mutually beneficial economic or social goals. There are three supranational institutions that issue obligations that are eligible investments for California local agencies: the International Bank for Reconstruction and Development (IBRD), International Finance Corporation (IFC), and Inter-American Development Bank (IADB).

# Glossary

**TOTAL RETURN**: Total return includes interest, realized gains and losses, and unrealized gains and losses over a given period of time.

**U.S. TREASURY OBLIGATIONS**: Debt obligations of the U.S. Government sold by the Treasury Department in the forms of bills, notes, and bonds. Bills are short-term obligations that mature in one year or less and are sold at a discount. Notes are obligations that mature between one year and ten years. Bonds are long-term obligations that generally mature in ten years or more.

**WEIGHTED AVERAGE MATURITY (WAM):** The average maturity of all the securities that comprise a portfolio, typically expressed in days or years.

**YIELD:** The rate of annual income return on an investment, expressed as a percentage. (a) INCOME YIELD is obtained by dividing the current dollar income by the current market price for the security. (b) NET YIELD or YIELD TO MATURITY is the current income yield minus any premium above par or plus any discount from par in purchase price, with the adjustment spread over the period from the date of purchase to the date of maturity of the bond.

**ZERO-COUPON BOND:** A bond on which interest is not payable until maturity (or earlier redemption), but compounds periodically to accumulate to a stated maturity amount. Zero-interest bonds are typically issued at a discount and repaid at par upon maturity.

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