

Independence Power and Light

Electric Utility Governance White Paper

Purchase Order: 24000832

Prepared for:

City of Independence, Missouri

DKMT Consulting LLC
Veteran-Owned Small Business
DUNS 079366847
CAGE 73XD5
4626 Loral Lane
Orefield, PA 18069
(847) 275-3780
www.dkmtconsulting.com

August 6, 2024

DKMT Consulting LLC was engaged to provide an independent analysis of the costs incurred and the benefits received from the City of Independence's ownership of Independence Power and Light, as well as a strategic plan and a review of electric utility governance models. The purpose of this document is to inform decision-makers and stakeholders in their evaluation of alternative governance models for IPL.

In the American Public Power Association's book, *Governing for Excellence — Raising the Bar on Public Power Governance*, author Jeff Tarbert notes that "today's (industry) evolution is driven not by anti-monopoly-leaning economists or the philosophical preferences of regulators. The prime movers today are new technologies, changing markets, innovative non-utility entrants, and changing customer expectations. Customer expectations will sustain this transition. Declining electric sales, increasing penetration of renewable energy, and community choice aggregation are three other forces stretching the industry and public power governance models.

There are two main public power utility governance models. A 2015 survey by APPA showed that smaller public power utilities tended to be governed by city councils, while larger members more often are governed by independent or semi-independent boards. Independence Power and Light is not a small utility. The 2024 APPA industry statistical report shows IPL ranked 56th in the number of customers and 95th in net generation among all public power entities in the country.

APPA data shows that independent boards perform the majority of governance functions among public power utilities with more than 50,000 customers.

The following table summarizes the functional authority breakdown by types of governance structure.

Governance Functions ¹

	Independent Boards	Council	Other
Set retail rates	70%	30%	0%
Approve utility budget	70%	30%	0%
Set salaries of key utility officials	87%	9%	4%
Issue long-term bonds	57%	39%	4%
Make financial investments for the utility	78%	4%	18%
Approve PPAs	83%	4%	13%
Exercise the right of eminent domain	52%	39%	9%
Hire and fire utility personnel	57%	0%	43%

In the city council model, the utility is a unit of the city government. The city council functions as the utility governing board and regulator, setting electric prices and deciding on important matters. In the independent board model, the utility is governed by an independent or semi-independent board.

The city council model offers a public power utility’s customer-owners the opportunity to vote for candidates who will ensure that the community’s views are implemented. Having to face the voters on election day nurtures accountability. A drawback to this model and an elected board model is that it does not remove politics from the governance of the municipal utilities. During a call with the City of Springfield, MO, it was mentioned that one of the primary reasons for their success was that their governance model removed politics from utility-related decisions and has strong protections to keep them out. For example, their charter states:

Section 16.5. - Restrictions on the board.

Not more than six members of the said board shall belong to the same political party, and the administration of such board shall be in all respects entirely nonpartisan. No member of the said board shall, during his term of office thereon, be a candidate for office, nor shall he hold any other office, either school board, city, county, state, or federal during his official term; nor shall he be a member of any party organization or committee to further the candidacy of any person for municipal public office. Upon becoming a candidate for public office or accepting any of the offices aforesaid, during the term, he shall be deemed thereby to have immediately resigned as a member of the said board, and his membership shall be thereby ipso facto vacated.

A member of the board shall be prohibited for a period of one (1) year after leaving his position on the board from being hired as an employee of the board.

¹ APPA *Governing for Excellence — Raising the Bar on Public Power Governance*

Other Governance Structure Examples

There are a number of other governance structures that are used within public power:

In Seattle, the Mayor appoints the General Manager (GM) of the electric utility and the GM is accountable to the Mayor and City Council. In addition, Seattle has a City Light Review panel, comprised of citizens, whose function is to solely review and assess Seattle City Light's strategic plan and provide an opinion to council. They also review rates not covered in the code and provide an opinion to the mayor, as well as assist in engaging the public. Annual rate increases are tied to the CPI and the city can control staffing of the utility through the HR and budgeting process.

Long Island Power Authority—the Governor of New York appoints a Board. Board members represent the areas served by LIPA, and make all decisions concerning policy, rates, and financial performance. The utility itself is managed by an Executive Director.

CPS Energy of San Antonio—This Board is an independent board comprised of appointed citizens approved by city council and represent each of the four geographic quadrants of the city. Board members are appointed for five-year terms which can be renewed for an additional five years. This particular structure is called for by covenants within the Bond Resolutions. While the Mayor of San Antonio is an ex-officio voting member of the Board, neither the mayor, nor any members of the City of San Antonio management, participate in the policies or operational activities of CPS Energy. In addition to approving Board members, City Council participation is restricted to approval of rate adjustments, debt issuance, and condemnation proceedings.

City Utilities of Springfield—City Utilities is governed by an 11-member Board of Public Utilities appointed by the Springfield City Council to serve three-year terms. The Board establishes policies on how to best serve customers and sets the long-term direction for the utility as outlined in the City Charter.

The following table summarizes the pros and cons of various governance models.

Strategic Function	City Council	Advisory Board	Independent Board
Budget Approval/Oversight	Pro – in small community Con for large utilities with significant budgets – council lacks time and expertise to focus on utility specific issues. The utility budget is reviewed and monitored along with every other department of the city which limits the amount of resources council can devote to strategic planning, monitoring, and reviewing performance.	Pro – when used properly, Advisory Board can have the time and resources to review budget and make informed recommendations to council, which if Advisory Board (AB) is delegated responsibilities and trusted by council, it can prove to be a useful resource.	Pro – the Utility is the sole focus of the Independent Board which has the time and resources to review the budget, ensure alignment with strategic goals, and work with the utility to establish accountability and reporting metrics for monitoring performance.
Rates	Pro – council has ultimate accountability for implementing rates that meet the needs of the community. Con - However, because of the limited time and expertise of council, deliberations can be lengthy, politically driven and the process not always understood, resulting in less than optimum decisions.	Pro – AB can devote time and through experience, have a deeper understanding of how rates are developed and the drivers of change and rate design. If used properly can be a resource for recommendations to the council. Con – no decision-making authority and council can choose to disregard AB recommendations.	Pro – because the board is independent, the rate review can be less politically driven, and more business focused. Allowing for financially driven changes and potential for innovation in rate design. More flexibility and nimbleness in decision making.
Strategic Planning/Innovation	Pro – council working jointly with the utility to develop a strategic plan and monitor the	Pro – similar to an independent board, if delegated authority to develop strategic	Pro – Because Independent Boards either come with specific expertise or

Strategic Function	City Council	Advisory Board	Independent Board
	<p>utility allows it to drive strategies that closely align with the community's values.</p> <p>Con – because it can be a lengthy process due to time availability of council, the product and process can be less optimal and targeted toward innovation.</p>	<p>plans, monitor, and report results to council, can be effective and a good liaison between community and utility.</p> <p>Con – if not delegated authority to develop and monitor strategic planning and goals, responsibility falls on city council. This is another item added to an already overburdened council and tends to not be a priority until things go wrong.</p>	<p>develop it during their tenure, they are focused only on the utility and can be better informed on trends, business drivers and needs of the community and the utility. The board has the time to devote to strategic planning and understanding the needs and impacts of the community. An independent board can also focus on public outreach and communication, serving as a liaison between utility and oversight. Therefore, more closely aligned with the overall community. Utilities governed by an independent board are more likely to have regular community engagement and be more innovative than other utilities with council forms of government. (Ex: CPS Energy, LCRA)</p>
Membership	Must be a city resident and no experience requirement other than what is required to run for office.	Typically, a resident of the city because appointed by the council but can have more flexibility. Council can establish experience requirements.	By charter can be both resident or non-resident if focus is on recruiting specific expertise or it may require representation of different sectors of the community, such as geographic or

Strategic Function	City Council	Advisory Board	Independent Board
			customer type. Governing document can establish job requirements that most benefit their role for the utility.

Board Member Roles

Regardless of the model, according to APPA, a board or city council member must master four different roles to oversee a municipal utility effectively. First, they need to recognize they are a Trustee and have legal and fiduciary responsibilities to ensure the utility remains financially stable. Second, they are a Regulator and have responsibilities to ensure the utility meets local, state, and federal regulations concerning environmental, safety, and market regulations. Third, they are a Representative of the community and must ensure that the community’s desires are reflected in the utility's strategic planning process. Lastly, they are an Advocate for public power and need to promote the benefits of public power. All these roles require different skill sets, and a well-functioning board will have individuals who have varying degrees of competence in each of these roles.

The board needs to keep foremost in mind that the goal of public power governance is not profit maximization. Rather, it is to ensure that the utility:

- Covers the cost of operations.
- Meets debt service requirements and funds infrastructure and technology needs.
- Provides service that is highly reliable and responsive.
- Goals, plans and programs reflect the priorities of the community.
- Supports compensation plans sufficient to attract and retain a skilled workforce.
- Sustains the organization’s financial stability by meeting standards of liquidity, funding necessary reserves, and protecting against risk.
- Charges fair, competitive, and transparent rates for service

The electric utility industry is complex and changing rapidly. Board member tenures must be long enough for them to educate themselves in the industry and seek training on specific issues. Board members are not expected to nor is there a desire for them to make decisions better left to utility management.

It is important that the board “stay in its lane” and that utility management does the same.

This Board is typically responsible for setting strategic direction and approval of a multi-year strategy which should reflect the community's goals and ambitions related to green energy/energy mix, electrification, customer service standards, and rate objectives. This Board is involved in defining what the utility should be providing to the citizens and utility customers.

The Board has the power to hire and fire the utility's General Manager and should trust management to carry out the strategic plan it adopted. Some governance models have an independent auditor, general counsel, comptroller, or secretary reporting to the board in addition to the General Manager to ensure third-party oversight.

Utility Leadership responsibilities include the following:

- Independently manages day-to-day utility operations,
- Supports the development of the Utility's strategic plans to support the city's strategic goals.
- Develops the budget to achieve those goals and manages the utility's financial reporting system.
- Ensure a well-trained workforce.
- Defines and models the culture of the utility, focusing on service.
- Develops and maintains an effective Safety Culture
- Updates Board and Council on progress toward achieving those goals and strategies.
- Meets the Board-Level established key performance targets.
- Sharing services as appropriate for the benefit of the city

According to APPA, there are five things that a successful board must do to have effective governance.

1. Meet Legal and Fiduciary Responsibilities

Board members need to ensure that they understand their oversight function, ethics laws, meeting and record-keeping requirements, communication protocols, and open records requirements.

2. Assure an effective General Manager

The Board has the power to hire and fire its head manager and is responsible for setting his or her performance goals. There should be a formal written process for evaluating General Manager performance, and performance measures should be tied to the utility's strategic goals. There should be clear and written delineations of authority regarding management and board responsibilities. For example, typically, senior managers who report to the General Manager are not interviewed by the Board prior to their hiring; that responsibility rests solely within the purview of the General Manager.

Apart from positions that report to the board, salary levels are typically the responsibility of the GM. The board approves the budget and should require the GM to provide regular reports on the financial status and operations of the utility, as well as performance in achieving strategic objectives.

3. Set strategic direction and priorities.

The board is responsible for developing the utility's strategic direction and long-term priorities in collaboration with outside experts, utility management, the financial community, the City Council, and the public. The Board should establish a formal strategic planning process that is updated at least every five years or sooner as conditions dictate. As part of the strategic planning process, the board should implement performance measures and targets that utility management is expected to achieve. For example, if lower rates are the most important measure of performance, what is the benchmark for measuring success?

The strategic plan guides utility management decisions and provides outside stakeholders a means to measure utility management performance.

4. Monitor performance.

The most frequently exercised board responsibility is monitoring utility performance. At least monthly, the General Manager should provide the board with a written status report on utility performance. Standard reporting items should include actual costs to budgets, reliability, working capital, and staffing.

The utility should oversee its financial reporting system, which should be aligned with the FERC chart of accounts (which allows comparability to other utilities) or a similar management reporting system. Regular reporting on budget to actual performance, cash reserve levels, debt service coverage and other debt or management requirements allows the board to exercise fiscal oversight. In addition, analysis of variances and corrective action or changes to plans should be presented to the board, when needed.

PILOT, inter-fund transfers, and shared services with the city should be reported monthly on the utility's cash flow statement. For IPL, this could look something like the table below.

Fund Transfer Activity	Last Year	YTD	Budget YTD
IPL Transfer to Water Dept for Customer Services	\$ (2,451,852)	\$ (1,225,926)	\$ (1,471,111)
IPL Transfer to Finance and Administration for Support	(2,893,851)	\$ (1,446,926)	\$ (1,736,311)
School District Transfer to IPL for Fiber Support	\$ 230,000.00	\$ 115,000	\$ 138,000
Water Department Transfer to IPL for Meter Reading	(2,092,268)	\$ (1,046,134)	\$ (1,255,361)
General Fund Contribution	\$ (1,168,553)	\$ (584,277)	\$ (701,132)
PILOT	\$ (14,000,000)	\$ (7,000,000)	\$ (8,400,000)

Capital projects, PPA performance and other salient attributes should also be reported on as agreed to by the board and utility management.

Ideally, the utility would create a dashboard of performance metrics, in conjunction with its oversight board, which are presented at regular intervals informing the board and the public about IPL's performance.

- Evaluate and improve governance performance!
Lastly, the board should evaluate its performance on an annual basis and identify areas for improvement in its current oversight functions.

Current State

City Governance for IPL

As with most public utilities, governance is typically addressed as part of the individual City Charter. Under the current Independence City Charter, governance organizations include:

- The City Council, which is composed of seven elected members, is responsible for oversight of all governmental activities. Their major responsibilities include:
 - To appoint and remove the City Manager
 - To enact municipal legislation relating to any or all subjects and matters within the powers of the City.
 - To adopt the budget, provide revenues, and make appropriations; regulate salaries, wages, and other compensation of officers and employees; and regulate all other fiscal affairs of the City.
 - To sell and convey any and all property belonging to the city both personal and real, after ample opportunity for competitive bidding,
 - To adopt in its entirety or in parts a master plan for the physical development of the city and its environs and to make changes therein.

- To appoint or elect and, with or without cause, remove the members of the personnel board, of the city planning commission, of the board of adjustment, of the public utilities advisory board, and of the board of ethics, and other quasi-legislative, quasi-judicial, or advisory officers and authorities, now or when and if established; and to provide the method of appointing or electing and removing them; and
- To create, change, and abolish all offices, departments, and agencies of the city government other than the offices, departments, and agencies created by this charter; and to assign additional powers, duties, and functions consistent with this charter to offices, departments, and agencies created by this charter.

The City Council has other powers and responsibilities, but those listed above are most relevant to the issue of governance in the City.

- The City Manager’s responsibilities include management of the day-to-day operations of the City’s departments. Section 3.3 describes the City Manager’s powers and duties. “The city manager shall be chief administrative officer and head of the administrative branch of the city government. The city manager shall execute the laws and ordinances and administer the government of the city and shall be responsible therefore to the council.”
- The Public Utility Advisory Board (PUAB) is addressed in Section 3.15. “There shall be a public utilities advisory board, composed of seven (7) members appointed by the council for overlapping four (4)-year terms.” The powers of the PUAB include the following:
 - May initiate on its own or upon request of the Council or City Manager investigations of public utilities operated within the City.
 - May conduct public hearings on matters relating to public utilities and, through its chairperson, administer oaths and affirmations.
 - May obtain from any city department, officer, and agency and from any public utility operated within the city any available information that is required for its work.
 - May recommend to the executive or legislative officials of the city, programs for the financing, use, ownership, service, operation, or franchising of public utilities operated within the city, including but not limited to recommendations regarding rate adjustments, long-range planning, the employment and termination of the services of consultants to the city, the review of

recommendations made by consultants to the city, the issuance of debt obligations of the City and the construction of new and expansion of existing facilities; and

- Shall report its findings and recommendations at least annually, to the council, the people of the City, the City Manager and the respective director(s) of the public utility operated within the City.

In addition, Section 3.18 requires that the Council consult with the PUAB, giving the Board ample time to evaluate recommendations of the IPL Director, and consider their recommendations. In circumstances where the Council does not adopt PUAB recommendations, the Council is required to give their reasons for the decision.

The majority of the powers of the PUAB are centered on audit, investigative, or enforcement type actions and are not typical of oversight board primary functions. However, what is significant is the provision to provide recommendations related to programs, financing, use, rates, etc. These are more in line with advisory boards but has not been a focus or delegation of authority to the PUAB.

- Electric Utility Director responsibilities include the development of strategies in the best interests of the city and the community, as well as of the day-to-day operations of IPL.

Section 3.17 of the City Charter states as follows:

“The municipally owned and operated electric system is a public utility and shall be operated in a businesslike manner.

The electric utility shall not be operated for the benefit of other municipal functions and shall not be used directly or indirectly as a general revenue producing agency for the city, but it may pay to the city an amount in lieu of such taxes as are normally placed upon private business enterprises. After providing for depreciation accruals and amortization of bonds, and for reasonable accumulation of surplus, the electric utility shall apply all annual profits to rate reductions.

The electric utility and such other public utilities and enterprises as the city may acquire shall be operated from funds separate from the general fund. An accounting system for each such fund shall be established within the general accounting system of the city and shall be so set up and maintained as to reflect annually or as often as the council may require the financial condition of the enterprise and its income and expense.”

What is also notable about the charter, is it does not preclude the utility from investing in programs that support economic growth which benefit the community.

Observations

Based upon interviews in both this engagement and the previous study performed by DKMT, we have observed the following concerning the governance of IPL.

- Through the election process there is a significant turnover of council membership, which leads to a lack of continuity in the understanding of issues facing IPL. If the city established an independent utility board with members appointed by the council for 3-4 year terms this could address this issue, along with staggered terms facilitating smooth succession and knowledge transfer, as well as limiting political drivers to decision making.
- The council has significant oversight responsibilities for every major aspect of the City, which limits the amount of time they can devote to IPL, the City's largest asset.
- The council lacks ownership for the strategic direction of IPL. There appear to be no council-adopted plans for IPL beyond the current fiscal year nor accountability for performance. An independent utility board would have the strategic plan for IPL as a singular focus.
- There is no process for tying a revenue requirement to electric rates. An independent board would have control over the finances of all utilities it oversees and would be tasked with developing a transparent rate process.
- IPL's financial records are opaque and the city controls IPL financial information. An independent board would oversee IPL finances and issue bonds with the concurrence of the City Council.
- Under current governance, it is difficult for IPL to assist with the economic development of the city. The Board should have the power to promote energy efficiency and support economic development within the City of Independence.
- The Public Utilities Advisory Board is underused based on the charter authority.
- Administrative requirements for Council decisions prolong and hinder common management functions, i.e., equipment purchases etc.. A Board with business or utility specific expertise should have the power to enter into PPA's and sign contracts which may be able to streamline this process.

- Utilities governed by independent boards, with targeted expertise, tend to be more progressive, engaged with their community and able to implement innovation to serve their community.