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# Financial Planning for Enterprise Funds: Tips/Strategies

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# **Enterprise Funds**

### Generally Accepted Accounting Principles (GAAP):



- Used to Account for "Business-Type Activities" Similar to Those Found in the Private Sector
- Business-Type Activities
   Include Services Primarily
   Funded Through User
   Charges



# **Planning for Enterprise Funds**

# Solid Business Foundation Based on Best Management Practices

# **Realistic Operational and Financial Plan**

Effective, Ongoing Communication Program



# Establishing a Solid Business Foundation Based on Best Management Practices



#### Publications from Credit Rating Agencies Discuss Enterprise Best Management Practices



- Credit Rating Agencies Will Usually Freely Provide These Publications to Issuers That They Rate, and Your Financial Advisor or Rate Consultant May Also Have Copies
- Rating Agencies Will Typically Request Copies of Financial Management Policy Documents
- Rating Criteria Are Always Evolving
  - Median Debt Service Coverage Ratios and Cash Balances Have Been Trending Upward



# The Local Government's Credit Rating Is a Reflection of Management (\*)

#### Assessment of Financial Risk

- Management Has Limited Control Over Some Elements of Financial Risk (e.g., One Large Customer Accounts for 50% of Revenues)
- Best Management Practices on Controllable Factors Help to Reduce Implied Financial Risk, and Can Lead to Lower Rates Over the Long Term
  - Higher Credit Ratings, Lower Interest Rates, and Lower Issuance Costs When Debt Financing



(\*) Management Includes Governing Body





# What Are the Management Practices of Highly-Rated Enterprises?





# **Highly-Rated Enterprises...**

 Exhibit Practices That Maximize Stability By Planning

- The More Written and Adopted Policies, Procedures, and Plans, the Better! (Rating Agencies Will Request Copies)
- Anticipate Future Regulatory and Growth Demands

 Reliably Implement Steady Rate Increases Over Time

 Have Liquidity to Meet Unexpected Sales Shortfalls / Emergencies

It's Never Too Late to Improve the Business Foundation!



# **Establishing the Business Foundation**

#### Establish Business Principles

- Serve as Basis for Long-Term Decision Making
- Examples:
  - Public Health and Safety
  - Maintain Financial Creditworthiness
  - Rates Affordable and Recover Full Cost of Service
  - Comply With Regulations
  - Uninterrupted Service
  - Customer Satisfaction
- Adopt Long-Term Business Plan
  - Expansion Plans
  - Sustainability Plans
  - Updated Every Few Years
- Adopt Formal Debt Management Policy



# **Establishing the Business Foundation (cont.)**

- Adopt Financial Management Policies and Performance Measures, Ideally in a Single Document
  - Debt Service Coverage
    - Should Exceed Minimum Required (e.g., 200% "All-In" Coverage)
  - Cash Reserve Policy
    - Working Capital
      - (e.g., 120 Days of Operating Revenue)



- Capital Replacement Deposits Based on Asset Management Plan or % of Revenues
  - Could Also Consider Annual Depreciation Expense
- Rating Agencies: Enterprise With Stronger Financial Profile Might Have Days Cash on Hand Equal to One Year or More

<u>Days Cash on Hand</u> = Unrestricted cash and investments divided by operating expenditures minus depreciation, divided by 365



# **Sample Asset Management Plan**

	Estimated	Percent to Be	Amount to Be	Asset Service	Annual	<b>In-Service</b>	Replacement
Description	Replacement Cost [1]	Cash-Funded [2]	Cash-Funded	Life (Years)	Funding Amount [3]	Year	Year
Asset 1	\$1,000,000	50.00%	\$500,000	30	\$16,667	1996	2026
Asset 2	25,000,000	25.00%	6,250,000	30	208,333	2012	2042
Asset 3	6,000,000	25.00%	1,500,000	30	50,000	2017	2047
Asset 4	50,000	100.00%	50,000	10	5,000	2017	2027
Asset 5	25,000	100.00%	25,000	5	5,000	2020	2025
Asset 6	5,000	100.00%	5,000	5	1,000	2019	2024
Asset 7	3,100,000	25.00%	775,000	30	25,833	1993	2023
Asset 8	400,000	50.00%	200,000	15	13,333	2017	2032
Asset 9	250,000	50.00%	125,000	10	12,500	2020	2030
Asset 10	12,500	100.00%	12,500	5	2,500	2021	2026
Total	\$35,842,500	_	\$9,442,500	-	\$340,167		

	Fiscal Year Ending September 30,											
Description	2022	2023	2024	2025	2026							
Starting Balance	\$3,648,000	\$3,988,167	\$3,553,333	\$3,888,500	\$4,203,667							
Annual Contributions	340,167	340,167	340,167	340,167	340,167							
Additional Contributions [4]	0	0	0	0	0							
Expenditures (Cash)	0	775,000	5,000	25,000	512,500							
Ending Balance	\$3,988,167	\$3,553,333	\$3,888,500	\$4,203,667	\$4,031,333							

Notes:

[1] Includes allowance of 3% per year construction cost inflation.

[2] Remainder to be funded from debt-financing or alternative funding source.

[3] Annual transfer to be funded from user rates.

[4] Includes additional contributions required to address funding deficiencies.

Time Asset Performance Curve

Rehab to Improve

Performance

Capital

Fund

Replacement

MM

#### **High-Level Capital Replacement Fund Balance Analysis**

#### **Utility Asset Analysis**

Description	Amount
Installed Cost of Depreciable Assets as of September 30, 2022	\$40,844,644
High-Level Replacement Cost of Assets	\$84,816,616
Weighted Average Service Life of Depreciable Assets (Years)	32
Annual Accrual for Capital Replacements	\$2,689,925
Weighted Average Age of Depreciable Assets	23
Calculated PayGo Capital Replacement Fund Balance	<u>\$62,880,087</u>



# **Establishing the Business Foundation (cont.)**

- Adopt Financial Management Policies and Performance Measures, Ideally in a Single Document (cont.)
  - Cash Reserve Policy (cont.)
    - Could Establish Reserves for: Rate Stabilization
       Anticipated Changes in Regulations
       Alternative Water Resource Funding
       Emergencies / Catastrophic Events
  - Benchmarking
    - Medians By Rating, Location, Etc.
       Published By Rating Agencies





- Many Financial Metrics, But Some Financial Ratios Are Especially Important for Credit Rating
- Some Key Financial Ratios:
  - All-In Debt Service Coverage
  - Senior Lien Debt Service Coverage
  - Days Cash on Hand (Cash as % of Spending for General Obligation Bonds)
  - Outstanding Long-Term Debt Per Customer and Per Capita
  - Free Cash as Percent of Depreciation



- All-In Debt Service Coverage
  - <u>Definition</u>: Revenues Available for Debt Service (Usually Gross Revenues Less Operating Expenses Not Including Depreciation and Other Non-Cash Expenses) Divided By Total Debt Service (Senior Plus Subordinate Lien)
  - Measures Financial Margin to Meet Debt Obligations
  - Better Indicator of Enterprise's Overall Ability to Pay Its Debt Than Senior Lien Debt Service Coverage Alone



- All-In Debt Service Coverage (cont.)
  - AA-Rated Enterprise May Have All-In Debt Service Coverage of 200% or Higher
  - Fitch 2020 Water and Sewer Medians

	AAA-Rated	AA-Rated	A-Rated	All Credits
All-In Debt Service Coverage:				
Without Impact Fees	2.6	2.5	1.7	2.4
With Impact Fees	3.2	2.7	1.9	2.7
Net of Transfers Out	3.1	2.6	1.9	2.6
Minimum Projected	2.7	2.0	1.4	2.0
<b>3-Year Historical Average</b>	3.1	2.6	1.8	2.5



- Senior Lien Debt Service Coverage
  - <u>Definition</u>: Revenues Available for Debt Service Divided By Senior Lien Debt Service
  - Measures Financial Margin to Meet Senior Lien Debt Obligations
  - Ratio Less Than Requirement Per Enterprise's Rate Covenant Represents Technical Default That May Mandate Further Action, Such as a Rate Review
  - Fitch 2020 Water and Sewer Medians

	AAA-Rated	AA-Rated	A-Rated	All Credits
Senior Lien Debt Service Coverage:				
Without Impact Fees	3.3	3.0	2.0	2.9
With Impact Fees	4.2	3.4	2.1	3.3
Net of Transfers Out	3.9	3.1	2.1	3.1
Minimum Projected	3.1	2.5	1.7	2.4
3-Year Historical Average	3.1	2.6	1.8	2.5



- Days Cash on Hand
  - <u>Definition</u>: Unrestricted Cash and Investments Divided By Operating Expenditures Minus Depreciation, Divided By 365
  - Measures Financial Flexibility to Pay Near-Term Financial Obligations
    - Utilities With Stronger Financial Profiles: Days Cash on Hand Equal to One Year or More
  - Fitch 2020 Water and Sewer Medians

	AAA-Rated	AA-Rated	A-Rated	All Credits
Days Cash on Hand	617	555	315	545



- Days Cash on Hand (cont.)
  - <u>Cash Is King</u>: Improving Enterprise's Cash Position and Having "Rainy Day Funds" = One of the Most Effective Approaches for Upgrading Credit Rating
- For General Fund, AAA Credit May Have Unrestricted Cash Equal to 15% of Spending
  - This Level Is Considered to Offer Excellent Level of Financial Resilience





- Outstanding Long-Term Debt Per Customer Outstanding Long-Term Debt Per Capita
  - <u>Definition</u>: Principal Amount of Debt Outstanding Divided By Number of Customers; Principal Amount of Debt Outstanding Divided By Number of Persons in Service Area
  - Measures Debt Burden for Ratepayers
  - Fitch 2020 Water and Sewer Medians

	AAA-Rated	AA-Rated	A-Rated	All Credits
Long-Term Debt Per Customer:				
Current	\$1,122	\$1,675	\$2,852	\$1,706
Projected Year 5	1,190	1,904	2,701	1,909
Long-Term Debt Per Capita:				
Current	\$322	\$511	\$784	\$492
Projected Year 5	307	530	762	511



#### Free Cash as Percent of Depreciation

- <u>Definition</u>: Current Surplus Revenues After Payment of Operating Expenses, Debt Service, and Operating Transfers Out Divided By Current Year Depreciation
- Measures Annual Financial Capacity to Maintain Existing Infrastructure at Current Level of Service from Existing Cash Flows
  - Utilities With Stronger Financial Profiles:
     Free Cash as Percent of Depreciation ≥ 100%
- Fitch 2020 Water and Sewer Medians

	AAA-Rated	AA-Rated	A-Rated	All Credits
Free Cash as Percent of Depreciation	131%	143%	127%	135%



# **Developing a Realistic Operational and Financial Plan**



### **Rate Cases For Enterprise Funds Are Usually Based on a Multi-Year Forecast of Revenue Requirements**

- + Cost of Operation and Maintenance
- + Debt Service Payments (Senior and Subordinate)
- + Transfers and Administration Payments
- + Capital Funding from Revenue (pay-as-you-go)
- + Working Capital Reserves / Rate Stabilization / Financial Compliance
- Other Operating Revenue
- Capacity / Impact Fees Used to Pay Growth-Related Debt Service
- Unrestricted Interest Income
- Transfers from Other Funds
- = <u>Net Revenue Requirements Funded from User Rates</u>



# Financial Planning For Enterprise Funds Should Ideally Accomplish Multiple Objectives

### Fund Revenue Requirements That Are "Right-Sized"



 Meet or Set Course to Eventually Meet Established Financial Targets

- Debt Service Coverage
- Working Capital Fund Cash Balance
- Capital Replacement Fund Cash Balance



# Financial Planning For Enterprise Funds Should Ideally Accomplish Multiple Objectives (cont.)

- Balanced Debt Risk
  - Outstanding Debt to Net Assets  $\leq 50\%$
  - Debt Per Customer and Per Capita
- Affordable Rates
- Competitive Rates
  - Rate / Bill Comparison
- Minimize "Rate Shock"
- Meet Statutory, Case Law, and Debt Instrument (e.g., Bond Ordinance / Resolution) Requirements



# Use of Graphical Management / Financial Dashboards Can Help Accomplish Objectives

#### Can Communicate Projected Financial Position and Demonstrate Reasonableness of Rate Recommendations

Local Government Logo	Utility System Financial Overview																	
Chart	1: Summar	of Revenu	e Adjustmen	ıts			Chart	h Available Year End Litility Fund (Westing Conital) Cash Palaness	Chart 5: Projected Overall / All-In Net Revenues Debt Service Coverage									
		Fiscal	Year Ending	September	30,		clian .	Available fear-End Utility Fund (working Capital) Cash Balances	400% ]	% ]								
Identified Revenue Adjustments:	2020	2021	2022	2023	2024	2025	\$2,500		350% -	% -								
Water System	0.00%	18.00%	18.00%	6.50%	6.50%	6.50%	\$2.000		300% -	///								
Wastewater System	0.00%	12.50%	12.50%	4.00%	4.00%	4.00%	( <b>s</b> )		250%									
Combined System	0.00%	14.84%	14.91%	5.13%	5.14%	5.16%	S1.500		23070									
Revenue Surplus / (Deficiency) Under Proposed Adjustments (\$ thousands): Water System	(\$491)	(\$252)	(\$275)	(\$214)	(\$185)	\$3	91,000 € \$1,000		200% - 150% - 100% -									
Wastewater System	\$358	\$146	\$76	\$337	\$341	\$421	₹ \$500		50% -									
Combined System	(\$133)	(\$106)	(\$199)	\$123	\$155	\$424	\$0		0%									
Effective Months of Revenue Adjustments: Water System Wastewater System	12 12	12 12	12 12	12 12	12 12	12 12	2020	2021 2022 2023 2024 2025 Ending Cash Balance - Utility Fund (Working Capital) Target Balance - 90 Days of Rate Revenue 90 Days of O&M		2020     2021     2022     2023     2024     2025       Calculated Debt Service Coverage								
S8,000 S7,000 S5,000 S5,000 S1,000 S0 2020	arized Revo	2022	2023 Capital Funded Net Debt Servic	lysis - Com 2024 from Rates		m	\$1,400 \$1,200 \$1,000 \$1,000 \$1,000 \$200 \$0 \$200 \$0 \$200 \$0 \$200	Chart 4: Available Year-End Renewal and Replacement (R&R) Account Cash Balances	\$7,4 (spursauds) \$5,1 \$4,1 \$3,4 \$2,1 \$1,1	Chart 6: Funding of Capital Improvement Program 57,000 56,000 50,000 50,000 50,000 51,000 50 2020 bit Proceeds from Bank Loan 1 Debt Proceeds from Bank Loan 1								
Operating Expenses			Projected Rever	nues Under Prop	osed Rates			Ending Cash Balance - R&R Water	Grants / Contributions									
- • Projected Revenues Under Existing R	Projected Revenues Under Existing Rates							Minimum Balance - 5% of Prior Year's Revenue     One Year of Depreciation (\$744,478)	<ul> <li>Funded by State Department of Transportation</li> <li>Operating Revenues / Reserves / Deposits to Renewal and Replacement Fund</li> </ul>									

#### EXHIBIT 1: Sample Management Dashboard



### **Sample Revenue Requirements Graph**





### **Sample Debt Service Coverage Graph**





### **Sample Cash Balances Graphs**







# **Dashboard Design Tips**

# All Dashboard Chart Data on One Tab

Easy to Print Out and Review

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6	Line				Fiscal Year Endin	g September 30,		
7	No.	Description	2020	2021	2022	2023	2024	2025
8								
29		Chart 2: Summarized Revenue Requirements Analysis - Combined System						
30		Revenue Requirements - Combined Systems						
31	1	Projected Revenues Under Proposed Rates	\$4,660,252	\$5,363,581	\$6,186,409	\$6,543,218	\$6,934,696	\$7,349,958
32	2	Projected Revenues Under Existing Rates	4,660,252	4,692,281	4,730,209	4,765,418	4,811,996	4,857,858
33	3	Operating Expenses	4,595,389	4,756,403	4,901,302	5,062,699	5,229,624	5,403,183
34	4	Net Debt Service	0	277,083	350,000	555,000	742,825	743,825
35	5	Transfer to Renewal and Replacement Fund	0	116,506	703,179	744,320	762,161	761,735
36	6	Capital Funded from Rates	198,328	319,252	430,440	57,800	44,800	16,800
37	7	Deposits to Working Capital-Additional Capital Funding	0	0	0	123,399	155,287	424,415
38								
39		Chart 3: Available Year-End Utility Fund (Working Capital) Cash Balances						
		Chart 4: Available Year-End						
40		Renewal and Replacement (R&R) Account Cash Balances						
41		Utility Fund (Working Capital) and R&R Fund Cash Balances						
42	8	Ending Cash Balance - Utility Fund (Working Capital)	\$1,569,268	\$1,463,604	\$1,265,092	\$1,388,491	\$1,543,777	\$1,968,192
43	9	Ending Cash Balance - R&R Water	0	49,376	461,337	860,130	667,312	209,857
44	10	Ending Cash Balance - R&R Wastewater	0	7,130	43,348	348,875	4/5,021	609,631
45	12	1 arget Balance - 90 Days of Rate Revenue	1,107,176	1,280,049	1,482,152	1,509,595	1,003,831	1,704,021
40	12	90 Days of OacM	1,155,110	1,1/2,812	1,208,540	1,248,337	1,289,490	1,332,292
4/	13	Minimum Balance - 5% of Prior Tear's Revenue	744 479	744 479	208,179	309,320	744 479	540,755
48	14	One Tear of Depreciation (\$744,478)	/44,478	/44,4/8	/44,4/8	/44,4/8	/44,478	/44,4/8
50		Chart 5: Projected Overall / All In Not Revenues Debt Service Coverage						
51		All-In Debt Service Coverage - Net Revenues Only						
52	15	Calculated Debt Service Coverage	0%	210%	367%	2670	230%	262%
53	16	Target Debt Service Coverage (150%)	150%	150%	150%	150%	a 150%	150%
54	17	Minimum Debt Service Coverage (125%)	125%	125%	125%	1259	6 125%	125%
	<u>2</u>	LEXINDIC 1 Presentation 3.Dash Data (+)		: 4				•



# **Dashboard Design Tips (cont.)**

#### Use of <u>Data → Group</u> Function Within Dashboard

- Can Hide and Unhide Assumption Tables to Make Changes Without Leaving Dashboard
- If Dashboard Included as Table in Final Report, Can Hide Charts More Appropriate for Management vs. Public

A	В	С	D	E	F	G	H	I	J	K	L	A	B	C	D	E	F	G	H	I	J	K	L
7		Wat	er and Wast	ewater Sys	tem Financi	al Overvie	W					7		Water a	and Waste	water Syste	em Financia	al Overview	£				
9					Fiscal Year	Ending Septe	ember 30,					9					Fiscal Year	Ending Septen	nber 30,				
0 High-Level Summary	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	10 High-Level Summary	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
11 Identified Revenue Adjustments												11 Identified Revenue Adjustments											
12 Water System	0.00%	4.00%	6 4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	96 12 Water System	0.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%
13 Wastewater System	0.00%	2.00%	6 2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	% 13 Wastewater System	0.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%
14 Combined System	0.00%	2.97%	6 2.97%	2.98%	2.99%	3.00%	3.01%	3.02%	3.02%	3.03%	3.04%	% 14 Combined System	0.00%	2.97%	2.97%	2.98%	2.99%	3.00%	3.01%	3.02%	3.02%	3.03%	3.04%
15 Effective Months	12	1	2 12	12	12	12	12	12	12	12	12	12 15 Effective Months	12	12	12	12	12	12	12	12	12	12	12
16 Unrestricted Cash Balance (\$ 000's)	\$ 22,221	\$ 13,23	7 \$ 14,218	\$ 13,496	\$ 12,984	\$ 14,034	\$ 13,778	\$ 14,579	\$ 16,328 \$	18,292	\$ 21,034	34 16 Unrestricted Cash Balance (\$ 000's)	\$ 22,221 \$	13,237 5	14,218	\$ 13,496	\$ 12,984 \$	14,034 \$	13,778	\$ 14,579 \$	16,328 \$	18,292 5	\$ 21,034
17 One Year Days Cash on Hand	16,217	17,48	2 18,816	20,015	21,193	22,090	23,028	24,006	25,026	26,091	27,187	87 17 One Year Days Cash on Hand	16,217	17,482	18,816	20,015	21,193	22,090	23,028	24,006	25,026	26,091	27,187
18 120 Days Rate Rev Plus One Year Depr	11,255	11,62	0 12,000	12,398	12,813	13,247	13,700	14,173	14,667	15,182	15,721	21 18 120 Days Rate Rev Plus One Year Depr	11,255	11,620	12,000	12,398	12,813	13,247	13,700	14,173	14,667	15,182	15,721
19 90 Days Rate Rev Plus One Year Depr	9,590	9,86	3 10,149	10,447	10,758	11,083	11,423	11,778	12,148	12,535	12,939	39 19 90 Days Rate Rev Plus One Year Depr	9,590	9,863	10,149	10,447	10,758	11,083	11,423	11,778	12,148	12,535	12,939
20 All-In Net Revenues Debt Coverage	182%	6 173	% 166%	167%	253%	270%	192%	204%	217%	231%	2469	6% 20 All-In Net Revenues Debt Coverage	182%	173%	166%	167%	253%	270%	192%	204%	217%	231%	246%
21 <u>Revenue Surplus / (Deficiency) (\$ 000's):</u>						a (100)						21 Revenue Surplus / (Deficiency) (\$ 000's):											
22 Water System	\$ (1,940)	) \$ (6,09	4) \$ 1,176	\$ 164	\$ (839)	\$ (433)	\$ (1,781)	\$ (697)	\$ 15 \$	1 (02)	\$ 6/9	79 22 Water System	\$ (1,940) \$	(6,094)	\$ 1,176	\$ 164	\$ (839) \$	(433) \$	(1,781) 5	\$ (697) \$	15 \$	73 \$	\$ 679
23 Wastewater System	(530)	) (3,23	4) (1,410)	(324)	1/	1,139	1,170	1,103	1,411	1,582	1,709	09 23 Wastewater System	(536)	(3,234)	(1,416)	(324)	17	1,139	1,176	1,163	1,411	1,582	1,769
Combined System	(2,4/0	(9,32	9) (240) 6 6 82.03	(100)	(822)	00/00	(005)	400	1,420	1,055	2,448	48 24 Combined System	(2,476)	(9,329)	(240)	(160)	(822)	706	(605)	400	1,426	1,655	2,448
25 Monthly Bill (a) 5,000 Gallons	\$ 78.30	3 80.7	0 5 83.03	3 83.34	3 87.72	3 90.22	5 92.70	3 95.58	3 98.08 1	2.82	3 103.80	80 25 Monthly Bill (a) 3,000 Gallons	\$ 78.50 \$	80.76	\$ 83.03	\$ 85.34	\$ 87.72	\$ 90.22 \$	\$ 92.76	\$ 95.38	98.08 9	100.90 5	\$ 103.80
7 Cost Per Gallon of Total Bill	\$ 0.026	\$ 0.02	7 \$ 0.028	\$ 0.028	\$ 0.029	\$ 0.030	\$ 0.031	\$ 0.032	\$ 0.033	\$ 0.034	\$ 0.035	35 27 Cost Bas College of Table Dill	e 0.006 0	2.20	2.27	2.31	2.38	2.50	2.34	2.02	2.70	2.82	2.90
Percent of MHI (Target < 2%)	1.72%	6 1.75	% 1.77%	1.79%	1.81%	1.84%	1.86%	1.89%	1.91%	1.94%	1.96%	6% Decent of MHI (Target < 2%)	1 72%	1 75%	1 77%	1 70%	1.81%	1.84%	1.86%	1 80%	1 01%	1.04%	1 06%
86												29 Customers - Water	22 188	22 706	23 224	23 742	24.260	24 778	25.206	25 814	26 332	26.850	27.368
1) Summarized Revenue Requir	rements Ana	lysis - Com	bined Systems		630.000		2) Unrestrie	ted Cash Ba	alances			30 Difference - Amount	518	518	518	518	518	518	518	518	518	518	518
38					\$30,000							31 Difference - Percent	2 30%	2 33%	2 28%	2 23%	2 18%	2 14%	2 09%	2.05%	2 01%	1 07%	1 03%
89 £ \$35,000					\$25,000					-		32 Customers - Wastewater	17.167	17.634	18 101	18.568	19.035	19.502	19.969	20.436	20.903	21.370	21.837
40 g \$30,000 -	-			_	(ş			-				33 Difference - Amount	467	467	467	467	467	467	467	467	467	467	467
A \$25,000					I \$20,000							34 Difference - Percent	2.80%	2.72%	2.65%	2.58%	2.52%	2.45%	2.39%	2.34%	2.29%	2.23%	2.19%
1 6 00000					snot							5 Capacity Fee Collection Level (\$ 000's)	\$ 2,100 \$	1,504 5	1,504	\$ 1,504	\$ 1,504 \$	1,504 \$	1,504	\$ 1,504 \$	1,504 \$	1,504 \$	\$ 1,504
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# **Developing a Realistic Plan**

# **Capital Program**

- Often Primary Driver of Need for Rate Increases
- Must Be Able to Explain Purpose (Justification) of Each Project and Have Good Cost Estimates
- Could Possibly Link to Asset Management Plan



![](_page_31_Picture_6.jpeg)

# Developing a Realistic Plan (cont.)

### Establish Criteria to Prioritize Capital Program

#### **Sample Criteria in Order of Priority:**

- Public Health and Safety
  - Project Addresses Working and Public Health / Safety Issues
- Regulatory Compliance
  - Project Promotes Regulatory and Contractual Compliance
- System Reliability
  - Project Reduces Risk and Consequences of Asset Failure and Addresses Other Attributes of Asset Management (Redundancy)
- Community / Customer Benefit
  - Project Addresses Service Issues Such as Pressure, Taste / Odor and Customer Satisfaction
- Sustainability
  - Project Will Result in Long-Term Cost Efficiencies and Has Environmental "Green" Benefits

![](_page_32_Picture_13.jpeg)

IMPORTANCE

# **Typical Capital Program Funding Sources**

#### Issuance of Debt

![](_page_33_Picture_2.jpeg)

#### Revenues

- Charges for Service / Rates
- Cash Reserves

Capacity / Impact Fees, Assessments, and Other Charges Collected from Growth

 Contributed Capital (e.g., Grants, Legislative Budget Appropriation), Facilities, and Property

![](_page_33_Picture_8.jpeg)

# **Grant Opportunities in Florida for Utilities – Small or Economically-Disadvantaged Communities**

![](_page_34_Picture_1.jpeg)

#### Florida Department of Environmental Protection (FDEP)

Small Community Wastewater Facilities Grant

![](_page_34_Picture_4.jpeg)

#### **United States Department of Agriculture (USDA) Rural Development**

Water and Waste Disposal Grants

![](_page_34_Picture_7.jpeg)

# Florida Department of Economic Opportunity Florida Small Cities Community Development Block Grant (CDBG) Program

![](_page_34_Picture_9.jpeg)

# **Grant Opportunities in Florida for Utilities – All Communities**

![](_page_35_Picture_1.jpeg)

#### Water Management Districts

Cooperative Funding Program (Up to 50% of Cost)

Florida Department of Environmental Protection Florida Department of Emergency Management Florida Department of Economic Opportunity County Grants to Their Municipalities

![](_page_35_Picture_5.jpeg)

![](_page_35_Picture_6.jpeg)
#### For Capital Needs Not Funded Through Contributed Capital, Assessments, and Impact Fees / Charges to Growth, Should Balance Between Debt Financing and Pay-As-You-Go Capital Funding

- Debt Financing
  - Most Appropriate for Assets With Longer Service Lives (e.g., 15 Years or More)
    - Pay-As-You-Go Capital Funding



- Appropriate for Assets With Shorter Service Lives (e.g., Less than 15 Years)
- Routine Capital Expenditures and Annual Renewals / Replacements
- Ideally: Accrue Funds Based on Asset Replacement Schedule



## **Why Debt Finance?**

#### **Advantages:**

- Annual Cash Flow Reduced to Level of Debt Service Over Debt Term
  - Can Help Prevent "Rate Shock" to Existing Customers
- Funding Available Immediately
- Recovery of Capital Project Costs Spread Over Life of Debt Instrument to Match Asset Utilization (e.g., 30-Year Repayment Schedule, 30-Year Asset Service Life)
  - May Be Greater Fairness to Ratepayers
- If Utility Has Growth-Related Fees Such as Impact Fees, Can Allow More Time for "Growth to Pay for Growth"



#### **Considerations When Evaluating Debt Instruments** (To Be Discussed With Government's Municipal Advisor)

- How Much Does the Enterprise Need?
- How Soon Does the Enterprise Need It?
- Single Project / Program to Be Funded or Multiple Projects?
- Administrative Costs Staff Time Required to Address Reporting Requirements
  - Could Also Outsource Reporting
- Availability of Funding and Probability That Financing Could Be Secured Under the Desired Terms
- Level of Complexity of Debt Instrument
  - Ease in Projecting Debt Payments for Financial Planning Purposes
  - Ease in Calculating Historical Coverage



## **Considerations (cont.)**

#### Borrowing Costs

- Interest Rate
- Issuance Costs
- Life Cycle Costs (Total Amount Paid During Debt Term)

	20-Year Clean Water SRF Loan	30-Year Revenue Bonds	20-Year Revenue Bonds	
Amount Borrowed	\$20,000,000	\$20,000,000	\$20,000,000	
Issuance Costs (% of Principal)	2.00%	3.00%	3.00%	
Interest Rate	0.02%	2.43%	2.10%	
Term (Years)	20	30	20	
Annual Debt Service	\$1,002,101	\$946,276	\$1,234,376	
Life Cycle Costs	\$20,042,027	\$28,388,289	\$24,687,528	

#### Political Climate for Raising Rates to Support Debt



#### Debt Structuring Option to Help Reduce "Rate Shock" If Level Debt Service Is Cost-Prohibitive (Not Available with All Options):

Wrapped Debt Service



Structuring Options to Provide More Time to Phase-In Rates to the Level Needed to Meet Debt / Coverage Obligations:

- Capitalized Interest (Standard with State Revolving Fund Loans)
- Line of Credit with Interest-Only Payments
  - Permanent Financing at Later Date



### **Debt Financing Programs Are Always Evolving**

- Recent Federal Infrastructure Acts
- Water Infrastructure Finance and Innovation Act (WIFIA)
  - Any Project Eligible for State Revolving Fund (SRF) Loan Financing Could Possibly Be Financed Through WIFIA
  - Up to 35-Year Repayment, With Up to Five-Year Deferral of Payments from Substantial Completion
  - Low, Fixed Interest Rate Equal to U.S. Treasury Rate of Similar Maturity
- Administrative Requirements for Federal Financing Programs Are Similar to Those of an SRF Loan



#### To the Extent Possible, Can Incorporate Best Management and Financial Practices Into Bond Resolution / Ordinance

 Binding Agreement Between Governing Body and Bondholders



- Credit Rating Agencies Prefer to See Stronger Coverage Requirements (e.g., 125%)
- Can Require Annual Renewal and Replacement Funding
- Can Make Enterprise Fund Closed-Loop, Meaning That All Funds Must Remain in Enterprise Fund and Can Only Be Used for Any Lawful Purpose of the Enterprise
- Can Have Maximum Annual Debt Service Additional Bonds Test
  - Promotes Interperiod Equity Cannot Push All Debt Service to the Future



#### **Before Issuing / Incurring Debt:**

- Adopt All Rate Increases Needed During Forecast Period
  - Shows a Commitment By Governing Body to Raise Rates When Needed
  - Many Debt Financing Options Require Demonstration That Enterprise Can Repay Debt / All Required Increases Have Been Adopted
- Consider Adopting Automatic Rate Increase Provisions Based on an Inflationary Index (e.g., CPI, ENR Construction Cost Index) or Other Method
- If Utility Is a Wholesale Customer of Another Utility, Consider Adopting Provisions to Pass-Through Future Rate Increases from Wholesale Provider



#### Several Local Governments Have Now Made Annual Rate Increases Automatic

- "Automatic" Means That Increases Are Implemented Without the Need for a Formal Hearing Unless Specific Action Is Taken By Governing Body
  - Often Linked to Index (Consumer Price Index, Municipal Cost Index, Engineering News-Record Construction Cost Index, etc.)

 Considered a Best Management Practice and Favored By Credit Rating Agencies

- From Financial Risk Standpoint, Provides More Assurance That Rates Will Keep Up With Inflation
- If Financial Projections Are Submitted as Part of Securing Debt Financing, Credit Rating Agencies (Moody's, Standard and Poor's, and Fitch Ratings) and Lenders Will Want to Know If All Rate Adjustments Needed to Support the Debt Have Been Adopted





#### **Operating Expenses**

- Substantial Differences Between Budgeted and Recent Actual Operating Expenses Could Be Challenged Easily
  - Need to Be Able to Easily Communicate Reasons

#### Efficiency and Effectiveness

- What Cost Reductions Can Be Implemented Without Sacrificing Level of Service?
- Keep Track of All Steps Taken to Reduce Costs
  - Could Communicate These Efforts When Requesting Rate Increases





#### **Other Financial Considerations**

- Best Management Practice Per Rating Agencies: Limit Non-Enterprise-Related Transfers to General Fund
  - Substantial Amount of Capital (Often Secured Through Debt Financing) Is Required to Provide Service



**Should Reinvest in System** 



#### What Is a Defensible Level of Transfers to General Fund from Enterprise Fund?

- Rates and Charges Must Be Just and Equitable
  - Counties: Florida Statute 153.11(1)(c) Water Service Charges and Sewer Service Charges; Revenues

"Such rates, fees and charges shall be just and equitable..."

Municipalities: Florida Statute 180.13(2)
 Administration of Utility; Rate Fixing and Collection of Charges

"The ...legislative body of the municipality...may establish just and equitable rates or charges..."



#### What Is a Defensible Level of Transfers to General Fund from Enterprise Fund? (cont.)

- Rosalind Holding Company, Etc., Appellant, v. The Orlando Utilities Commission, et al., Appellee. District Court of Appeal of Florida, Fifth District. July 22, 1981.
  - "Absent a controlling statute, a municipal utility, like any other utility, is entitled to earn a reasonable rate of return on its capital and its rates may be set so that it earns a rate of return on its equity comparable to other similar businesses."
  - "The parties all agree that basing rates on cost of capital is the most universally adopted and reasonable method in the industry."





#### What Is a Defensible Level of Transfers to General Fund from Enterprise Fund? (cont.)

- Defensible Transfers to General Fund from Enterprise Fund:
  - Allocable Costs Direct or Indirect
  - Reasonable Rate of Return
- Potential Approaches for Determining Reasonable Rate of Return
  - Estimating Allowable Return on Investment If Enterprise Were Private and Regulated By Florida Public Service Commission (Cost of Capital Analysis)
  - Consistent With Industry Norms
- Should Monitor Future Bills By Florida Legislature
  - Historical Efforts By Representatives to Limit Non-Utility-Related Transfers to General Fund



**Other Financial Considerations (cont.)** 

- Address Liabilities Associated With Other Post-Employment Benefits (OPEB) and Pensions
- Minimize Dependence on Fees Charged to New Growth (e.g., Impact Fees) to Pay Debt
  - User Rates Alone Should Ideally Generate Sufficient Revenues to Meet Financial Targets







Support Policy of "Growth Paying for Growth"



- Dual Rational Nexus Requirements Established Through Case Law
  - Fee Must Be Proportionate to Benefit Received
- Can Legally Be Used to Pay for Growth-Related Projects or Growth-Related Debt Service
  - Should Maintain Expansion Factor for Debt



- Florida Impact Fee Act Section 163.31801, Florida Statutes
  - Calculation of Impact Fees Must Be Based on Most Recent
     and Localized Data
  - Impact Fee Collections and Expenditures Must Be Accounted for in a Separate Accounting Fund
  - Administrative Charges for Collection of Impact Fees Must Be Based on Actual Costs
  - Notice Must Be Provided No Less Than 90 Days Before Effective Date of Ordinance Imposing a Higher Impact Fee — No 90-Day Notice Required for Impact Fee Decreases
  - If Impact Fees Challenged, Government Has Burden of Proving By Preponderance of Evidence That Fees Meet Requirements of Impact Fee Act and State Legal Precedent



- Does Not Apply to Water and Sewer Connection Fees

   (Not All Attorneys Agree That Water and Sewer Impact Fees Are Exempt Based on This Language)
- Additions to Florida Impact Fee Act in 2021
  - Increase in Impact Fee Rate of Not More Than 25% Must Be Implemented in Two Equal Annual Increments
  - Increase in Impact Fee Greater Than 25% But Not More Than 50% Must Be Implemented in Four Equal Installments
  - Impact Fee Increase May Not Exceed 50% of Current Fee
  - Impact Fee May Not Be Increased More Than Once Every 4 Years



- Additions to Florida Impact Fee Act in 2021 (cont.)
  - Local Government Can Increase Impact Fees Beyond the Phase-In Limitations If:
    - A Demonstrated Needs Study Has Been Completed Within Past 12 Months That Expressly Demonstrates Extraordinary Circumstances Necessitating Need to Exceed Phase-In Limitations
    - Local Government Holds Two Publicly Noticed Workshops
       Dedicated to the Extraordinary Circumstances
    - Impact Fee Increase Is Approved By At Least Two-Thirds
       Vote of Governing Body

Local Government Should Obtain Guidance from Its Attorney to Ensure That Implementation of Any Impact Fee Increases Is in Compliance With Florida Law!



- Spend Fees in Timely Manner
  - Fees May Have to Be Refunded If Not Spent Within Certain Period of Time
- Maintain Paper Trail of Growth-Related Projects or Growth-Related Debt Service Funded With User Rates or Other Funding Source Due to Insufficiency of Impact Fee Collections at the Time
  - May Be Able to Reimburse User Rate / Operating Funds at a Later Date When Impact Fee Cash Balances Are Available
- Develop Formal Procedure for Applicants to Submit Alternative Impact Fee Calculation If They Believe Their Impact Would Be Less Than Under Current Methodology



#### **Utility Rates**

#### Consider Affordability (Hot Topic in Utility Industry)

- <u>Rating Agencies</u>: Affordable = Monthly Utility Bill for Combined Water and Wastewater Service ≤ 2% of Median Household Income (MHI) of Service Area or ≤ 1% If Only One Service (Water or Wastewater)
- <u>EPA</u>: Affordable = Monthly Utility Bill for Combined Water and Wastewater Service  $\leq 4.5\%$  of MHI of Service Area
- Census.gov Is Good Source for MHI Information and Percent of Persons Below Poverty Level (Another Consideration)





## Utility Rates (cont.)

#### Outside-Municipality Surcharges

- Florida Statute 180.191 Limitation on Rates Charged Consumer Outside City Limits
- Should Monitor
   Future Legislation –
   Historical Attempts
   to Limit Outside Municipality
   Surcharges

"[A municipality] may charge rates, fees, and charges that are just and equitable and which are based on the same factors used in fixing the rates, fees, and charges for consumers inside the municipal boundaries. In addition thereto, the municipality may add a surcharge not to exceed 25 percent of such rates, fees, and charges for said services to consumers outside the boundaries. However, the total of all such rates, fees, and charges for the services to consumers outside the boundaries shall not be more than 50 percent in excess of the total amount the municipality charges consumers served within the municipality for corresponding service."



#### **Utility Rates (cont.)**

- Customer
   Notifications of
   Rate Increases
   Are Required
  - Florida Statute 180.136 Water or Sewer Utilities; Notice

"Before a local government water or sewer utility increases any rate, charge, or fee for water or sewer utility service, the utility shall provide notice of the proposed increase to each customer of the utility through the utility's billing process. The notice shall state the date, time, and place of the meeting of the governing board of the local government at which such increase will be considered."



#### **Utility Rates (cont.)**

#### Consider Revenue Enhancement Opportunities

- Miscellaneous Service Charges
  - Recover Direct Costs Associated With Service That Benefits One Customer Instead of Entire Customer Base
- Guaranteed Revenue Charges
- Capital Financing Recovery Fees
- Fire Protection Charges









## What We Would Like to Avoid...



**Obtaining Public Support and Buy-In for the Enterprise Financial Plan Can Sometimes Be Challenging!** 



## **Elements of Communication Program**

 Establishing the Foundation or Mindset for Funding Enterprise or Raising Rates



 Communicating Rate Increases



## **Establishing the Foundation or Mindset for Funding Enterprise or Raising Rates**

- Communicate That Enterprise Is a Business and, Like Many Businesses, a Major Objective Is Customer Satisfaction
  - Utility May Be Largest Business of Local Government (e.g., Accounted for in Enterprise Fund Established for Business-Type Activities)
- Communicate System Attributes and Size of Asset Base (\$\_\_\_\_\_Million of Utility Infrastructure Managed)
- Establish Link Between Rate Increases and Long-Term Interests of Customers from Operational, Service and / or Financial Perspective
  - Public Health and Safety Is Top Priority
  - Utility Provides Essential Service
     24 Hours Per Day, 7 Days Per Week



## Establishing the Foundation or Mindset for Funding Enterprise or Raising Rates (cont.)

- Establish Link Between Rate Increases and Long-Term Interests of Customers from Operational, Service and / or Financial Perspective (cont.)
  - Highly-Regulated by FDEP, Water Management Agencies, and Health Departments (cont.)
    - Permits Require Satisfactory Performance
    - Possibility of Fines or Consent Orders If Enterprise
       Does Not Remain in Regulatory Compliance or Causes
       Pollution (Could Be More Expensive for Ratepayers)
  - Need to Balance Operational and Financial Considerations When Developing Rate Recommendations



## Establishing the Foundation or Mindset for Funding Enterprise or Raising Rates (cont.)

- Outline Rate Guiding Principles
- Develop a Solid Business Foundation Based on Best Management Practices Recognized By Industry and Credit Rating Agencies
  - Communicate These Practices
  - Build Long-Term History / Track Record of Following These Practices
    - Will Need to Show or Demonstrate History to Third Parties When Debt Financing
- If Enterprise Already Has High Credit Rating (e.g., AA or Higher), Emphasize Desire to Maintain Rating and Benefits of Rating (Lower Interest Rates and Issuance Costs, Lower User Rates Over Long-Term)



## Establishing the Foundation or Mindset for Funding Enterprise or Raising Rates (cont.)

- Educate Regulators and Public on Revenue Requirements to Be Funded Through User Rates (What Do the Rates Pay For?)
- Provide Regular Updates to Regulators About Enterprise's Operating Conditions, Financial Position, and Major Issues Affecting System
- Provide Regulators With Tours of Facilities



- One-on-One Meetings Before Public Hearings on Rate Increases and Other Enterprise Issues
  - Could Make Public Hearing Smoother and Significantly Improve Chances of Adoption



#### Outline Major Issues Affecting Enterprise System

#### **Common Issues Include:**

- Need to Fund Capital Program
  - New / Additional Debt
  - Deposits to Capital / R&R Accounts for Pay-As-You-Go Capital Funding
  - May Be Driven By New Regulations
- Revenue Collections Are Lower Than Previously Projected
- Operating Expenses Continue to Increase



- Bring the Enterprise to the Regulators / Stakeholders
  - Utility Infrastructure Is Often "Out of Sight, Out of Mind"
  - Use Pictures and Samples at Public Meetings to Demonstrate Renewal and Replacement Needs
    - Communicate That Renewal and Replacement Needs Will Not Go Away, But Will Be More Expensive to Address in the Future
    - If Applicable, Communicate Line Break Statistics for Utility





 Bring the Enterprise to the Regulators / Stakeholders (cont.)

NEW

- Use "BEFORE" and "AFTER" Pictures to Demonstrate Historical Accomplishments
  - Can Be Useful to Show Regulators the Results of Prior Rate Increases





OLD

NEW



OLD

- Communicate Efforts to Control Costs, But Mention That Most Costs Are Fixed, and That There Are Several Costs Over Which Enterprise Has No Control (e.g., Electricity, Chemicals, Fuel)
  - Some Costs Driven By Global Markets / Supply and Demand
  - Competition for Scarce Resources Such as Concrete and Building Materials
- <u>Explain That Permanent Increases in Costs Must</u> <u>Ultimately Be Passed Through to Customer Rates</u>

	Fiscal Year Ending September 30,						
	2016	2017	2018	2019	2020	2021	
Total Operating Expenses (Audited) 5-Year Compound Annual Growth Rate	\$15,541,971	\$14,811,265	\$15,239,965	\$14,784,667	\$15,334,586	\$15,744,725 0.26%	



- Communicate Historical Multi-Year Inflationary Trends to Demonstrate High Probability of Increases in Cost of Providing Service
  - Consumer Price Index
  - Municipal Cost Index
  - Engineering News-Record Construction Cost Index
  - Commodity Increases (e.g., Electricity, Chemicals, Fuel)

		Historical Compound Annual Growth Rate			
			10-Year	20-Year	
ltems	1-Year Change	5-Year Change	Change	Change	
BUREAU OF LABOR STATISTICS					
CPI – U.S. City Average (June 2019)	1.7%	1.5%	1.6%	2.3%	
Water and Sewerage Maintenance Index – U.S. City	3.3%	4.1%	5.6%	4.9%	
Average (June 2019)					
ENGINEERING NEWS-RECORD					
Construction Cost Index - Annual Average (2018)	3.0%	3.0%	2.9%	3.2%	
AMERICAN CITY AND COUNTY					
Municipal Cost Index (May 2019)	1.3%	1.5%	2.1%	2.8%	

#### HISTORICAL INFLATIONARY TRENDS


# **Communicating Drivers for the Need to Increase Rates (cont.)**

- Be Able to Provide Basis for Projected Cost Increases That Would Be Acceptable to Third-Party Reviewer
  - Develop Understanding of Cost Drivers
    - <u>Electricity and Chemicals</u>: Might Be Driven By Commodity Costs Plus Changes in Plant Flows
    - <u>General Insurance</u>: Might Be Driven By Changes in Fixed Asset Base Due to Implementation of Capital Program
    - <u>Uniforms</u>: Might Be Driven By Inflation in Cost of Uniforms Plus Changes in Number of Employees
- Perform Reality Check Between Budgeted Amounts and Recent Actuals, and Be Able to Explain Differences



# **Communicating Drivers for the Need to Increase Rates (cont.)**

- Some References for Developing Projections: (Most Are Free)
  - Enterprise History
  - Bureau of Labor Statistics (<u>www.bls.gov</u>)
  - Congressional Budget Office for Inflation Projections Budget and Economic Outlook (<u>www.cbo.gov</u>)
  - Engineering News-Record for Construction Cost Index (www.enr.com)
  - American City and County for Municipal Cost Index (<u>www.americancityandcounty.com</u>)
  - Other Federal and State Government Websites



#### **Communicating User Rate Increases**

- Determine Whether to Express Rate Increases in Percentages, Dollars, or Both
  - Dollars Often More Palatable; Both Dollars and Percentages May Be Reported By Any Media Covering the Proceedings
  - Could Relate Monthly Increase to Cost of Everyday Item (e.g., Coffee at Favorite Coffeehouse)
  - Cost Per Gallon Communicates Value of Water and Wastewater Service When Compared with Cost Per Gallon of Other Commodities (e.g., Bottled Water, Milk, Gas, etc.)





#### **Proposed Rate Adjustments Through Fiscal Year 2033**

Fiscal Year	Effective Date	Already Adopted	Add'l Adj.	Total Adj. [1]	Bill for Average SFR Customer Using 9,000 Gallons	Increase in SFR Customer Monthly Bill [2]	Total Cost Per Gallon of Water and WW Service [2]	% of Median Household Income (< 4.5% Considered Affordable By EPA) [3]
	Existing				\$66.01			1.2%
2024	11/1/2023	2.5%	5.5%	8.0%	71.33	\$5.32	0.7¢	1.3%
2025	10/1/2024	2.5%	5.5%	8.0%	77.10	5.77	0.8¢	1.3%
2026	10/1/2025	2.5%	5.5%	8.0%	83.32	6.22	0.8¢	1.4%
2027	10/1/2026	2.5%	2.5%	5.0%	87.46	4.14	0.9¢	1.5%
2028	10/1/2027	2.5%	2.5%	5.0%	91.86	4.40	0.9¢	1.5%
2029	10/1/2028	2.5%	0.5%	3.0%	94.62	2.76	0.9¢	1.5%
2030	10/1/2029	2.5%	0.5%	3.0%	97.41	2.79	1.0¢	1.5%
2031	10/1/2030	0.0%	3.0%	3.0%	100.32	2.91	1.0¢	1.6%
2032	10/1/2031	0.0%	3.0%	3.0%	103.36	3.04	1.0¢	1.6%
2033	10/1/2032	0.0%	3.0%	3.0%	106.43	3.07	1.1¢	1.6%

[1] Inflationary (Consumer Price Index) adjustments are recognized after Fiscal Year 2028.

[2] Based on proposed rates applied to single family residential ("SFR") customer with 9,000 gallons of monthly usage.

[3] EPA = United States Environmental Protection Agency. Assumes annual 2% cost of living salary increases after Fiscal Year 2024.



 Use Graphs (e.g., from Management Dashboard) to Communicate Projected Financial Position and Demonstrate Reasonableness of Projected Rate Increases

#### **Sample Utility Management Dashboard**





#### Explain What Might Happen to Financial Position If Rate Increases Not Approved



- Non-Compliance Risk (e.g., Coverage Not Met) Technical Default: Risk of Credit Rating Downgrade
- Non-Compliance Risk Nonpayment: Risk of Bonds / Loans Being Called and All Principal Due



- Explain What Might Happen to Financial Position If Rate Increases Not Approved (cont.)
  - Could Utilize Scenario Analysis Graphs





- **Demonstrate Rate Competitiveness Bill Comparison** With Other Neighboring Enterprises (or Enterprises **Benchmarked Against**)
  - Explain That Bill Comparison Is Not Report Card Report Card ٠ on How Well Enterprises Are Being Managed



- Could Outline Reasons Why User Rates Differ Among • **Utilities:** 
  - Size of Existing Customer Base / Available System Growth
  - Demographics (e.g., Customers Spread Out vs. Close **Together, Types of Customers Served)**
  - Level of Capital Improvements to Meet Service Area Growth
  - Amount of Needed Renewals and Replacements / **Remaining Service Life of Assets**



- Demonstrate Rate Competitiveness Bill Comparison
   With Other Neighboring Enterprises (or Enterprises
   Benchmarked Against) (cont.)
  - Could Outline Reasons Why User Rates Differ Among Utilities: (cont.)
    - Amount of General Fund and Administrative Fee Transfers
    - Differences in Bond / Debt Covenants
    - Source of Water Supply and Treatment Process Costs
    - Plant Capacity Utilization and Assistance in Funding of Such Capacity (e.g., Grants, Impact Fees)
    - Time of Last Rate Review





- In Bill Comparison, Show Utilities Involved in Rate Studies or Planning to Increase Rates
- If Monthly Bill for Utility Appears High By Comparison
  - Explain Why Rates Are Higher
  - See If Bill Is Comparable to Those of Utilities With Similar Service Area Characteristics



- Same Treatment Process
- Same Wholesale Service
   Provider
- Same Level of Service
- Should Develop Set of Utilities Appropriate for Benchmarking



#### Comparison of Monthly Charges for Combined Water and Wastewater Service for Single Family Residential Customers Using 3,000 Gallons



[\*] Utility is currently involved in a rate study, is planning to conduct a rate study, or plans to implement a rate revision or price index / passthrough adjustment within the next twelve months following the comparison preparation date



- If Monthly Bills Are Highest in Area, Could Possibly Show:
  - Enterprises in State of Florida With Higher Rates
  - Enterprises in Other States With Higher Rates
- To Address Common "We Can't Afford This," Demonstrate Rate Affordability
  - Explain Median Household Income Financial Metric Used By EPA, FDEP, USDA and Credit Rating Agencies
  - Could Consider Establishing Low-Income Affordability Program Funded from Sources Other Than User Rates (e.g., General Fund, Late Fees, etc.)

Description	City Amount
Monthly Water and Wastewater Bill for Average Single Family	
Residential Customer Under Proposed Rates (5,000 Gallons)	\$62.81
Monthly Median Household Income Per U.S. Census Bureau [*]	\$5,561.67
Percent of Total	<u>1.1%</u>
[*] CC 740 appual median boundhold income for City / 12 month	

[\*] \$66,740 annual median household income for City / 12 months



#### Could Show Recent Rate Increase Activity of Other Entities (Planned or Implemented)

Utility 1	<b>68%</b>	FY 2022 Through 2026
Utility 2	92.5%	FY 2023 Through 2027
Utility 3	<b>16%</b>	FY 2022 Through 2025
Utility 4	<b>52%</b>	FY 2022 Through FY 2024
Utility 5	<b>170%</b>	FY 2021 Through FY 2025
Utility 6	Water: 88%, Sewer: 55%	FY 2023 Through FY 2027
Utility 7	25.4%	FY 2023 Through 2027
Utility 8	<b>44%</b>	FY 2022 Through FY 2024
Utility 9	25%	FY 2022
Utility 10	<b>40%</b>	FY 2023
Utility 11	21.5%	FY 2022 Through 2025
Utility 12	75.6%	FY 2021 Through FY 2024

**Others Considering:** 

Utility 13, Utility 14, Utility 15, Utility 16



- Communicate National Trends in Water and Wastewater Rate Increases
  - Water and Sewerage Maintenance Index (Series ID = CUSR0000SEHG01)
    - Component of National CPI That Considers Average Cost of Water and Wastewater Service in Each Bureau of Labor Statistics (<u>www.bls.gov</u>) CPI Pricing Area
    - https://data.bls.gov/cgi-bin/srgate Can Be Used to Look
      Up Any Index Just Need Series ID Sureau of Labor Statistics
      Home Subjects \* Data Tools \* Publications \* Economic

Wa	ter and Sewe	rage
Maint	enance Index	(April)
Year	Index	Change
2019	564.836	
2020	581.338	2.92%
2021	599.364	3.10%
2022	623.523	4.03%
2023	656.603	5.31%

eries ID Formats nter series id(s) below: CUSR0000SEHG01	



If Enterprise Has Not Adjusted Rates in a Long Time, Compare Bills Under Rate Increases to Bills Under Current Rates Adjusted for Historical Inflation (CPI, ENR Construction Cost Index, etc.)





- Consider Developing a Rate "Questions and Answers" Document
  - Addresses Questions from Customers and Members of the Governing Body
  - Could Possibly Distribute to Members of Governing Body Prior Public Hearing or Customer Notifications
  - Could Possibly Publish on Website
  - Could Possibly Include as Part of Agenda Item for Public Hearing



#### Consider Developing a Rate "Questions and Answers" Document (cont.)

- 1. What do we get for the rate increases?
- 2. Are the City's water and wastewater rates high?
- 3. Why is the proposed Fiscal Year 2024 rate increase so high? Can it be lowered?
- 4. How many years of rate adjustments should be adopted?
- 5. What would happen if the rates were not increased?
- 6. Why is a bond rating important?
- 7. Is the utility at risk of a bond rating downgrade?
- 8. How often should the City perform a utility rate study?
- 9. Why should I pay a monthly service availability charge if I don't use any water?
- 10. Is the utility's multi-year capital program really needed?
- 11. Why have the utility salaries and benefits increased so much over the past few years?
- 12. Can grants be used to reduce the rate increases?
- 13. Why do transfers to the General Fund make up about 20% of the utility's operating expenses?
- 14. Are affordability programs available to help low-income residents pay their water and wastewater bills?



#### Consider Developing a Rate "Questions and Answers" Document (cont.)

How many years of rate adjustments should be adopted?

Five (5) years of rate adjustments are recommended to be adopted. To implement the multi-year capital program, the City staff needs to know how much revenue the utility will collect since projects usually take more than one year to complete.

If the utility seeks debt financing for a portion of the capital program, bond rating agencies and lending institutions / programs typically want to see five years of projections. In the evaluation of the utility's ability to repay the debt, only rate adjustments that have already been adopted will be counted.



- Have a Well-Developed Rate Resolution or Ordinance
  - Summarizes Basis for Rate Case
  - Can Help "Set the Mood" for Raising Rates
- Well-Written Resolution/Ordinance Facilitates Public Understanding and Provides a Public Record for Customers to Reference Regarding Why the Rate Decisions Were Made
  - During Challenging Times, Wording in Resolution/Ordinance Is One More Communication Tool That Can Be Utilized By the Enterprise





- Tips and Strategies for Optimizing Rate Resolution or Ordinance
  - Stating That the Local Government Owns a Utility System That Provides an Essential Service on a Continual Basis
  - Mentioning How the Utility Operates in a Highly Regulated Environment and Must Comply With all State and Local Regulations
  - Describing the Costs That the Rates, Fees, or Charges Pay for / Recover





- Tips and Strategies for Optimizing Rate Resolution or Ordinance (cont.)
  - If Applicable, Providing a History of the Last Time the Rates Were Increased and How Inflation Has Continued to Affect the Utility's Operating and Capital Costs
  - Discussing Why Rate Increases Are Needed, Such as the Need to Fund Critical Capital Needs for the Next Several Years
  - Mentioning How the Rate Adjustments Are Needed to Provide Access to Capital Markets





- Tips and Strategies for Optimizing Rate Resolution or Ordinance (cont.)
  - Stating That Securing Debt Financing Requires the Utility to Demonstrate to Lenders, Bondholders, and Credit Rating Agencies That the Utility Has Adopted a Schedule of Rates to Support the Debt
  - Outlining All Public Outreach Activities Conducted as Part of Developing the Rate Recommendations and the Results of Such Activities (e.g., Financial Advisory Committee or Development Advisory Committee Voted Unanimously to Accept the Recommendations)





- Tips and Strategies for Optimizing Rate Resolution or Ordinance (cont.)
  - Referencing Any Financial Policy Document Adopted for the Enterprise and the Need to Maintain Compliance with the Financial Policies for the Long-Term Benefit of Customers
  - Mentioning How the Proposed Rates Are Considered Competitive
  - Discussing How the Proposed Rates Are Considered Affordable by Utility Industry Standards





### **SOME FINAL THOUGHTS:**

 Developing Financial Plan and Rate Recommendations: Many Possibilities (No Single "Right Answer")



- Should Make Sure Any Financial Advice Is Objective
- Debt Financing Programs and Grant Opportunities Continue to Evolve
- May Not Be Able to Solve All Financial Issues at Once, Especially If Enterprise Is "Playing Catch Up"
  - May Need to Take Small Steps Over Time to Gradually Build the Financial Position to an Optimal Level



## **SOME FINAL THOUGHTS (cont.):**

#### Financial Plan Should:

- Be Reasonable and Affordable
- Allow Enterprise to Accomplish Objectives
- Promote Sustainability
- Enable Enterprise to Meet Financial Targets (Without Significantly Exceeding Them)
- Should Ideally Build / Establish Long-Term History of Following Plan and Meeting Targets
- For the Long-Term Interests of Customers, Operational and Financial Planning – Including Ratemaking – Should Be Proactive, Not Reactive
  - Keep Up With Inflation or Permanent Increases in Costs
  - Lower User Rates Over the Long-Term
  - Balanced Debt Risk
  - Higher Credit Rating (and Lower Interest Rates) When Debt Financing



## **QUESTIONS AND DISCUSSION**







If You Have Questions Regarding This Presentation or Would Like Additional Information, Please Contact Us! Bryan A. Mantz, CMC, CGFM President GovRates Phone: (833) GOV-PLAN (833) 468-7526 Email: bmantz@govrates.com Website: www.govrates.com







