Wastewater Treatment Division Financial Plan for the 2019 Proposed Sewer Rate

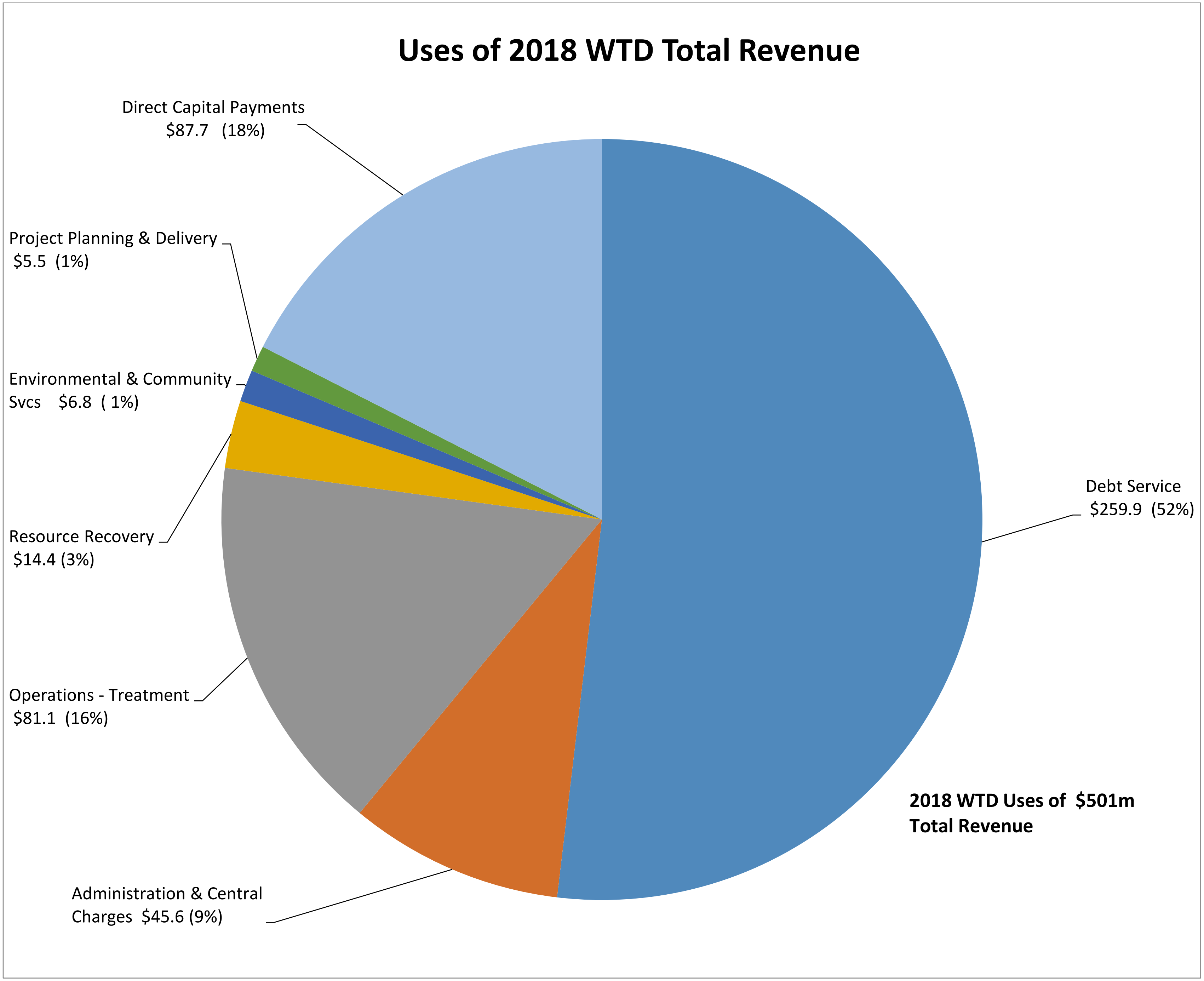
	2017 Unaudited	2018 Forecast	2019 Forecast	2020 Forecast	2021 Forecast	2022 Forecast	2023 Forecast	2024 Forecast
CUSTOMER EQUIVALENTS (RCEs)	757.24	761.79	765.98	770.73	775.50	780.31	785.15	790.02
MONTHLY RATE	$44.22	$44.22	$45.33	$45.33	$ 47.37	$ 47.37	$ 48.45	$ 49.56
% Increase	5.21%	0.00%	2.51%	0.01%	4.50%	0.00%	2.27%	2.3%
BEGINNING OPERATING FUND	$ 59,882	$ 61,055	$ 62,212	$ 62,800	$ 63,250	$ 63,930	$ 50,414	$ 31,492
OPERATING REVENUE:								
Customer Charges	$ 401,650	$ 404,234	$ 416,660	$ 419,277	$ 440,852	$ 443,606	$ 456,493	$ 469,818
Capacity Charge	82,630	75,623	81,204	87,187	93,513	100,266	104,868	109,614
Other Income	17,014	13,957	14,381	14,819	15,270	14,595	15,033	15,484
Investment Income	5,986	7,221	8,158	6,925	9,765	11,261	12,079	12,988
Rate Stabilization	-	-	-	-	-	14,400	19,850	-
TOTAL OPERATING REVENUES	$ 507,280	$ 501,035	$ 520,403	$ 528,207	$ 559,401	$ 584,128	$ 608,324	$ 607,904
OPERATING EXPENSE	(148,052)	(159,620)	(165,500)	(170,000)	(176,800)	(185,640)	(194,922)	(207,468)
DEBT SERVICE PARITY DEBT (incl WIFIA)	(159,580)	(164,423)	(172,188)	(169,270)	(176,719)	(189,757)	(201,226)	(211,367)
DEBT SERVICE PARITY LIEN OBLIGATIONS	(53,995)	(50,215)	(42,672)	(50,238)	(52,408)	(52,343)	(50,017)	(49,942)
SUBORDINATE DEBT SERVICE	(26,263)	(53,080)	(52,069)	(51,800)	(50,897)	(52,700)	(49,152)	(48,381)
DEBT SERVICE COVERAGE PARITY DEBT	2.25	2.08	2.06	2.12	2.17	2.10	2.05	1.89
DEBT SERVICE COVERAGE TOTAL PAYMENTS	1.50	1.28	1.33	1.32	1.37	1.35	1.38	1.29
AMORTIZATION OF VARIABLE RATE DEBT	(920)	(1,685)	(1,779)	(1,875)	(1,973)	(11,178)	(12,295)	(12,961)
LIQUIDITY RESERVE CONTRIBUTION	(1,173)	(1,157)	(588)	(450)	(680)	(884)	(928)	(1,255)
TRANSFERS TO CAPITAL	(74,533)	(87,681)	(98,155)	(95,042)	(109,627)	(100,847)	(109,078)	(84,735)
RATE STABILIZATION RESERVE	$ 46,250	$ 46,250	$ 46,250	$ 46,250	$ 46,250	$ 31,850	$ 12,000	$ 12,000
OPERATING LIQUIDITY RESERVE BALANCE	14,805	15,962	16,550	17,000	17,680	18,564	19,492	20,747
OPERATING FUND ENDING BALANCE	$ 61,055	$ 62,212	$ 62,800	$ 63,250	$ 63,930	$ 50,414	$ 31,492	$ 32,747
CONSTRUCTION FUND								
BEGINNING FUND BALANCE	$ 92,978	$ 77,445	$ 5,000	$ 5,000	$ 5,000	$ 5,001	$ 5,001	$ 5,000
REVENUES:								
Parity Bonds	-	-	-	15,552	164,637	179,294	157,886	139,595
Variable Debt Bonds (new money only)	50,000	-	-	-	-	-	-	-
Interim Debt	-	-	-	-	-	11,178	12,295	12,961
SRF Loans & WIFIA Parity Debt, 2020	26,471	28,190	-	**134,500**	**-**	**-**	-	-
Other (Brightwater, 2018-2020)	500	19,779	112,576	14,084	500	500	500	500
Transfers From Operating Fund	74,533	87,681	98,155	95,042	109,627	100,847	109,078	84,735
TOTAL REVENUES	$ 151,504	$ 135,650	$ 210,731	$ 259,177	$ 274,764	$ 291,819	$ 279,760	$ 237,790
CAPITAL EXPENDITURES	(192,197)	(208,020)	(219,708)	(263,490)	(267,466)	(275,666)	(265,134)	(225,617)
DEBT ISSUANCE COSTS	(250)	(500)	-	(311)	(3,293)	(3,586)	(3,158)	(2,792)
BOND RESERVE TRANSACTIONS	10,000	-	7,811	2,930	(6,285)	(13,026)	(11,470)	(10,141)
ADJUSTMENTS	15,927	425	1,167	1,694	2,281	459	0	761
ENDING FUND BALANCE	$ 77,445	$ 5,000	$ 5,000	$ 5,000	$ 5,001	$ 5,001	$ 5,000	$ 5,001
CONSTRUCTION FUND RESERVES								
Parity Reserve Account	150,491	150,491	142,680	139,750	146,035	159,061	170,530	180,672
SRF Reserve Account	11,612	12,873	13,485	13,666	13,358	12,899	12,899	12,137
Asset Management & Brightwater Settlement	159,939	140,660	28,584	15,000	15,000	15,000	15,000	15,000
TOTAL FUND RESERVES	$ 322,042	$ 304,024	$ 184,749	$ 168,416	$ 174,394	$ 186,960	$ 198,429	$ 207,809
CONSTRUCTION FUND BALANCE	$ 399,487	$ 309,023	$ 189,749	$ 173,416	$ 179,395	$ 191,961	$ 203,430	$ 212,811

Summary of WTD's Operating Budget

- Status Quo Summary
    - Inflationary assumptions for labor and central charges (using countywide assumptions).
    - Assumes business as usual.
    - Assumes same amount of FTEs as 2017 and 2018 adopted budget.
    - Total below target in financial plan.

  Additions Being Considered to WTD's 2019-2020 Operating Budget

    - Request For Additional Staff
        - Staffing Due To New Construction & Capacity Improvements
            - Plant Operations: support critical engineering, electrical, planning & scheduling, inventory controls and safety functions and allow staff and work order scheduling issues to be resolved.
            - Decennial Flow Monitoring Program: support to gather data over two wet seasons to meet requirements in Ord. 16033 which will provide critical data for future CIP development.
            - Enhance West Point Offsite Response Crews: support for dual purpose teams which will provide support to the staffed offsite teams during the wet weather season and provide support at West Point during the dry season construction and maintenance period. This includes supporting the new Georgetown Wet Weather facility beginning in July 2020.
        - Planning , Responsiveness and Administrative Services
            - Administrative Services: support in several administrative areas (WaterWorks Grant, Human Resources & Right of Way/Property Acquisition).
            - Planning and Asset Management: support to provide additional asset management and planning needs.
    - Increase $'s for staff development
        - Expands Operator in Training program, which supports areas where significant retirements are expected to occur.
    - Other Operating Budget additions
        - Biosolids Compost Study: study which will (a) identify areas of opportunity in the compost market; (b) assess alternatives for process and undertake a pilot project at South Plant; (c) perform potential capital project analyses and (d) increase awareness of Loop and solicit community involvement in product development.
        - Additional operations and maintenance costs associated with West Point co-gen unit, which is funded by annual cogen revenue.
        - Additional operations and maintenance costs to generate RIN revenue, which is supported by annual RIN revenue.
        - Additional Environmental Lab support in WLRD to meet projected workload.
        - Escrow Automation project costs for additional BRC support to complete project, which will reduce or reallocate several Capacity Charge Program staff.


Uses of 2018 WTD Total Revenue
Direct Capital Payments $87.7 (18%)
Project Planning & Delivery $5.5 (1%)
Environmental & Community Svcs $6.8 (1%)
Resource Recovery $14.4 (3%)
Operations - Treatment $81.1 (16%)
Administration & Central Charges $45.6 (9%)
Debt Service $259.9 (52%)
2018 WTD Uses of $501m Total Revenue

MWPAAC

Metropolitan Water Pollution
Abatement Advisory Committee

King Street Center, 201 South Jackson Street, MS KSC-NR-0512
Seattle, WA 98104 206-263-6070

December 28, 2015

Pam Elardo, P.E.
Director
King County Wastewater Treatment Division
201 South Jackson Street
KSC-NR-0501
Seattle, WA 98104

SUBJECT: **MWPAAC Debt Review Recommendation**

Dear Director Elardo:

In response to concerns about significant increases in the amount of debt that has been issued to fund Brightwater and that is planned to be issued for upcoming capital projects, the Metropolitan Water Pollution Abatement Advisory Committee (MWPAAC) created the Debt Review Team (Team) in 2013. The Team was created to (1) develop a shared understanding of the information utilized by to the King County Wastewater Treatment Division (WTD) staff to inform decision makers, and (2) develop recommendations for MWPAAC to propose the WTD Director. This review has been an opportunity to look at the current financial policies and evaluate what changes might be beneficial to WTD's long term financial health. The amount of WTD debt outstanding currently totals $3.8 billion or 54% of WTD revenues. This amount is forecasted to increase to $4.6 billion by 2030 and decreasing to $4.0 billion by 2045. MWPAAC recommends that WTD increase its debt service coverage ratio from the existing 115% to a target or goal of 140% by 2030 and presents the following three recommendations as a set of public policy options to achieve this goal.

Recommendation #1:
Institute a measured, multi-pronged strategy of rate increases and use of Rate Stabilization Fund balance

To reduce the amount of outstanding debt faced by WTD, MWPAAC recommends that WTD institute a multi-pronged approach that will place less reliance upon debt financing of WTD's capital program. This approach would utilize the following core strategies:

- ✓ Strategy #1: Moderately increase rates to generate additional cash that would be used to further fund the capital program. From 2017 to 2030 (based on staff analysis), this will increase the average annual rate increase to 3.0% from the current estimate of 2.1%.
- ✓ Strategy #2: Use the Rate Stabilization Fund (RSF) balance that is not needed by 2017.

Using the additional revenue generated to fund capital projects will allow WTD to reduce the size of its bond issues and thus debt portfolio moving forward. In turn, the additional revenue, combined with lower debt service, will increase WTD's debt service coverage ratio from the existing 115% to a target or goal of 140% by 2030.

This increase should be undertaken incrementally, and the target debt service coverage of 140% by 2030 should be characterized as a mechanism rather than an objective. The objective of the above strategies is to lower WTD's debt burden in the long term to $4.2 billion by 2030 and $2.1 billion by 2045 by using a greater amount of cash generated through rate revenue instead of debt to fund its capital projects.

Recommendation #2:
Maintain a 140% Debt Coverage Ratio

MWPAAC also recommends that if rate forecasts indicate rate reductions in a given year as debt burden declines, WTD consider maintaining a constant sewer rate in that year after 2030, provided the rate achieves or exceeds the 140% target. This would allow for continued decrease of debt and also allows flexibility for the utility to respond and adapt to unanticipated events requiring capital investments. This is illustrated in the attached Charts 1 and 2.

It should be recognized that increasing debt service coverage to 140% by 2030 is not intended to improve bond ratings, but rather to continue to strengthen WTD's financial capability to respond to future regulatory requirements and other capital needs.

Recommendation #3:
Maintain flexibility in financial policies to meet
the intent of Recommendations #1 and #2.

MWPAAC also proposes some flexibility in policy revisions to achieve the desired flexibility and responsiveness of the financial program to changing needs. Specifically, restricted transitional revisions to target coverage should be enabled during major capital undertakings. For example, a temporary reduction from 140% to 130% coverage might be authorized (by explicit and affirmative action) provided that a financial plan is adopted that indicates a return to the full target within no more than five years. This may also provide adaptability if temporarily allowed when other significant financial pressures arise. The utility has already increased the amount of cash-funded capital to a range of 30% to 40% annually (e.g., $78M cash funded in 2014, estimated $70M in 2015, and an estimated $55M-$75M in 2016-2021) and this recommendation would provide for this trend to continue, reaching over 60% by 2030.

In conclusion, MWPAAC's recommendations provide an alternative future financial plan that achieves debt reduction by 2030 and beyond while maintaining a smooth, stable rate pattern and provides flexibility to adapt to changing conditions. Modest changes to WTD's financial policies, such as described above, should be part of the utility's efforts toward overall debt reduction. We believe this will improve WTD's flexibility in facing future operational or regulatory challenges.

Sincerely,

Scott Thomasson, MWPAAC Chair

cc: MWPAAC Members

Chart 1

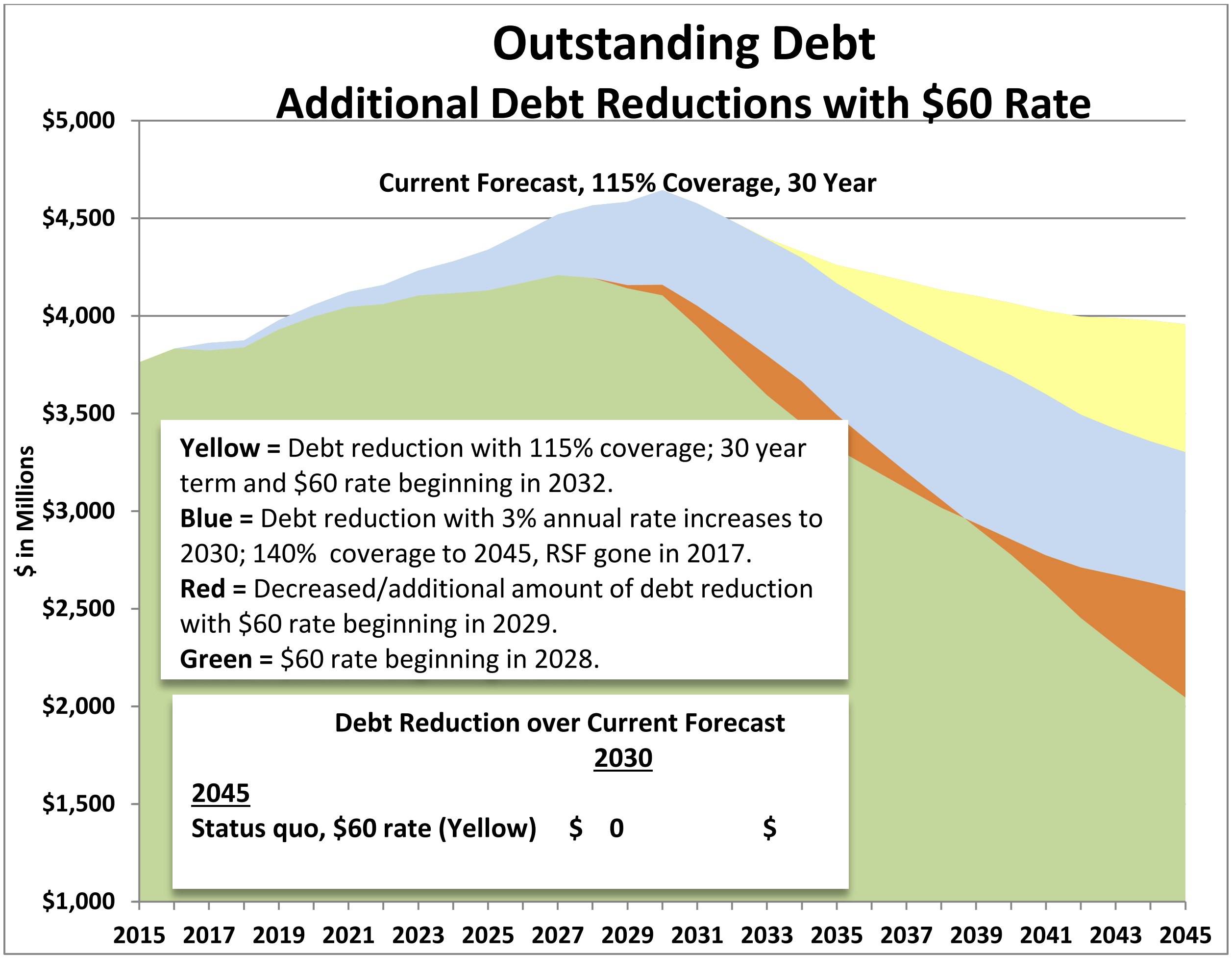
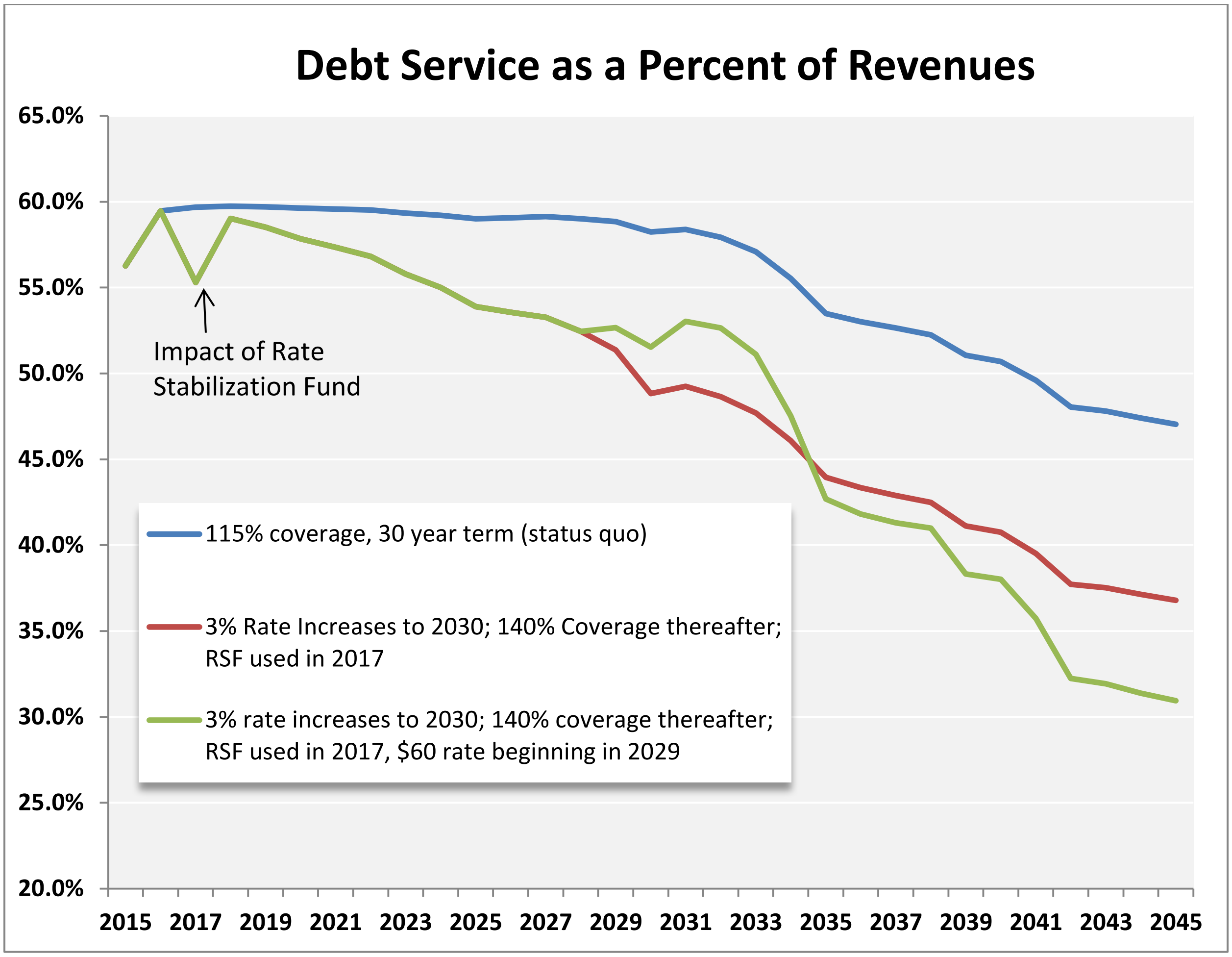
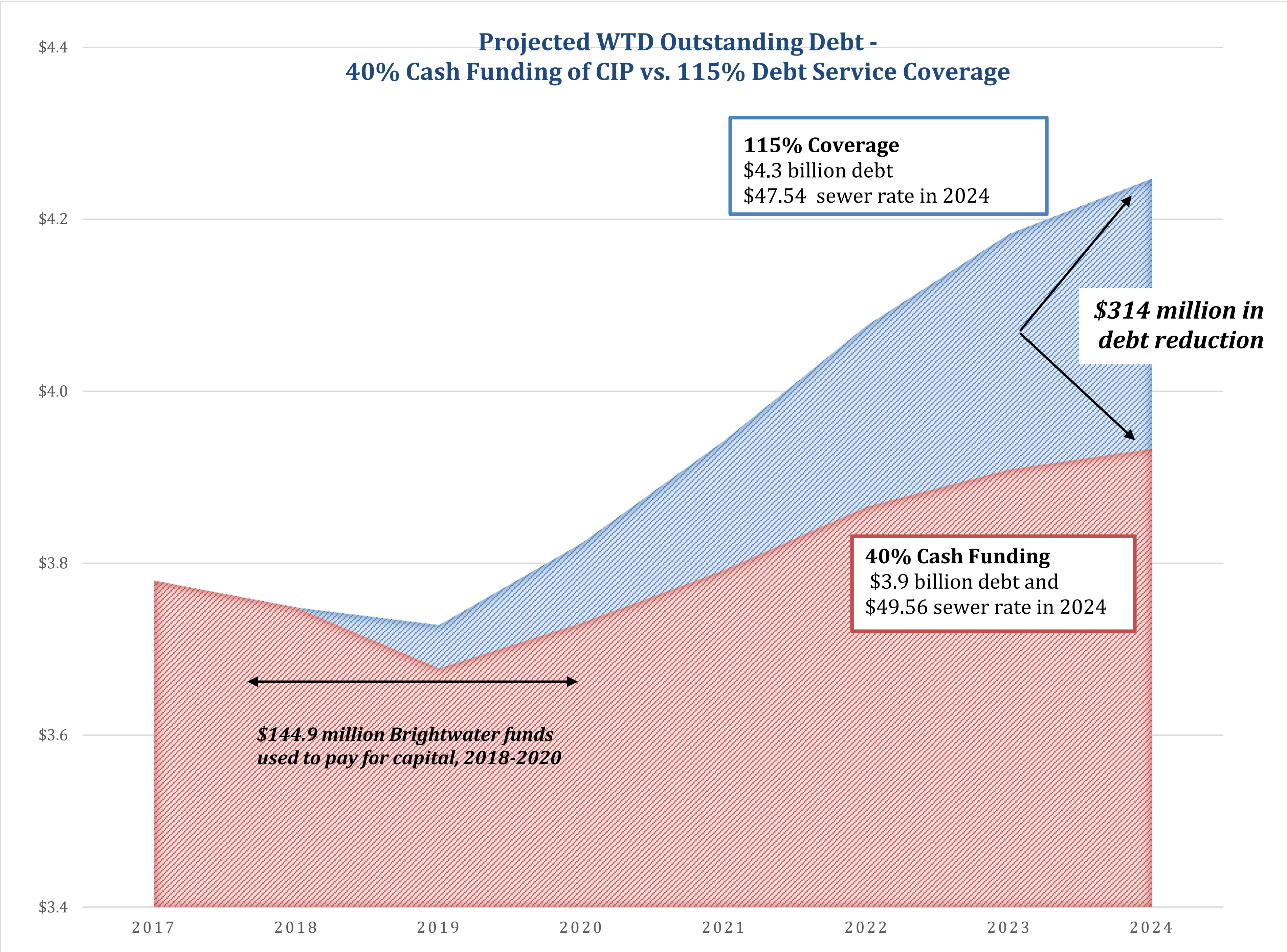
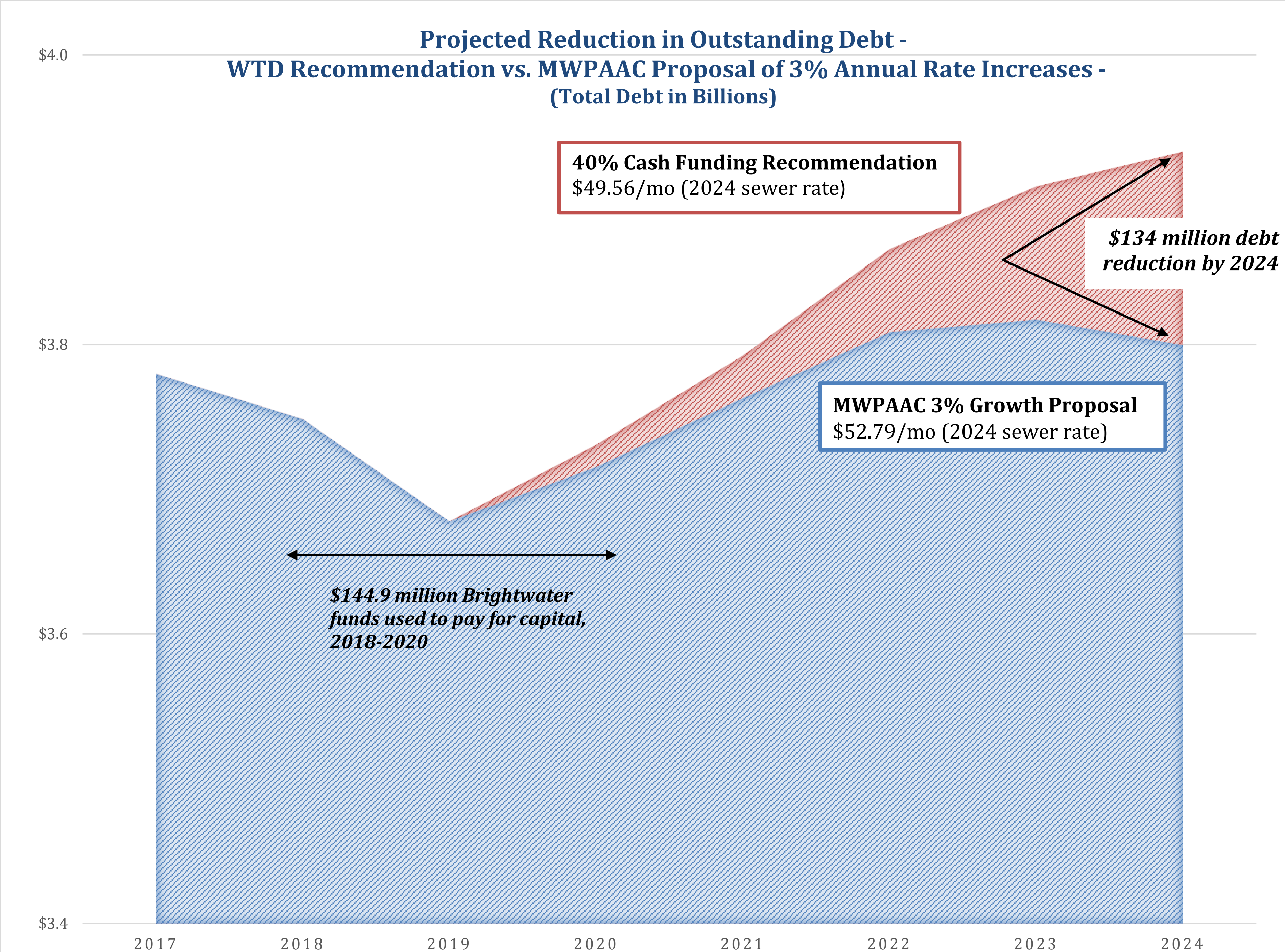

Outstanding Debt
Additional Debt Reductions with $60 Rate
Current Forecast, 115% Coverage, 30 Year
$5,000
$4,500
$4,000
$3,500
$3,000
$2,500
$2,000
$1,500
$1,000
$ in Millions
2015 2017 2019 2021 2023 2025 2027 2029 2031 2033 2035 2037 2039 2041 2043 2045
Yellow = Debt reduction with 115% coverage; 30 year term and $60 rate beginning in 2032.
Blue = Debt reduction with 3% annual rate increases to 2030; 140% coverage to 2045, RSF gone in 2017.
Red = Decreased/additional amount of debt reduction with $60 rate beginning in 2029.
Green = $60 rate beginning in 2028.
Debt Reduction over Current Forecast
2030
2045
Status quo, $60 rate (Yellow) $ 0 $

Chart 2


Debt Service as a Percent of Revenues
65.0%
60.0%
55.0%
50.0%
45.0%
40.0%
35.0%
30.0%
25.0%
20.0%
2015
2017
2019
2021
2023
2025
2027
2029
2031
2033
2035
2037
2039
2041
2043
2045
Impact of Rate Stabilization Fund
115% coverage, 30 year term (status quo)
3% Rate Increases to 2030; 140% Coverage thereafter; RSF used in 2017
3% rate increases to 2030; 140% coverage thereafter; RSF used in 2017, $60 rate beginning in 2029


Projected WTD Outstanding Debt -
40% Cash Funding of CIP vs. 115% Debt Service Coverage
115% Coverage
$4.3 billion debt
$47.54 sewer rate in 2024
$314 million in debt reduction
40% Cash Funding
$3.9 billion debt and
$49.56 sewer rate in 2024
$144.9 million Brightwater funds used to pay for capital, 2018-2020
$4.4
$4.2
$4.0
$3.8
$3.6
$3.4
2017
2018
2019
2020
2021
2022
2023
2024


Projected Reduction in Outstanding Debt -
WTD Recommendation vs. MWPAAC Proposal of 3% Annual Rate Increases -
(Total Debt in Billions)
$4.0
$3.8
$3.6
$3.4
40% Cash Funding Recommendation
$49.56/mo (2024 sewer rate)
$134 million debt reduction by 2024
MWPAAC 3% Growth Proposal
$52.79/mo (2024 sewer rate)
$144.9 million Brightwater funds used to pay for capital, 2018-2020
2017
2018
2019
2020
2021
2022
2023
2024