Citizens Rates and Governance Advisor Committee

KVID Rate Analysis Results
Revenue Requirements

Tuesday November 7, 2017

Tom Bourassa, CPA

Todays Presentation

- Overview of the rate analysis process
- The Revenue Requirements for KVID that came out of the rate analysis process
- KVID’s staff recommendation to the Board of Directors

Rate Analysis – Financial Planning

Rate Analysis – Financial Planning

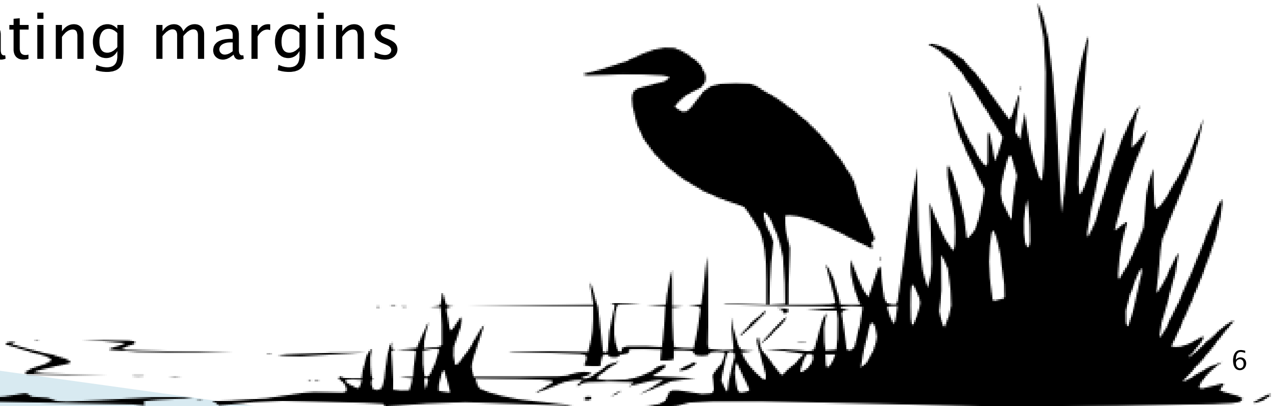
- Objective – Create 10-Year Plan Supporting:
  - Operations and maintenance
  - Capital improvements and replacement
  - Possible debt financing and retirement

Rate Analysis – Financial Planning (continued)

- Plan Includes Reserves for Operations and Maintenance
  - For purposes of this analysis KVID’s reserves have been set at a minimum of $750,000
  - $500,000 for emergency reserves
  - $250,000 for operational reserves

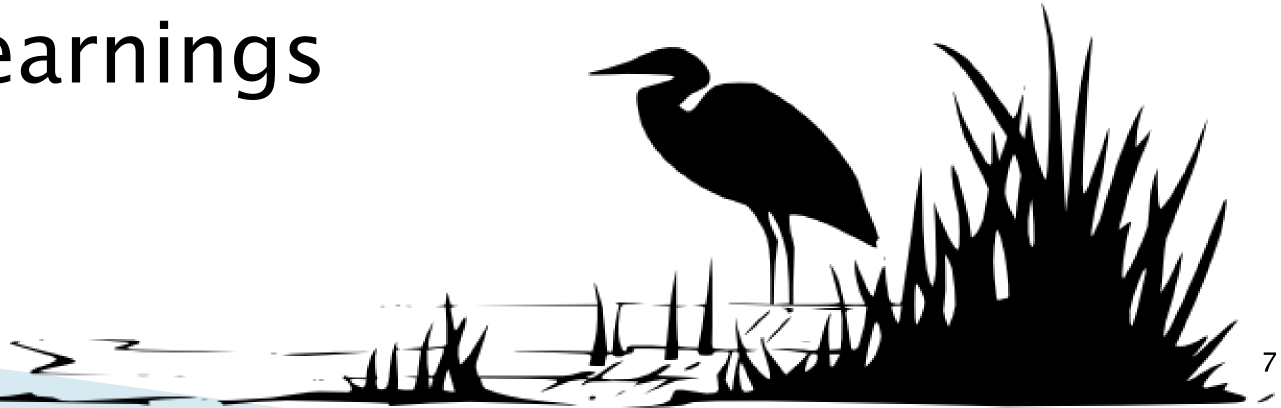
Rate Analysis – Financial Planning (continued)

- Revenue Requirement Analysis:
  - Operating revenues under current rates
  - Capacity fee revenues – for additional connections
  - Other revenues
  - Operation and maintenance expenses
  - Depreciation and Amortization
  - Administrative expenses
  - Capital expenditures
  - Reserves and appropriate operating margins (apply County Policy)



Rate Analysis – Financial Planning (continued)

- Operating Revenue Sources
  - Service rates (payment for water & wastewater services)
  - Service fees (establishment fees, late fees, etc.)
- Capital Revenue Sources
  - Connection fees
  - Advances & contributions in aid of construction
  - Grants, loans & interest earnings

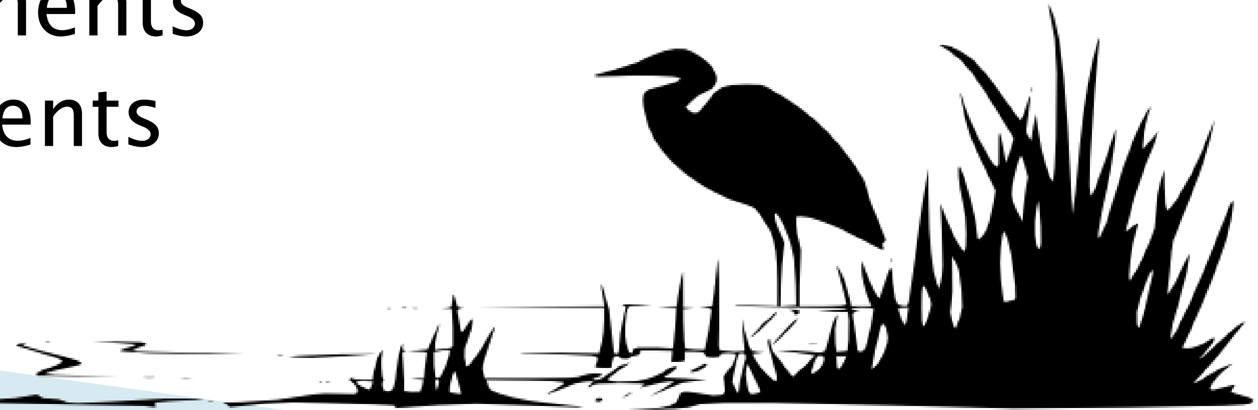


Rate Analysis – Financial Planning (continued)

- Operation & Maintenance Expenses
  - Cost to treat, supply, store, and transport water & wastewater
  - Cost of technical services (laboratory fees, engineering, etc.)
  - Administrative costs
    - Direct costs such as meter reading, billing, etc.
    - Indirect costs such as salaries of senior management, accounting, public relations, contracting

Rate Analysis – Financial Planning (continued)

- Long-Term Capital Improvement Plan (CIP)
  - Addresses utility system needs
  - Funded by revenues, reserves, loans, advances in aid of construction (AIAC), and contributions in aid of construction (CIAC)
  - Possible Debt Service Requirement
  - Includes principal payments
  - Includes interest payments



Rate Analysis – Financial Planning (continued)

- Capital Replacement & Maintenance Reserves
  - Must be adequate to meet capital needs
- Debt Service Reserves
  - Protect from defaulting on debt service payments during times of financial distress
- Operating Reserves
  - Meet ongoing cash flow requirements & emergency needs

Rate Analysis – Financial Planning (continued)

- Cost of Service
  - Allocates Revenue Requirements to Customer Classes
  - Based on Cost of Service to Each Customer Class
  - Not Necessarily Needed Here – 99% of Customers in Same Class (Residential)
  - Understanding of seasonal resident changes and impacts on revenues (evaluation of base rate)

KVID –Accounting Practices

KVID –Accounting Practices

- Current KVID Accounting Practices
  - Cash-based accounting
  - Using County accounting codes and categories
  - Adherence to County guidelines regarding capital expenditures and assets
  - Recording connection and infrastructure fees as revenue

KVID –Accounting Practices (continued)

Additional Recommendations

- Use an accrual basis for accounting (common for water/wastewater districts)
- Accrual system better matches revenues and expenses
- Develop a Uniform System of Accounts (USOA), better suited to presentation and analysis
- Record capital expenditures as fixed assets and record depreciation
- Record non-refundable developer-paid connection fees and infrastructure fees as Contributions-In Aid of Construction (CIAC). These fees are capital related and can be amortized.

KVID – Revenue Requirements

KVID – Revenue Requirements

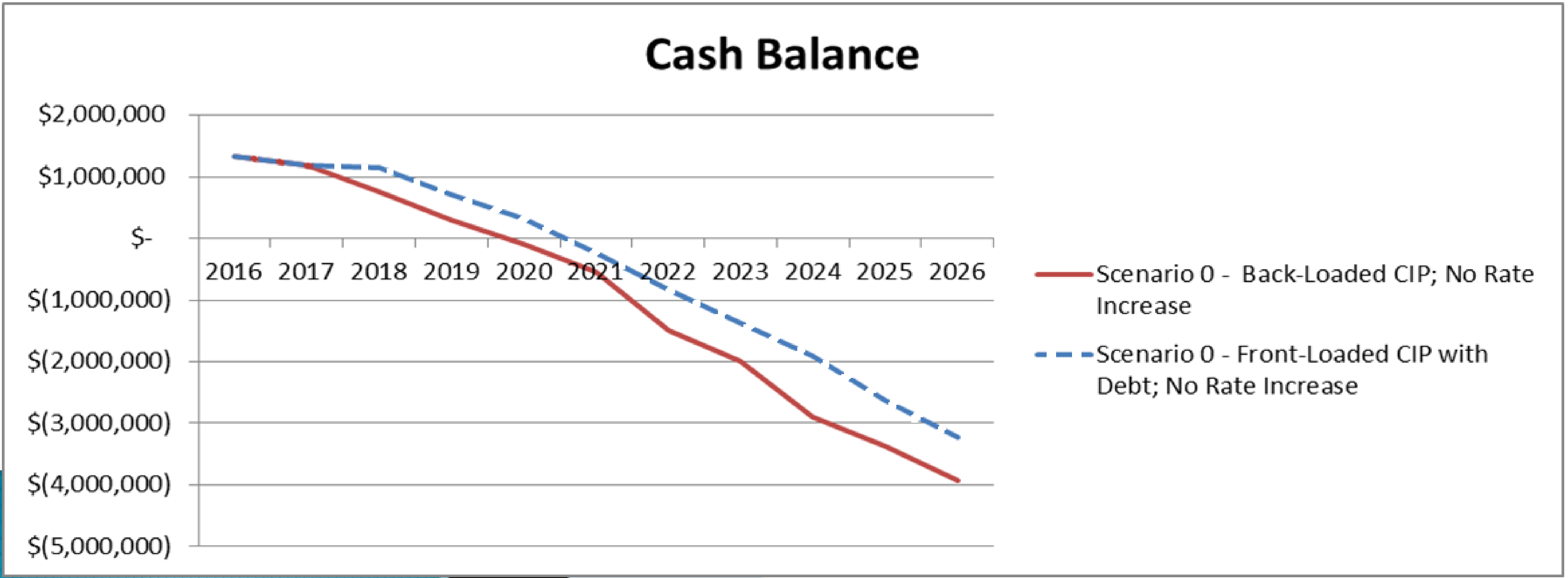
- Revenue Scenarios and Rate Models
    - Looking at the identified needs, Staff is presenting three potential scenarios regarding our Revenue Requirements.
    - Options for potential Rate Models to capture the needed revenue will be discussed later.

KVID – Revenue Requirements (continued)

Scenario 0 – No change in rates as KVID pursues the identified improvements

KVID – Revenue Requirements (continued)

- Scenario 0 – Results
  - Current predictions indicate that if KVID maintains current operations and pursues the recommended Capital Improvements, then KVID will run out of cash by 2020.



KVID – Revenue Requirements (continued)

- Scenario 1 – PayGo
  - Spreading out CIP items as much as is advisable to accommodate a **pay as you go** approach.
  - Address critical items (sludge handling, clarifier, altitude valves) immediately using the revenue stream and some existing fund balance, moving on to the infrastructure replacement as the fund balance recovers.
  - Accommodate expected operational costs and potential governance transition.
  - Maintain minimum fund balance reserves of $750,000

KVID – Revenue Requirements (continued)

- Scenario 1 – PayGo – Results
  - Overall additional revenue requirements increased by 59.7% ($690,000 annually).
  - Suggested three-year phase in:
    - Year One – 23.88% increase in costs to customers
    - Year Two – 16.00% increase in costs to customers
    - Year Three – 13.51% increase in costs to customers

KVID – Revenue Requirements (continued)

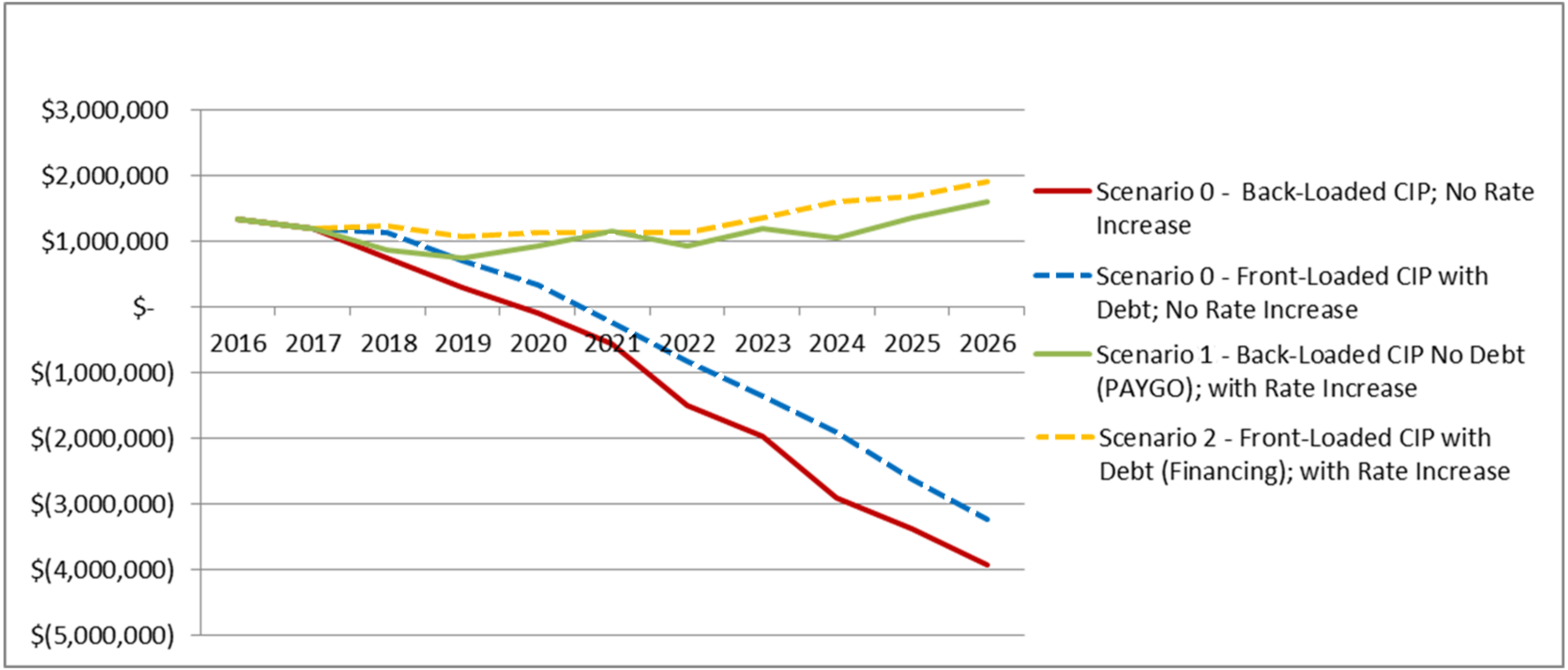
- Scenario 2 – Financing
  - Address critical items (sludge handling, clarifier, altitude valves) immediately with financing to implement needed items sooner, then implementation of overall infrastructure replacement over time.
  - Pursue debt financing through WIFA (20 year terms at approximately 3%).
  - Accommodate expected operational costs and potential governance transition.
  - Maintain fund balance reserves of $750,000

KVID – Revenue Requirements (continued)

- Scenario 2 – Financing – Results
  - Overall additional revenue requirements increased by 51.48% ($595,000 annually).
  - Suggested three-year phase in:
    - Year One – 20.59% increase in costs to customers
    - Year Two – 14.00% increase in costs to customers
    - Year Three – 12.05% increase in costs to customers

KVID – Revenue Requirements (continued)

Cash Projections – includes recommended revenue increase in 2023



Potential Rate Models

Potential Rate Models

- With the increased cost of operations and pursuit of the CIP necessitating an increase in revenue, the next step is to develop Rate Models that will capture the needed revenue.
- A detailed discussion of rate models will occur in a future meeting, however to provide a perspective on the proposed rate increase a quick look is presented here.

Potential Rate Models (continued)

Current Rates:

- On average a single family residence will use 2,800 gallons monthly, resulting in a water and sewer bill of around $60
- A residential customer using 5,000 gallons a month will see a water and sewer bill that is around $78

Potential Rate Models (continued)

Model 1 – Increases Across the Board

- Maintains the same structure as our current rates
- 73% of revenue captured from the fixed charge of the base rate (water and sewer combined), offsets the cost of on demand service and offsets seasonal fluctuation of revenue.
- All customers, regardless of classification, will see the same percentage of an increase to their bills (assuming their usage remains unchanged).

Potential Rate Models (continued)

Model 1 – Increases Across the Board

- The 2,800 gallon average Single Family Residential user's monthly bill (combined water and sewer) of approximately $60 will increase to approximately:

- Scenario 1 – PayGo
- $74 per month in 2018
- $85 per month in 2019
- $96 per month in 2020

- Scenario 2 – Financing
- $72 per month in 2018
- $81 per month in 2019
- $91 per month in 2020

Potential Rate Models (continued)

Model 1 – Increases Across the Board

- The 5,000 gallon average Single Family Residential user's monthly bill (combined water and sewer) of approximately $78 will increase to approximately:

- Scenario 1 – PayGo
- $97 per month in 2018
- $111 per month in 2019
- $125 per month in 2020

- Scenario 2 – Financing
- $94 per month in 2018
- $106 per month in 2019
- $118 per month in 2020

Staff Recommendation:

- Staff considers <u>Revenue Requirement Scenario 2 – Financing</u>, with the increase being spread out over 3 increases, to be the frontrunner of this process.

- This recommendation supports investment in KVID's critical infrastructure needs, operational costs, and the potential of a governance transition.

Questions and Discussion