

SECTION 9

FINANCIAL PLAN

Introduction

The financial plan matches funding sources with the capital program identified in the Comprehensive Water System Plan (CWSP) and develops a multi-year rate strategy to demonstrate financial viability in meeting the total costs of providing water service, which include:

- Financial policies
- Operating and maintenance (O&M) costs
- Administrative and overhead costs
- Capital related costs

The analysis considers the historical financial performance of the utility, the financial impact of executing the capital program, the sufficiency of current utility revenues, and the affordability of rates. The current water rate structure is also evaluated in terms of achieving revenue stability, efficiency of use and customer equity.

Financial Structure

The City of Battleground (City) legally owns and operates a water utility fund. The water utility is responsible for funding all of its related costs through user fees. It does not depend on general fund resources. The primary source of funding for the water utility is monthly user rates, with additional revenues generated from water service fee penalties, meter installations and NSF check recovery fees. The City controls the level of user charges by ordinance and, subject to statutory authority, can adjust user charges as needed to meet financial objectives.

The City maintains a fund structure and implements financial policies that target management of a financially viable and fiscally responsible enterprise fund utility.

Financial Policies

This analysis is based on a framework of fiscal policies that promote the financial integrity and stability of the water utility. A brief summary of the key financial policies employed by the City, as well as those recommended and incorporated in the financial plan are discussed below.

Reserve Funds

Like any business, a municipal utility requires certain minimum levels of cash reserves to operate. These reserves address variability and timing of expenditures and receipts, as well as occasional disruptions in activities, costs or revenues. Given the City's responsibility to provide an essential service at a certain standard, protection against financial disruptions is even more important than it would be for a private sector or non-essential counterpart.

In addition to protecting the utility against financial disruption, a defined reserve structure serves to maintain appropriate segregation of funds and promote the use of resources for their intended purposes. The following reserve funds are evaluated.

The operating reserve is designated to provide a liquidity cushion to ensure that adequate cash working capital is maintained to deal with cash balance fluctuations from unanticipated cash expenses or lower than expected revenue collections.

The rate stabilization reserve maintains funds to cushion the impact of significantly lower than expected rate revenue collections caused by wet summers, loss of a large water user or other unexpected circumstances. Maintaining this reserve mitigates the impact of lower revenue collection and allows for rates to be less conservatively set.

The City's current policy is to maintain a minimum operating reserve target of 90 days of O&M expense and an additional 90 days of O&M for rate stabilization reserves. This target is within industry standards for a water utility. Based on 2013 O&M of \$1,138,977, a minimum target balance of \$280,844 is established for each reserve for a combined reserve of \$561,687, increasing with the O&M forecast to \$901,807 by the end of the study period (2032).

The capital contingency reserve is an amount of cash set aside in case of an emergency should a piece of equipment or a portion of the utility's infrastructure fail. The reserve could also be used for other unanticipated capital needs including capital project cost overruns. Industry practice ranges from maintaining a balance equal to 1 to 2 percent of fixed assets, an amount equal to a 5-year rolling average of capital improvement program (CIP) costs, or an amount determined sufficient to fund an equipment failure (other than catastrophic failure). The final target level should balance industry standards with the risk level of the City. A target of 2 percent of fixed assets has been used in this analysis, ranging from \$530,808 in 2013 to \$1,037,937 in 2032 as completed CIP projects increase the total cost of fixed assets.

The debt reserve fund is generally set by covenant requirements when debt is issued. The City has no outstanding debt.

System Reinvestment

The purpose of system reinvestment funding is to provide for the replacement of aging system facilities to ensure sustainability of the system for ongoing operation. Each year, the utility's assets lose value, and as they lose value they move toward eventual replacement. This accumulating loss in value and future liability is typically measured for reporting purposes through an annual depreciation expense, based on the original cost of the asset over its anticipated useful life. While this expense reflects the consumption of the existing asset and its original investment, the replacement of that asset will likely cost much more when factoring in inflation and construction conditions. Therefore, the added annual replacement liability is even greater than the annual depreciation expense.

The 2011 depreciation expense of \$605,964, plus estimated additional depreciation expense from new CIP projects as they are booked as assets through 2013, totals \$665,101. To maintain rate increases at about inflationary levels, this analysis assumed funding at about 65

percent of annual depreciation expense, ranging from \$432,316 to \$516,525 over the 6-year period. This level is projected to cash fund 92 percent of the 20-year CIP.

Past Financial Performance

This section includes a historical summary of financial performance as reported by the City on the water utility Statement of Revenues, Expenses and Changes in Fund Equity and Statement of Net Assets. Noteworthy findings and trends are discussed below to demonstrate the historical performance and condition of the utility.

**Table 9-1a
Statement of Revenues, Expenses and Change in Fund Net Assets**

Statement Revenues Expenses and Change in Fund Net Assets	2006	2007	2008	2009	2010	2011
Operating Revenues						
Charges for Services	\$ 1,910,340	\$ 1,983,061	\$ 2,027,589	\$ 2,232,671	\$ 2,037,375	\$ 2,115,368
Miscellaneous	2,929	3,937	2,907	4,015	6,504	7,871
Total Operating Revenues	\$ 1,913,269	\$ 1,986,998	\$ 2,030,496	\$ 2,236,686	\$ 2,043,879	\$ 2,123,239
Operating Expenses						
Personnel Services	\$ 626,586	\$ 661,353	\$ 760,680	\$ 733,763	\$ 732,863	\$ 709,705
Supplies	105,772	85,568	78,796	74,861	87,250	87,621
Professional Services	75,807	87,067	71,368	71,893	76,688	84,009
Utilities	161,829	174,200	187,968	192,320	158,034	160,788
Miscellaneous	88,129	74,642	63,824	83,473	96,702	-
Repairs and Maintenance	52,213	50,672	77,473	34,143	53,944	45,030
Taxes	95,285	100,494	98,310	105,919	97,506	96,299
Intergovernmental Services	-	-	-	-	-	32,340
Insurance claims and expenses	-	-	-	-	-	-
Allocated expenses	-	-	-	-	-	-
Other	-	-	-	-	-	58,009
Depreciation	549,297	586,361	638,237	638,987	643,969	605,964
Total Operating Expenses	\$ 1,754,918	\$ 1,820,357	\$ 1,976,656	\$ 1,935,359	\$ 1,946,956	\$ 1,879,765
Operating Income/Loss	\$ 158,351	\$ 166,641	\$ 53,840	\$ 301,327	\$ 96,923	\$ 243,474
Nonoperating Revenues [Expenses]						
Interest Earnings	\$ 70,552	\$ 99,682	\$ 68,683	\$ 32,757	\$ 23,291	\$ 52,584
State and Federal Grants	-	-	-	-	-	-
Interest and Fiscal Charges	(34,978)	(18,312)	(4,154)	-	-	-
Gain [Loss] on Disposal of Capital Assets	(10,170)	-	-	-	-	-
Total Nonoperating Revenues [Expenses]	\$ 25,404	\$ 81,370	\$ 64,529	\$ 32,757	\$ 23,291	\$ 52,584
Income [Loss] Before Contributions and Transfers	\$ 183,755	\$ 248,011	\$ 118,369	\$ 334,084	\$ 120,214	\$ 296,058
Capital Contributions	\$ 712,637	\$ 1,392,073	\$ 1,599,666	\$ 596,648	\$ 205,168	\$ 175,117
Transfers Out	(167,252)	(184,414)	(192,195)	(151,412)	(172,589)	(178,975)
Increase [Decrease] in Net Assets	\$ 729,140	\$ 1,455,670	\$ 1,525,840	\$ 779,320	\$ 152,793	\$ 292,200
Total Net Assets at Beginning of Year	\$ 15,289,561	\$ 16,018,701	\$ 17,474,371	\$ 19,053,778	\$ 19,803,183	\$ 19,831,748
Prior Year Adjustments	-	-	53,567	(29,915)	(124,228)	-
Total Net Assets at End of Year	\$ 16,018,701	\$ 17,474,371	\$ 19,053,778	\$ 19,803,183	\$ 19,831,748	\$ 20,123,948

**Table 9-1b
Statement of Net Assets**

Statement of Net Assets	2006	2007	2008	2009	2010	2011
ASSETS						
Current Assets						
Cash and Cash Equivalents	\$ 1,297,647	\$ 2,021,170	\$ 1,951,385	\$ 1,752,260	\$ 1,431,955	\$ 1,359,523
Cash with Fiscal/Escrow Agent		-				
Investments	385,371	88,457	473,355	1,399,288	2,215,412	2,749,148
Receivables (net)						
Accounts	133,046	162,418	210,144	361,499	264,384	278,148
Interest	4,855	1,743	5,833	4,935	4,400	6,050
Restricted Assets	-	-	-	-	-	-
Prepaid Expenses	-	-	-	-	-	66
Interfund Advance Receivable	-	-	-	-	-	-
Total Current Assets	\$ 1,820,919	\$ 2,273,788	\$ 2,640,717	\$ 3,517,982	\$ 3,916,151	\$ 4,392,935
Noncurrent Assets						
Property, Plant and Equipment (Net)	15,135,223	15,637,261	16,648,218	16,531,404	16,163,688	15,926,639
Total Noncurrent Assets	\$ 15,135,223	\$ 15,637,261	\$ 16,648,218	\$ 16,531,404	\$ 16,163,688	\$ 15,926,639
TOTAL ASSETS	\$ 16,956,142	\$ 17,911,049	\$ 19,288,935	\$ 20,049,386	\$ 20,079,839	\$ 20,319,574
LIABILITIES						
Current Liabilities						
Accounts Payable	\$ 46,639	\$ 52,090	\$ 51,217	\$ 28,345	\$ 37,566	\$ 36,489
Advances from Other Funds	200,000	200,000	-	-	-	-
Accrued Interest Payable	5,906	2,008	35,507	34,613	34,741	34,034
Other Accrued Liabilities	46,692	50,711	90,595	120,510	105,040	44,122
Compensated Absences	812	845	1,446	1,569	1,769	2,025
Bonds, Notes and Loans Payable from Restricted Assets - Current	307,697	98,061	-	-	-	-
Total Current Liabilities	\$ 607,746	\$ 403,715	\$ 178,765	\$ 185,037	\$ 179,116	\$ 116,670
Noncurrent Liabilities						
Advances from Other Funds	200,000	-	-	-	-	-
Bonds, Notes and Loans Payable	98,021	-	-	-	-	-
Compensated Absences	31,674	32,963	56,392	61,166	68,975	78,956
Total Noncurrent Liabilities	\$ 329,695	\$ 32,963	\$ 56,392	\$ 61,166	\$ 68,975	\$ 78,956
TOTAL LIABILITIES	\$ 937,441	\$ 436,678	\$ 235,157	\$ 246,203	\$ 248,091	\$ 195,626
NET ASSETS						
Invested in Capital Assets, Net of Related Debt	14,729,505	15,539,200	16,648,218	16,531,404	16,163,688	15,926,639
Restricted for Capital Purposes	-	-	-	-	-	-
Restricted for Debt Service	-	-	-	-	-	-
Unrestricted	1,289,196	1,935,171	2,405,560	3,271,779	3,668,060	4,197,309
TOTAL NET ASSETS	\$ 16,018,701	\$ 17,474,371	\$ 19,053,778	\$ 19,803,183	\$ 19,831,748	\$ 20,123,948

Key findings include:

- Charges for Services increased 11 percent over the historical period due to a combination of customer growth and rate increases, with a peak in revenue collection in 2009.

- The Operating Ratio (total operating expenses divided by total operating revenues) remained at about 60 percent in all years, indicating operating revenues are sufficient to meet operating expenses. A ratio greater than 90 percent would indicate that there is little room for new debt service and capital replacement without additional rate increases. A ratio greater than 100 percent would indicate that operating expenses exceed operating revenues and would be indicative of an unsustainable financial condition. The utility had no outstanding debt, providing ample debt capacity to fund future capital.
- A Quick Ratio (current assets divided by current liabilities) increasing from 3:1 to 38:1 reflects the positive cash position of the water utility from 2006 to 2011. Current Assets, comprised of primarily cash and investments, grew by 141 percent during this period.

Capital Costs and Funding Strategy

The CIP developed for this CWSP identifies total capital obligations for a 6-year (2013-2018) and 20-year (2013-2032) planning period. The capital funding plan defines a strategy for funding the CIP considering available cash reserves, system development charges, external contributions from grants / developers and new debt proceeds, if required.

Capital costs are stated in 2012 dollars and escalated annually at 3 percent construction cost inflation to the year of planned spending for financing projections. The CIP identifies \$6.4 million (\$7.1 million escalated) in project costs over the 6-year planning horizon and \$19.8 million (\$26.8 million escalated) over the 20 year period.

Table 9-2 provides the detail CIP (escalated) and assumed funding sources. As shown, each year has varied capital obligations depending on construction schedules and infrastructure planning needs. About 27 percent of capital program costs are scheduled for the 6-year period.

**Table 9-2
Capital Financing Forecast**

Capital Funding	2013	2014	2015	2016	2017	2018	2013-2018 CIP	2013-2032 Total CIP
CIP 2013-2032 [1]								
New Intertie Booster Pump Station on Ne 219th St	\$ 1,400,800	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 1,400,800	\$ 1,400,800
New Intertie 219th St Booster Pump Station Upgrade	-	-	-	-	-	-	-	172,182
Regional Source Transmission Development	-	-	1,502,500	759,718	782,510	805,985	3,850,713	18,035,179
New 1.4 MG Reservoir	-	-	-	-	-	-	-	2,491,621
Annual Water Main Replacement Program	51,500	53,045	54,636	56,275	57,964	59,703	333,123	2,434,525
8" Diameter Distribution Main on SW 2nd Ct	-	-	-	-	-	-	-	129,137
8" Diameter Distribution to Hydrant on SW 3rd St	-	-	-	-	-	-	-	12,299
8" Diameter Distribution on NE Grace Ave	-	-	-	-	-	-	-	584,190
12" Main on SW 20th Street	-	-	-	-	-	674,640	674,640	674,640
Well Replacement	-	-	874,182	-	-	-	874,182	874,182
Total Capital Projects	\$ 1,452,300	\$ 53,045	\$ 2,431,318	\$ 815,994	\$ 840,474	\$ 1,540,327	\$ 7,133,458	\$ 26,808,755
Projected Capital Cash Flow								
Water SDC/Capital Fund Beginning Balance	\$ 87,302	\$ 1,013,750	\$ 3,189,472	\$ 1,407,444	\$ 1,260,844	\$ 1,117,207	\$ 87,302	\$ 87,302
Transfer from Water Fund (above reserve levels)	1,800,000	1,645,000	-	-	-	3,674	3,448,674	7,632,283
SDC Revenue	146,258	147,720	149,198	150,690	152,196	153,718	899,780	12,007,231
Rate-Funded System Reinvestment	432,316	433,005	484,145	504,629	525,728	516,525	2,896,348	14,608,900
Interest Earnings	175	3,041	15,947	14,074	18,913	22,344	74,494	1,805,144
Debt Proceeds	-	-	-	-	-	1,580,000	1,580,000	2,185,000
CIP Costs	(1,452,300)	(53,045)	(2,431,318)	(815,994)	(840,474)	(1,540,327)	(7,133,458)	(26,808,755)
Ending Balance	\$ 1,013,750	\$ 3,189,472	\$ 1,407,444	\$ 1,260,844	\$ 1,117,207	\$ 1,853,141	\$ 1,853,141	\$ 11,517,104

[1] Future Cost based on 3% annual inflation (conservative approximation of last 12 months ENR change).

The capital funding strategy assumes the following funding priority:

- Accumulated capital cash reserves
- Annual revenue collections for current connection charges (SDCs)
- Annual cash from rates earmarked for system reinvestment funding
- Annual transfers of excess cash (over minimum balance targets) from the operating fund, if any
- Debt issuance

The capital funding analysis demonstrates that the water utility is projected to have sufficient cash to fund 92 percent of the total CIP due to significant existing cash reserves, policy for ongoing rate-funding for system reinvestment, and SDC revenue collections. The remaining 8 percent is projected to be debt-funded. Projected borrowing totals \$2.2 million from issuances in 2018 and 2023.

Revenue Requirements Forecast

The revenue requirement analysis forecasts the amount of operating and capital related costs to determine the annual revenue required from rates. Although the capital funding plan is completed for the 20-year time horizon, the financial plan focuses on the 6-year planning period.

The analysis incorporates operating revenues, O&M expenses, debt service payments, rate funded capital needs, and any other identified revenues or expenses related to utility operations, and determines the sufficiency of the current level of rates. Revenue needs are

also impacted by debt covenants (typically applicable to revenue bonds) and specific fiscal policies and financial goals of the utility.

Typically, two (2) revenue sufficiency criteria are tested to determine the annual revenue need: 1) cash needs must be met and 2) debt coverage requirements must be realized.

The financial forecast is developed from the City's 2012 projected year-end performance, along with other key factors and assumptions listed below:

- Water rate revenues are forecasted based on projected year-end 2012 water rate revenue plus 1 percent annual customer growth.
- Interest earnings on cash balances are assumed at 0.2 percent in 2013 phasing up to 2 percent by the end of the 6-year forecast.
- Operating costs are based on the 2013-2014 Biennial Budget.
- O&M expenses are escalated at 2.5 percent per year for labor and general system costs and 7 percent for employee benefit costs. State taxes are calculated using prevailing tax rates.
- Revenue bond borrowing is projected at 3.5 percent interest and 1.5 percent issuance cost with a 20-year repayment term. The revenue bond coverage factor is 1.25 beginning in the first year of repayment.

Table 9-3 summarizes the annual revenue requirement for the 6-year horizon.

**Table 9-3
Revenue Requirement Forecast**

Revenue Requirements	Projected Y-E	Projected					
	2012	2013	2014	2015	2016	2017	2018
Revenues							
Rate Revenues Under Existing Rates	\$ 1,889,231	\$ 1,908,123	\$ 1,927,205	\$ 1,946,477	\$ 1,965,941	\$ 1,985,601	\$ 2,005,457
Non-Rate Revenues	247,845	251,412	251,939	250,925	256,709	262,841	276,608
Total Revenues	\$ 2,137,076	\$ 2,159,536	\$ 2,179,143	\$ 2,197,402	\$ 2,222,651	\$ 2,248,442	\$ 2,282,065
Expenses							
Cash Operating Expenses	\$ 1,487,023	\$ 1,668,954	\$ 1,733,195	\$ 1,774,984	\$ 1,817,803	\$ 1,861,676	\$ 1,906,739
Existing Debt Service	-	-	-	-	-	-	-
New Debt Service	-	-	-	-	-	-	121,546
Rate-Funded System Reinvestment	-	432,316	433,005	484,145	504,629	525,728	516,525
Total Expenses	\$ 1,487,023	\$ 2,101,269	\$ 2,166,200	\$ 2,259,129	\$ 2,322,432	\$ 2,387,405	\$ 2,544,810
Annual Surplus / (Deficiency)	\$ 650,053	\$ 58,266	\$ 12,943	\$ (61,727)	\$ (99,781)	\$ (138,963)	\$ (262,745)
Net Revenue from Rate Increases	\$ -	\$ -	\$ 40,679	\$ 83,405	\$ 128,263	\$ 175,344	\$ 224,741
Net Surplus / (Deficiency)	\$ 650,053	\$ 58,266	\$ 53,623	\$ 21,678	\$ 28,482	\$ 36,381	\$ (38,003)
Annual Rate Adjustment [1]		0.00%	3.00%	3.00%	3.00%	3.00%	3.00%
Cumulative Rate Adjustment		0.00%	3.00%	6.09%	9.27%	12.55%	15.93%

[1]Rate increase for 2013 and 2014 adopted with the Biennial Budget.

The City has adopted the 2013-2014 biennial budget, which assumes no rate increase for 2013 and a 3 percent increase for 2014. Future annual increases of 3 percent are planned so that sufficient revenue is collected to meet rising costs and to make annual debt payments on the 2018 revenue bond. This rate strategy is projected to fund the financial obligations of the water utility including operating, capital, and reserve requirements through the forecast period.

Table 9-4 shows a summary of the projected operating and capital fund ending fund balances over the 6-year period. As previously discussed, the operating fund has a minimum operating reserve target of 90 days of O&M plus an additional 90 days of O&M for rate stabilization. The capital fund minimum balance is set at 2 percent of fixed assets. Minimums are met in each year of the planning period.

**Table 9-4
Ending Cash Balance Summary**

Ending Fund Balances	2012	2013	2014	2015	2016	2017	2018
Water Fund - Operating	\$ 3,925,641	\$ 2,183,907	\$ 592,530	\$ 614,208	\$ 642,689	\$ 679,071	\$ 637,394
Water SDC Fund - Capital	87,302	1,013,750	3,189,472	1,407,444	1,260,844	1,117,207	1,853,141
Debt Reserve	-	-	-	-	-	-	121,546
Total	\$ 4,012,943	\$ 3,197,657	\$ 3,782,002	\$ 2,021,652	\$ 1,903,533	\$ 1,796,278	\$ 2,612,081
Combined Minimum Target Balance		\$ 1,092,495	\$ 1,112,168	\$ 1,174,542	\$ 1,204,946	\$ 1,236,184	\$ 1,403,371

Current and Projected Rates

The existing water rate structure consists of a monthly basic meter charge of \$11.80, which includes three (3) ccf of water. Residential customers pay \$2.05 per ccf for use above the three (3) ccf and up to 15 ccf. Use above 15 ccf is charged at \$2.56 per ccf. All other customers pay a basic meter charge that increases with meter size and a volume charge of \$2.20 per ccf for all water use.

While the existing structure adequately encourages water conservation, further refinements could be made to improve efficiency of use and customer equity including:

- Eliminate the water usage allowance and charge for all use in volume rates
- Implement a third tier in the residential block rate to target highest water users and provide greater relief to low water users
- Consider seasonal rates for non-residential customers

The following table compares existing and proposed rates under the existing water rate structure.

**Table 9-5
Existing and Projected Water Rates**

Monthly Rates		Existing	Across-the-Board Increases					
		2012	2013	2014	2015	2016	2017	2018
Basic Meter Charge	Inside-City per month rate - includes 3 ccf	\$11.80	\$11.80	\$12.80	\$13.18	\$13.58	\$13.99	\$14.41
Residential Consumption	Inside-City per 100 cubic feet							
	4 - 15 ccf	\$2.05	\$2.05	\$2.05	\$2.11	\$2.17	\$2.24	\$2.31
	>15 ccf	\$2.56	\$2.56	\$2.56	\$2.64	\$2.72	\$2.80	\$2.88
Basic Meter Charge Commercial	5/8" meter	\$19.35	\$19.35	\$19.35	\$19.93	\$20.53	\$21.14	\$21.78
	3/4" meter	\$21.35	\$21.35	\$21.35	\$21.99	\$22.65	\$23.33	\$24.03
	1" meter	\$36.50	\$36.50	\$36.50	\$37.60	\$38.72	\$39.88	\$41.08
	1.5" meter	\$65.20	\$65.20	\$65.20	\$67.16	\$69.17	\$71.25	\$73.38
	2" meter	\$101.00	\$101.00	\$101.00	\$104.03	\$107.15	\$110.37	\$113.68
	3" meter	\$201.00	\$201.00	\$201.00	\$207.03	\$213.24	\$219.64	\$226.23
	4" meter	\$321.00	\$321.00	\$321.00	\$330.63	\$340.55	\$350.77	\$361.29
Commercial Consumption	Inside-City per 100 cubic feet	\$2.20	\$2.20	\$3.20	\$3.30	\$3.39	\$3.50	\$3.60
Commercial Irrigation	Annual connection	\$45.00	\$45.00	\$45.00	\$46.35	\$47.74	\$49.17	\$50.65
	De-activation charge	\$20.00	\$20.00	\$20.00	\$20.60	\$21.22	\$21.85	\$22.51
Outside the City	Rates and charges are all 1.5 times the in-City rates and charges							

Note: Table 9-5 reflects changes to basic residential meter charges and commercial consumption charges adopted in 2014.

Affordability

The Washington State Department of Health and Public Works Board use an affordability index to prioritize low-cost loan awards depending on whether utility bills exceed 2 percent of the median household income for the service area. This is a commonly used metric in the industry. If monthly bills are less than 2 percent of the median household income for the demographic area, rates are generally considered affordable. Table 9-6 presents the City’s estimated median income, affordability thresholds, and project water bills over the study period. As shown, the City’s projected water rates and corresponding customer bills are forecasted to remain well under the affordability threshold.

**Table 9-6
Affordability Benchmark**

	2012	With Projected Increases					
		2013	2014	2015	2016	2017	2018
Median Income	\$ 61,216	\$ 62,746	\$ 64,315	\$ 65,923	\$ 67,571	\$ 69,260	\$ 70,992
Affordability Threshold [1]	\$ 204.05	\$ 209.15	\$ 214.38	\$ 219.74	\$ 225.24	\$ 230.87	\$ 236.64
Projected Bi-Monthly Bill [2]	\$44.10	\$44.10	\$45.42	\$46.79	\$48.19	\$49.63	\$51.12

[1] Based on 2% of Median Household Income for a two-month period.

[2] Based on 16 ccf usage for a two-month period.

Available Funding Assistance and Financing Resources

Feasible long-term capital funding strategies must be defined to ensure that adequate resources are available to fund the identified CIP. In addition to cash reserves, capital revenues, and rate revenues designated for capital purposes, capital needs can be met from outside sources such as grants, low-interest loans, and bond financing. The following is a summary of potential resources.

Utility Resources

Water utility resources appropriate for funding capital needs include accumulated cash in the capital reserve, rate revenues designated for capital spending purposes, and capital-related connection charges and other connection fees. The first two (2) resources were discussed in the Financial Policies section (9.3). Capital related charges are discussed below.

Connection Charge

A connection charge (referred to as System Development Charge by the City), as provided for in RCW 35.92.025, refers to a one-time charge imposed on new customers as a condition of connecting to the utility system. The purpose of the connection charge is two-fold: 1) to promote equity between new and existing customers and 2) to provide a source of revenue to fund capital projects. Connection charges provide a mechanism for new customers to share in the capital costs incurred to support their addition to the system. Revenues from connection charges provide a source of cash flow that is used to support utility capital needs. The revenue can only be used to fund utility capital projects or pay debt service incurred to finance capital projects. In the absence of such charges, growth-related capital costs would be borne in large part by existing customers. In addition, the net investment in the utility already collected from existing customers, whether through rates, charges and/or assessments, would be diluted by the addition of new customers, effectively subsidizing new customers with prior customers' payments.

While connection charges commonly incorporate the cost of both existing system assets and future facilities based on the CIP, the City has elected to base the SDC exclusively on future system costs.

For the purposes of the financial analysis, the existing (2012) SDC is \$2,210 for new single family residential water customers. Based on projected infrastructure needs identified in the 20-year CIP presented in Section 8 and system capacity, an updated charge of \$3,074 per equivalent residential unit (ERU) was calculated for 2013. The updated SDC will be implemented in 2014 and adjusted for 2015 inflation. The proposed 2015 charge, incorporating inflation projected at 3 percent annually, is \$3,261 per ERU. The updated charge calculation and schedule of charges are as follows:

**Table 9-7a
2013 System Development Charge Calculation**

SDC UNIT COST	
Allocable Future Facilities Cost Basis	\$ 16,922,813
Incremental Future Capacity (ERUs)	5,505
Charge per ERU	\$ 3,074

**Table 9-7b
SDC by Meter Size**

Existing Water SDCs		Planned 2014 SDC		Proposed 2015 SDCs	
Meter Size	Charge	Meter Size	Charge	Meter Size	Charge
5/8"	\$ 2,210	5/8"	\$ 3,074	5/8"	\$ 3,261
3/4"	\$ 3,315	3/4"	\$ 4,611	3/4"	\$ 4,892
1"	\$ 5,525	1"	\$ 7,685	1"	\$ 8,153
1.5"	\$ 13,260	1.5"	\$ 18,444	1.5"	\$ 19,568
2"	\$ 22,100	2"	\$ 30,741	2"	\$ 32,613
3"	\$ 50,830	3"	\$ 70,704	3"	\$ 75,010
4"	\$ 90,610	4"	\$ 126,037	4"	\$ 133,713

Local Facilities Charge

While a connection charge is the manner in which new customers pay their share of general facilities costs, local facilities funding is used to pay the costs of local facilities that connect each property to the system's infrastructure. Local facilities funding is often overlooked in a rate forecast since it is funded upfront by either connecting customers and developers or through an assessment to properties, but typically not from rates. Although these funding mechanisms do not provide a capital revenue source toward funding CIP costs, the discussion of these charges is included because they impact the new system customers.

There are a number of mechanisms that can be considered toward funding local facilities. One (1) of the following scenarios typically occurs: a) the utility charges a connection fee based on the cost of the local facilities (under the same authority as the connection charge); b) a developer funds the extension of the system to their development and turns those facilities over to the utility (contributed capital); or c) a local assessment is set up called a Utility Local Improvement District (ULID/LID) that collects property assessments from benefited properties.

A Local Facilities Charge (LFC) is a variation of the connection charge authorized by RCW 35.92.025. It is a Utility-imposed charge to recover the cost related to extending service to local properties. Often called and applied as a front-footage charge imposed based on the length of water main footage “fronting” a particular property, it is usually implemented as a reimbursement mechanism to a utility for the cost of a local facility that directly serves a property. It is a form of connection charge and, as such, can accumulate up to ten years of interest. LFCs typically apply to instances where no developer-installed facilities are needed through developer extension due to the prior existence of available mains already serving the developing property.

A Developer Extension is a requirement that a developer install onsite and sometimes offsite improvements as a condition of extending service. These are in addition to the connection charge required and must be built to utility standards. Utilities are authorized to enter into developer extension agreements under RCW 35.91.020. Part of the developer extension agreement between a utility and developer might include a latecomer agreement, resulting in a latecomer charge to new connections to the developer extension.

Latecomer Charges are a variation of developer extensions whereby a new customer connecting to a developer-installed improvement makes a payment to a utility based on their share of the developer’s cost (RCW 35.91.020). The utility passes this payment to the developer who installed the facilities. This is part of the developer extension process, and defines the allocation of costs and records latecomer obligations on the title of affected properties. No interest is allowed, and the reimbursement agreement cannot exceed 15 years in duration.

A ULID/LID is another mechanism for funding infrastructure that assesses benefited properties based on the special benefit received by the construction of specific facilities (RCW 35.43.042). Most often used for local facilities, some ULIDs also recover related general facilities costs. Substantial legal and procedural requirements can make this a relatively expensive process, and there are mechanisms by which a ULID can be rejected by a majority of property ownership within the assessment district boundary.

Outside Funding Sources

Often utility resources from service revenue and connection charges are insufficient to cash-fund the cost of all CIP projects upfront. The City would look to external funding and financing options to complete the program. These include primarily state and federal low cost loan programs, grants, and revenue bonds.

Grants and low cost loans for Washington State utilities are available from the Departments of Ecology and the Department of Commerce. Each includes programs for which the City might be eligible, but are primarily targeted at sewer programs or low income and/or rural communities.

Washington State Department of Ecology

The Department of Ecology Water Quality Program administers three (3) major funding programs that provide low interest loans, grants or loans and grant combinations for projects that protect, preserve and enhance water quality in Washington State. These are primarily for wastewater projects and are not applicable to the City's water CIP. Further detail is available in the Funding Guidelines found at

<http://www.ecy.wa.gov/programs/wq/funding/funding.html>.

Washington State Department of Commerce

The Department of Commerce has four (4) grant and loan programs that the City could potentially be eligible for:

- Community Development Block Grants General Purpose Grant;
- Community Economic Revitalization Board Grant and Loan Program;
- Public Works Trust Fund Loan Program; and
- Drinking Water State Revolving Fund Loan Program.

Community Development Block Grants (CDBG) General Purpose Grants

CDBGs are made available to Washington State small cities, towns and counties in carrying out significant community and economic development projects that principally benefit low and moderate income persons. Eligible applicants are Washington State cities and towns with a population less than 50,000 and counties with a population less than 200,000 that are non-entitlement jurisdictions or are not participants in a HUD Urban County Entitlement Consortium. Eligible projects include public facilities for water, wastewater, storm sewer and streets. The application period is September through November annually.

Community Economic Revitalization Board (CERB)

CERB, a division of the Washington State Department of Commerce, primarily offers low cost loans; grants are made available only to the extent that a loan is not reasonably possible. The CERB targets public facility funding for economically disadvantaged communities, specifically for job creation and retention. Priority criteria include the unemployment rates, number of jobs created and/or retained, wage rates, projected private investment, and estimated state and local revenues generated by the project. Traditional construction projects are offered at a maximum dollar limit of \$1 million per project. A local match of 25 percent is targeted.

Eligible applicants include cities, towns, port districts, special purpose districts, federally recognized Indian tribes and municipal corporations.

The CERB's policy is that all loans will be secured by a general obligation pledge of the taxing power of the borrowing entity. Terms do not exceed 20 years, including available payment deferral of interest and principal for up to five (5) years. Interest rates match the

most current rate of Washington State bonds (not to exceed 10 percent). Application deadlines are 45 days prior to a CERB meeting, which are scheduled six (6) times per year. For more information, see

www.commerce.wa.gov/commissions/CommunityEconomicRevitalizationBoard/Pages/CERB-B-Traditional-Programs.aspx.

Public Works Trust Fund (PWTF)

While the PWTF has historically been a resource to cities, towns, counties and special purpose districts to fund water projects, it is not funded in the current biennium. In addition, the state legislature passed a statute with the intent of redirecting tax revenue from the Public Works Assistance Account for six (6) years to the state General Fund.

For more information, see: <http://www.pwb.wa.gov/Documents/Letter-to-2014-PWTF-Construction-Applicants.pdf>

Drinking Water State Revolving Loan Program (DWSRL)

The DWSRL is jointly administered by the Public Works Board and the Department of Health. The program is intended to improve drinking water systems and protect public health for publicly and privately owned systems.

There is no match required, terms are not to exceed 20 years and project completion time is 4 years after loan execution. The loan limit is \$12 million, with a loan fee of 1 percent, and interest rates range from 1 to 1.5 percent depending upon the income level of households in the water service area.

For more information, see: http://www.doh.wa.gov/ehp/dw/our_main_pages/dwsrf.htm

General Obligation Bonds

General obligation (GO) bonds are secured by the full faith and credit of the issuing agency, committing all available tax and revenue resources to debt repayment. With this high level of commitment, GO bonds have relatively low interest rates and few financial restrictions. However, the authority to issue GO bonds is restricted in terms of the amount and use of the funds, as defined by the Washington State Constitution and statute. Specifically, the amount of debt that can be issued is linked to assessed valuation.

RCW 39.36.020 states:

(ii) Counties, cities, and towns are limited to an indebtedness amount not exceeding one and one-half percent of the value of the taxable property in such counties, cities, or towns without the assent of three-fifths of the voters therein voting at an election held for that purpose.

(b) In cases requiring such assent counties, cities, towns, and public hospital districts are limited to a total indebtedness of two and one-half percent of the value of the taxable property therein.

While bonding capacity can limit availability of GO bonds for utility purposes, these can sometimes play a valuable role in project financing. A rate savings may be realized through two (2) avenues: 1) the lower interest rate and related bond costs; and 2) the extension of repayment obligation to all tax-paying properties (not just developed properties) through the authorization of an ad valorem property tax levy.

Revenue Bonds

Revenue bonds are commonly used to fund utility capital improvements. The debt is secured by the revenues of the issuing utility and the debt obligation does not extend to a utility's other revenue sources. With this limited commitment, revenue bonds typically bear higher interest rates than GO bonds and also require security conditions related to the maintenance of dedicated reserves (a bond reserve) and financial performance (added bond debt service coverage). The utility agrees to satisfy these requirements by ordinance as a condition of the bond sale.

Revenue bonds can be issued in Washington State without a public vote. There is no bonding limit, except perhaps the practical limit of the utility's ability to generate sufficient revenue to repay the debt and provide coverage. In some cases, poor credit might make issuing bonds problematic.

Conclusion

The results of this analysis indicate that 3 percent annual rate increases are necessary to fund ongoing operating needs and projected debt associated with the identified capital program. Implementation of proposed rate increases should provide for continued financial viability.

It is recommended that the City regularly review and update the key underlying assumptions that serve as the foundation of the multi-year financial plan to ensure that adequate revenues are collected to meet the total water utility financial obligations.