

## NACWA 2014 Wet Weather Consent Decree Workshop

The New Enforcement Paradigm: Strategies and Tools to  
Maximize Economic Flexibility and Environmental Benefit



# Financial Capability Assessments for Wastewater Consent Decree Negotiations: *Lessons of the Political Economy*

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# Presentation Outline

**1. EPA Financial Capability Guidance**

**2. Rethinking Financial Capability Assessment**

**3. Evolving Landscape of FCAs / Affordability**

**4. Negotiation Strategy & Dynamics**

# **EPA Financial Capability Guidance**



# EPA Assessment Methodology – a 2-Part Test

Permittee Financial Capability Indicators Score	Residential Indicator (Cost Per Household as a % of MHI)		
	Low (Below 1.0%)	Median (Between 1.0% and 2.0%)	High (Above 2.0%)
Weak (Avg. Below 1.5)	Medium Burden	High Burden	High Burden
Mid-Range (Avg. Between 1.5 and 2.5)	Low Burden	Medium Burden	High Burden
Strong (Avg. Above 2.5)	Low Burden	Low Burden	Medium Burden

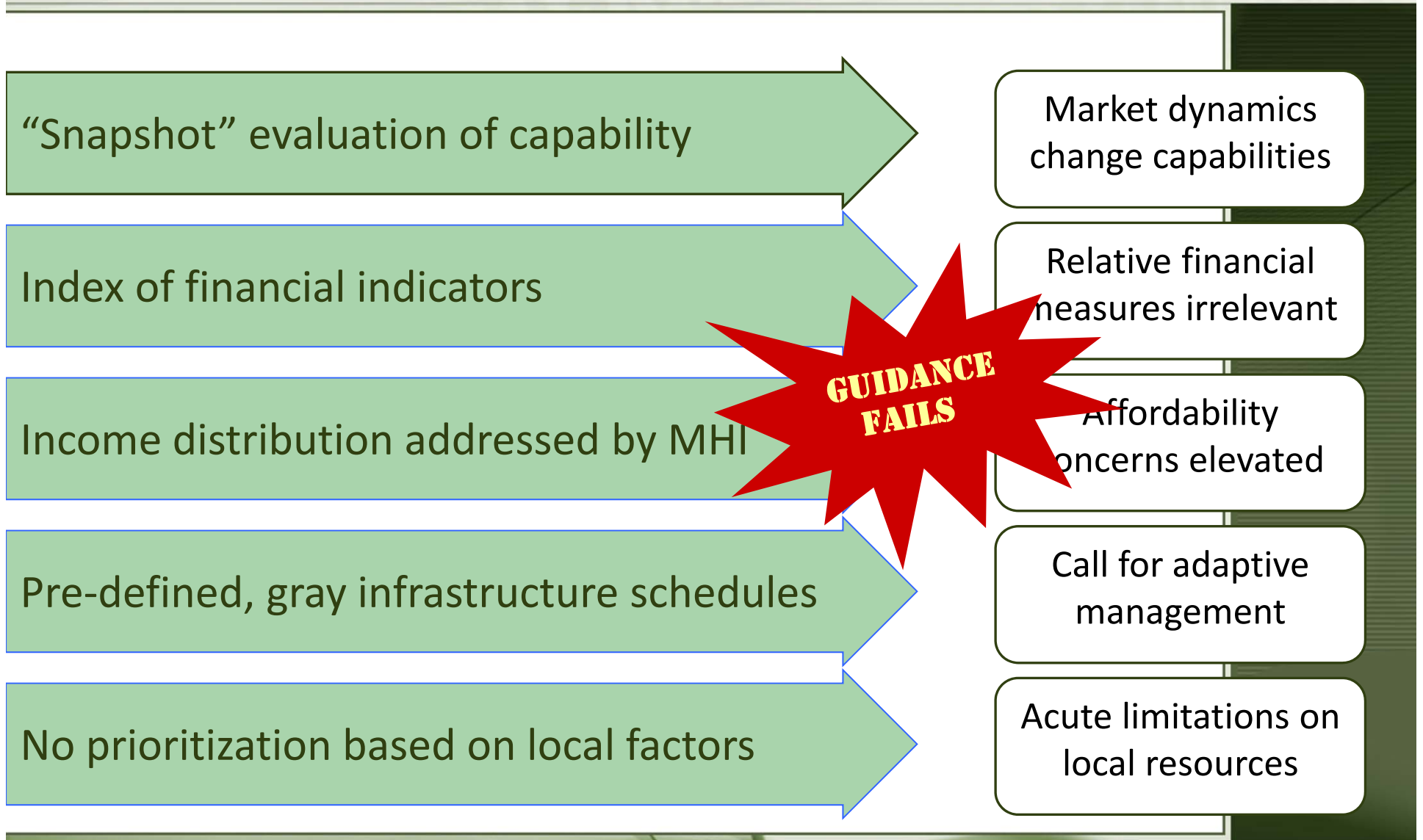
# Residential Indicator Calculation

	Guidance Line No.	
Current WWT Costs (O&M and Debt Service)	102	
Projected Annual O&M expenses	103	
Projected Debt Service for Program CIP	104	
<u>Projected WWT &amp; Program CIP Costs</u>	<u>105</u>	
Total Current & Projected Costs		106
Residential Share of WWT Costs	107	
Total Number of Households in Service Area	<u>108</u>	
WWT Costs Per Household		109
Census Year Median Household Income (MHI)	201	
MHI Adjustment Factor	<u>202</u>	
Adjusted MHI		203
Annual WWT and CSO Control Cost Per Household	204	
<b>Residential Indicator:</b>		
Annual WWT & CSO Cost Per Household as a Percent of MHI		205

# Financial Capability Indicators

	Strong (1)	Medium (2)	Weak (3)
<b>Debt Indicators</b>			
• Bond Rating (S&P)	AAA- A	BBB	BB - D
• Overall Net Debt as a Percent of Full Market Property Value	$X < 2\%$	$2\% < X < 5\%$	$X > 5\%$
<b>Socioeconomic Indicators</b>			
• Unemployment Rate (vs. U.S. Avg.)	$X < 1\%$	$1\% < X < 1\%$	$> 1\%$
• Median Household Income (vs. Adjusted U.S. Avg.)	$X > 25\%$	$25\% > X > 25\%$	$X < 25\%$
<b>Financial Management Indicators</b>			
• Property Tax Revenue as a Percent of Full Market Property Value	$X < 2\%$	$2\% < X < 4\%$	$X > 4\%$
• Property Tax Revenue Collection Rate	$X > 98\%$	$98\% > X > 94\%$	$X < 94\%$

# Guidance Limitations





# Additional Considerations

- Guidance calls for submittal of information on “additional considerations” that more fully reflect Permittees’ financial capabilities
- **No defined mechanism to employ in matrix format for determination of level of burden**
- Other Permittees:
  - Economic trends—population, employment decline
  - Low-income populations
  - Housing / shelter costs
    - Multi-generational households
  - **Green Infrastructure options / potential**



# Rethinking Financial Capability Assessment



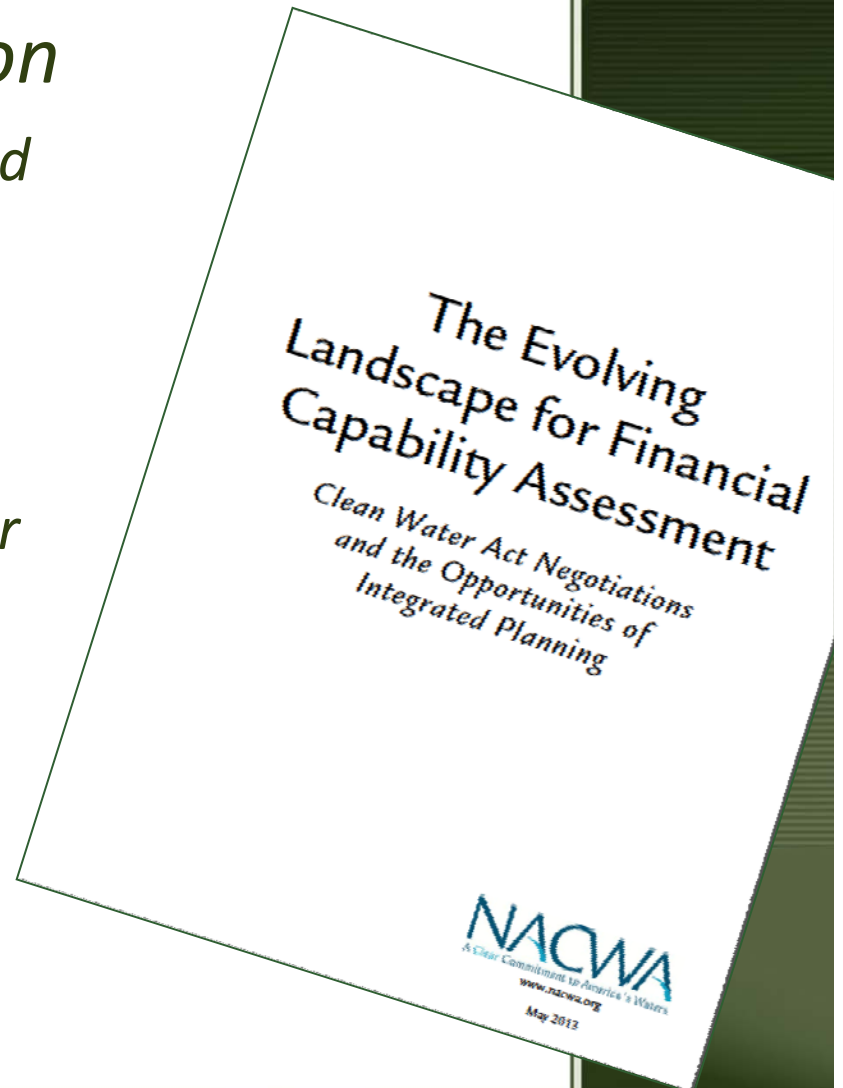
# Rethinking Financial Capability

- What the EPA guidance and enforcement posture gets right:
  - Claim on MHI is one reasonable metric
  - Schedule relief, if substantive, mitigates burden
  - Service is generally under-priced
    - Limiting the merit of claims for subsidy / support
- Yet, a static workbook approach to assessment denies that financial capability:
  - changes with changing conditions
  - reflects “local” factors
  - must be considered holistically



# NACWA's Recommendation

- *Structured CIP prioritization*
  - *Demonstrates that projects yield greatest environmental returns*
- *Cash flow analysis*
  - *Demonstrates the permittee's project financing capacity under tenable rate increase programs*
- *Evaluation of disproportionate burden*
  - *Demonstrates low-income impacts under rate program*



# Strategic Financial Planning Model Structure

- 30-year cash flow analysis
- Revenues
  - Existing rates (including growth)
  - System-wide rate increases
- O&M expenses
  - O&M forecast via escalation factors
- Capital financing
  - Existing and future debt obligations
    - Alternative forms of debt
  - Cash financing of capital
- Financial policies / metrics
  - Debt service coverage targets
  - Minimum fund balances

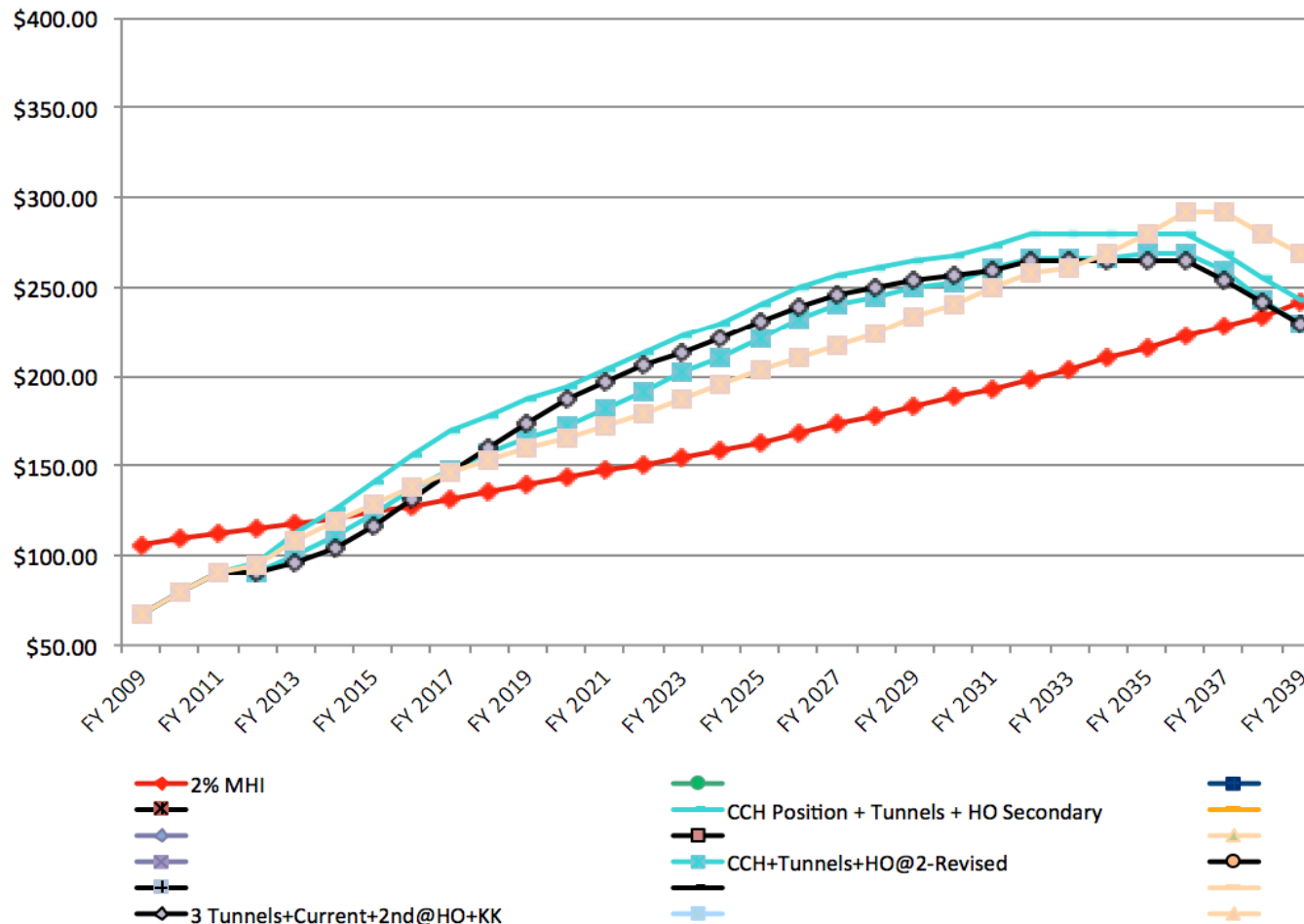
# EX: Strategic Financial Planning Model

☒ Projected MHI

## City and County of Honolulu Global Settlement Analyses

### Projected Bills vs 2% Median Household Income FY 2009-2039

- ☐ Staged 2nd at Sand Island
- ☐ Early 2nd at SI and Honouliuli
- ☐ Early Tunnels + Staged 2nd
- ☒ 11-18 Current CIP + CCH Pos



- ☐ CCH CIP
- ☐ CCH CIP +10%
- ☐ CCH CIP +20%
- ☐ CCH CIP +40%
- ☐ CCH CIP + EPA Position
- ☒ CCH + Tunnels + HO@2
- ☐ CCH Collect System Position
- ☐ CCH + EPA + Secondary
- ☒ CCH+Tunnels+HO@2 - Rev
- ☐ CCH+2nd@HO&KK+ Prim@S
- ☐ 3 Tunnels + Current CIP
- ☐ CCH CIP + 20% + Treatment
- ☐ 3 Tunnels Accel + Current CIP
- ☒ 3 Tunnels + 2nd@HO+KK
- ☐ CCH CIP + 100% + Treatment

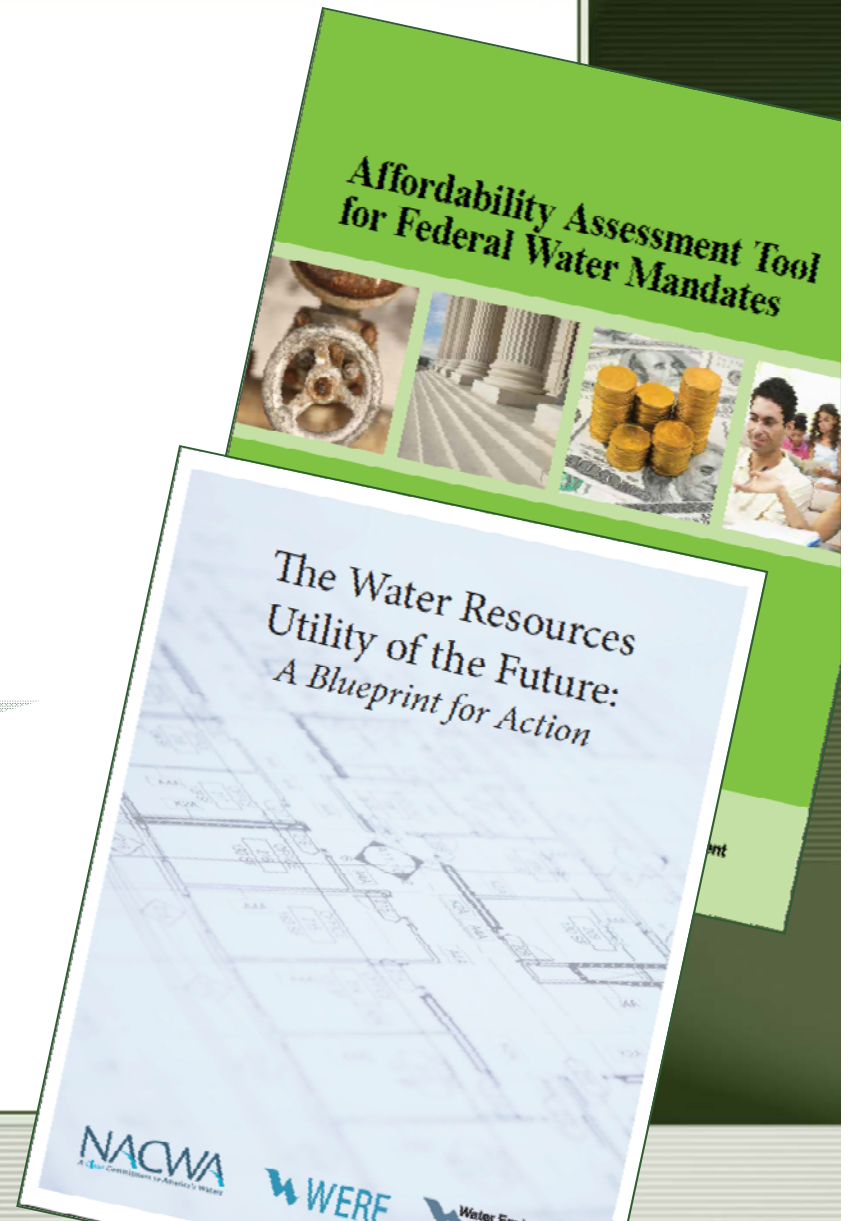
# **Evolving Landscape of FCAs / Affordability**





# Advocacy on Multiple Fronts

- Local Elected Officials
    - U.S. Conference of Mayors
  - Professional Societies
    - AWWA
    - WERF
    - WEF
    - **NACWA**
- 
- Remains incumbent on Permittee to submit additional information





# Permittee Experience: Shifting Landscapes

Issue	Pre- 2007 Permittee Experience	Recent Permittee Experience	Examples
High Burden Determination	No major metro permittee's burden acknowledged	Several communities designated as under "High Burden"	Atlanta, Honolulu, NEORSD, St. Louis
Anticipated Percent of MHI claim		Actual / projected MHI burdens approach 3%	Atlanta, Cincinnati, Honolulu
Schedule Limits	Fixed 20-year viewed as absolute maximum due to High Burden	25-year schedules and/or flexibility afforded	Kansas City, NEORSD, Cincinnati, Honolulu
Cash-flow Analysis	No framework for consideration of "additional info"	Utilities' strategic financial planning models used	Akron, Atlanta, Honolulu, St. Louis

# Negotiation Strategy & Dynamics



# Negotiation Strategy Considerations

- Perform EPA Guidance workbook calculations
  - Scenario analyses:
    - Program components (Green Infrastructure?)
    - Forecast assumptions
- Identify “additional considerations” and options for submittal
- Review EPA-developed Financial Capability Assessments (and program requirements)
- ***Develop / expand SFP modeling***
  - *Develop position on structure and schedule needs*
- ***Refine / formalize CIP prioritization structure***
- ***Consider low-income affordability options***

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