

2018-2023 Rate Path Options

First Presentation to the Customer Review Panel
January 25, 2016

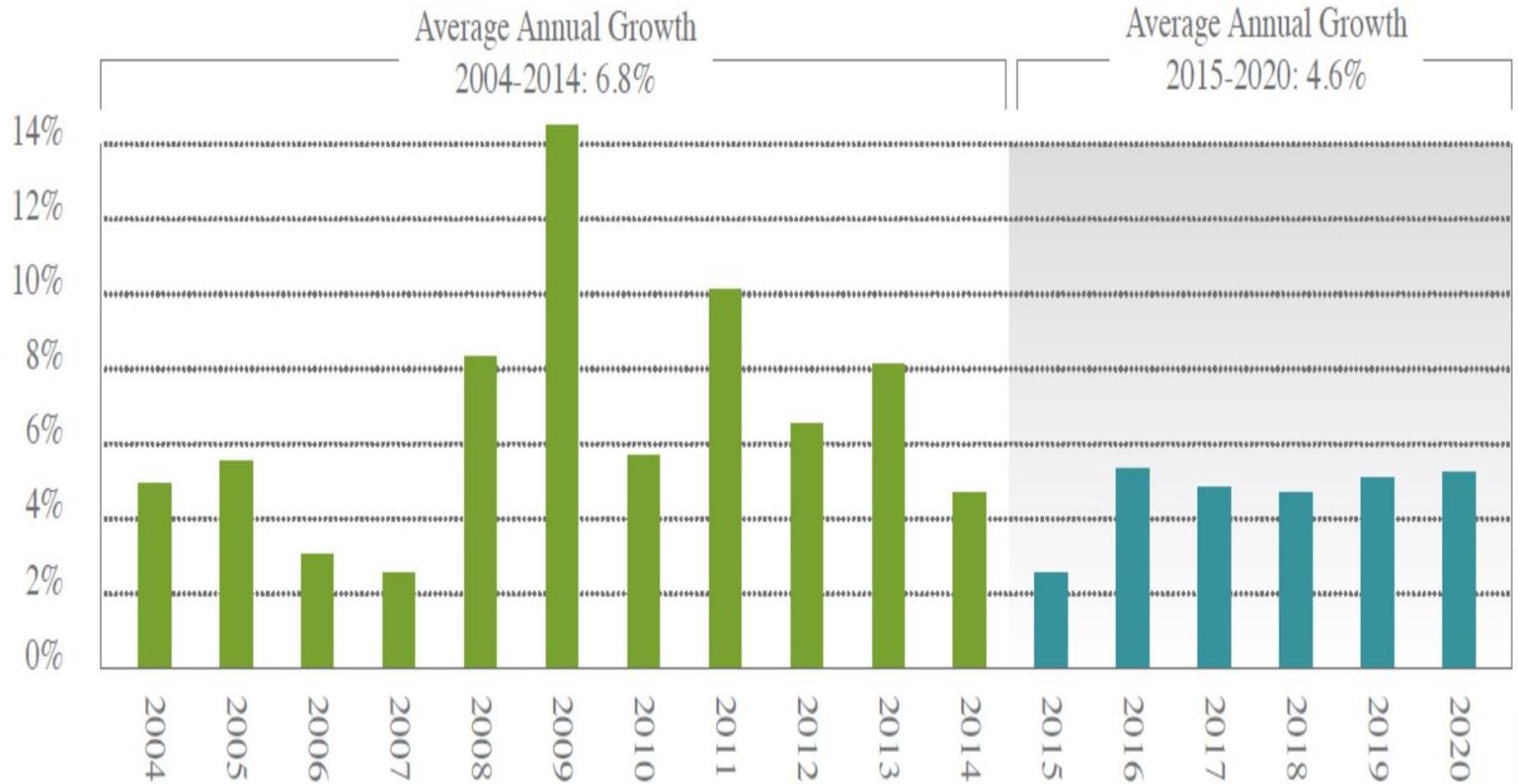


Purpose of this Presentation

Provide a first look at SPU's rate path options for 2018-2023

1. Financial overview reminders and big drivers
2. Unveil the rate path options and main components: baseline; savings; action plans
3. Understand the baseline and financial assumptions
4. Savings overview
5. Action plan overview
6. Options to reduce rates

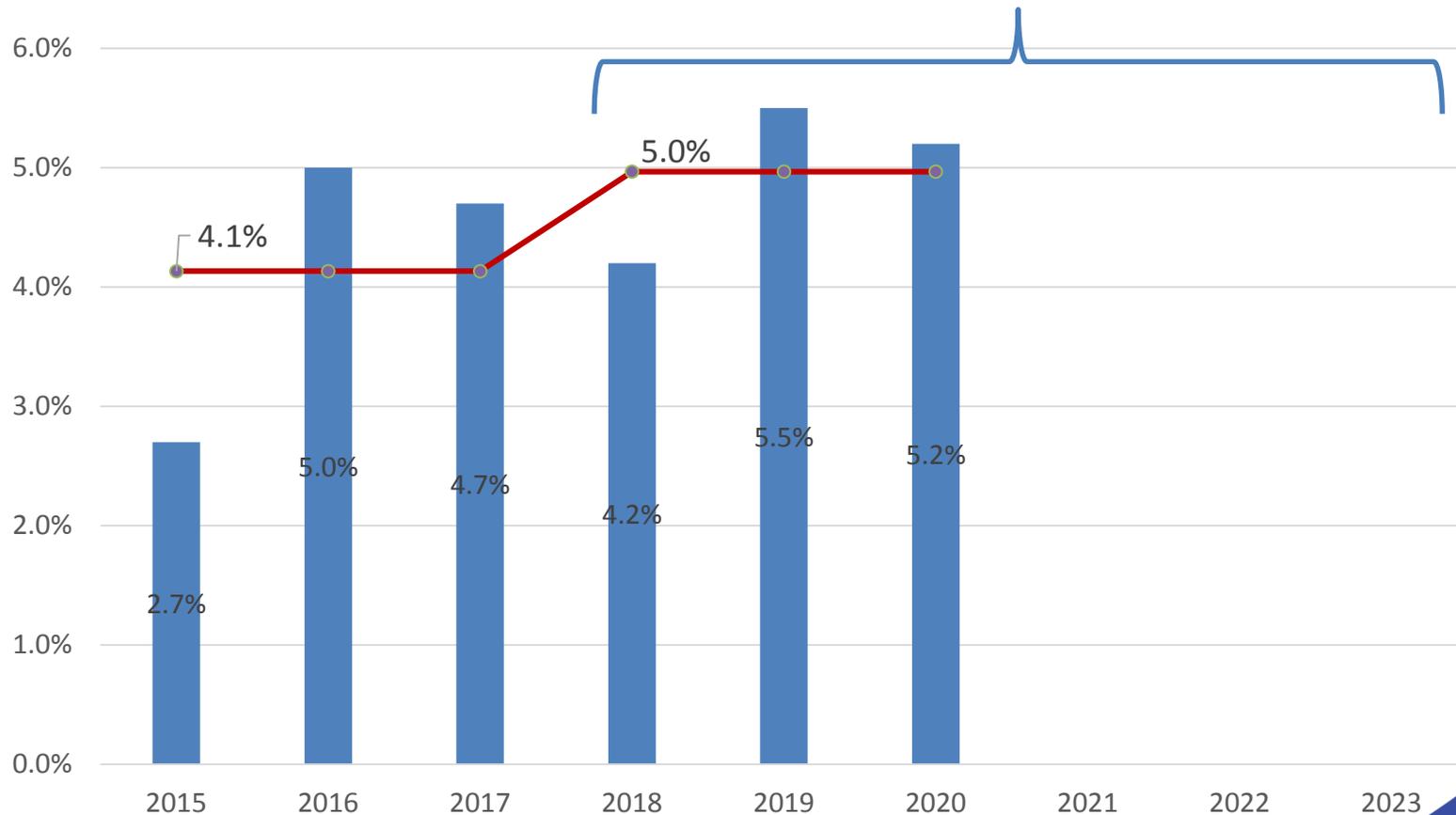
Reminder: Rates Growing at Slower Pace



The Plan is projected to create more predictable, lower rate increases than during the previous 10-year period.

Reminder: Strategic Business Plan Endorsed Rate Path of 4.6% is Back-Loaded

Plan Update: 6-year endorsed rate path TBD



What Happened in 2015-2016?

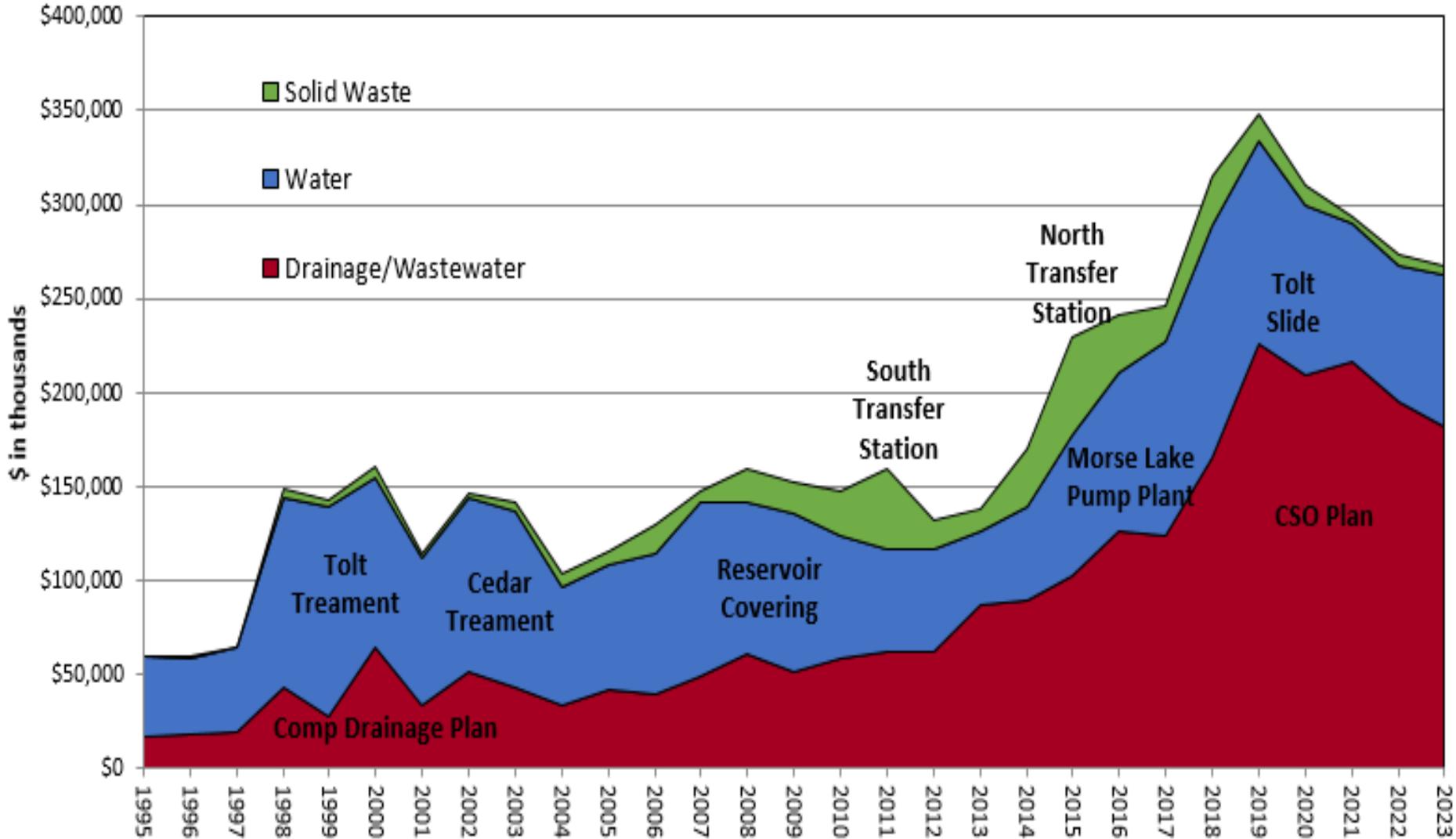
- Lost major drainage customer, the Port of Seattle, resulting in \$4M less in revenue per year.
- Faced new cost pressures, such as:
 - Moved up Ship Canal project to meet regulatory requirement timelines.
 - New requirements for privacy controls and payment card industry changes.
 - Costs to operate our new billing and customer information system were higher than planned.

How Did We Manage to Stay Within Endorsed Rates?

- Deferred capital projects and curbed operations and maintenance spending.
- Higher than planned water revenue due to hot summers.
- Lower than expected interest rates on debt service.
- Secured a few large low-interest-rate loans.

Rate Driver: Infrastructure Investments

Total CIP
(1995-2023)



Rate Driver: Infrastructure Investments



- Regulatory requirements increasing and shifting in from later years.
- Completion of the Facilities Master Plan (2015-2020 action plan) resulted in identification of significant deficiencies that are larger than planned and needed earlier than anticipated.
- Utility work to support transportation projects are large and more concentrated in the first few years.

Rate Driver: Operations and Maintenance Costs (O&M)

- Under-estimated costs of operating the new assets coming on line, especially in drainage and wastewater:
 - Gaining experience with new technologies and real time controls.
- Expanded regulatory requirements.



Rate Driver: Staffing Resources

Position Needs & Savings	2015-2017		
	2015-2020 SBP	Updated	Difference
Needs	67	72	5
Reallocations/Efficiencies	(49)	(33)	16
Budget Adds	18	39	21
Budget Reductions	(5)	0	5
Cumulative Totals	13	39	26

What Was Different than the 2015-2020 Plan?

- Ship Canal (7)
- Customer billing and information system (6)
- Privacy, payment card industry, internal controls, public disclosure (4)
- Clean City program (2)
- Did not realize all planned efficiencies

Purpose of this Presentation

Provide a first look at SPU's rate path options for 2018-2023

1. Financial overview and big drivers
2. Unveil the rate path options and main components :
baseline; savings; action plans
3. Understand the baseline and financial assumptions
4. Savings overview
5. Action Plan overview
6. Options to reduce rates

2018-2023 Rate Path Options and Rate Math

Starting Point (September 2016) 6.8%

- *Scrubbed base & assumptions*
- *Prioritized & removed investments*
- *Expenditure reductions of \$171M*

Current baseline operations 5.2%

Plus action plan investments 0.7%

Minus additional savings (0.3%)

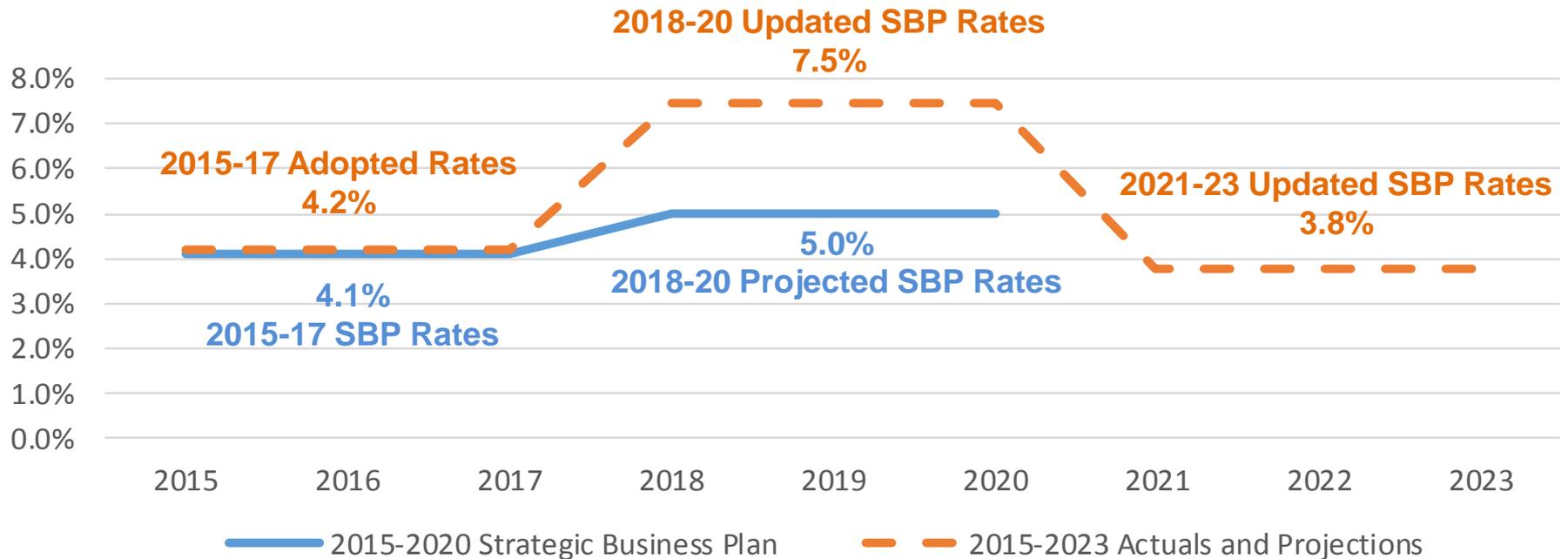
Option A: Average Annual Rate Increase 5.6%

Option B: Medium Risk 5.4%

Option C: Higher Risk 5.3%

Year-by-Year of the 5.6% & Comparison with Last Time

2015-2020 Strategic Business Plan versus
2015-2023 Actuals & Projections



Purpose of this Presentation

Provide a first look at SPU's rate path options for 2018-2023

1. Financial overview and big drivers
2. Unveil the three main rate path components : baseline; savings; action plans
3. Understand the baseline and financial assumptions
4. Savings overview
5. Action Plan overview
6. Options to reduce rates

Baseline Rates Overview

Baseline Definition:

- Baseline rates are the future cost of “*business as usual*.”

Why we calculate a baseline:

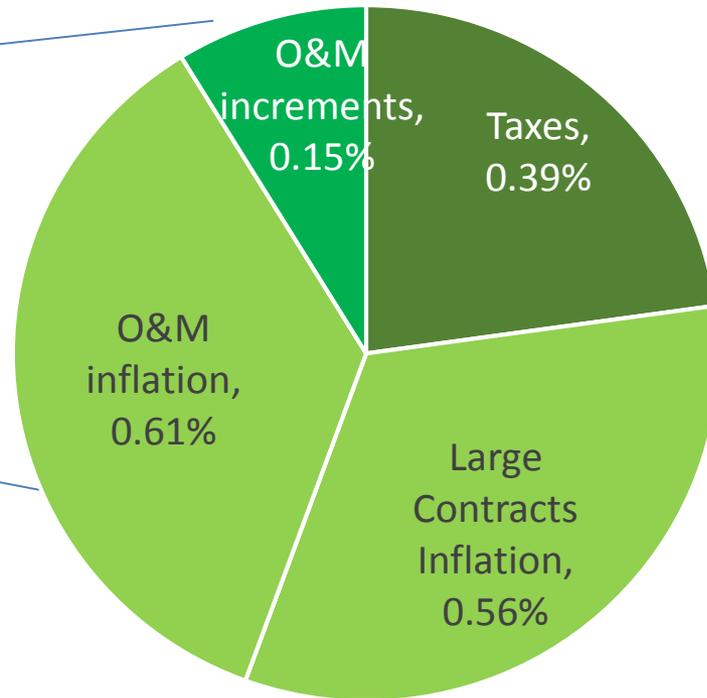
- The baseline is our *starting point* for rate discussions.

Why are baseline rates higher than inflation?

- See the next slide for *components of the baseline rate*

Baseline Rates Overview

Baseline = 5.2%



Components of the 1.70% increase in operations above general inflation

Baseline Rates Overview: 0.15% Operations Increments

\$20M regulations and recycling programs. Examples:

- Duwamish monitoring
- New pet waste and diaper composting program

\$10M Operating new assets. Examples:

- Staffing to operate, monitor and control new assets
- Green storm water infrastructure maintenance



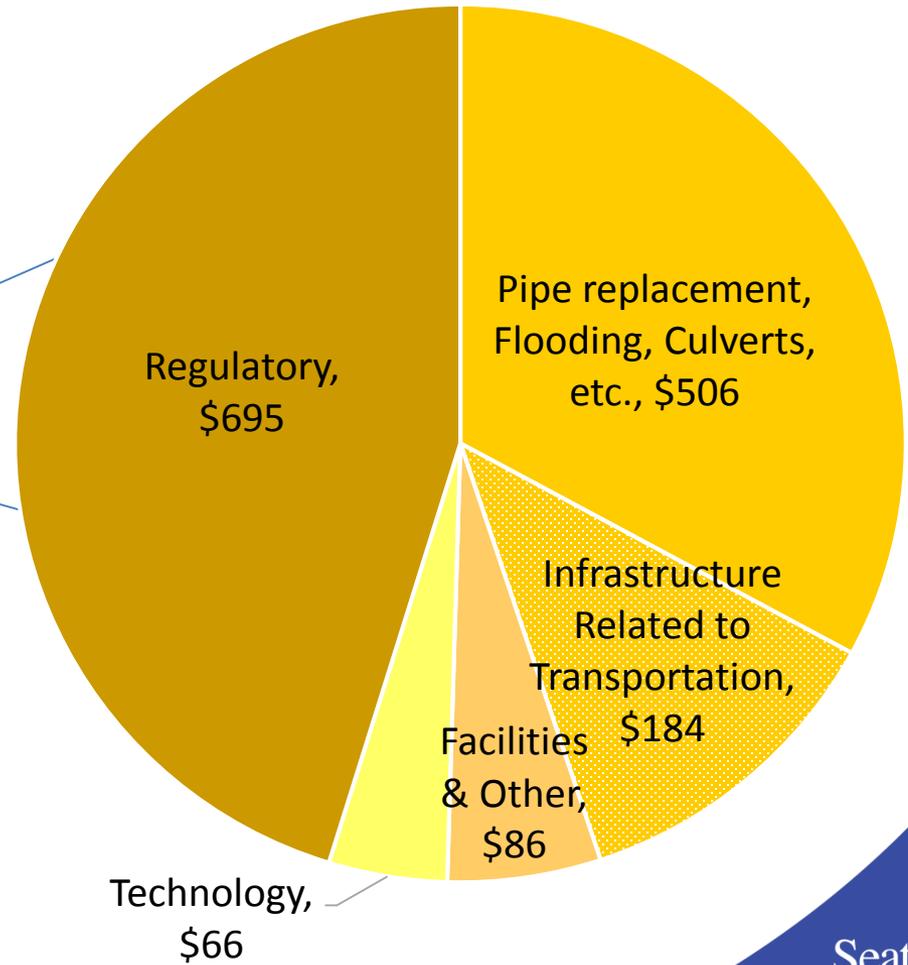
Baseline Rates Overview

Baseline = 5.2%



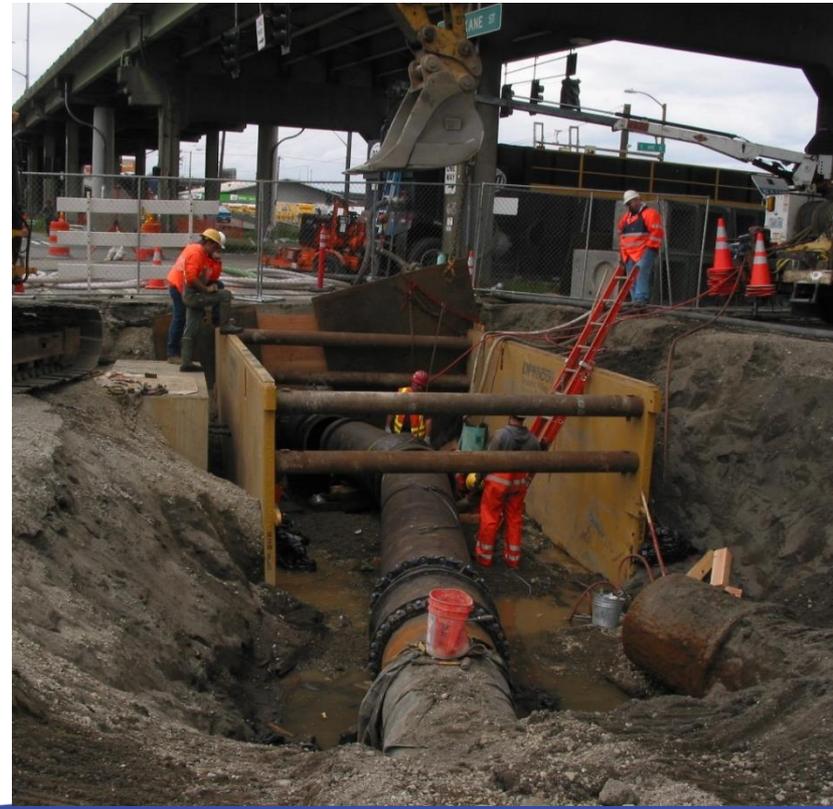
2018-2023 Baseline CIP = \$1.5B

\$s in millions



Baseline Rates Overview: 0.84% Capital Increments

- \$356M shifting the Ship Canal Project in to meet the consent decree.
- \$120M increase in interagency projects



Baseline Rate Path

Baseline Rates							<u>Average</u>
	<u>2018</u>	<u>2019</u>	<u>2020</u>	<u>2021</u>	<u>2022</u>	<u>2023</u>	<u>2018-23</u>
Water	1.6%	5.6%	5.6%	4.0%	5.9%	5.3%	4.7%
Wastewater	1.2%	9.3%	8.3%	4.5%	5.4%	2.5%	5.2%
Drainage	7.9%	14.9%	11.6%	10.8%	2.8%	5.0%	8.8%
Solid Waste	3.1%	3.3%	2.9%	4.2%	4.3%	2.8%	3.4%
Combined	2.8%	7.8%	6.9%	5.5%	4.8%	3.7%	5.2%

Typical Monthly

Residential Bill	<u>2018</u>	<u>2019</u>	<u>2020</u>	<u>2021</u>	<u>2022</u>	<u>2023</u>
Water	41.79	44.14	46.62	48.50	51.37	54.10
Wastewater	56.24	61.47	66.57	69.57	73.32	75.16
Drainage	38.90	44.70	49.87	55.27	56.80	59.65
Solid Waste	48.78	50.46	51.97	54.28	56.70	58.37
Combined	185.71	200.78	215.03	227.62	238.20	247.28
<i>Change</i>	<i>5.65</i>	<i>15.07</i>	<i>14.26</i>	<i>12.59</i>	<i>10.58</i>	<i>9.08</i>

Why is the Rate Path Spiky in 2018-2020?

- Rates are adopted through 2018 in Drainage and Wastewater and set too low.
- SPU is using extra cash to stay within rates in 2018; this is unsustainable for another 6-year period.

Drainage and Wastewater

(\$s in millions)

	2016	2017	2018	2019	2020	2021	2022	2023
Expense	\$367	\$392	\$440	\$492	\$542	\$548	\$572	\$594
Revenue	\$372	\$396	\$408	\$469	\$537	\$551	\$572	\$597
Shortfall	\$5	\$4	(\$32)	(\$22)	(\$6)	\$3	\$0	\$3
Wastewater	3.6%	5.4%	1.2%	9.3%	8.3%	4.5%	5.4%	2.5%
Drainage	9.9%	10.9%	7.9%	14.9%	11.6%	10.8%	2.8%	5.0%

NOTE: Negatives = use of cash

What Would It Take to Get to a 4.6% Baseline?

An estimated \$228M expenditure reductions in 2018-2023 across all lines of business:

- \$71M capital reductions or deferrals.
- \$157M operations and maintenance reductions – equivalent to about 200 positions.
 - Only 27% of all O&M is not fixed(Ex. contracts & taxes)
 - 67% of the non-fixed spending is labor.



Next Time on Baseline Rates

- Detailed review of operations increments
- Detailed review of capital expenditures
- Detailed review of financial policies

Purpose of this Presentation

Provide a first look at SPU's rate path options for 2018-2023

1. Financial overview and big drivers
2. Unveil the three main rate path components : baseline; savings; action plans
3. Understand the baseline and financial assumptions
4. Savings overview
5. Action Plan overview
6. Options to reduce rates

Savings Overview

\$105 million in additional savings between 2018-2023:

- \$82M in capital projects and programs:
 - Shifting out some investments in culverts, pump stations, localized flooding, and reservoirs; and
 - Permanent decrease in the Tolt Slide project due to finding a significantly less expensive solution.
- \$23M in operations and maintenance that support various initiatives but with little programmatic impact.

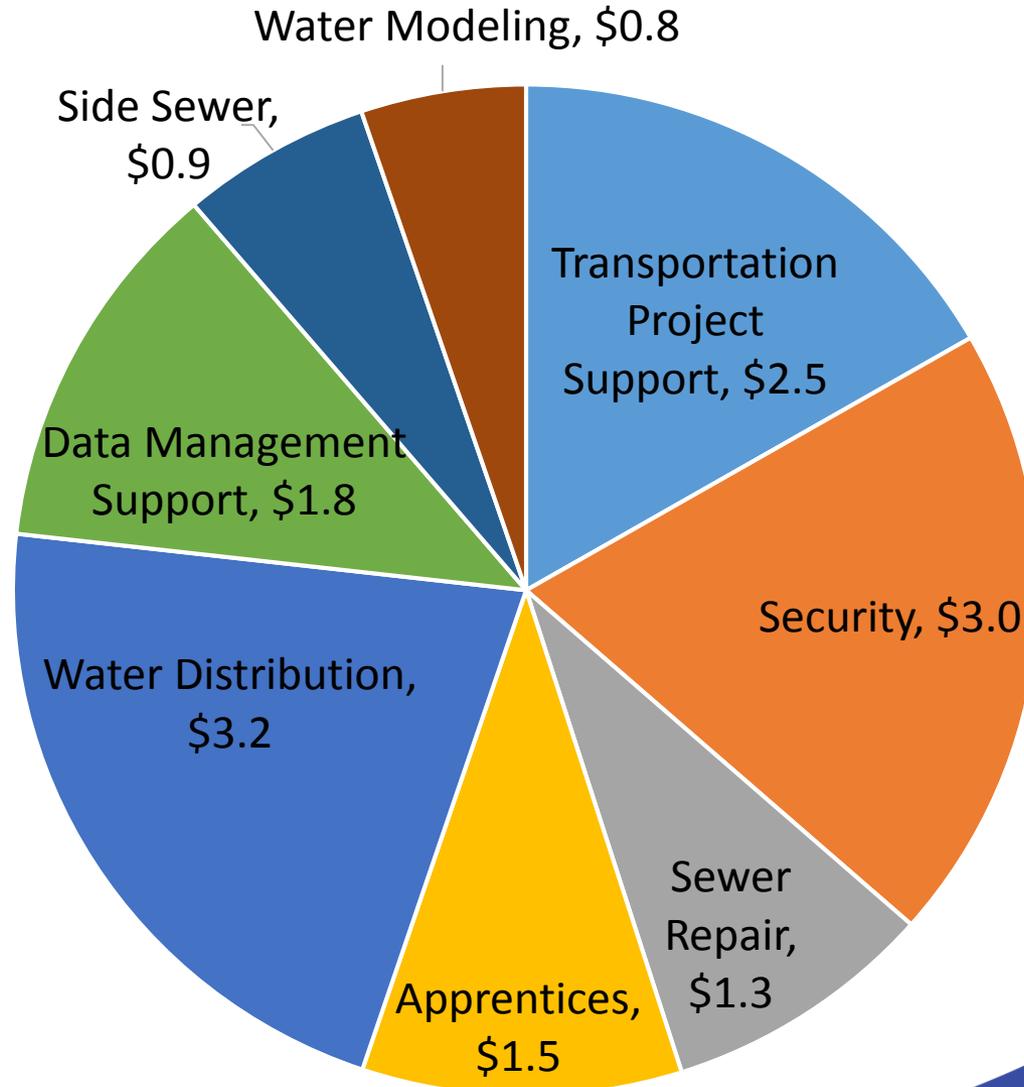
Purpose of this Presentation

Provide a first look at SPU's rate path options for 2018-2023

1. Financial overview and big drivers
2. Unveil the three main rate path components : baseline; savings; action plans
3. Understand the baseline and financial assumptions
4. Savings overview
5. Action Plan overview
6. Options to reduce rates

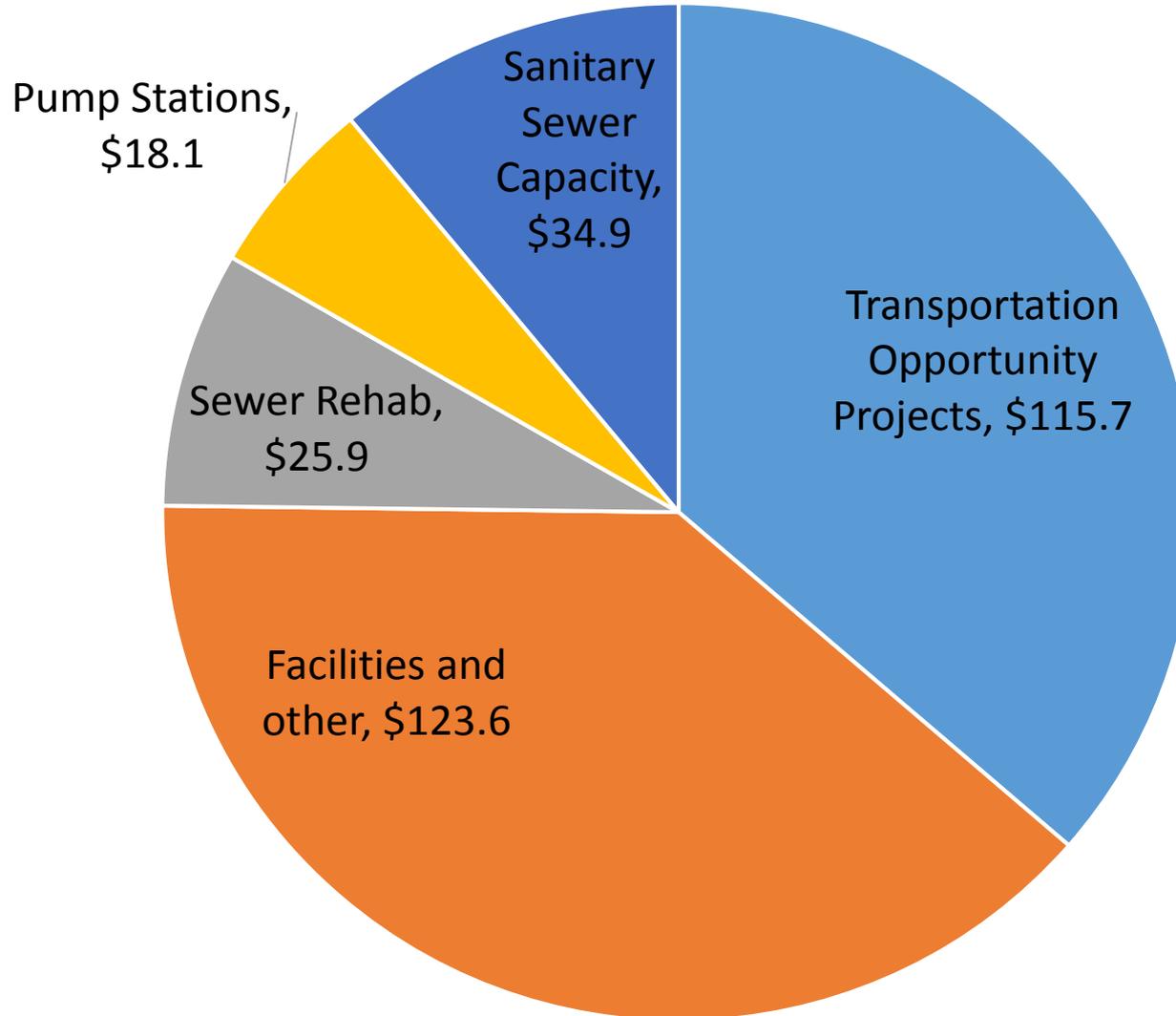
Highlights of Action Plans: Operations & Maintenance

6-year action plan operating costs = \$15M or about \$3M annually



Highlights of Action Plans: Capital

6-year action plan capital project costs = \$318M



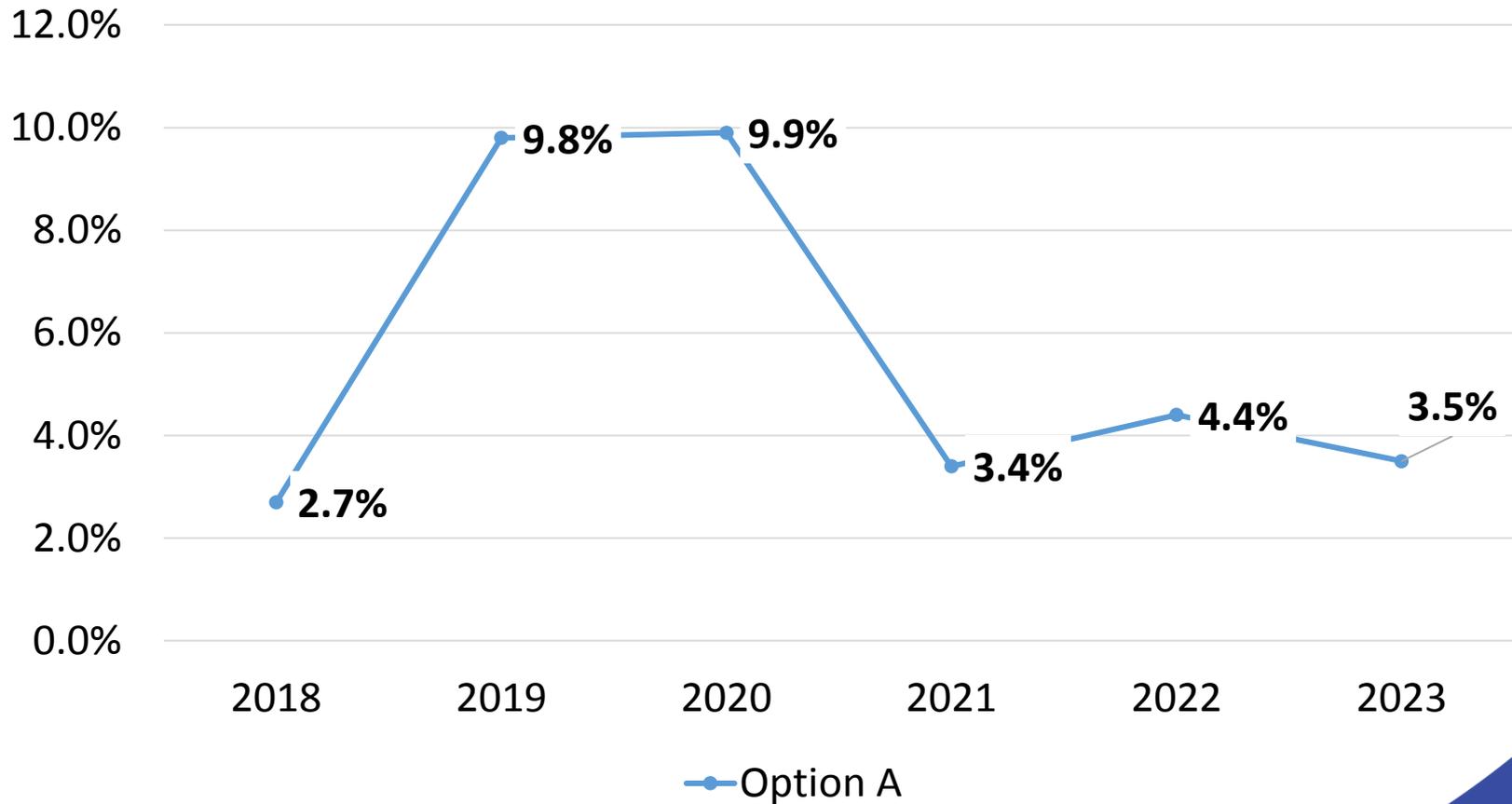
Next Time on Action Plans

Detailed information on each Action Plan:

- What outcome will this action achieve?
- What problem does it solve?
- What are the costs and benefits?
- Description of activities already in the baseline.
- Implementation plan, budget and timeline.
- Alternatives considered.
- Possible race and social justice implications.
- Plan to evaluate success or progress of this action.

Option A Rate Path: Baseline – Savings + Action Plans

Option A: Six-Year Annual Average = 5.6%



Option A Rate Path: Baseline – Savings + Action Plans

Option A Rates	<u>2018</u>	<u>2019</u>	<u>2020</u>	<u>2021</u>	<u>2022</u>	<u>2023</u>	<u>Average</u> <u>2018-23</u>
Water	1.4%	5.9%	5.8%	5.7%	5.8%	5.6%	5.0%
Wastewater	1.2%	14.6%	14.8%	1.2%	3.3%	1.6%	5.9%
Drainage	7.9%	15.7%	15.0%	4.2%	5.1%	5.3%	8.8%
Solid Waste	3.1%	3.3%	2.9%	4.2%	4.3%	2.8%	3.4%
Combined	2.7%	9.8%	9.9%	3.4%	4.4%	3.5%	5.6%

Monthly Typical

Residential Bills	<u>2018</u>	<u>2019</u>	<u>2020</u>	<u>2021</u>	<u>2022</u>	<u>2023</u>
Water	41.70	44.17	46.74	49.42	52.27	55.21
Wastewater	56.24	64.45	73.99	74.88	77.35	78.59
Drainage	38.90	45.00	51.76	53.94	56.67	59.66
Solid Waste	48.78	50.46	51.97	54.28	56.70	58.37
Combined	185.62	204.08	224.46	232.51	242.99	251.82
	5.56	18.46	20.38	8.05	10.47	8.84

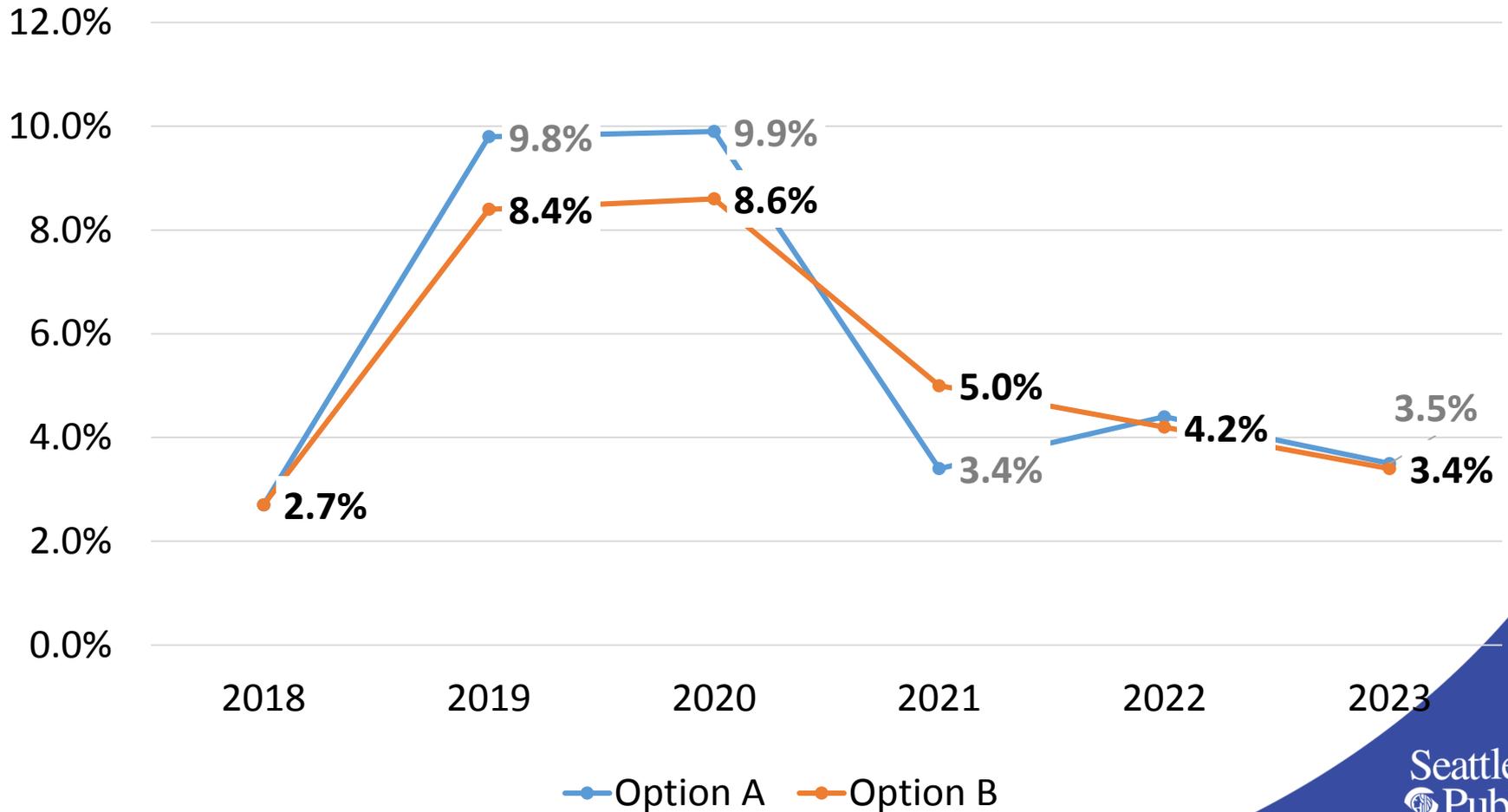
Purpose of this Presentation

Provide a first look at SPU's rate path for 2018-2023

1. Financial overview and big drivers
2. Unveil the three main rate path components : baseline; savings; action plans
3. Understand the baseline and financial assumptions
4. Savings overview
5. Action Plan overview
6. Options to reduce rates

Option B Rate Path: Medium Risk

Option B: Six-Year Annual Average = 5.4%



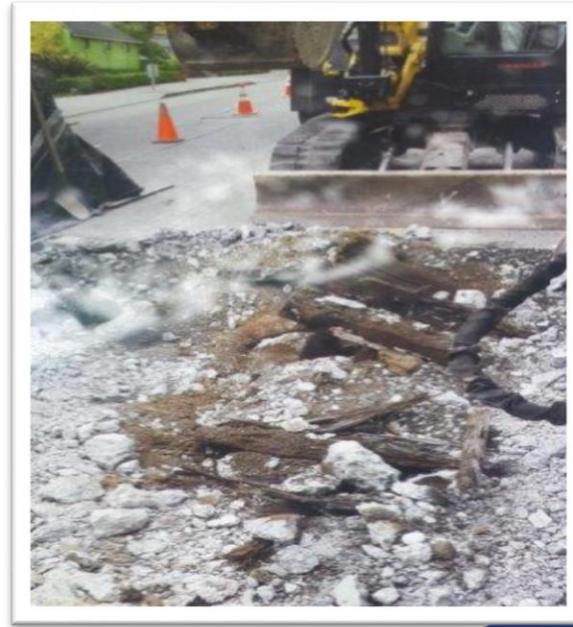
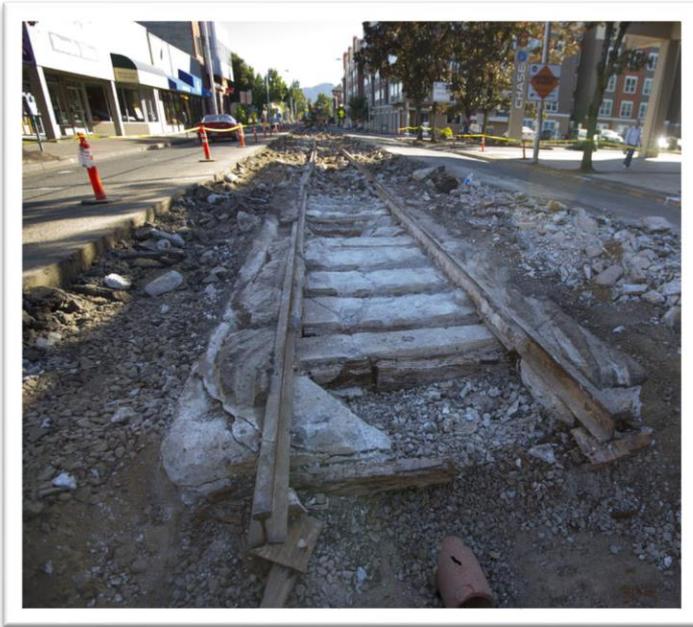
Option B Rate Path: Medium Risk

- Meet environmental objectives by evaluating the 70% recycling goal to determine if an alternative approach might be similarly effective.
- Reduction in culvert program, delaying projects.
- Decrease investment in rodent control.



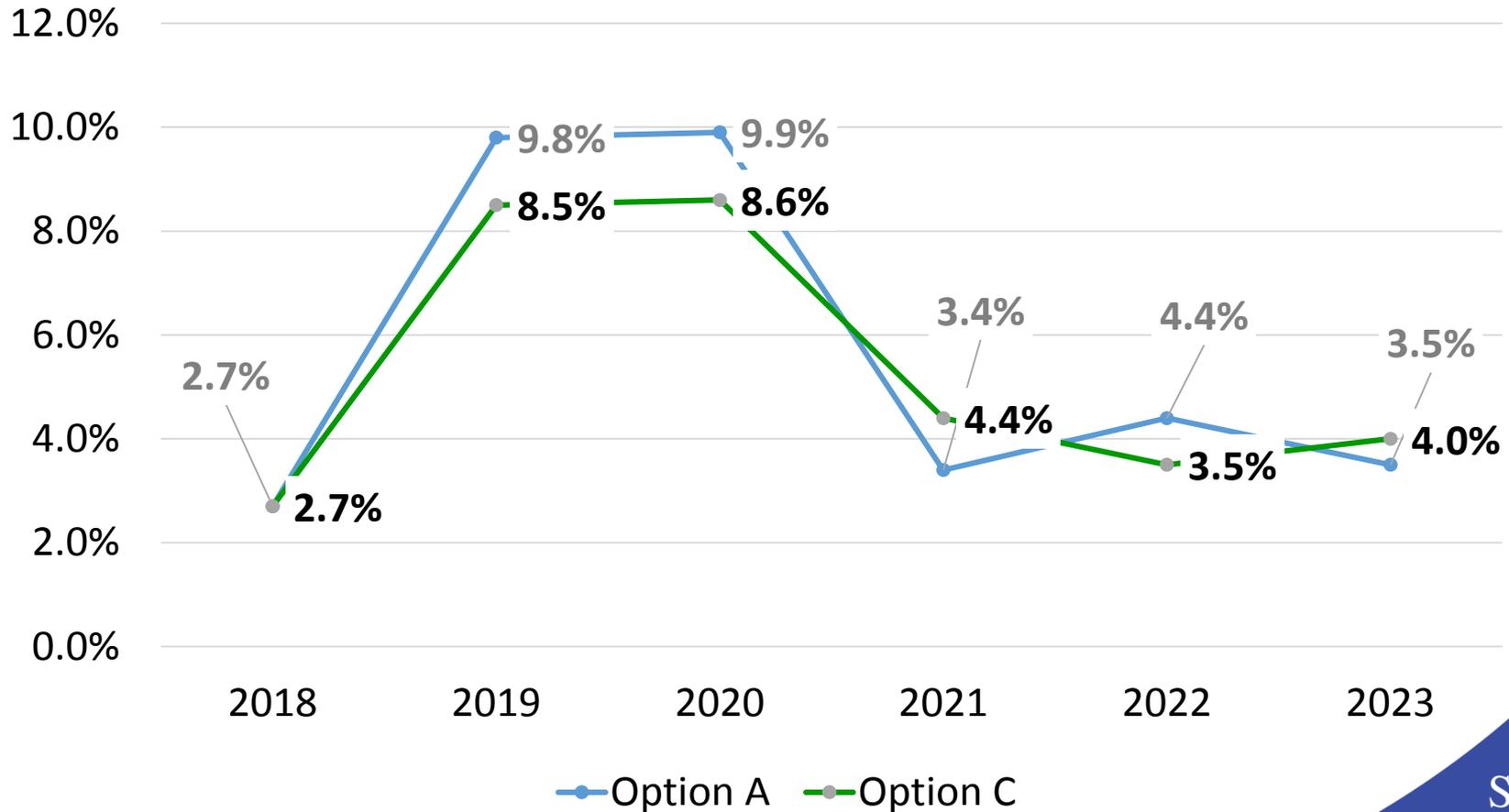
Option B Rate Path : Medium Risk

- Eliminate Move Seattle opportunity projects for Drainage and Wastewater.
- Remove a placeholder for storm water regulatory compliance.



Option C Rate Path: Higher Risk

Option C: Six-Year Annual Average = 5.3%



Option C Rate Path: Higher Risk

- Decrease the level of sewer cleaning.
- Eliminate SPU's contribution to Green Seattle Partnership.
- Reduce the level of risk reserves.
- Continue billing in advance for Solid Waste bills.



Option C Rate Path: Higher Risk

- Decrease investment in sanitary sewer capacity.
- Reduce Move Seattle opportunity projects for Water.
- Assume lower Solid Waste contract inflation.



Next Time on Rate Path Options:

Detailed information on each reduction, including:

- Description of the cost reduction
- Impacts or risks of cost reduction
- Ways to mitigate these risks
- Possible race and social justice implications

Next:

- January 31st
 - Answer questions from this session
 - Baseline details
 - Financial policy details
- February 22nd
 - Action Plan details
 - If time permits, details on reduction options, otherwise in March

QUESTIONS?

