Public Power Benefit Program
Financial Criteria Review
March 30, 2020

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CHELAN COUNTY

Why We're Here

1. Action item from the 2020-2024 Strategic Plan:

   Public Power Benefit Program
   - Program will be retained so long as financial resources are in place to support the effort
   - Financial criteria will be modified to provide for continuation of the Program should the PUD reenter the capital borrowing market

2. Discuss recommendation for updated financial criteria

No Action Required Today

Existing Financial Criteria

Three-step process:

1. Look back to the prior year audited financial results and calculate the amount that actual results exceeded what was needed to meet our financial targets (like debt coverage and liquidity targets) and multiply that number by 10%
2. Look forward to the projected liquidity balances for the next 5 years and calculate the amount that the lowest individual year balance exceeds the liquidity target and multiply that number by 10%
3. Choose the lower amount between step 1 and step 2. This is the calculated amount. The calculated amount provides guidance to the Board who makes the final decision.

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What Has Changed

- District has had financially very successful years
- District has achieved and gone below its debt target borrowing
  - In the future is no longer threat to key strategic goal
- Strategic Plan identifies new Public Power Benefit items
  - Dryden Wastewater, Fiber Acceleration, Wenatchee River Access, Discovery Center, solicitations for new projects
- We raised rates to protect against low revenue scenario and will be storing those revenues

What Has Not Changed

- High priority to invest in assets
- Maintaining debt ratio
  - PPB dollars should not threaten these two objectives

Recommended Criteria Guidelines

1. Look backwards to bottom line – consider revenue already earned
2. Look forward – consider forecasted capability to meet all District financial metrics
3. Establish a preliminary funding level that is included in the 5-year forecasts
4. Adjust annual forecast based on prior year actual financial performance

Recommended Financial Criteria

First: Establish preliminary amount to include in 5-year forecast

1. Look back to the prior strategic planning audited financial results
   a. Looking backward creates focus on actual results rather than a forecast
   b. Using 10% reflects that strategic plan priority was reducing debt and investing in assets
   c. Look back at the 5-year bottom line, divide by 5, and multiply that number by 10% - roughly equal to $10 million annually

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Recommended Financial Criteria

2. Look forward to the projected results for the next 5 years
   a. Creates focus on assuring PPB spending does not threaten financial metrics
   b. The two most important financial metrics in this strategic planning period will be debt service coverage ratio and debt ratio
   c. Debt service coverage ratio has an expected value target for a AA-rated entity (2.0x) and a bond covenant floor (1.25x). This proposal suggests the expected value forecast not drop below the AA-rated benchmark and that 10% of the difference between the low-revenue scenario forecast and the floor be used as PPB guidance
   d. Having achieved the debt ratio, this proposal suggests tracking whether the trend is either continuing debt reduction or neutral impact. An upward trend in debt could be cause for concern about PPB spending. (depending upon risk of exceeding 35%)
   e. Using the forecasted results, calculate the 1.25x debt cover requirements under low-revenue conditions for the next 5 years, calculate the amount that each individual year exceeds the 1.25x target and multiply those numbers by 10%.
   f. Compare the 10% annual amounts against the expected value 2.0x cover target and do not exceed 50% for any year given the nature of forecasted results. Forward looking would justify a modest increase without risking financial metrics in expected scenarios

Recommended Financial Criteria

3. Set the 5-year amount based on consideration of the analysis
4. Refresh the analysis annually in Spring to determine whether to modify the following year's PPB budget (e.g. review in Spring 2020 to set 2021 budget)

2020 Example

Step 1: Backward looking:

	FY15	FY16	FY17	FY18	FY19	Total
5-yr Bottom Line	$102M	$95M	$105M	$105M	$114M	$521M
Divide by 5 (annual average)						$104M
Multiply by 10% (10% of annual average)						$10.4M

Step 2: Forward looking:

	FY20	FY21	FY22	FY23	FY24
Projected debt ratio (trend is acceptable)	27%	24%	23%	23%	21%
Debt cover (10% X Low revenue surplus above 1.25x bond covenant)	$6.3M	$4.8M	$5.0M	$4.5M	$3.4M
Not to exceed 50% of surplus above 2.0 debt cover target for AA Rating	$13.7M	$7.9M	$10.2M	$12.4M	$13.2M
Resulting range based on forecast	$6.3M	$4.8M	$5.0M	$4.5M	$3.4M

Calculated range for consideration: $3.4M - $10.4M

Recommended Criteria

- Backward looking
- Forward looking
- Establish 5-year forecast in 2020
- Set 2021 PPB budget this spring
- This creates minimal risk to District financial metrics and assures adequate funds to maintain existing PPB programs and cover costs of new commitments in Strategic Plan

Summary

1. Protects against negative financial scenarios by funding from revenue already earned and available after financial metrics are met
2. Enables funding when forecasts include routine borrowing in the 5-year planning cycle
3. Ensures preservation of ability to borrow and meet debt service requirements over the long term in alignment with District financial metrics
4. Establishes a preliminary funding level that is included in the 5-year forecasts, then calculate an annual adjustment (up or down)

Discussion

Next Steps

March 30 – April 12	• Board questions and feedback
April 13	• Resolution requesting Board approval

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