



**King County**

**Metropolitan King County Council  
Budget and Fiscal Management Committee**

**AGENDA ITEM** 8 **DATE:** June 8, 2010  
**PROPOSED No.:** 2010-0262 **PREPARED BY:** Amy Tsai

*Proposed Ordinance 2010-0262 advances the Council's priority of Financial Stewardship and its goal to exercise sound financial management in adopting a balanced budget that reflects the values of King County residents and builds the county's fiscal strength.*

**STAFF REPORT**

**SUBJECT:** AN ORDINANCE setting the sewer rate and capacity charge for 2011.

**SUMMARY:** This proposed ordinance would:

- Set the 2011 **monthly sewer rate at \$35.15** per residential customer equivalent (RCE) per month, which is a 10.2 percent or \$3.25 increase over the 2010 rate of \$31.90;
- Set the **monthly capacity charge** for new connections to the regional system occurring in 2011 **at \$50.45**, which is a 2.8 percent or \$1.38 increase over the 2010 rate of \$49.07.

This staff report presents the Executive's and additional rate scenarios that vary in whether they are a rate for one year or two years, the type of bond financing, and how the rate stabilization fund is used. Further analysis of the components of the rate did not reveal any areas where additional cuts can be made.

At the May 18 briefing, Councilmembers asked about the extent of deferred maintenance on projects, impact on water quality programs, and the possibility of a 30-year capacity charge. These issues are not expected to impact rate considerations at this time for reasons discussed in this report.

King County's sewer rates are set for the following year by June 30 of each year. Therefore the Council must adopt a rate by June 14 unless it declares an emergency.

*Errata: The WLRD reduction is \$1.5M, not \$1.2M as previously reported. This does not change the rate because the Executive's computations assumed \$1.5M. The WTD to WLRD transfer portion of the rate increases by \$0.03 to \$0.18 and "Central Rate Adjustments/Other" decreases by \$0.03 from \$0.41 to \$0.38.*

**BACKGROUND:**

On May 18, 2010, the Budget and Fiscal Management Committee heard a staff report on this item and received testimony from Scott Thomasson, chair of the Metropolitan Water Pollution Abatement Advisory Committee (MWPAAC) (see also Attachment 5, letter from MWPAAC to Council dated April 28, 2010 discussed at May 18 BFM meeting). Also in attendance answering questions were Wastewater Treatment Division staff and the county's bond advisor, Rob Shelley.

This staff report summarizes the May 18 staff report (see Attachment 6 for entire May 18 staff report). This report then answers questions which were posed by Councilmembers at the May 18 BFM meeting, and analyzes sewer rate options.

**Wastewater Services Contracts**

King County provides wastewater services for 34 municipalities or sewer districts in King County, southern Snohomish County and the northern tip of Pierce County. There are two charges to customers, a monthly sewer fee and a capacity charge for new connections to the system.

The contracts specify that the sewer rate be in place by June 30 of each year. **For a non-emergency ordinance, after Council approval, the Executive would need to sign by June 18 (the 20<sup>th</sup> is a Sunday) to meet this deadline. Therefore the Council would need to adopt the rate by its June 14 meeting.**

**Monthly Sewer Rate**

The monthly sewer rate goes towards all WTD expenses, including operating costs, debt service, and capital expenses. For the monthly sewer rate, cities and special districts are charged based on Residential Customer Equivalent (RCE) units. One RCE represents the average amount of wastewater a single family residence generates in a month. Each residential unit is charged one RCE; commercial businesses are charged based on usage. Cities and special districts that contract with King County then charge their customers based on water usage (assuming a like amount is discharged to sewers) or one RCE per unit. Cities and special districts bill also for local district costs to maintain and/or expand their local system of collection, in addition to the regional charge for wastewater treatment and conveyance. An average single household would be charged \$35.15 per month for regional services in 2011 under the Executive's proposal (see bolded line in Table 1 below).

**Table 1. Sewer Rates (1996-2010 Actual; 2011-2016 Projected)**

<b>Year</b>	<b>Rate (\$/Mo/RCE)</b>	<b>% Increase</b>
1996 - 1999	\$19.10	
2000	19.50	2.1%
2001	19.75	1.3%

2002 - 2004	23.40	18.5%
2005 - 2006	25.60	9.4%
2007 - 2008	27.95	9.2%
2009 - 2010	31.90	14.1%
<b>2011</b>	<b>35.15</b>	<b>10.2%</b>
2012	38.25	8.8%
2013	39.10	2.2%
2014	39.90	-2.0%
2015	42.52	6.6%
2016	42.81	0.7%

### Capacity Charge

New connections to the regional wastewater system are assessed a capacity charge. The capacity charge helps pay for capital improvements required to provide capacity for these new customers. This is in accordance with the adopted policy of "growth pays for growth" (K.C.C. 28.86.160 FP-15 and Ordinance 14219).

The Executive's proposal includes raising the monthly capacity charge to \$50.45 per month (see bolded line in Table 2 below). The charge is billed directly to the owner of the property after the sewer connection is made (unlike an 'impact fee' that is charged at the time of permit application.) Customers are provided the opportunity to pay their capacity charge in full or over fifteen years. The capacity charge as proposed for 2011 at \$50.45 would amount to \$9,081 if paid monthly for the full term of 15 years. An up-front payment, discounted at 5.5% compounded over the 15 years, would amount to \$6,241.

**Table 2. Capacity Charge (1996 – 2010 Actual; 2011-2016 Projected)**

Year	Rate (\$/Mo/RCE)	% Increase
1996 - 1997	\$7.00	
1998 - 2001	10.50	50.0%
2002	17.20	63.8%
2003	17.60	2.3%
2004	18.00	2.3%
2005 - 2006	34.05	89.2%
2007	42.00	23.3%
2008	46.25	10.1%
2009	47.64	3.0%
2010	49.07	3.0%
<b>2011</b>	<b>50.45</b>	<b>2.8%</b>
2012	51.96	3.0%
2013	53.52	3.0%
2014	55.13	3.0%
2015	56.78	3.0%
2016	58.49	3.0%

The capacity charge is based on 30-year projections and the projections are updated every three years. The projections were updated this year, in 2010, for the 2011 proposed capacity charge.

**Budget**

The 2010 Wastewater Treatment Division (WTD) budget is 7.6% of the County's total \$5 billion budget, down from being 9% of the County's \$4.9 billion budget in 2009. The WTD budget is comprised of Operations, Debt Service, and CIP, as shown in Table 3.

**Table 3. 2009-2010 Adopted WTD Budget**

Appropriation Unit	2009 Adopted	2009 % of Total	2010 Adopted	2010 % of Total
WTD Operations	\$102,916,802	23.0%	\$108,872,937	28.7%
WTD Debt Service	177,902,230	39.7%	178,569,346	47.1%
WTD CIP	167,601,619	37.4%	91,993,254	24.2%
Total	\$448,420,651	100.0%	\$379,435,537	100.0%

The revenue forecast for 2010 is \$304 million (see Attachment A to Proposed Ordinance, WTD Financial Plan for the 2011 Proposed Sewer Rate). WTD has a revenue forecast of \$346 million in 2011. Over 95 percent of the total revenue comes from the monthly sewer rate and capacity charge.

***Operating***

The 2011 operating expense projection represents a 4.0% increase compared to 2010. The majority of operating expenses come from wastewater treatment operations (56%). Administration and central charges make up 21%, down from 34% last year, with the remaining operating expenses coming from Water and Land Resources Division transfers (9%), biosolid resource recovery (7%), project planning and delivery (4%), and environmental and community services (3%).

For the Executive's proposed rate, increases in operating expenses come from labor (cost of living allowances 'COLA' and benefits), Brightwater operating costs as the treatment plant comes on-line, and increases in chemical and energy costs (including switching from chlorine to the safer but more expensive hypochlorite at the West Point plant).

Decreases in operating expenses come primarily from a reduction in central charges and reductions in funding to WLRD. Utilization of the rate stabilization reserve also offsets increases in the operating expenses. Staffing levels at WTD have remained the same for a long period of time (from 598.7 FTEs in 2005 to 592.7 FTEs in 2010) which also helps to keep operating expenses down.

## Capital

Capital expenditures peaked in 2008 and 2009. The capital program drives the need for cash flow to be provided through short and long-term debt. Debt in turn drives debt service and has a direct impact on both the monthly rate and the capacity charge.

As the capital need drops in the out-years, so does pressure on the rate. The 0.7% rate increase that is projected for 2016 is indicative of the tapering off that is expected to occur with rate increases through 2020. In addition, the capacity charge amounts projected to be collected from 2015 - 2030 will add to the stability if not reduction of the rate, in comparison to inflation, assuming no additional major projects are added to the capital plan during the 2030 period.

**Table 4. WTD Total CIP (2008-2015) in \$Millions**

<b>Brightwater</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>
2010 Adopted	369.8	447.1	228.6	81.9	25.4			
2011 Update	369.8	357.9	312.8	121.7	10.1			
Difference	0	-89.2	84.3	39.8	-15.3			
<b>Other Capital</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>
2010 Adopted	106.1	107.7	99.4	109.3	102.0	159.1	159.3	159.7
2011 Update	106.1	97.6	81.5	110.9	102.4	140.4	152.9	207.2
Difference	0	-10.1	-17.9	1.5	0.4	-18.7	-6.4	47.5
<b>Total Capital</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>
2010 Adopted	475.9	554.8	327.9	191.2	127.4	159.1	159.3	159.7
2011 Update	475.9	455.5	394.3	232.6	112.5	140.4	152.9	207.2
Difference	0	-99.3	66.4	41.3	-14.9	-18.7	-6.4	47.5

The capital program accomplishment rate refers to the cash flow requirement generated by the capital program. For example, a capital budget of \$100 at an accomplishment rate of 95% means \$95 of cash must be available. During the past five years, the average accomplishment rate for WTD capital programs has been 87 percent. For 2010 through 2016, the projected Brightwater CIP accomplishment rate is 95% each year. Non-Brightwater rates are assumed to be 85% annually.

### **Debt Service Coverage Ratio**

The debt service coverage ratio is basically the amount of money that needs to be available compared to how much debt needs to be paid. The debt service coverage ratio needed for the county's bond covenants is 1.25 for parity bond debt service and 1.15 for total debt service. Maintaining that ratio is one of the primary considerations of the revenue and expenditure balancing decisions. The parity and total debt service coverage ratios are maintained at the appropriate levels (above 1.25 and 1.15, respectively) through 2016 (see Attachment A to Proposed Ordinance, WTD Financial Plan for the 2011 Proposed Sewer Rate).

## **ADDITIONAL ANALYSIS (see previous staff report for original analysis)**

With the slowed economy, the lower number of paying customers has reduced WTD revenue. Decrease in revenue can be offset in a number of ways, including:

1. Reducing projected operating expenses
2. Reviewing and prioritizing all capital projects to determine if any can be delayed
3. Increasing the sewer rate.

As discussed on May 18, the main drivers of the rate increase are 1) the county's long-term debt payments that must be made (i.e., its long-term investment in infrastructure) and 2) the poor economy, which decreases revenue and increases borrowing costs.

Brightwater is part of the long-term debt service costs just like all other wastewater capital projects. These projects generate jobs and have helped the wastewater treatment and conveyance system keep pace with growth that otherwise was originally projected to max out the system, and therefore the region's capacity to add jobs and new housing units, by 2010. Additional costs due to the Brightwater tunnel system delays have only added approximately \$0.07 to the monthly sewer rate.

As discussed on May 18, the operating expenses and capital expenses appear to be as pared down as they can be. The WLRD reduction and deferred capital projects are discussed in greater detail below, in addition to member questions regarding the capacity charge.

### **WLRD Reduction**

The WTD to WLRD transfer funds WTD activities including meeting NPDES wastewater permit and other regulatory requirements, monitoring water potentially affected by sewage treatment outfalls, designing and operating treatment plants or Combined Sewer Outfall (CSO) control facilities, monitoring recycled products such as biosolids, conducting sediment remediation for contaminated soils, and participating in cooperative studies with other governmental and research agencies on issues related to wastewater and the environment.

As mentioned in the introduction, the WLRD reduction as proposed by the Executive is \$1.5M, not \$1.2M. The WTD to WLRD transfer was \$12.62M in 2009. It increased from \$12.68M in 2005 to a high of \$13.75M in 2008. There is also an additional \$3M that is spent on water quality monitoring activities from other sources such as grants and interlocal agreements. The \$1.5M reduction from the transfer is roughly a 10% cut to WLRD water monitoring activities.

It is too early in the budgetary process to know what the cuts would be. DNRP is still conducting its evaluation of the water quality monitoring programs and other services. They have, however, indicated that they are concentrating on opportunities to reduce monitoring by reducing the number of sites that are monitored in a given area and by reducing sampling and data collection where possible. They believe there are

opportunities where they can reduce the frequency and still monitor environmental conditions, such as where data sets have remained unchanged over a long period of time.

In addition, there are currently five vacancies, four of which have been unfilled for a year or more. Not including one position which WLRD deems essential to fill, these positions represent approximately \$350k in salaries and benefits. These are potential savings that would not cost people's jobs or decrease water quality monitoring activities compared to this year. Another possible area to explore could be investment in a volunteer lakes monitoring program, if it does not violate fair labor practices of the County. The county currently manages a program for contract cities that covers 12 urban lakes. Many years ago the state ran a successful volunteer program that was able to monitor 50 lakes around the state with one FTE program manager.

Because specific cuts are not yet determined, there is insufficient data for the Council to evaluate whether more or less can or should be cut from the program and what its effects on water monitoring in the county would be. Therefore, this analysis concludes that the division should be allowed to continue its process of finding efficiencies to meet the Executive's proposed cuts. The Council will see the Executive's budget proposal this fall, and can exercise its appropriation authority at that time to ensure that water quality monitoring efforts continue to meet the county's needs.

### Deferred Capital Projects

WTD staff indicated that WTD has established and follows a 'best practices' maintenance program as part of its recently re-structured Asset Management Program. WTD makes regular investments in infrastructure and has an active inspection program and asset management program to avoid failures that lead to the kinds of massive rate hikes that some other jurisdictions are experiencing across the country. (See, e.g., 'Huge Hikes in Water, Sewer Rates on Tap across USA', 12/27/07 USA Today, and 'Saving U.S. Water and Sewer Systems Would be Costly,' 3/14/10, NY Times).

WTD staff stated that older assets are often inspected more frequently to help ensure that system integrity is maintained and that needed repairs are identified before they become more expensive to complete.

Recent asset management project delays include:

- Fremont Siphon Project (\$67.9M) - Rehabilitate a 98-year-old siphon. Project construction is delayed one year from 2014 to 2015 based on engineering assumptions as to the rate of deterioration of the siphon material and assessment of the current condition of the siphon. Monitoring will continue as the project proceeds through the design phase.
- South Treatment Plant Odor Control Phase III (\$33.1M) – Odor control. Project start has been delayed two years from 2010 to 2012 in order to have more time to explore alternatives. Only one odor control complaint was recorded in 2009,

and WTD is continuing to work with the City of Renton on operational methods to keep odors in check.

- Conveyance Pipeline H2S Corrosion Rehabilitation (\$15M) – Rehabilitate sections of pipeline identified to have suffered moderate to severe corrosion due to the presence of Hydrogen Sulfide. Sections of pipeline with the most severe corrosion are addressed first. Rehabilitation consists of relining the corroded pipelines. This project budget was reduced from \$20M to \$15M and the project start delayed one year from 2011 to 2012. It will result in the need to replace larger amounts of pipe each year.
- South Plant Raw Sewage Pumps, Motors and Drives project (\$9.7M) – Replacement and upgrade of South Plant raw sewage pumps, motors and drives that transport the raw sewage from the influent pipelines to the treatment plant. This project was originally scheduled to start in 2009 and has been delayed to 2012. As a result, existing pumps will require ongoing maintenance and potential rebuild rather than replacement in order to keep them in operation.
- Minor Asset Management Programs (\$1.8M) – Electrical, mechanical, sites/structures and process improvements. These projects were reduced in budget from \$2.8M to \$1.8M for 2010 and 2011. With the budget reduced, WTD will work on a smaller number of the highest priority minor asset management projects. Projects that are not funded will be prioritized as part of the 2012 capital budget request.

WTD's deferred upgrades or replacements on capital projects to adapt to cashflow constraints appears to be reasonable, as they employ best practices, do regular inspections, and work with engineers and project team members in making their deferment decisions.

### **Capacity Charge**

The capacity charge is calculated using methodology laid out in Wastewater Financial Policy 15 (FP-15), K.C.C. 28.86.160. As noted in FP-15, the sewer rates and capacity charges are to be designed to have "growth pay for growth." The Regional Water Quality Committee will be revisiting the methodology behind the capacity charge this year based on recommendations emerging from its chartered Financial Policies Work Group.

It was asked at the May 18 meeting whether the capacity charge might be adjustable via means such as increasing the pay period from the current 15-year billing. The 15-year period is a holdover from state law which used to allow collection over a 15-year period. The state law changed in 2000 and now refers to it as a "monthly" charge. K.C.C. 28.84.050(O)(3) requires that the capacity charge be charged monthly over 15 years with an ability to pay off the total remaining amount discounted at 5.5%. Therefore, increasing the capacity charge pay period (to 20 or more years, for example) would not require a change in state law, but would require a change in county code.



Increasing the pay period would decrease monthly payments but increase the total amount paid (due to interest). For example, allowing customers to pay the capacity charge over 30 years instead of 15 would reduce monthly payments by approximately \$15 but would increase the total paid over the term by approximately \$3,500. Side effects of a longer pay period would be an increase in the sewer rate, and an increase in administrative and collection costs as the number of customers tracked by WTD increased over time.

Presently, WTD is seeing a rise in the number of people choosing to pay their capacity charge in full up front. Customers paying in full can incorporate the amount into their mortgage, which helps the customer by extending the payments out over the life of the mortgage and reaping the benefit of federal tax credits, while giving the county the benefit of having the capacity charge paid off up-front.

### Sewer Rate Alternatives

As mentioned above, there did not appear to be any additional savings in operational or capital costs that could be used to drive down the sewer rate. Therefore, the two main tools at the Council's disposal to adjust the monthly sewer rate are use of the rate stabilization reserve and the choice of bond financing (one year vs. two year, capitalized interest through mid-2012 for 2011 bonds vs. non-capitalized interest for 2011 bonds).

#### **One-Year vs. Two-Year Rate**

King County Code 28.86.160 sets forth the county's financial policies in accordance with the Regional Wastewater Services Plan. Financial Policy 15 specifically states, "**King County should attempt to adopt a multi-year sewer rate to provide stable costs to sewer customers.**" As can be seen at the bottom of Table 1 (p.3), King County has adopted a multi-year rate every year since 2002.

The advantage of a multi-year rate is that it adds stability and predictability by allowing clients to plan, knowing what the rate costs will be for the next two years, which is in accordance with FP-15. The downside of a multi-year rate is that in the first year of a two-year rate it is higher than a one-year rate would be. However, this also has the positive fiscal effect of placing more funds in a reserve as prudent savings.

The advantage of a one-year rate at this time is that in the first year it gives some economic relief to ratepayers in a poor economy, since the rate is less than a two-year rate. In addition, it gives flexibility to adapt to changing costs and trends, since a different rate is adopted in the second year. It should be noted, however, that a two-year rate also has this flexibility, because the two-year rate is a policy decision by the Council to base the first year's rate on a projection that assumes the second year's rate holds steady. The Council adopts the rate each year regardless of whether the model is a one-year or two-year rate.

The other downside of a one-year rate is the flip side of the benefit of a two-year rate that provides stable multi-year rates. That is, with a one-year rate, the rate is guaranteed to rise the second year, assuming the same expenses, inflation and no new or additional sources of revenue. The savings in ratepayers' pockets in the first year result in a bigger hit to the ratepayers' pocket in the second year, which can be equally difficult for ratepayers if the economic downturn continues.

### **Capitalized vs. Noncapitalized Interest**

The use of capitalized interest on bonds that are issued leads to different rate possibilities for one-year and two-year rate scenarios. Capitalized interest is where the county issues a bond where the principal includes an extra amount that is used to make interest payments. The result is more borrowing up front and more debt service paid over the life of the bond, but the benefit is that it frees up cash flow in the beginning, which drives down sewer rates. To put capitalized interest in perspective, for a bond of about \$200 million, capitalized interest would require borrowing \$20 million more upfront, which with interest over time results in a total debt service obligation that is \$25 million greater than a bond without capitalized interest.

Capitalized interest is a commonly used financial tool. RCW 35.58.460 allows the county to use this financing method "during the period of construction...plus six months." The Executive's proposal includes capitalizing interest on 2010 bond sales through mid-2012. Capitalizing interest on 2011 bond sales would be viewed more negatively by the bond rating agencies, as the majority of Brightwater will be complete by then.

King County has a AA+ rating from Standard & Poor's and a Aa2 rating from Moody's (this was not an upgrade to King County's Aa3 rating but was merely a byproduct of Moody's making adjustments to its scales). Although capitalizing interest on 2011 bond sales would be unlikely to result in a downgrade to King County's credit rating, not capitalizing the 2011 bonds would be viewed more favorably by the rating agencies.

### **The Alternatives**

Two-year rates appear to offer more stability and financial predictability than one-year rates, and not capitalizing interest on bonds in 2011 would save the county more money in the long-run and be viewed more favorably by the rating agencies than capitalizing interest on bonds in 2011. Therefore, on balance, a two-year non-capitalized rate scenario is a strong candidate for the Council's consideration. The difference between one-year versus two-year, capitalized for 2011 bonds and non-capitalized for 2011 bonds are presented in the table below.

**Table 5. Alternative Sewer Rate Scenarios**

<b>5. Non-Capitalized in 2011, One-Year Rate (Exec Proposed)</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2010-12 Borrowing</b>
<b>Sewer Rate</b>	\$31.90	\$35.15	\$38.25	\$39.10	\$39.90	\$42.52	\$42.81	\$490M
<b>% Change</b>	0.00%	10.20%	8.80%	2.20%	2.00%	6.60%	0.70%	
<b>\$ Change/Mo</b>	\$ -	\$3.25	\$3.10	\$0.85	\$0.80	\$2.62	\$0.29	
<b>Difference from 2010 adopted</b>	\$0.00	(\$0.91)	(\$1.54)	(\$3.60)	(\$3.32)	(\$1.12)	(\$1.05)	
<b>Rate stabilization (Add)/Use</b>	(\$10.70)	\$2.40	\$8.20	\$16.80	\$18.40	\$0.00	\$0.00	
<b>Non-Capitalized in 2011, Two-Year Rate</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2010-12 Borrowing</b>
<b>Sewer Rate</b>	\$31.90	\$36.10	\$36.10	\$39.98	\$39.98	\$42.54	\$42.82	\$490M
<b>% Change</b>	0.00%	13.20%	0.00%	10.70%	0.00%	6.40%	0.70%	
<b>\$ Change/Mo</b>	\$ -	\$4.20	\$ -	\$3.88	\$ -	\$2.56	\$0.28	
<b>Difference from 2010 adopted</b>	\$0.00	\$0.04	(\$3.69)	(\$2.72)	(\$3.24)	(\$1.10)	(\$1.04)	
<b>Rate stabilization (Add)/Use</b>	(\$10.70)	(\$6.00)	\$25.80	\$9.00	\$17.10	\$0.00	\$0.00	
<b>4. Capitalized in 2011, One-Year Rate</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2010-12 Borrowing</b>
<b>Sewer Rate</b>	\$31.90	\$34.00	\$36.25	\$38.80	\$41.50	\$42.71	\$42.99	\$510
<b>% Change</b>	0.00%	6.60%	6.60%	7.00%	7.00%	2.90%	0.70%	
<b>\$ Change/Mo</b>	\$ -	\$2.10	\$2.25	\$2.55	\$2.70	\$1.21	\$0.28	
<b>Difference from 2010 adopted</b>	\$0.00	(\$2.06)	(\$3.54)	(\$3.90)	(\$1.72)	(\$0.93)	(\$0.87)	
<b>Rate stabilization (Add)/Use</b>	(\$10.70)	(\$1.20)	\$19.20	\$21.00	\$6.80	\$0.00	\$0.00	
<b>6. Capitalized in 2011, Two-Year Rate</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2010-12 Borrowing</b>
<b>Sewer Rate</b>	\$31.90	\$35.70	\$35.70	\$39.90	\$39.90	\$42.71	\$42.99	\$510M
<b>% Change</b>	0.00%	11.90%	0.00%	11.80%	0.00%	7.00%	0.70%	
<b>\$ Change/Mo</b>	\$ -	\$3.80	\$ -	\$4.20	\$ -	\$2.81	\$0.28	
<b>Difference from 2010 adopted</b>	\$0.00	(\$0.36)	(\$4.09)	(\$3.00)	(\$3.52)	(\$0.93)	(\$0.87)	
<b>Rate stabilization (Add)/Use</b>	(\$10.70)	(\$15.40)	\$23.80	\$15.60	\$21.80	\$0.00	\$0.00	

\* For cross-referencing, the number by the scenario is the number used in the Executive's Issue Paper transmitted with the proposed ordinance.

As can be seen in the table above, the non-capitalized two-year rate is less than a dollar more than the Executive's proposal and keeps more in ratepayers' pockets over the two-year period of 2011 through 2012. The non-capitalized two-year rate scenario presented here is \$0.15 less than the Executive's non-capitalized two-year rate

scenario presented in his issue paper, with that difference shifted to 2013-2014. The result is around 10% less banked up-front in the rate reserve, which slightly reduces some cash flow flexibility, but eases the ratepayer burden in 2011 and 2012.

### **REASONABLENESS:**

Proposed Ordinance 2010-0262 would raise sewer rates from \$31.90 to \$35.15 (10.2% increase) and increase the capacity charge from \$49.07 to \$50.45 (2.8% increase). The amendment if it passes would raise sewer rates from \$31.90 to \$36.10 (13.2% increase) and the capacity charge would be the same as proposed.

Both rate models assume non-capitalized interest-only payments through 2013 for bonds issued in 2011, which saves the county money in the long run compared to capitalized bonds. The amendment would hold rates steady through 2012 in keeping with the wastewater financial policies that encourage stable multi-year rates.

Both rate options appear to be a reasonable and prudent policy decision, depending upon whether the Council prefers to adopt a one-year or two-year rate plan.

### **AMENDMENTS:**

Yes, there is a proposed amendment that 1) makes a technical correction to add strikeout formatting and 2) changes the proposed 2011 monthly sewer rate from \$35.15 to \$36.10.

### **INVITED:**

- Bob Burns, Interim Director, Department of Natural Resources and Parks (DNRP)
- Christie True, Director, Wastewater Treatment Division, DNRP
- Tim Aratani, Manager, Finance and Administrative Services, Wastewater Treatment Division, DNRP
- Tom Lienesch, Economist, Wastewater Treatment Division, DNRP
- Dwight Dively, Director, Office of Management and Budget
- Rob Shelley, Bond Advisor

### **ATTACHMENTS:**

1. Amendment 1 to Proposed Ordinance 2010-0262
2. Proposed Ordinance 2010-0262 (with Attachment)
  - A. WTD Financial Plan for the 2011 Proposed Sewer Rate
3. Fiscal Note
4. Executive's Transmittal Letter and Attachments
5. MWPAAC letter to Council, April 28, 2010
6. 2010-0626 Staff Report, May 18, 2010

1

6-8-10

Sponsor: Phillips, Patterson, Gossett

at

Proposed No.: 2010-0262

1 **AMENDMENT TO PROPOSED ORDINANCE 2010-0262, VERSION 1**

2 On page 1, strike line 15, and insert:

3 "council hereby adopts a ~~((2010))~~ 2011 sewer rate of ~~((thirty-one dollars and ninety~~  
4 ~~cents))~~ thirty-six dollars and ten cents"

5 **EFFECT: Changes the 2011 sewer rate from the Executive-proposed \$35.15 to**

6 **\$36.10.**





KING COUNTY

Signature Report

June 8, 2010

Ordinance

Proposed No. 2010-0262.1

Sponsors Patterson

1 AN ORDINANCE determining the monetary requirements  
 2 for the disposal of sewage for the fiscal year beginning  
 3 January 1, 2011, and ending December 31, 2011, setting  
 4 the sewer rate for the fiscal year beginning January 1, 2011,  
 5 and ending December 31, 2011, and approving the amount  
 6 of the sewage treatment capacity charge for 2011, in  
 7 accordance with RCW 35.58.570; and amending Ordinance  
 8 12353, Section 2, as amended, and K.C.C. 4.90.010, and  
 9 Ordinance 11398, Section 1, as amended, and K.C.C.  
 10 28.84.055.

11 BE IT ORDAINED BY THE COUNCIL OF KING COUNTY:

12 SECTION 1. Ordinance 12353, Section 2, as amended, and K.C.C. 4.90.010 are  
 13 each hereby amended to read as follows:

14 A. Having determined the monetary requirements for the disposal of sewage, the  
 15 council hereby adopts a ((2010)) 2011 sewer rate of thirty-five dollars and fifteen cents  
 16 per residential customer equivalent per month. Once a sewer rate ordinance becomes  
 17 effective, the clerk of the council is directed to deliver a copy of that ordinance to each  
 18 agency having an agreement for sewage disposal with King County.

19 B. The King County council approves the application of Statement of Financial  
20 Accounting Standards No. 71 (FAS 71) to treat pollution remediation obligations and the  
21 first year start-up costs after construction on new plants as regulatory assets, and establish  
22 a rate stabilization reserve for the purpose of leveling rates between years.

23 C. As required for FAS 71 application, amounts are to be placed in the rate  
24 stabilization reserve from operating revenues and removed from the calculation of debt  
25 service coverage. The reserve balance shall be an amount at least sufficient to maintain a  
26 level sewer rate between ~~((2009 and 2010))~~ 2011 and 2012, and shall be used solely for  
27 the purposes of: maintaining the level sewer rate in ~~((2010))~~ 2012; and if additional  
28 reserve balance is available, moderating future rate increases beyond ~~((2010))~~ 2012. If  
29 the estimated amount of the reserve, as shown in the financial forecast, Attachment A to  
30 ~~((Ordinance 16554))~~ this ordinance, needs to be reduced to meet debt service coverage  
31 requirements for ~~((2009))~~ 2010, the county executive shall notify the council of the  
32 change by providing an updated financial forecast.

33 D. The executive shall provide monthly cost reports to the council on Brightwater  
34 as outlined in K.C.C. 28.86.165.

35 SECTION 2. Monetary requirements for the disposal of sewage as defined by  
36 contract with the component sewer agencies for the fiscal year beginning January 1,  
37 2011, and ending December 31, 2011. The council hereby determines the monetary  
38 requirements for the disposal of sewage as follows:

39 Administration, operating, maintenance repair and replace (net of other income):  
40 \$62,940,569.

41 Establishment and maintenance of necessary working capital reserves:



42 \$4,646,190.

43 Requirements of revenue bond resolutions (not included in above items and net of  
44 interest income): \$228,939,223.

45 TOTAL: \$296,526,983.

46 SECTION 3. Ordinance 11398, Section 1, as amended, and K.C.C. 28.84.055 are  
47 each hereby amended as follows:

48 A. The amount of the 1994 metropolitan sewage facility capacity charge adopted  
49 by K.C.C. 28.84.050.O. shall be seven dollars per month per residential customer or  
50 residential customer equivalent for fifteen years.

51 B. The amount of the 1995 metropolitan sewage facility capacity charge adopted  
52 by K.C.C. 28.84.050.O. shall be seven dollars per month per residential customer or  
53 residential customer equivalent for fifteen years.

54 C. The sewage treatment capacity charge shall be seven dollars per month per  
55 residential customer or equivalent for fifteen years for sewer connections occurring  
56 between and including January 1, 1996, and December 31, 1996.

57 D. The amount of the sewage treatment capacity charge adopted by K.C.C.  
58 28.84.050.O. shall be seven dollars per month per residential customer or equivalent for  
59 fifteen years for sewer connections occurring between and including January 1, 1997, and  
60 December 31, 1997.

61 E. The amount of the sewage treatment capacity charge adopted by K.C.C.  
62 28.84.050.O. shall be ten dollars and fifty cents per month per residential customer or  
63 equivalent for fifteen years for sewer connections occurring between and including  
64 January 1, 1998, and December 31, 1998.

65 F. The amount of the sewage treatment capacity charge adopted by K.C.C.  
66 28.84.050.O. shall be ten dollars and fifty cents per month per residential customer or  
67 equivalent for fifteen years for sewer connections occurring between and including  
68 January 1, 1999, and December 31, 1999.

69 G. The amount of the sewage treatment capacity charge adopted by K.C.C.  
70 28.84.050.O. shall be ten dollars and fifty cents per month per residential customer or  
71 equivalent for fifteen years for sewer connections occurring between and including  
72 January 1, 2000, and December 31, 2000.

73 H. The amount of the sewage treatment capacity charge adopted by K.C.C.  
74 28.84.050.O. shall be ten dollars and fifty cents per month per residential customer or  
75 equivalent for fifteen years for sewer connections occurring between and including  
76 January 1, 2001, and December 31, 2001.

77 I. The amount of the sewage treatment capacity charge adopted by K.C.C.  
78 28.84.050.O. shall be seventeen dollars and twenty cents per month per residential  
79 customer or equivalent for fifteen years for sewer connections occurring between and  
80 including January 1, 2002, and December 31, 2002.

81 J. The amount of the sewage treatment capacity charge adopted by K.C.C.  
82 28.84.050.O. shall be seventeen dollars and sixty cents per month per residential  
83 customer or equivalent for fifteen years for sewer connections occurring between and  
84 including January 1, 2003, and December 31, 2003.

85 K. The amount of the sewage treatment capacity charge adopted by K.C.C.  
86 28.84.050.O. shall be eighteen dollars per month per residential customer or equivalent

87 for fifteen years for sewer connections occurring between and including January 1, 2004,  
88 and December 31, 2004.

89 L. The amount of the sewage treatment capacity charge adopted by K.C.C.  
90 28.84.050.O. shall be thirty-four dollars and five cents per month per residential customer  
91 or equivalent for fifteen years for sewer connections occurring between and including  
92 January 1, 2005, and December 31, 2005.

93 M. The amount of the sewage treatment capacity charge adopted by K.C.C.  
94 28.84.050.O. shall be thirty-four dollars and five cents per month per residential customer  
95 or equivalent for fifteen years for sewer connections occurring between and including  
96 January 1, 2006, and December 31, 2006.

97 N. The amount of the sewage treatment capacity charge adopted by K.C.C.  
98 28.84.050.O. shall be forty-two dollars per month per residential customer or equivalent  
99 for fifteen years for sewer connections occurring between and including January 1, 2007,  
100 and December 31, 2007.

101 O. The amount of the sewage treatment capacity charge adopted by K.C.C.  
102 28.84.050.O. shall be forty-six dollars and twenty-five cents per month per residential  
103 customer or equivalent for fifteen years for sewer connections occurring between and  
104 including January 1, 2008, and December 31, 2008.

105 P. The amount of the sewage treatment capacity charge adopted by K.C.C.  
106 28.84.050.O. shall be forty-seven dollars and sixty-four cents per month per residential  
107 customer or equivalent for fifteen years for sewer connections occurring between and  
108 including January 1, 2009, and December 31, 2009.

109 Q. The amount of the sewage treatment capacity charge adopted by K.C.C.  
110 28.84.050.O. shall be forty-nine dollars and seven cents per month per residential  
111 customer or equivalent for fifteen years for sewer connections occurring between and  
112 including January 1, 2010, and December 31, 2010.

113 R. The amount of the sewage treatment capacity charge adopted by K.C.C.  
114 28.84.050.O. shall be fifty dollars and forty-five cents per month per residential customer  
115 or equivalent for fifteen years for sewer connections occurring between and including  
116 January 1, 2011, and December 31, 2011.

117 In accordance with adopted policy FP-15.3.d. in the Regional Wastewater  
118 Services Plan, K.C.C. 28.86.160.C., it is the council's intent to base the capacity charge  
119 upon the costs, customer growth and related financial assumptions used in the Regional  
120 Wastewater Services Plan.

121 In accordance with adopted policy FP- 6 in the Regional Wastewater Services  
122 Plan, K.C.C. 28.86.160.C, the council hereby approves the cash balance and reserves as  
123 contained in the attached financial plan for ((2010)) 2011.

124 In accordance with adopted policy FP- 15.3.c., King County shall pursue changes  
125 in state legislation to enable the county to require payment of the capacity charge in a

126 single payment, while preserving the option for new ratepayers to finance the capacity  
127 charge.  
128

KING COUNTY COUNCIL  
KING COUNTY, WASHINGTON

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Robert W. Ferguson, Chair

ATTEST:

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Anne Noris, Clerk of the Council

APPROVED this \_\_\_\_ day of \_\_\_\_\_, \_\_\_\_\_.

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Dow Constantine, County Executive

**Attachments:** A. Water Treatment Division Financial Plan for the 2011 Proposed Sewer Rate



**ATTACHMENT A: Wastewater Treatment Division Financial Plan for the 2011 Proposed Sewer Rate**

	2009 Preliminary	2010 Forecast		2011 Forecast		2012 Forecast		2013 Forecast		2014 Forecast		2015 Forecast		2016 Forecast		
<b>CUSTOMER EQUIVALENTS (RCEs)</b>	703.80	691.48	688.02	691.46	696.65	702.92	709.24	715.63								
MONTHLY RATE	\$31.90	\$31.90	\$35.15	\$38.25	\$39.10	\$39.90	\$42.52	\$42.81								
			10.2%	8.8%	2.2%	2.0%	6.6%	0.7%								
<b>BEGINNING OPERATING FUND</b>	29,587	45,448	56,484	54,516	46,916	30,585	12,672	13,179								
<b>OPERATING REVENUE:</b>																
Customer Charges	271,560	264,698	290,207	317,381	326,867	336,557	361,899	367,608								
Investment Income	5,601	3,146	5,236	6,592	10,540	12,301	13,550	12,885								
Capacity Charge	40,754	38,038	40,171	43,647	48,231	53,315	59,251	65,037								
Rate Stabilization	(10,650)	(10,650)	2,400	8,200	16,800	18,400	-	-								
Other Income	9,869	8,741	8,049	8,193	8,275	8,358	8,608	8,867								
<b>TOTAL OPERATING REVENUES</b>	312,384	303,973	346,063	384,013	410,713	428,930	443,308	454,397								
<b>OPERATING EXPENSE</b>	(102,981)	(106,842)	(111,160)	(117,164)	(121,850)	(126,724)	(131,793)	(137,065)								
	0%	0%	0%	0%	0%	0%	0%	0%								
<b>DEBT SERVICE REQUIREMENT PARITY DEBT</b>	(145,408)	(146,626)	(172,586)	(197,710)	(215,781)	(227,330)	(235,323)	(240,322)								
<b>SUBORDINATE DEBT SERVICE</b>	(12,506)	(16,082)	(19,346)	(23,946)	(26,922)	(29,315)	(29,892)	(29,936)								
<b>DEBT SERVICE COVERAGE RATIO PARITY DEBT</b>	1.44	1.34	1.36	1.35	1.34	1.33	1.32	1.32								
<b>DEBT SERVICE COVERAGE RATIO TOTAL PAYMENTS</b>	1.33	1.15	1.15	1.15	1.15	1.15	1.15	1.15								
<b>KC POOL LOAN REPAYMENT</b>	(21,263)	(20,700)	(20,625)	(20,600)	(20,300)	(20,600)	(20,600)	(20,300)								
<b>LIQUIDITY RESERVE CONTRIBUTION</b>	(461)	(386)	(432)	(600)	(469)	(487)	(507)	(527)								
<b>TRANSFERS TO CAPITAL</b>	(29,766)	(13,337)	(21,914)	(23,994)	(25,391)	(45,074)	(45,794)	(46,547)								
<b>RATE STABILIZATION RESERVE</b>	35,150	45,800	43,400	35,200	18,400	0	0	0								
<b>OPERATING LIQUIDITY RESERVE BALANCE</b>	10,298	10,684	11,116	11,716	12,185	12,672	13,179	13,706								
<b>OPERATING FUND ENDING BALANCE</b>	45,448	56,484	54,516	46,916	30,585	12,672	13,179	13,706								
<b>CONSTRUCTION FUND</b>																
<b>BEGINNING FUND BALANCE</b>	8,794	5,000	11,571	5,727	6,562	6,702	6,147	5,000								
<b>REVENUES:</b>																
Parity Bonds	550,000	250,000	195,448	43,450	87,398	89,659	124,630	77,645								
Variable Debt Bonds	(79,315)	180,397	0	44,213	21,825	1,748	14,617	1,295								
Grants & Loans	20,797	6,640	4,024	707	0	500	500	500								
Other	500	500	500	500	500	500	500	500								
Transfers From Operating Fund	29,766	13,337	21,914	23,994	25,391	45,074	45,794	46,547								
<b>TOTAL REVENUES</b>	521,748	450,874	221,887	112,864	135,114	136,981	185,541	125,986								
<b>CAPITAL EXPENDITURES</b>	(455,453)	(366,478)	(209,848)	(108,036)	(127,490)	(129,962)	(176,099)	(128,427)								
<b>DEBT ISSUANCE COSTS</b>	(9,404)	(5,327)	(3,909)	(1,090)	(1,857)	(1,802)	(2,566)	(1,559)								
<b>BOND RESERVE TRANSACTIONS</b>	(44,076)	(31,671)	13,894	3,660	(5,626)	(5,772)	(8,024)	4,001								
<b>DEBT SERVICE, CAPITALIZED INTEREST RESERVE ADJUSTMENTS</b>	(4,665)	(29,484)	(27,867)	(6,562)	0	0	0	0								
	(11,943)	(11,344)	0	0	0	0	0	0								
<b>ENDING FUND BALANCE</b>	5,000	11,571	5,727	6,562	6,702	6,147	5,000	5,000								
<b>CONSTRUCTION FUND RESERVES</b>																
Bond & Loan Reserves	162,690	194,361	180,467	176,807	182,433	188,205	196,229	192,228								
Policy Reserves	21,000	22,500	22,500	22,500	22,500	22,500	22,500	22,500								
<b>TOTAL FUND RESERVES</b>	183,690	216,861	202,967	199,307	204,933	210,705	218,729	214,728								
<b>CONSTRUCTION FUND BALANCE</b>	188,691	228,432	208,694	205,869	211,635	216,852	223,729	219,729								





## FISCAL NOTE

Ordinance/Motion No. 2010-XXXX  
 Title: 2011 Sewer Rate Monetary Requirements  
 Affected Agency and/or Agencies: Wastewater Treatment Division, Department of Natural Resources and Parks  
 Note Prepared By: Greg Holman  
 Note Reviewed By: Tim Aratani

Impact of the above legislation on the fiscal affairs of King County is estimated to be:

**Revenue to: (000's)**

Fund/Agency	Fund Code	Revenue Source	2010	2011	2012	2013
Water Quality/WTD	4610	Customer Charges		26,833	26,967	27,169
Water Quality/WTD	4610	Capacity Charge		1,323	4,575	4,217
<b>TOTAL</b>	<b>4610</b>		<b>0</b>	<b>28,155</b>	<b>31,542</b>	<b>31,386</b>

**Expenditures:**

Fund/Agency	Fund Code	Department Code	2010	2011	2012	2013
<b>TOTAL</b>			<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>

**Expenditures by Category**

	2010	2011	2012	2013
Salaries & Benefits				
Supplies and Services				
Capital Outlay				
Other				
<b>TOTAL</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>

Assumptions: This legislation increases the sewer rate to \$35.15 for 2011. Fiscal impacts for 2012-13 are based on the \$35.15 rate. The capacity charge would increase from \$49.07 to \$50.45 per residential customer equivalent for 15 years for customers that connect in 2011. Most of the revenue impact is delayed until after 2010 due to a lag in the beginning of the 15 year billing period. Revenues increase sharply in 2012 as a portion of the new customers choose to make a lump sum payoff of their future payments. The capacity charge for customers connecting in previous years remains fixed at rates established for their year of



April 15, 2010

The Honorable Bob Ferguson  
Chair, King County Council  
Room 1200  
COURTHOUSE

Dear Councilmember Ferguson:

I am transmitting a proposal for the consideration of the King County Council to establish a 2011 monthly sewer rate of \$35.15 per residential customer equivalent, which represents an increase of 10.2 percent over the current rate that was adopted by the council in 2008 and 2009. Additionally, I am proposing a monthly capacity charge of \$50.45 for 2011, an increase of 2.8 percent from the current 2010 rate.

This proposal introduces a new level of fiscal discipline that enables me to propose rates that are **significantly lower than our original rate forecast in the 2010 Budget**. This proposal was developed pursuant to the county's adopted financial policies for the wastewater utility and reflects the county's commitment to building and operating facilities that protect public health, support regional environmental goals, and bolster the creation of public and private sector jobs during an economic recovery. It also carefully considers the recommendations of the 34 customer agencies that contract with the county for wastewater treatment services.

The contracts with our component sewer agencies require that King County adopt the 2011 sewer rate by June 30, 2010.

My proposal emphasizes three key objectives:

- 1. Establishing a one-year rate to provide economic relief to ratepayers.** It is only appropriate for our ratepayers to keep their money in their pockets until the Wastewater Treatment Division (WTD) requires the additional revenue. Under my proposal, the monthly sewer rate is approximately \$1.10 less per month in 2011 than it would be as a two-year rate and \$0.91 less per month than projected in the 2010 Budget. This measure keeps approximately \$8.7 million dollars with the ratepayers in 2011.

2. **Emphasis on prudent financing methods that helps protect our bond ratings.** I directed WTD to move toward more conservative financing practices. Previously, it was assumed that interest from the 2011 bond sale would be capitalized as a means of managing rate patterns. While capitalized interest has served as a powerful tool in shaping the profile of rate increases, discontinuing this strategy not only protects the current strong bond ratings, but it also results in lower costs and rates in the long run. Maintaining our credit ratings will help to ensure favorable interest rates when we go to market with new bonds this year. I expect the proposal of \$35.15 for the monthly rate and \$50.45 for the capacity charge will generate the necessary revenue and debt service coverage to preserve the utility's credit ratings of Aa3 by Moody's and AA+ by Standard and Poor's.
  
3. **Reduction of capital and operating expenditures while protecting the public health and environment.** Between 2009 and 2014, WTD has reduced planned capital spending by over \$30 million by reprioritizing project schedules and requesting funding only for projects with a critical need to proceed during this time frame. The division lowered planned operating expenditures by \$5.8 million in 2011 and \$8 million in 2012, achieving these savings in part by operating new facilities in Vashon and Carnation with no net increase in full-time employees (FTEs). The savings will continue when we open Brightwater while maintaining the same number of FTEs we had in 2000. Additional reductions and efficiencies include chemical reductions at the treatment plants; efficiencies in digester cleaning and disposal; implementation of a new technology equipment replacement plan; reduced travel; reduced number of vehicles in WTD's fleet; and decentralizing billing processes for sewer, septage and industrial waste customers. These efforts, in addition to WTD's continued sound financial management, provide for significantly lower rates than those projected in the 2010 Budget.

Under my proposal, WTD will continue to implement its capital program. During the next two years, WTD will complete several major projects including the odor control facilities near Qwest Field and the Bellevue pump station. As spending winds down on these projects, new spending will commence on others, such as the Fremont Siphon repair and improvements to the influent screening equipment at West Point. These and the dozens of other projects now being carried out by the county's clean-water utility inject millions of dollars into the economy each year and support creation of private sector jobs. The infrastructure also supports planned growth and economic development over the long term.

I have proposed the elimination of the Culver program, which receives funding from WTD's operating program. **This change will save approximately \$1.6 million a year**, or about 20 cents on the rate. Finally, I have directed the prudent use of rate stabilization funds and more conservative financing to better manage the sewer rate increases between now and 2016, when rate increases are expected to moderate as the amount of borrowing declines.

The Honorable Bob Ferguson  
April 15, 2010  
Page 3

Another important component of the proposal is that it reflects the valuable input I have received from the Metropolitan Water Pollution Abatement Advisory Committee, which represents the 34 customer agencies that contract with the county for wastewater treatment services. (See enclosure.)

Attached you will find an ordinance as required by King County Code (KCC) 28.86.160, Financial Policy 13, which includes several attachments to provide the council with detailed information to understand our rate setting methodology. A current detailed financial forecast for the wastewater utility for the period 2010-2016 is enclosed. Also included is an issue paper that includes a discussion of critical forecasting parameters, assumptions, and policy options in accordance with Financial Policy 16.

If you have any questions, please feel free to contact Christie True, Division Director of the Wastewater Treatment Division in the Department of Natural Resources and Parks, at 206-684-1236, or at [christie.true@kingcounty.gov](mailto:christie.true@kingcounty.gov).

Thank you for your consideration of this ordinance. I welcome the opportunity to assist you as you deliberate on the 2011 sewer rate and capacity charge.

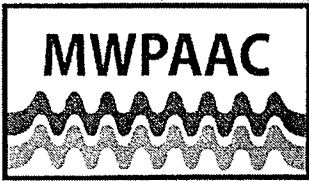
Sincerely,

Dow Constantine  
King County Executive

Enclosures

cc: King County Councilmembers  
    ATTN: Tom Bristow, Chief of Staff  
          Anne Noris, Clerk of the Council  
    Rob Shelley, Financial Advisor, Seattle NW Securities  
    Dwight Dively, Director, Office of Management and Budget  
    Caroline Whalen, County Administrative Officer, Department of Executive  
        Services (DES)  
    Ken Guy, Director, Finance and Business Operations, DES  
    Bob Burns, Interim Director, Department of Natural Resources and Parks (DNRP)  
    Christie True, Division Director, Wastewater Treatment Division, DNRP





## Metropolitan Water Pollution Abatement Advisory Committee

King Street Center, 201 South Jackson Street, MS KSC-NR-0512  
Seattle, WA 98104 206-263-6070

### MEMBERS:

*Alderwood Water and  
Wastewater District*

*City of Algona*

*City of Auburn*

*City of Bellevue*

*City of Black Diamond*

*City of Bothell*

*City of Brier*

*City of Carnation*

*Cedar River Water and Sewer District*

*Coal Creek Utility District*

*Cross Valley Water District*

*Highlands Sewer District*

*City of Issaquah*

*City of Kent*

*City of Kirkland*

*City of Lake Forest Park*

*Lakehaven Utility District*

*City of Mercer Island*

*Midway Sewer District*

*Northeast Sammamish Sewer District*

*Northshore Utility District*

*Olympic View Water and Sewer District*

*City of Pacific*

*City of Redmond*

*City of Renton*

*Ronald Wastewater District*

*Sammamish Plateau Water and  
Sewer District*

*City of Seattle*

*Skyway Water and Sewer District*

*Soos Creek Water and Sewer District*

*Southwest Suburban Sewer District*

*City of Tukwila*

*Val Vue Sewer District*

*Vashon Sewer District*

*Woodinville Water District*

April 9, 2010

The Honorable Dow Constantine  
King County Executive  
401 Fifth Ave., Suite 800  
Seattle, WA 98104

### SUBJECT: **Wastewater Treatment Division 2011 Rate Recommendation**

Dear Executive Constantine:

The Metropolitan Water Pollution Abatement Advisory Committee (MWWPAAC) remains concerned with the trend in wastewater treatment rates. While the funding of the Brightwater Treatment Facility remains the primary cause of rate increases, other financing, funding and cost imposition decisions of the County contribute to the escalating regional wastewater rates. The inevitable prospect of a sewer rate and capacity charge that combined will exceed \$100 for new homes and equivalent businesses in King County is extraordinary by both local and national standards and threatens to further inhibit a slow economic recovery. With this perspective in mind, MWWPAAC and its Finance and Rates Subcommittee have reviewed preliminary rate forecasts and scenarios. Based on this review, MWWPAAC recommends the following regarding rates and finance and specifically for rate strategies for 2011 and beyond:

- 1) **One Year Rate.** MWWPAAC recommends adoption of a one year rate, rather than a multi-year rate or adoption of a series of increases, given uncertainty regarding financing cost and structure, start-up costs at Brightwater, growth rates and patterns, developing trends in cost containment, and related Department efforts to further mitigate upward rate trends. Adopting a one year rate provides the necessary funding to continue essential programs and maintain the utility's fiscal health while providing the flexibility to adapt subsequent increases to changing costs and trends.

- 2) **Rate Stabilization Reserve.** MWPAAC recommends that the projected rate stabilization reserve balance of \$40 million be utilized as intended to mitigate rate increases during the current rate transition period. The purpose of the rate stabilization reserve (RSR) is to mitigate and attenuate near-term rate increases, and the current rate transition is a clear application of this intent. The RSR should be materially exhausted for this purpose during the 2011-2013 rate periods.
- 3) **Structure New Debt to Phase in Impacts.** In addition to the RSR, new issues can be structured to defer or phase in full debt service payments as a means to manage rate progressions. We applaud the Wastewater Treatment Division's (WTD) continued attention to this option, especially during a low growth period, and conclude that a structure with progressive payments during early years, such as interest only or reduced near-term maturities, can provide a reasonable mechanism for shifting costs into the future when more project beneficiaries are connected and supporting related costs. At the same time, we have philosophical concerns with the use of capital interest as a tool that both defers and increases costs. While recognizing that current economic conditions coupled with the need for substantial rate increases may warrant consideration of this tool at present, we also observe that rate stabilization funds are earning minimal interest far below the cost of borrowing new funds. Given this, we strongly favor more aggressive near-term use of available reserves in lieu of deferral of growing debt obligations.
- 4) **Revisit the Culver Fund policy.** The current policy allows up to 1.5% of the WTD's operating budget to be used for non-wastewater programs. For 2010, we strongly recommend limiting awards under this program and utilizing the savings to mitigate one-time costs such as the Green River flood protection costs borne by the division and escalating program costs. For the future, we recommend eliminating funding this program for reasons of economy and consistency with recent court actions (see *Lane v. Seattle*).
- 5) **Continue and Enhance Cost Containment Programs.** We applaud the WTD's efforts and accomplishments in cost containment, particularly as related to staffing, and encourage continued efforts in cost containment related to WTD activities and County overhead.
- 6) **Enhance Returns of Debt Reserves.** As bond reserves increase in value due to increasing debt load and market conditions, securing adequate returns on these invested funds is material to the resulting rate. We support the WTD's evaluation of methods for enhancing investment returns, possibly including removal of such funds from the King County Investment Pool and direct investment in longer term maturities, and wish to remain active in the review and evaluation of this option.



- 7) **Avoid Short-term Budget Actions that Increase Overall Costs.** Any decision to defer costs should be made with a purpose of stabilizing rates and finances. Recent decisions such as the deferral of PERS contributions have exacerbated the peak rate increases by deferring costs into, rather than out of, a critical rate period. MWPAAC recommends that management of cost trends is only valid in the context of a coherent rate policy that looks beyond immediate cost avoidance and considers the overall impacts of such decisions. We are fully aware that several such options are noted above in this letter, and note that these are targeted toward mitigating and attenuating rate trends, and not avoiding financial realities.

MWPAAC makes these recommendations with an eye toward a stable, affordable and predictable rate strategy. We hope you will give them due consideration.

MWPAAC would also like to express its appreciation of the time and effort put forth by the WTD staff in support of and as part of our evaluation.

Sincerely,



Dave Christensen, Vice Chair  
for Scott Thomasson, MWPAAC Chair

cc: MWPAAC Members  
Bob Burns, Interim Director, Department of Natural Resources and Parks (DNRP)  
Christie True, Division Director, Wastewater Treatment Division, DNRP





**King County**

**Metropolitan King County Council  
Budget and Fiscal Management Committee**

<b>AGENDA ITEM</b>	<u>4</u>	<b>DATE:</b>	<u>May 18, 2010</u>
<b>PROPOSED No.:</b>	<u>2010-0262</u>	<b>PREPARED BY:</b>	<u>Amy Tsai</u>

**STAFF REPORT**

**SUBJECT:** AN ORDINANCE setting the sewer rate and capacity charge for 2011.

**SUMMARY:** King County's sewer rates are set for the following year by June 30 of each year. This proposed ordinance would:

- Set the 2011 **monthly sewer rate at \$35.15** per residential customer equivalent (RCE) per month, which is a 10.2 percent or \$3.25 increase over the 2010 rate of \$31.90;
- Set the **monthly capacity charge** for new connections to the regional system occurring in 2011 **at \$50.45**, which is a 2.8 percent or \$1.38 increase over the 2010 rate of \$49.07.

**BACKGROUND:**

**Wastewater Services Contracts**

King County provides wastewater services for 34 municipalities or sewer districts in King County, southern Snohomish County and the northern tip of Pierce County. The municipalities constitute approximately three-fourths of the county's ratepayer base and the sewer districts constitute roughly one fourth of the ratepayer base.

The County does not provide wastewater services directly to residential or business customers. Rather, the County collects wastewater from the cities or utility districts in large interceptor lines, and conveys the wastewater to County treatment plants for treatment and discharge. The sewerage service provided by the County includes construction, operation and maintenance of main trunk and interceptor sewers, pumping stations, and treatment plants.

There are two main sewer charges to customers, a monthly sewer fee and a capacity charge for new connections to the system. The monthly sewer rate collected by the county goes towards all WTD expenses, including operating costs, debt service, and

capital expenses. The capacity charge goes towards capital improvements required to provide capacity for new customers.

The County charges the contracted city and sewer district agencies the monthly sewer rate, who in turn bill the customers to whom they provide sewage collection services. Many residents see these charges on their sewer bills, but they are not paying the County directly. Their utility providers, as direct service providers, set their own rates to recoup the payments to the County for wastewater treatment plus their own "local" cost of service. Unlike the monthly sewer rate, the capacity charge is directly billed by and paid to King County.

The contracts specify that the sewer rate be in place by **June 30<sup>th</sup>** of each year.

### Monthly Sewer Rate

The monthly sewer rate for both residential and commercial customers is calculated on the basis of Residential Customer Equivalents (RCEs). One RCE (750 cubic feet of wastewater) represents the average amount of wastewater a single family residence would generate in a month. Commercial and industrial customers are charged based on the amount of wastewater generated, converted into RCEs.

The Executive's proposal includes raising the monthly sewer rate charge to \$35.15 per RCE per month. Historical sewer rates are provided in the following table, along with the Executive's projections through 2016:

**Table 1. Sewer Rates (1996-2010 Actual; 2011-2016 Projected)**

Year	Rate (\$/RCE/ Month)	% Increase
1996 - 1999	\$19.10	
2000	19.50	2.1%
2001	19.75	1.3%
2002 - 2004	23.40	18.5%
2005 - 2006	25.60	9.4%
2007 - 2008	27.95	9.2%
2009 - 2010	31.90	14.1%
2011	35.15	10.2%
2012	38.25	8.8%
2013	39.10	2.2%
2014	39.90	2.0%
2015	42.52	6.6%
2016	42.81	0.7%

The Executive's proposed sewer rate of \$35.15 is a 10.2 percent increase over the 2010 rate, or an increase of \$3.25. As the Executive noted in his transmittal letter, the proposed rate is \$0.91 less per month than was projected in the 2010 budget.

Most of the sewer rate (61%) goes towards debt service payments. About a quarter of the rate (28%) goes towards operating expenses. The remainder pays for overhead charges from county agencies (4%) and direct capital payments (6%).

### Capacity Charge

New connections to the regional wastewater system are assessed a capacity charge that is payable over a fifteen year period, or it can be paid up front, which is done by 15-20% of customers. The capacity charge along with the monthly sewer rate on new customers is designed to pay for capital improvements required to provide capacity for these new customers. This is in accordance with the adopted policy of “growth pays for growth” (K.C.C. 28.86.160 FP-15 and Ordinance 14219).

The Executive's proposal includes raising the monthly capacity charge to \$50.45 per month. A recent history of the capacity charge along with projections through 2016 is provided in the following table:

**Table 2. Capacity Charge (1996 – 2010 Actual; 2011-2016 Projected)**

Year	Rate/Month/RCE 15-yr. duration	% Increase
1996 - 1997	\$7.00	
1998 - 2001	10.50	50.0%
2002	17.20	63.8%
2003	17.60	2.3%
2004	18.00	2.3%
2005 - 2006	34.05	89.2%
2007	42.00	23.3%
2008	46.25	10.1%
2009	47.64	3.0%
2010	49.07	3.0%
2011	50.45	2.8%
2012	51.96	3.0%
2013	53.52	3.0%
2014	55.13	3.0%
2015	56.78	3.0%
2016	58.49	3.0%

The sharp increase in 2005-2006 was due to a Regional Wastewater Services Plan (RWSP) update, with new cost estimates for all components of the RWSP, including Brightwater.

The executive's proposed capacity charge of \$50.45 is an increase of 2.8%, or \$1.38 from the 2010 capacity charge of \$49.07. The capacity charge is based on 30-year projections and therefore tends to be stable over time.

New connection customers are locked into the capacity charge rate that is in effect at the time they sign their contract with the county. New connection customers are provided the opportunity to pay their capacity charge in advance rather than paying over the fifteen years. The capacity charge as proposed for 2011 at \$50.45 would amount to \$9,081 if paid monthly for the full term of 15 years. An up-front payment, discounted at 5.5% compounded over the 15 years, would amount to \$6,241.

## Budget

The 2010 Wastewater Treatment Division (WTD) budget is 7.6% of the County's total \$5 billion budget, down from being 9% of the County's \$4.9 billion budget in 2009. The WTD budget is comprised of Operations, Debt Service, and CIP, as shown in Table 3.

**Table 3. 2009-2010 Adopted WTD Budget**

Appropriation Unit	2009 Adopted	2009 % of Total	2010 Adopted	2010 % of Total
WTD Operations	\$102,916,802	23.0%	\$108,872,937	28.7%
WTD Debt Service	177,902,230	39.7%	178,569,346	47.1%
WTD CIP	167,601,619	37.4%	91,993,254	24.2%
Total	\$448,420,651	100.0%	\$379,435,537	100.0%

As shown in Table 4 below, the revenue forecast for 2010 is \$304 million (see Attachment A to Proposed Ordinance, WTD Financial Plan for the 2011 Proposed Sewer Rate), as opposed to the \$329 million that was forecast for 2010 at the time of the 2009 rate adoption last year. This difference is due primarily to a different use of the rate stabilization fund, which is used to smooth out rates over time. WTD has a revenue forecast of \$346 million in 2011. **Over 95 percent of the total revenue comes from the monthly sewer rate and capacity charge.**

**Table 4. 2009-2010 Wastewater Treatment Revenue**

Revenue Source	2010 Rate	2010 Revenue Forecast (from 2010)	2010 Revenue Forecast (from 2011)	2011 Proposed Rate	2011 Revenue Forecast
Sewer Rate	\$31.90	\$265,855,634	\$264,698,003	\$35.15	\$290,207,340
Capacity Charge	\$49.07	37,254,755	38,038,070	\$50.45	40,170,818
Other Income		9,466,000	8,740,700		8,048,600
Investment Income		5,033,317	3,146,197		5,236,136
Rate stabilization		11,550,000	(10,650,000)		2,400,000
Total Revenue		\$329,159,706	\$303,972,971		\$346,062,894

The debt service ratio needed for the county's bond covenants is 1.25 for parity bond debt service and 1.15 for total debt service. Maintaining that debt service ratio is one of the primary considerations of the revenue and expenditure balancing decisions. Table 5 shows the debt service ratio for 2010 and 2011.

**Table 5. 2010-2011 Wastewater Treatment Debt Service Ratio**

	2010	2011
Operating Revenue	\$303,973,000	\$346,063,000
Operating Expenses	106,842,000	111,160,000
Debt Service Requirement Parity Debt	146,626,000	172,586,000
Parity Debt Service Coverage Ratio*	1.34	1.36
Total Debt Service Coverage Ratio	1.15	1.15

\* [(Operating Revenue minus Operating Expenses)/Debt Service]

The parity and total debt service ratios are maintained at the appropriate levels (above 1.25 and 1.15, respectively) through 2016 (see Attachment A to Proposed Ordinance, WTD Financial Plan for the 2011 Proposed Sewer Rate).

## **ANALYSIS**

With the slowed economy, RCEs and new connections have been down significantly. Decrease in revenue can be offset in a number of ways, including:

1. Reducing projected operating expenses
2. Reviewing and prioritizing all capital projects to determine if any can be delayed
3. Increasing the sewer rate.

The \$35.15 proposed monthly sewer rate is an increase of \$3.25 over last year's adopted rate of \$31.90. The components balanced by the Executive that result in that rate include the following cost increases and decreases.

### Increased costs:

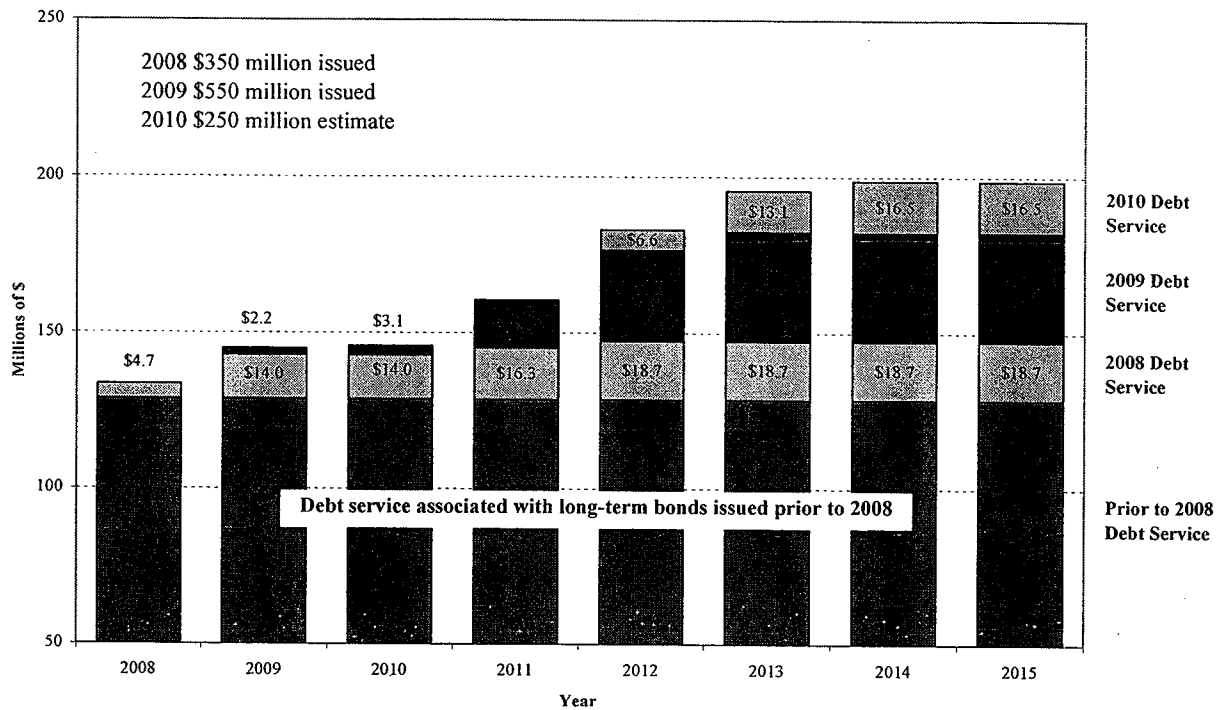
- Debt service from 2008-2009 bond issues \$1.87
- Debt service on 2011 bond issue \$1.37
- Labor (COLA and benefits) \$0.66
- Higher interest on existing subordinate debt \$0.62
- Brightwater operating costs \$0.53
- Lower RCEs \$0.47
- Chemical and energy costs \$0.35

### Decreased costs:

- Use of rate stabilization fund (\$1.79)
- Central rate adjustments (\$0.41)
- No Culver funding (\$0.20)
- Reduced transfer to WLRD (\$0.15)
- Capacity charge revenue (\$0.07)

The bad economy, which contributes to lower RCEs and higher interest rates, accounts for over \$1 of the \$3.25 rate increase (as discussed in greater detail below). Debt service obligations account for most of the rest of the rate increase. As shown in the figure below, debt service payments for existing long-term bonds increase over time.

**Figure 1. Cumulative Debt Service Associated with Long-term Bonds Issued through 2010**



The main offset of increasing costs is the use of the rate stabilization fund. Depending on which model the Council adopts (discussed later in this staff report), the rate stabilization fund can be used in varying amounts to help smooth out rates from year to year. The planned use of the reserve goes until 2014 when the forecasted amount of money in the rate stabilization reserve reaches \$0.

Other offsets include changes in how central rates are computed, not funding the Culver program and reducing the transfer to WLRD. The Culver program is a program that has transferred 1.5% of WTD's operating budget to WLRD for over ten years for general water quality and pollution abatement activities. The funds have supported organizations and grants for resource land activities such as community restoration, planting and water quality educational projects. The transfer would normally be \$1.58 million in 2011.

The other reduced transfer to WLRD would be a reduction of \$1.2 million. The services and programs that would be cut due to that reduction are still being discussed between WTD and WLRD with additional details available sometime around July. In their planning WLRD remains cognizant of the continued importance of monitoring.

**Residential Customer Equivalent (RCE) Growth and New Connections**

Higher growth in RCEs means more revenue and therefore less need to raise the rate. One RCE is equivalent to 750 cubic feet of wastewater produced in a month.

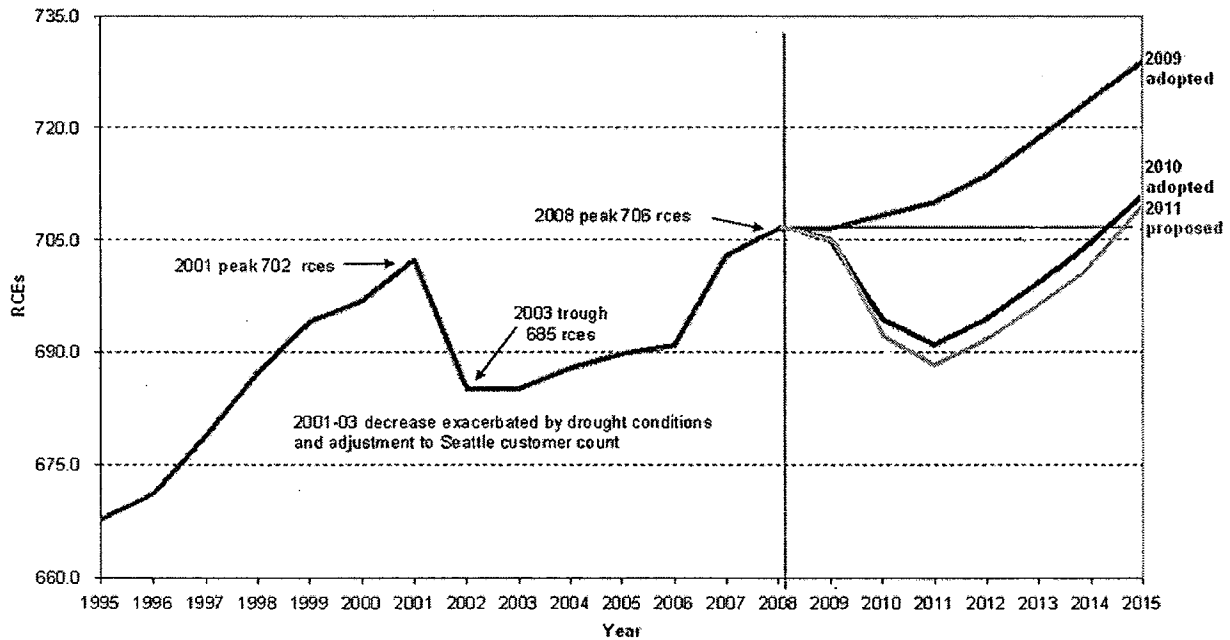


Due to the recent economic downturn and cutbacks in industrial use, WTD projects a decline in RCEs through 2011, with RCEs gradually increasing thereafter but not bouncing back to 2009 levels until 2014 (see Issue Paper, p. 14, attached to Executive's transmittal letter). The decline in projected RCEs is 0.5% lower for 2010 than had been predicted last year, or 3,020 fewer RCEs (see bolded numbers in Table 6).

**Table 6. WTD Projected RCEs and New Connections (2009-2015)**

RCEs	2009	2010	2011	2012	2013	2014	2015
<b>Proposed 2011</b>	703,800	691,480	688,020	691,460	696,650	702,920	709,240
Percent change	-0.43%	<b>-1.75%</b>	-0.50%	0.50%	0.75%	0.50%	0.90%
<b>Adopted 2010</b>	703,310	694,500	691,030	694,490	699,350	704,590	710,930
Percent change	-0.50%	<b>-1.25%</b>	-0.50%	0.50%	0.70%	0.50%	0.90%
<b>Difference</b>	490	<b>(3,020)</b>	(3,010)	(3,030)	(2,700)	(1,670)	(1,690)
New Connections	2009	2010	2011	2012	2013	2014	2015
<b>Proposed 2011</b>	6,700	5,500	6,500	8,500	9,500	11,000	11,000
<b>Adopted 2010</b>	7,500	6,000	6,000	7,500	9,000	10,500	11,000
<b>Difference</b>	(800)	(500)	500	1,000	500	500	0

**Figure 2. Comparison of RCE Outlook Scenarios**



In the current economic slump, new connections drop off over the next few years and do not bounce back to 2009 levels until 2012. RCE growth and new connections are not directly related, because RCE growth is influenced by customers leaving the system or reducing their “consumption”.

Despite a steady decline in new connections through 2010, capacity charges maintain a steady annual increase of 3% based on inflation, because capacity charges are based on a 30-year projection that is updated every three years. The county is currently in year one of the 3-year cycle, and is even slightly under last year's projection with a projected rate increase of 2.8% instead of 3.0%.

### Operating Expenses

The operating budget, \$108,872,937, is 28% of the total Wastewater Treatment Division budget (Table 3).

The 2011 operating expense projection represents a 4.0% increase compared to 2010. That is similar to the 3.7% increase from 2009 to 2010 (based on the forecasted values, see Attachment A to Proposed Ordinance, WTD Financial Plan for the 2011 Proposed Sewer Rate). The majority of operating expense costs comes from wastewater treatment operations (56%). Administration and central charges make up 21%, down from 34% last year, with the remaining operating expenses coming from Water and Land Resources Division transfers (9%), biosolid resource recovery (7%), project planning and delivery (4%), and environmental and community services (3%).

As noted above, increases in operating expenses are expected from labor (COLA and benefits), Brightwater operating costs as the treatment plant comes on-line, and increases in chemical and energy costs (including switching from chlorine to the safer but more expensive hypochlorite at the West Point plant).

It is worth noting that staffing levels at WTD have remained the same for a long period of time. WTD finds efficiencies by moving staff around as treatment plant needs change. For example, some vacant positions are being held for when Brightwater becomes operational.

**Table 7. 2005-2010 WTD Adopted Staffing Levels**

Staffing	2005	2006	2007	2008	2009	2010
FTEs (full-time)	598.7	598.7	598.7	598.7	598.7	593.7
TLTs (term-limited)	35.0	32.0	34.0	42.0	32.0	33.0

### Capital Expenditures and Accomplishment Rate

Capital expenditures peaked in 2008 and 2009. The capital program drives the need for cash flow to be provided through short and long-term debt. Debt in turn drives debt service and has a direct impact on both the monthly rate and the capacity charge.

**Table 8. WTD Total CIP (2008-2015) in \$Millions**

<b>Brightwater</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>
2010 Adopted	369.8	447.1	228.6	81.9	25.4			
2011 Update	369.8	357.9	312.8	121.7	10.1			
Difference	0	-89.2	84.3	39.8	-15.3			
<b>Other Capital</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>
2010 Adopted	106.1	107.7	99.4	109.3	102.0	159.1	159.3	159.7
2011 Update	106.1	97.6	81.5	110.9	102.4	140.4	152.9	207.2
Difference	0	-10.1	-17.9	1.5	0.4	-18.7	-6.4	47.5
<b>Total Capital</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>
2010 Adopted	475.9	554.8	327.9	191.2	127.4	159.1	159.3	159.7
2011 Update	475.9	455.5	394.3	232.6	112.5	140.4	152.9	207.2
Difference	0	-99.3	66.4	41.3	-14.9	-18.7	-6.4	47.5

The delay of the Brightwater conveyance system has caused a shifting of costs from 2009 to the outyears, plus there has been an increase in Brightwater costs of \$16.1 million (\$10.5 million for conveyance system and \$5.6 million for treatment plant).

Cost shifting into later years has occurred with some non-Brightwater projects, which helps offset the burden of the peak periods for Brightwater. Those cost shifts include:

- Completion dates for Magnolia, Murray, North Beach and Barton combined sewer overflow (CSO) projects delayed four years
- Southwest Interceptor project split into two projects with the first to be completed in 2013, compared to the originally scheduled completion date of 2010
- Ballard Siphon project completion date moved from 2009 to 2013
- Sunset/Heathfield Pump Station Replacement and Forcemain Upgrade completion date moved from 2014 to 2017
- South Plant Phase III/Odor Control project completion date moved from 2015 to 2017.

In addition, the Regional Wastewater Services Plan Local Systems Inflow and Infiltration project was reduced in scope, and the Black Diamond Storage Facility project was cancelled.

The capital cost reductions are offset somewhat by new projects and updated cost estimates, including the following:

- Fremont Siphon Repair to replace a 98 year old pipe
- Increased cost estimate of about \$30 million for CSO Control and Improvement Projects at Murray and Magnolia (which had previously relied on pre-baseline conceptual planning estimates)
- Influent Screening at West Point Treatment Plant to meet new state biosolids management regulations
- Interbay Pump Station upgrade.

*This staff report does not analyze the merits of the capital project changes; additional information can be researched upon request.*

The capital program accomplishment rate refers to the cash flow requirement generated by the capital program. For example, a capital budget of \$100 at an accomplishment rate of 95% means \$95 of cash must be available. During the past five years, the average accomplishment rate for WTD capital programs has been 87 percent. As the Brightwater major construction projects have gotten underway, the accomplishment rate has risen (95% for Brightwater in 2007 and 88% for non-Brightwater projects).

For 2010 through 2016, the projected Brightwater CIP accomplishment rate is 95% each year. Non-Brightwater rates are assumed to be 85% annually.

### **Rate Stabilization Reserve**

Rate stabilization is a way of reserving operating revenues for use in subsequent years to help smooth out rate increases that would otherwise fluctuate more with the ups and downs in the revenues and expenses that occur. Under the 2011 financial plan, \$10.65 million is put into the reserve in 2010 for a reserve balance of \$45.8 million. Under the proposal, the rate of \$35.15 for 2011 does not generate any additional rate stabilization reserve. The 2011 proposed rate uses \$2.4 million, leaving \$43.4 million in reserves. The reserve would be drawn down to zero by 2014.

### **Bond and Investment Interest Rates and Earnings**

Bond interest rates cost the county, while investment interest rates provide revenue to the county. Low interest rates therefore help on the bond front while hurting on the investment front. They are both discussed here.

Unfortunately, rates of return continue to be low in the current economy. Investment returns averaged 1.7% in 2009. The Executive's 2011 rate proposal projects investment rates of 1.25% in 2011. They are projected to increase to 2.0% in 2012 and up to 3.5% by 2015.

WTD assumes a bond interest rate of 5.25% through 2010 (down from a 6.0% estimate for 2010 last year), and 5.75% thereafter. WTD's recent \$300 million 30-year bond sale had favorable interest rates of 5.13%, which is within the assumed interest level of 5.75%. WTD also expects to issue an additional \$250 million in bonds later this year.

### **One-Year vs. Two-Year Rate**

King County Code 28.86.160 sets forth the county's financial policies in accordance with the Regional Wastewater Services Plan. Financial Policy 15 specifically states, "**King County should attempt to adopt a multiyear sewer rate to provide stable costs to sewer customers.**"

The multiyear rate adds stability and predictability by allowing clients to plan knowing what the rate costs will be for the next two years. As can be seen by the rates in Table 1, the county has consistently adopted multiyear rates since 2002.

However, the Executive's proposed rate is based on a one-year rate (designed to increase next year instead of hold steady next year), in order to provide economic relief to ratepayers during this poor economy. In his transmittal letter, the Executive notes that the proposed rate would allow ratepayers to retain \$8.7 million during 2011.

The Metropolitan Water Pollution Abatement Advisory Committee (MWPAAC), comprised of King County's wastewater clients, also recommends adoption of a one-year rate. Their reasoning is that a one-year rate provides the flexibility to adapt to changing costs and trends. MWPAAC cites uncertainty regarding financing cost and structure, start-up costs at Brightwater, growth rates and patterns, developing trends in cost containment, and departmental efforts to mitigate upward rate trends. In short, the one-year rate would allow the county to set a rate increase next year based on whatever new information is available at that time.

In deciding whether to adopt a one-year or two-year rate, there are various financing scenarios available to the Council. The types of bonds that are issued (capitalized versus non-capitalized interest) and how the rate stabilization reserve is used leads to different rate possibilities for one-year and two-year rate scenarios.

#### Use of Capitalized Interest

The Executive's proposed rate is based on a single-year rate; interest on 2010 bonds is capitalized through mid-2012; there is no capitalization of 2011 bond issues; bonds used in 2010-2012 are interest-only through 2013; and the rate stabilization reserve is used through 2014.

Table 9 presents the Executive's proposed scenario of no capitalized interest on 2011 bonds for one-year (the proposed rate) and two-year rates. Additional scenarios that use capitalized interest or interest-only bonds are presented on p.4 of the Issue Paper attached to the Executive's transmittal letter.

To put capitalized interest in perspective, for a bond of about \$200 million, capitalized interest would require borrowing \$20 million more upfront, which with interest over time results in a total debt service obligation that is \$25 million greater than a bond without capitalized interest.

**Table 9. One-year vs. Two-Year Rate, Capitalized vs. Non-Capitalized**

<b>Non-Capitalized One-Year</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>
Sewer Rate	\$31.90	<b>\$35.15</b>	<b>\$38.25</b>	\$39.10	\$39.90	\$42.52	\$42.81
% Change	0%	<b>10.2%</b>	<b>8.8%</b>	2.2%	2.0%	6.6%	0.7%
Difference from 2010 adopted	\$0	-\$0.91	-\$1.54	-\$3.60	-\$3.32	-\$1.12	-\$1.05
<b>Capitalized One-Year</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>
Sewer Rate	\$31.90	\$34.00	\$36.25	\$38.80	\$41.50	\$42.71	\$42.99
% Change	0%	6.6%	6.6%	7.0%	7.0%	2.9%	0.7%
Difference from 2010 adopted	\$0	-\$2.06	-\$3.54	-\$3.90	-\$1.72	-\$0.93	-\$0.87
<b>Non-Capitalized Two-Year</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>
Sewer Rate	\$31.90	<b>\$36.25</b>	<b>\$36.25</b>	\$39.90	\$39.90	\$42.53	\$42.81
% Change	0%	<b>13.6%</b>	<b>0%</b>	10.1%	0%	6.6%	0.7%
Difference from 2010 adopted	\$0	\$0.19	-\$3.54	-\$2.80	-\$3.32	-\$1.11	-\$1.05
<b>Capitalized Two-Year</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>
Sewer Rate	\$31.90	\$35.70	\$35.70	\$39.90	\$39.90	\$42.71	\$42.99
% Change	0%	11.9%	0%	11.2%	0%	7.6%	0.7%
Difference from 2010 adopted	\$0	-\$0.36	-\$4.09	-\$3.00	-\$3.52	-\$0.93	-\$0.87

Use of Rate Stabilization Reserve

Alternatively, the rates per year can be adjusted depending on how one uses the rate stabilization reserve. The following scenarios present the Executive's one-year non-capitalized rate scenario, plus two more scenarios that use the same types of bonds but apportion the rate stabilization funds in equal amounts, or to generate equal percentage increases each year.

**Table 10. Non-Capitalized One-Year with Different Rate Stabilizations**

<b>Exec Proposed</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>
Sewer Rate	\$31.90	<b>\$35.15</b>	<b>\$38.25</b>	\$39.10	\$39.90	\$42.52	\$42.81
% Change	0%	<b>10.2%</b>	<b>8.8%</b>	2.2%	2.0%	6.6%	0.7%
<b>Equal Rate Stabilization Use</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>
Sewer Rate	\$31.90	\$33.97	\$37.76	\$39.65	\$40.64	\$42.55	\$42.83
% Change	0%	6.5%	11.2%	5.0%	2.5%	4.7%	0.7%
<b>Equal Percentage Increases</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>
Sewer Rate	\$31.90	\$34.25	\$36.70	\$39.30	\$42.10	\$42.52	\$42.81
% Change	0%	7.4%	7.2%	7.1%	7.1%	1.0%	0.7%

## **Rate Reasonableness**

Information on monthly sewer rates in other jurisdictions suggests that King County's rates are in line with other sewer agencies (see, e.g., graphs on p. 16 of issue paper attached to Executive's transmittal letter, showing King County at approximately the average rate compared to other jurisdictions around the country). It is difficult to compare rates because many variables affect the comparison, such as the availability of other sources of funding, whether rates are computed based on actual use or other units of measurement, treatment plant technology, whether rehabilitation of aging equipment is included in the rate, development opportunities for increasing the service area, and the complexity of the terrain.

Nevertheless, as sewer systems age, it is clear that sewer rates everywhere are on the rise (see, e.g., 'Saving U.S. Water and Sewer Systems Would Be Costly', NY Times, 3/14/10).

For example, in Pierce County where sewer rates have remained at \$29.65 for a long time thanks to state and federal funding support for its original capital projects, as they plan for their future expansion needs they project a \$3.93 rate increase in 2010 and exceeding \$40 by 2013. King County would not exceed the \$40 mark until 2015 under the Executive's proposal.

Pierce County is exploring ways to keep their costs down, such as different charges for different areas. As rates continue to rise, King County will need to continue to hunt for new ways of bringing down costs as well.

### **REASONABLENESS:**

Proposed Ordinance 2010-0262 would raise sewer rates from \$31.90 to \$35.15 (10.2% increase) and increase the capacity charge from \$49.07 to \$50.45 (2.8% increase). Operating expenses have been held fairly level. Cashflow needs for capital expenditures have been balanced to keep projects on target through 2015. Approving Proposed Ordinance 2010-0262 appears to be a reasonable and prudent policy decision. However, the Council may wish to consider whether a two-year rate plan is preferred in order to maintain stable multi-year rates in accordance with the wastewater financial policies.

### **INVITED:**

- Bob Burns, Interim Director, Department of Natural Resources and Parks (DNRP)
- Christie True, Director, Wastewater Treatment Division, DNRP
- Tim Aratani, Manager, Finance and Administrative Services, Wastewater Treatment Division, DNRP
- Tom Lienesch, Economist, Wastewater Treatment Division, DNRP
- Dwight Dively, Director, Office of Management and Budget

### **ATTACHMENTS:**

1. Proposed Ordinance 2010-0262 (with Attachment)
  - A. WTD Financial Plan for the 2011 Proposed Sewer Rate
2. Fiscal Note
3. Executive's Transmittal Letter and Attachments

