



Customer Rates Meeting
Water Supply System
Meeting #3 – Projected FY 2012-13
Revenue Requirements

January 19, 2012

Introductory Remarks



DWSD's FY 2012-13 financial plan will be the first developed under the new Board structure

- The new Board has established a Finance Committee to review specifics of the financial plan
 - ✓ *Board is also staffed by a financial liaison to aid in this review and oversight*
- “Additional Considerations” of Judge Cox’s November 2011 Order remain under review and development by the Root Cause Committee
- Outstanding items that could impact the financial plan presented today
 - ✓ *Final review by Board prior to recommendations*
 - ✓ *Emergence of issues from Root Cause Committee*



DWSD is under new leadership. Please meet Director Sue McCormick



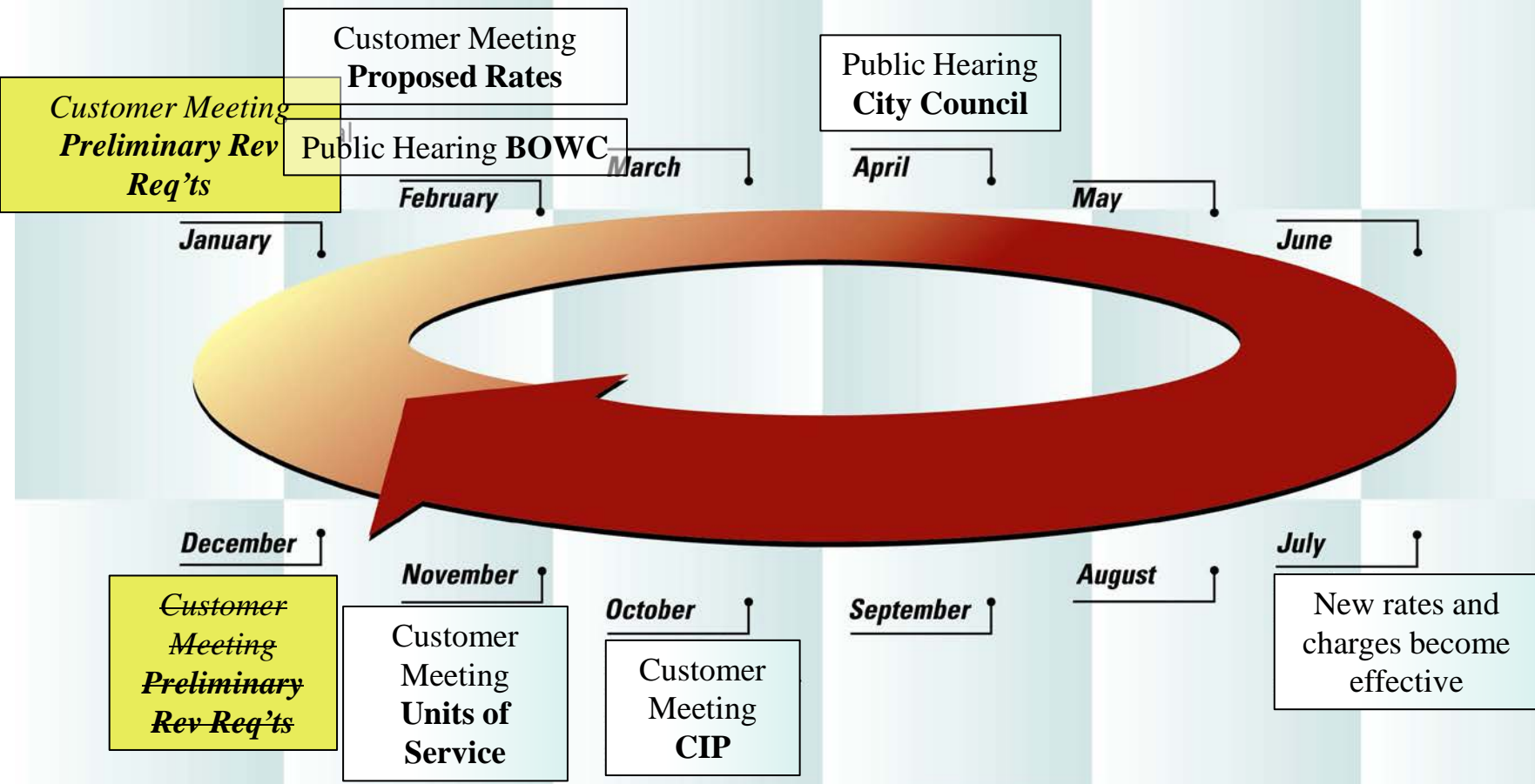
DWSD is finalizing a proposed financing plan for FY 2012-13

- This plan includes increased revenue requirements, and an increase in revenues over those provided by existing Water rates of approximately 8.5%
- **This does not mean that all rates will increase by 8.5%**
 - ✓ *The specific amounts for Detroit and Suburban Customers in general, and the amounts for individual Suburban Customer Communities, are still being developed and will be presented as soon as possible*
 - No later than next meeting on February 16



DWSD operational changes have resulted in a slight deviation from the traditional schedule

Rate Development Milestone Cycle



Presentation of Preliminary FY 2012-13 Financial Plan



Customer Rate Season Schedule

- This is the third of a series of meetings
 - ✓ 10/20/2011 –Capital Improvement Program Presentation
 - ✓ 11/17/2011 – Units of Service
 - ✓ **1/19/2012 - Preliminary SYSTEM Revenue Levels**
 - ✓ 2/16/2012 – Preliminary Individual Rate Proposals
 - ✓ 2/22/2012 – BOWC Public Hearing
 - ~~✓ 3/ /2012 – City Council Public Hearing~~
 - *For City of Detroit Retail Rates Only*
 - ✓ 7/1/2012 – Effective Date for Rates
- Parallel meetings of TAC Work Groups



Information Portals

- DWSD web site
 - ✓ www.dwsd.org
 - ✓ Customer Information / “Wholesale Customers Season Rate Schedule”
- DWSD Customer Outreach Portal
 - ✓ www.dwsdoutreach.org
 - ✓ For information contact Teresa Newman
 - ✓ teresa@projectinnovations.com



Today's Agenda

- Update of Units of Service
- Preliminary Revenue Requirements for FY 2012-13 Water Rates
 - ✓ *Summary of FY 2010-11 Results*
- Preview of Subsequent Meeting Material
 - ✓ *Cost of Service Allocation / Rate Design Issues Status Report*
- Review of DWSD Debt Portfolio



There are 3 Fundamental Steps in the Water Rate Methodology

- Revenue Requirement Projections
 - ✓ *How Much Money is Needed?*
- Cost of Service Analysis
 - ✓ *From Whom Should the Money be Collected?*
- Design of Recommended Rates
 - ✓ *How Should DWSD Services be Priced?*



Units of Service presented in November have changed slightly

- Amended Exhibit B's for "Group 3" Reopeners have been received and are in the process of being incorporated
 - ✓ *Revenue projections assume 7.5% reduction in annual billed volumes for this customer group*
 - ✓ *Specific modifications under review*
- Modified projected volume for "Old Contract" customers
 - ✓ *Grosse Ile Twp from 55,000 Mcf to 58,000 Mcf*
- Detroit peaking factors under review
 - ✓ *Data from new retail metering system*



The need for rate increases is a function of projected revenues and revenue requirements

- Revenue Projections
 - ✓ *Product of expected sales and existing rates*
- Revenue Requirement Projections
 - ✓ *Operation and Maintenance Expenses*
 - Based on budget request
 - ✓ *Capital Financing Requirements*
 - Based on financing plan for July 2011 CIPs
 - ✓ *Other Elements related to November 4 Order and Plan of Action*



Projected sales are (preliminarily) equivalent to the baseline from the current rates

- Billable volumes are essentially unchanged from FY 2012
 - ✓ *Despite anticipated reductions from Amended Exhibit Bs*
- Billable revenues also essentially unchanged
 - ✓ *Impact of fixed charges*

	FY 2011-12 <u>Baseline</u>	FY 2012-13 <u>Projection</u>	<u>Variance</u>	<u>% Variance</u>
<u>Billable Volumes - Mcf (millions)</u>				
Detroit Retail	4.05	4.10	0.05	1.2%
Suburban Wholesale	16.97	16.92	(0.05)	-0.3%
	-----	-----	-----	
Suburban Wholesale	21.02	21.02	(0.00)	0.0%
<u>Projected Revenue - \$ millions</u>				
Detroit Retail	89.21	90.03	0.82	0.9%
Suburban Wholesale	266.92	266.21	(0.72)	-0.3%
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Total	356.13	356.23	0.10	0.0%

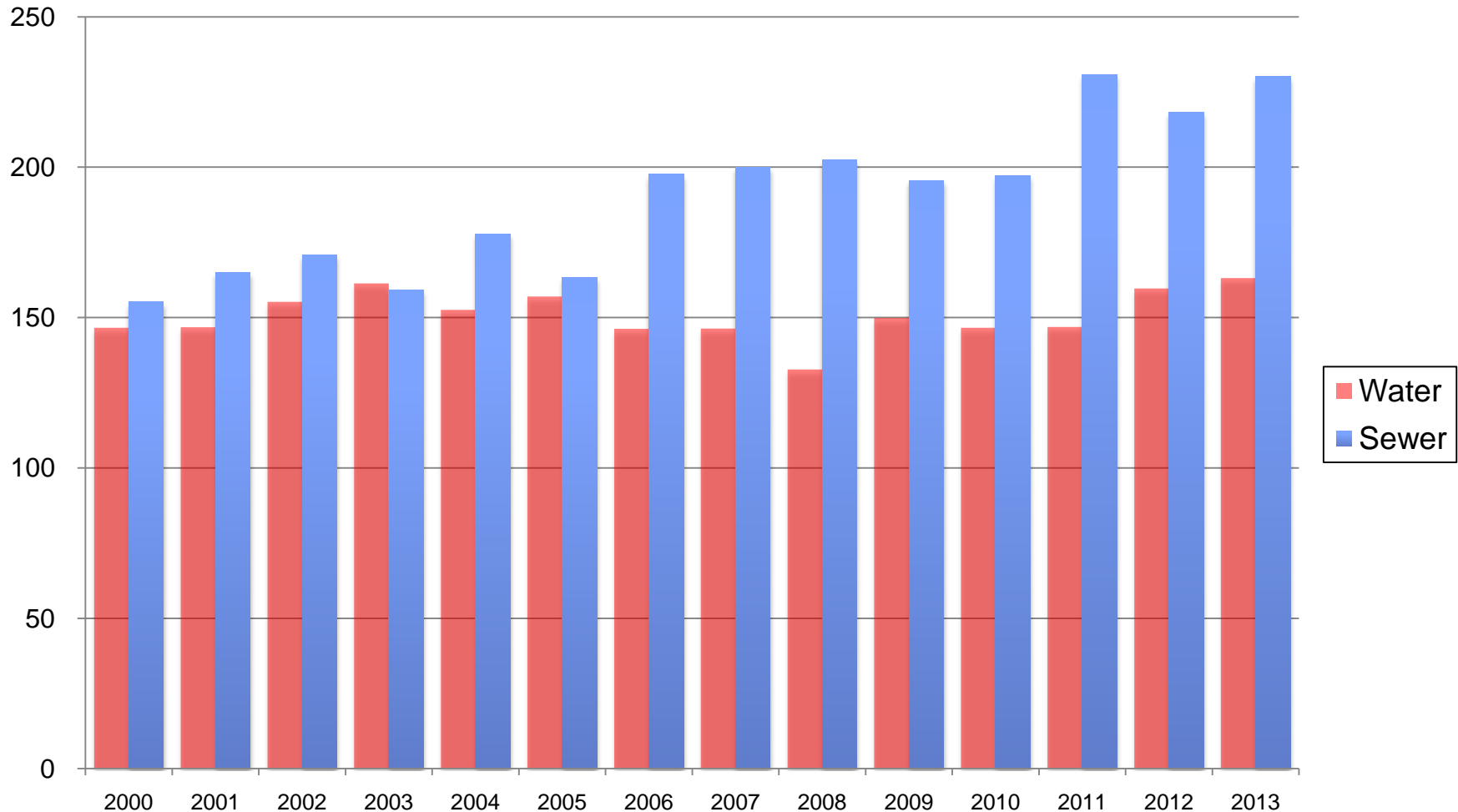


The budget request process has been subjected to intense and inclusive review

- Initial requests in early October
- One month iterative review process by DWSD Budget Section
 - ✓ *Modifications by individual managers*
- Initial review by AD Financial Services
 - ✓ *Identification of additional adjustments*
 - ✓ *Additional modifications by individual managers*
- Final review by AD Financial Services
 - ✓ *Final modifications and adjustments*
- Overall Water Budget Request is approximately
 - ✓ *2% higher than FY 2012 Budget*



The 2013 Budget Request reflects the remarkable stability in Water Operating Expenses, and the recent increases in Sewer (*figures in \$millions*)



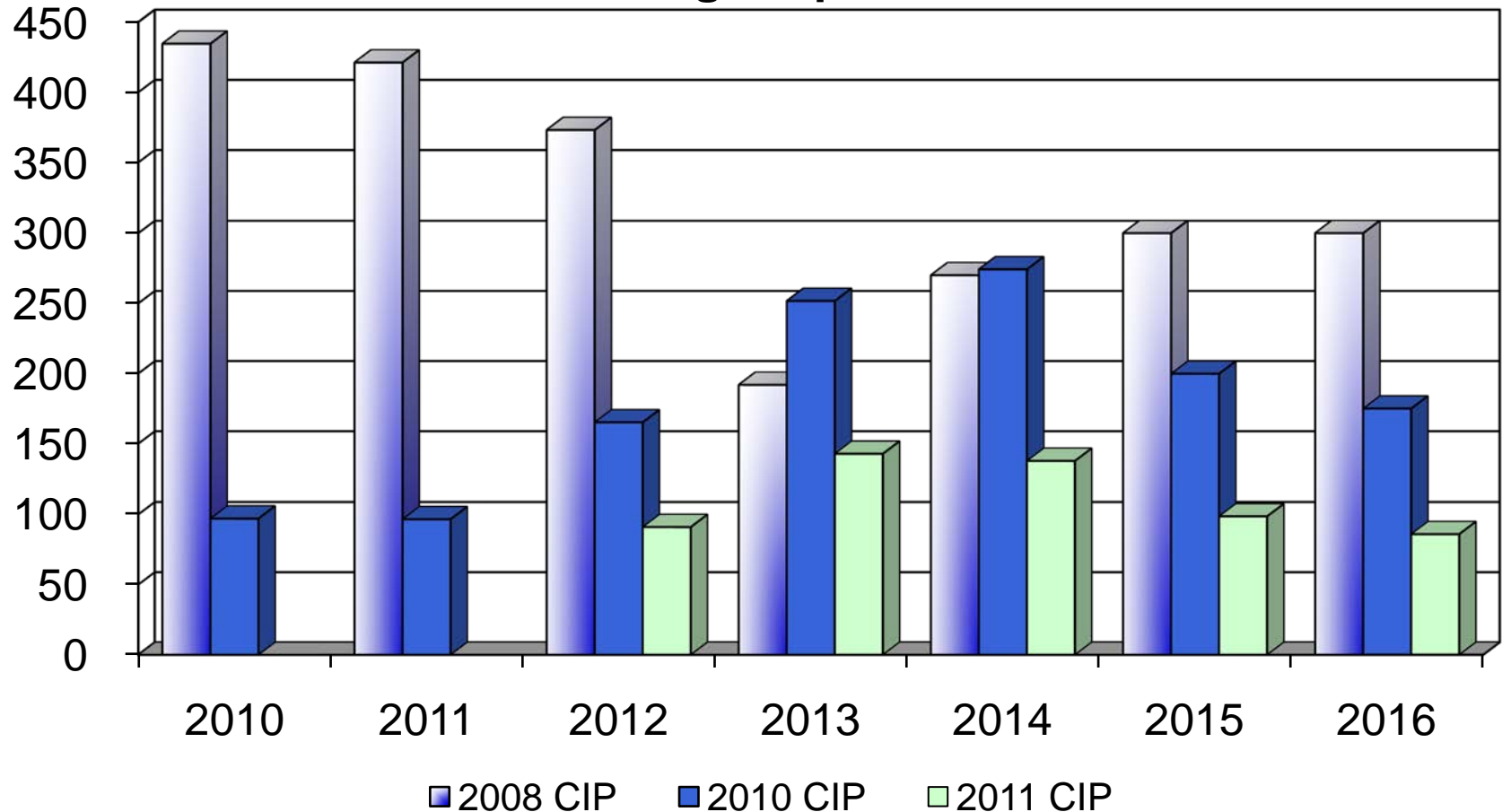
The budget request generally follows traditional protocol but reflects DWSD specific needs

- Includes funding for vacancies identified as “critical need”
 - ✓ *Critical need vacancies were subjected to rigorous review*
 - Pared from ~260 to ~80
 - ✓ *Removes all other vacant positions*
- Includes new funding for BOWC activities
- Still includes payments to City of Detroit for traditional services rendered
 - ✓ *Haven't adjusted for independent resources yet*
 - ✓ *Once established, budgeted funds will finance self supported functions, rather than payments to COD*
- Still following basic City of Detroit budget parameters



The July 2011 CIP approved by the Board reflects a dramatic re-evaluation of the Water System Capacity and Facility Plan, and resulted in lower capital req'ts

Annual CIP Financing Requirements - \$ millions



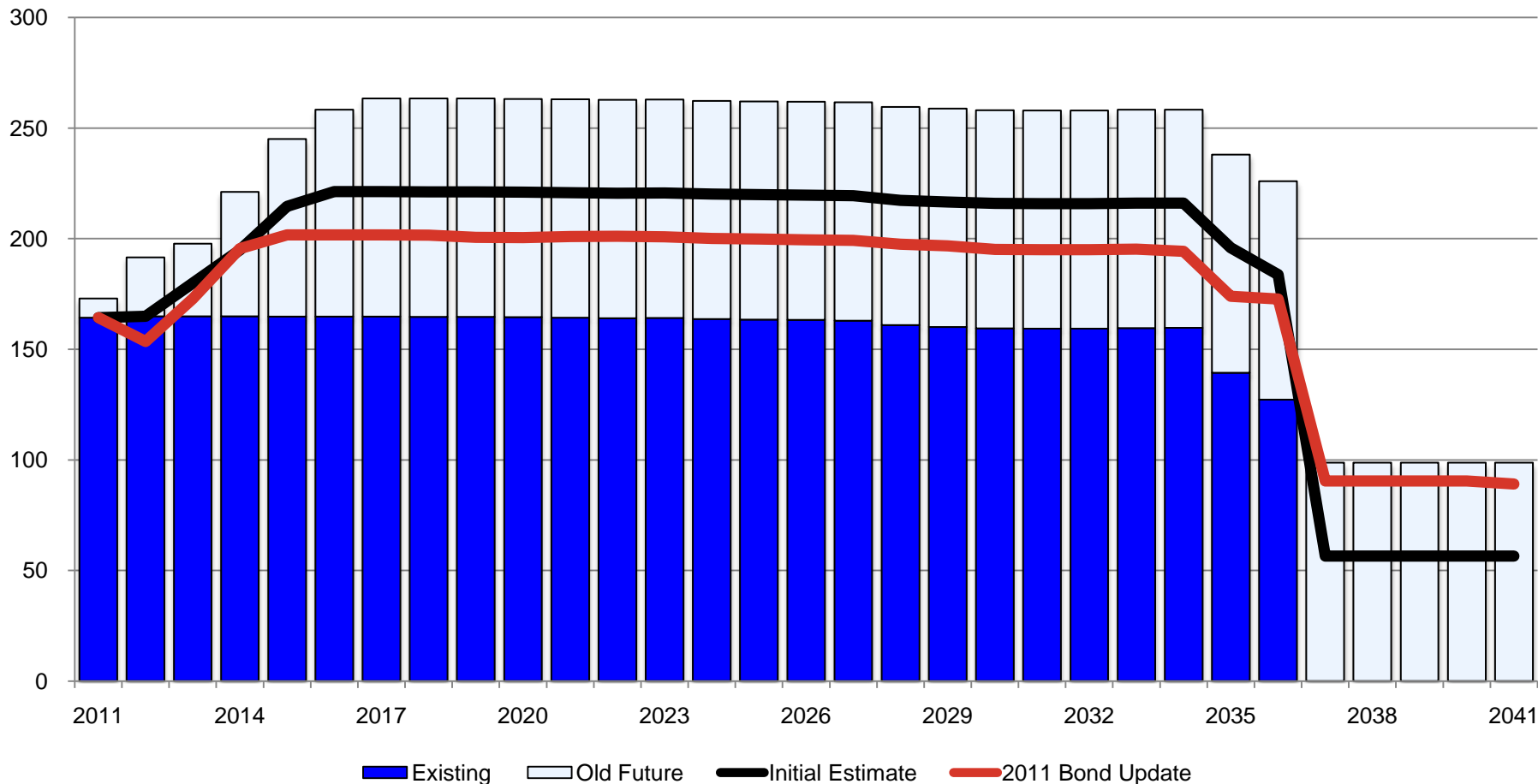
Financing for the Water CIP is being provided by the Series 2011 Water Bonds, closed December

- Provides financing for the CIP through FY 2013
 - ✓ *Moderate balance available for 2014*
- Terminates all outstanding swaps
 - ✓ *Reduces balance sheet risk*
- Refunds certain outstanding Bonds
 - ✓ *Results in Debt Service savings*
- Mid and long-term CIP Financing Plan envisions more revenue financing, and less reliance on debt
 - ✓ *Will result in higher debt service coverage ratios*
 - ✓ *Key to “Improve Ratings” Strategic Initiative*



The recent deferrals of major projects in the Water CIP have reduced potential annual debt service projections, and the 2011 Bonds terminate swap risk efficiently

Annual Debt Service – Water (\$millions)



The 5-year financing plans are designed to

- Utilize more revenue to finance capital improvements, with less reliance on future debt
 - ✓ *Will result in higher debt service coverage ratios*
 - ✓ *Key to “Improve Ratings” Strategic Initiative*
- Designed to enhance balance sheet
 - ✓ *Inclining reported net assets*
- Designed to improve System liquidity
 - ✓ *Inclining unrestricted fund balances*



Our Capital Financing strategies are driven by covenants made to our bondholders and policies established by the Board

- The debt/revenue mix to finance capital improvements is designed to meet the BOWC Policy regarding debt service coverage levels

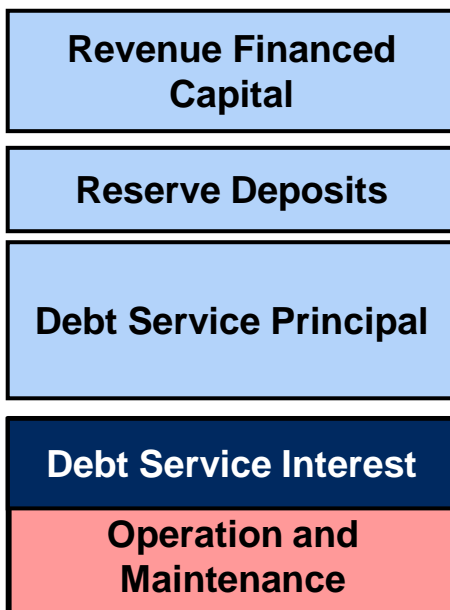
	Ordinance Requirements	Board Minimum
Senior Lien	120%	135%
Senior plus Second Lien	110%	125%
Senior plus Second plus SRF Junior Lien Bonds	100%	115%



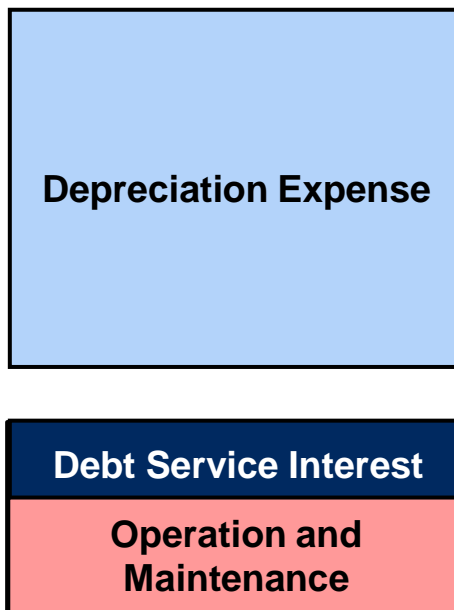
Our revenue requirements are evaluated from three separate perspectives, to ensure all requirements are met by rates

- DWSD sets rates designed to generate revenues that are sufficient to meet projected annual “cash basis” revenue requirements consisting of:
 - Operation & Maintenance Expense
 - Debt Service on Revenue Bonds
 - Revenue Financed Capital
 - Reserve Fund Maintenance
- In addition, DWSD reviews other measures of “revenue requirements” in order to ensure that financial plans are protecting value and complying with legal and policy covenants

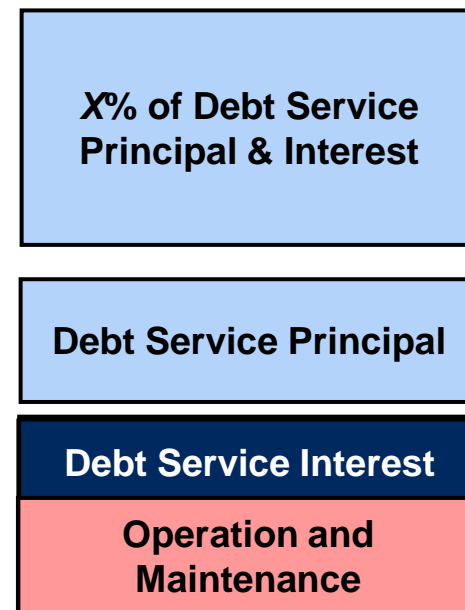
Cash Requirements (RATES)



Accrual Requirements (FINANCIAL STATEMENTS)



Coverage Req'ts (BOND COVENANTS)



Water 5-Year Financial Plan

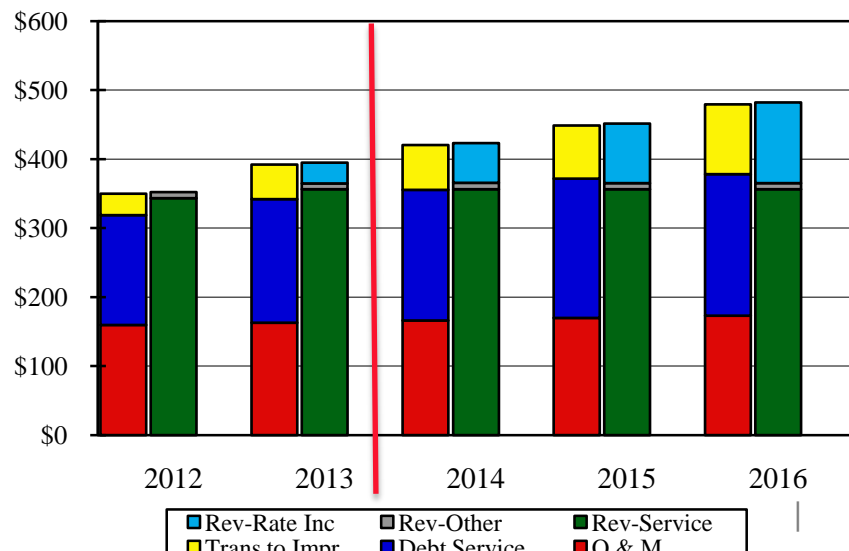
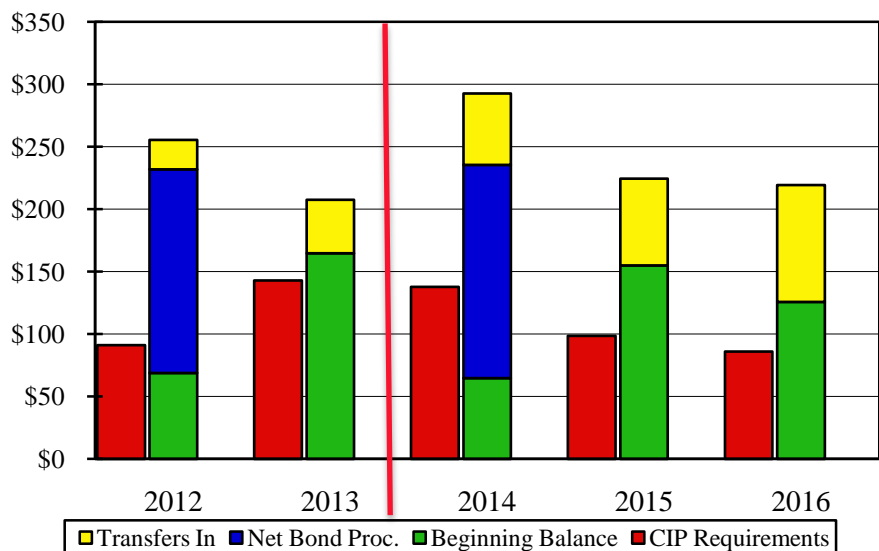
CIP and Operating Fund Financing

CAPITAL IMPROVEMENT PROGRAM FINANCING - \$ millions

	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
CIP Req't	91.0	142.8	137.7	98.6	85.9
<u>Sources</u>					
Beg Balance	68.7	164.5	64.7	154.9	125.6
Bond Sale	500.7	0.0	200.0	0.0	0.0
less: Issue Exp	(337.6)	0.0	(29.2)	0.0	0.0
Revs / Op Funds	23.7	43.0	57.1	69.4	93.5
Total Sources	255.5	207.5	292.6	224.3	219.1
End Balance	164.5	64.7	154.9	125.6	133.2

REVENUE / OPERATING FUND FINANCING PLAN - \$ millions

	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
Rate Revenue	343.5	356.2	356.2	356.2	356.2
Rate Increases		8.5%	7.0%	7.0%	7.0%
Rate Increase Rev	0.0	30.2	57.2	86.1	117.1
Other	8.7	8.6	9.5	9.1	9.0
Total Revenue	352.2	395.0	423.0	451.5	482.3
O&M Expense	159.7	163.1	166.3	169.7	173.1
Debt Service	159.1	178.7	189.1	201.8	204.9
Rev Fin CIP	31.2	50.5	64.8	77.2	101.4
Total Rev Req'ts	349.9	392.2	420.2	448.6	479.4
Balance - Rsrvs	2.2	2.8	2.8	2.9	2.9
DS Covg	125%	134%	140%	144%	156%



Water 5-Year Financial Plan

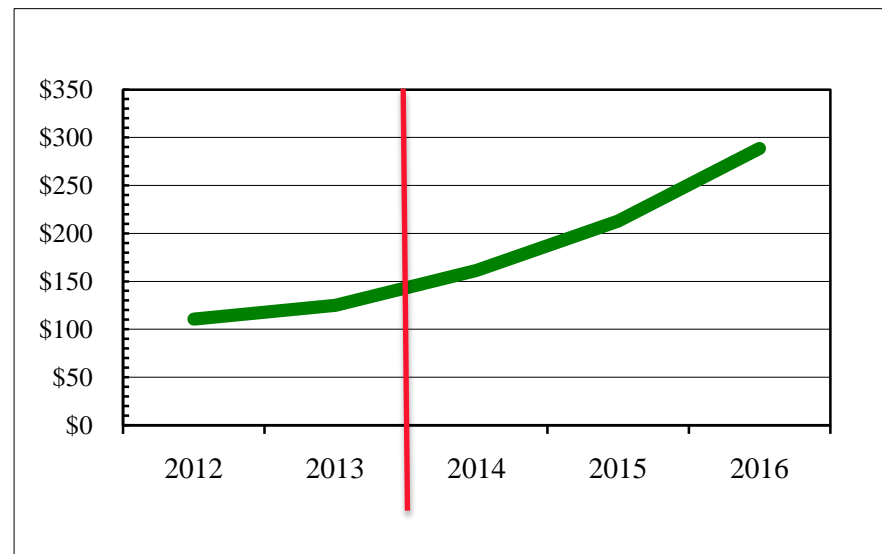
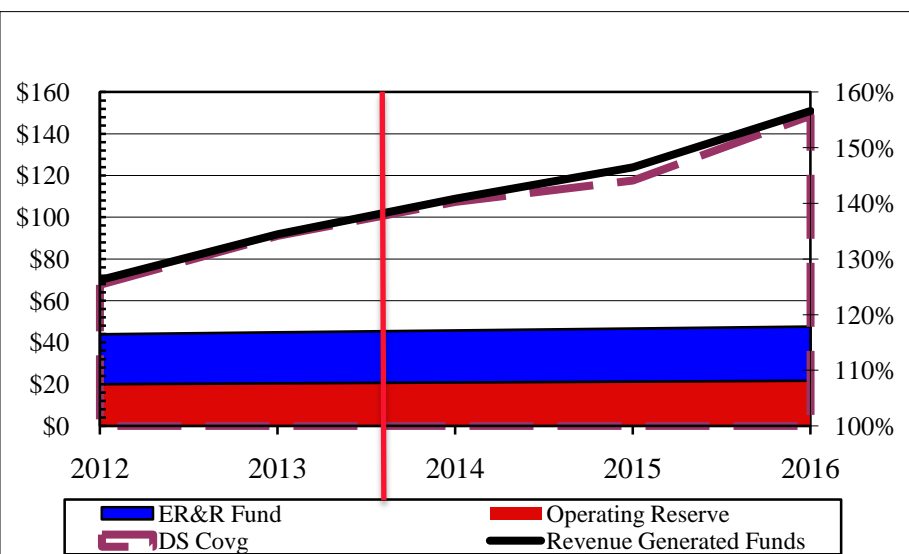
Fund Balance / Balance Sheet Summary

FUND BALANCE SUMMARY - \$ millions

	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
Fund Balance Mins					
Operating Reserve	20.0	20.4	20.8	21.2	21.6
ER&R Fund	23.9	24.5	25.0	25.5	26.0
I&E Fund	<u>0.0</u>	<u>0.0</u>	<u>0.0</u>	<u>0.0</u>	<u>0.0</u>
Subtotal	43.9	44.8	45.7	46.7	47.6
Projections					
Operating Reserve	22.2	24.4	26.8	29.1	31.5
ER&R Fund	23.9	24.5	25.0	25.5	26.0
I&E Fund	<u>23.7</u>	<u>43.0</u>	<u>57.1</u>	<u>69.4</u>	<u>93.5</u>
Rev Gen Funds	69.8	91.9	108.8	123.9	151.0
DS Covg	125%	134%	140%	144%	156%

PROFORMA NET ASSET CHANGE SUMMARY - \$ millions

	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
Net Revenues	192.5	231.9	256.7	281.8	309.2
Contributions	0.1	0.1	0.1	0.1	0.1
OPEB & Other (b)	(12.0)	(12.2)	(12.5)	(12.7)	(13.0)
Depreciation Exp	(85.3)	(87.8)	(91.8)	(95.7)	(98.5)
Interest Exp	<u>(108.2)</u>	<u>(117.6)</u>	<u>(116.0)</u>	<u>(122.1)</u>	<u>(122.0)</u>
Net Asset Change	(12.9)	14.4	36.4	51.3	75.8
Begin Net Assets	123.5	110.5	124.9	161.3	212.7
Ending Net Assets	110.5	124.9	161.3	212.7	288.5

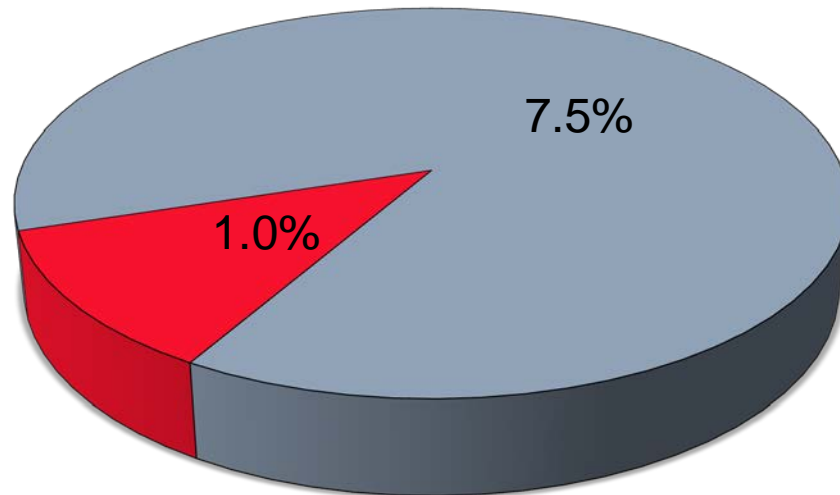


The anatomy of a revenue req't increase

Drivers of Water revenue increase needs

	FY 2011-12	FY 2012-13			% Rate	
	<u>Baseline</u>	<u>Projection</u>	<u>Variance</u>	<u>% Variance</u>	<u>Impact</u>	
<u>Revenue Base</u>						
1	Detroit	89.21	90.03	0.82	0.9%	-0.2%
2	Suburban	266.92	266.21	(0.72)	-0.3%	0.2%
3	Total	356.13	356.23	0.10	0.0%	0.0%
4	O&M	159.66	163.08	3.42	2.1%	1.0%
5	Debt Service	164.91	172.90	7.99	4.8%	2.2%
6	Subtotal					3.2%
7	Other Revenue Req'ts	31.56	50.47	18.91	59.9%	5.3%
8	TOTAL					8.5%

- Revenue Base
- OM
- Capital



We are not prepared to present potential impact on customer classes until next month

- Items that will impact the remaining Cost of Service Allocation analysis:
 - ✓ *Completion of final review of fixed asset data*
 - ✓ *Final determination of units of service (new Exhibit Bs)*
 - ✓ *Emergence of issues from Root Cause Committee*
- Items that will impact the Rate Design analysis:
 - ✓ *Should not be any for Wholesale Water Rates*
 - ✓ *Fixed cost portion for FY 2012-13 = 100% of “Plant and Pipe” capital costs*
 - Recommended by TAC Water Rates Work Group
 - Supported by full TAC
 - DWSD intends to implement



Takeaways

- DWSD has presented a preliminary financial plan for the Water Supply System for FY 2012-13, which calls for an increase in revenues over those provided by existing rates of approximately 8.5%
 - ✓ *Review is ongoing and this may change*
 - ✓ *IMPACTS ON INDIVIDUAL CUSTOMERS HAVE NOT BEEN DETERMINED*
 - ✓ *IT IS NOT ACCURATE TO ASSUME THAT ALL RATES ARE GOING TO BE INCREASED BY THIS AMOUNT*
- DWSD and the Root Cause Committee continue to evaluate the potential impact of Judge Cox's November 4 Order on financial operations for FY 2012-13
- DWSD will announce specific community rates no later than the next meeting, scheduled for February 16

