

## SPU Summary of 2015-2020 Financial Baseline

**Definition of Financial Baseline:** The change in annual rate revenues, or average annual rates, needed to maintain existing service levels, plus meet firm regulatory requirements.

- *What do we mean when we say “maintain existing service levels?”* We mean that **actual** service quality (as opposed to **targeted** service quality) neither degrades nor improves. See attached table for examples of current service level targets in the Environmental focus area.

**What the Baseline Does NOT Include:** The baseline does NOT:

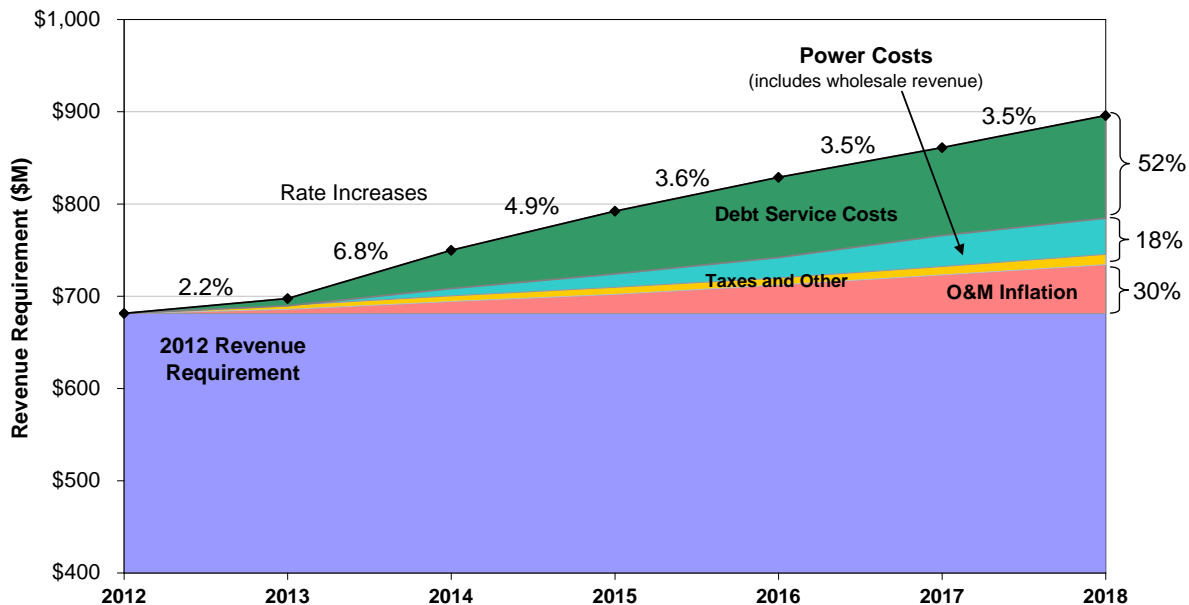
- Adjust for any anticipated, future efficiencies
- Prioritize existing expenditures and eliminate or reduce lower priority projects/programs
- Include capital projects in the 6-year Capital Improvement Program that are new efforts not required by regulators or are necessary to maintain existing service levels
- Include funding for new initiatives to address gaps in meeting SPU’s strategic objectives.

**Why the Baseline Does Not Simply Increase By the General Rate of Inflation:** Some of the more significant reasons that the baseline does not rise at the general level of inflation are listed below, and are placed into two categories: (1) changes to expenditures; (2) changes in other factors affecting the rate path. Most of these reasons cause the baseline to rise **faster** than the general rate of inflation.

1. Changes to expenditures. Below are some reasons that expenditures will increase or decrease through 2020 at rates different than the general rate of inflation. These are:
  - a. Increasing debt service payments. Much of the cost of SPU’s capital projects is debt financed over 30 years. Since most of our existing debt is less than 30 years old, previously-issued debt is not being retired as new debt is issued (generally every 18-24 months), resulting in upward pressure on rates.
  - b. Operations “tail” of new infrastructure projects. Construction of new infrastructure (as opposed to replacement infrastructure) is generally associated with operations and maintenance needs above status quo levels. These costs have been included in the baseline figures.
  - c. Changing regulatory requirements. SPU’s capital and operating expenditures vary considerably with changing regulatory requirements. Increasing requirements for combined sewer overflows, and sediment remediation/liability allocation associated with the Duwamish Superfund site, place upward pressure on rates.
  - d. Cost changes to large contracts. SPU has several large contracts for utility services. In Wastewater, King County estimates treatment rates will increase 5.4% in 2015, 1.8% in 2016, 4.2% in 2017, 1.5% in 2018, and 1.6% in 2019. In Solid Waste, the various contracts SPU has for collection, hauling, processing, and disposal of organics, recyclables, and garbage each have their own built-in inflation calculations.
  - e. Varying inflators for varying cost centers. The general CPI inflator through 2020 is assumed to be 2% per year. However, there are many SPU cost centers that will inflate differently (and generally at a higher rate) than this. Some examples are:

- i. Labor costs, where increases above CPI are primarily but not exclusively due to medical benefits and the City’s contribution to pensions for retirees.
  - ii. Construction costs, which are expected to rise more quickly than general inflation due to increases in the cost of skilled labor and building materials.
  - iii. Other costs, such as fuel, are expected to rise faster than the general rate of inflation.
2. Changes to other factors affecting the rate path. Two other factors not related to expenditures have significant implications on the baseline rate path figures. These are:
- a. Customer demand. With the exception of the drainage line of business, SPU expects demand for its services to fall. This means that SPU’s fixed costs are spread over a smaller demand base, resulting in higher increases in rates (though not necessarily higher customer bills).
  - b. Meeting Financial Policies. SPU has several adopted financial policies for each fund, including net income, debt service coverage, year-end cash, and CIP cash financing. There are times when rates need to increase to meet our financial policies. Fortunately, there are also some times when a fund has exceeded its target, such as year-end cash, and can be used to keep rates lower than they otherwise would be.

**City Light Example:** To maintain its current level of service and programs, City Light’s Financial Baseline document showed rate increases averaging about 4.1% per year for 2013-2018. As shown in the chart pictured below from the City Light Baseline Report (January 2012 update), the main drivers of this increase were a growing debt service burden, growth in the cost of power, and inflation in O&M costs:



- City Light’s projected revenue requirement path, presented in their Strategic Plan, was the combined result of the baseline forecast, planned efficiency actions, and a set of new investments:

Baseline	4.1% increase per year
Efficiencies	(0.4%) decrease per year
Investments	1.0% increase per year
<b>Total</b>	<b>4.7% increase per year</b>

**ATTACHMENT. BASELINE DESCRIPTION & SERVICE LEVELS FOR “ACHIEVE ENVIRONMENTAL COMPLIANCE & STEWARDSHIP”**

STRATEGIC OBJECTIVES	DESCRIPTION OF BASELINE	CURRENT SERVICE LEVELS
Meet or exceed environmental and public health mandates	<p>This is the second of the top two “bread and butter” strategic objectives for SPU. Many staff are engaged in ensuring this objective is met, including:</p> <ul style="list-style-type: none"> <li>▪ Staff running SPU’s water quality laboratory</li> <li>▪ Utility Service Teams’ staff who test customer backflow assemblies</li> <li>▪ Water operational staff who regulate releases of water from the Lake Youngs reservoir</li> <li>▪ Planning staff and engineering staff working on CSO compliance</li> <li>▪ Transfer station staff who clean the stations of garbage by the end of the day</li> <li>▪ Inspectors who find and eliminate illicit connections to the storm system or illicit discharges to the system</li> </ul>	<p><b>Water</b></p> <ul style="list-style-type: none"> <li>▪ Supply drinking water that meets or exceeds state DOH regulations</li> <li>▪ Provide agreed-upon instream water for fish and meet other tribal, regional, state, and federal commitments</li> </ul> <p><b>DWW</b></p> <ul style="list-style-type: none"> <li>▪ Meet or exceed CSO-related legal and regulatory requirements</li> <li>▪ Meet NPDES stormwater permit requirements.</li> <li>▪ Meet SPU goals for stormwater pollutant removal (remove an additional 0.1% of TSS annually from stormwater baseline)</li> <li>▪ Meet sediments-related legal and regulatory requirements, e.g., comply with Record of Decision for Duwamish Superfund site.</li> </ul> <p><b>Solid Waste</b></p> <ul style="list-style-type: none"> <li>▪ Meet health &amp; safety requirements at the transfer stations</li> <li>▪ Provide services according to regional Local Hazardous Waste Management Plan</li> </ul>
Conduct all SPU operations in a sustainable way	<p>SPU has taken proactive steps to measure its “carbon footprint” in terms of electricity use, fuel use, and incorporation of carbon-enhancing materials in construction (such as certain concrete). We monitor and manage the long term impact of several historic landfills.</p>	<ul style="list-style-type: none"> <li>▪ Achieve carbon neutrality by 2015 (upcoming Executive Order)</li> <li>▪ Achieve a LEED Gold rating at a minimum on SPU projects &gt; \$5M</li> </ul>
Partner with stakeholders, public and private entities to achieve environmental objectives	<p>SPU participates extensively with a wide range of governmental and non-governmental parties in order to achieve our environmental objectives. Examples include Watershed Councils, regional Salmon Recovery efforts, the Puget Sound Partnership, and the Muckelshoot Indian Tribe. We coordinate with NGOs in buiding raingardens on private property.</p>	<ul style="list-style-type: none"> <li>▪ Capture 700M gallons of stormwater by 2025 [Recent Executive Order/Resolution]</li> <li>▪ Contribution to interlocal agreements establishing WRIAs 8 and 9</li> </ul>
Anticipate and adapt to changing circumstances	<p>Staff in the Corporate Strategies Division are working on climate change proposals, and methods to become carbon neutral.</p>	None
Promote conservation and sustainable use of utility services	<p>SPU supports an annual investment in water conservation activites as set by the Water Use Efficiency Goal. Similar investments are made toward reaching the current Recycling goal of 60% by 2015.</p>	<ul style="list-style-type: none"> <li>▪ Achieve water conservation goals as described by the Saving Water Partnership</li> <li>▪ Achieve the City’s Waste Reduction &amp; Recycling goals (60% by 2015; 70% by 2022; C&amp;D recycling by 70% in 2020)</li> </ul>

