

Agenda Item: 8.

MEMORANDUM TO: Programs, Projects & Operations Subcommittee

SUBJECT: Financial Merger of Washington County Rural Water #2 with Washington County RW #1

DATE: April 4, 2013

FROM: Dick Sklenar

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Of concern to the District's staff is the financial forecast of Washington County Rural Water #2 (WCRW#2) in the next few years. The heavy debt load, coupled with few new hookups, will undoubtedly cause WCRW #2 to default on its bank loan and revenue bonds in a couple of years.

**BACKGROUND:**

WCRW #2 development was initially thrust forward after receiving a petition from numerous residents in southeast Washington County asking the District to investigate an alternative water supply for their residence. Lack of good groundwater quality, and quantity, were the reasons for the petition. Based on the petition received, a feasibility study area was developed. The City of Blair agreed to provide the water supply with the condition that the District finance the construction of the water tower (currently south of Blair) and oversizing the main trunk line (see attached map) so as to provide emergency delivery of water from Washington County Rural Water #1 (WCRW#1). Aware of the population growth potential, the Washington County Board agreed to provide funds to oversize the smaller feeder lines within the study area. The entire system itself was oversized to allow for future growth as well. Subsequently, the District obtained a bank loan and issued revenue bonds (20-year period) to accommodate the construction and engineering costs for developing WCRW#2. The City has agreed to repay the District for the cost of the water tower and oversizing the trunk line over a 10-year period, 3 years of which are remaining.

Anticipation of another successfully operated rural water system was high. Washington County during the early part of this century was experiencing exceptional population growth (1 of the top 4 in the State) and the overall economic outlook was strong. Over 250 applications for rural water service were on hand when operation of WCRW #2 began in late 2005. The projection was that additional 12-15 new services would be added annually to the system based on experience from the adjoining WCRW #1 system. However, within a short period of time that projection failed to materialize. The economic downturn in the economy stagnated new housing starts, and thus hookups to the WCRW#2 system. The number of new hookups annually continues to be poor to this day, as evidenced below;

| Year | New Hookups | Projected | Difference | Accumulated Difference |
|------|-------------|-----------|------------|------------------------|
| 2007 | 10          | 12 – 15   | 2 to 5     | 2 to 5                 |
| 2008 | 9           | 12 – 15   | 3 to 6     | 5 to 11                |
| 2009 | 2           | 12 – 15   | 10 to 13   | 15 to 24               |
| 2010 | 7           | 12 – 15   | 5 to 8     | 20 to 32               |
| 2011 | 2           | 12 – 15   | 10 to 13   | 30 to 45               |
| 2012 | 7           | 12 – 15   | 5 to 8     | 35 to 53               |

With each year passing, the situation compounds itself as evidenced in the right hand column. Increasing water rates alone cannot overcome the lack of anticipated growth. Rates have increased 3 times (7% -10% each time) in the last 6 years, and every effort has been made to cut operating costs without affecting service.

Table #1 reflects a tentative draft budget for WCRW#2 from Fiscal Year 2014 thru Fiscal Year 2017. A potential shortfall commences in F.Y. 2015. Keep in mind that this table assumes that all budgeted expenditures will be spent, something that does not happen every year.

#### **DEBT SERVICE:**

WCRW #2 currently has a bank loan and revenue bonds to address. After July 1, 2013, the principal on the bank loan will be \$600,000 (5.25% interest). Principal on the revenue bonds will be at \$2,425,000 (1.00% to 5.00% interest). The revenue bonds were refinanced in 2011 and are not callable for refinancing until 2016. The loan term with the Washington County Bank will expire in 2 years, at which point it will be renegotiated.

#### **PROBABLE ALTERNATIVES:**

A potential alternative would be a financial merger of WCRW #1 with WCRW #2. The cash on hand for WCRW #1 is close to \$700,000, and such funds could be used to help address debt service.

Table #2 is the forecast for the financial merger of both the WCRW #1 and WCRW #2 budgets. It assumes that the annual retirement of debt service to the bank (\$50K) and revenue bonds would continue in subsequent years. This table indicates a delay in the potential shortfall that is expected to occur later during Fiscal Year 2019. The District may need to undertake refinancing, or other measures, preceding the shortfall of that fiscal year.

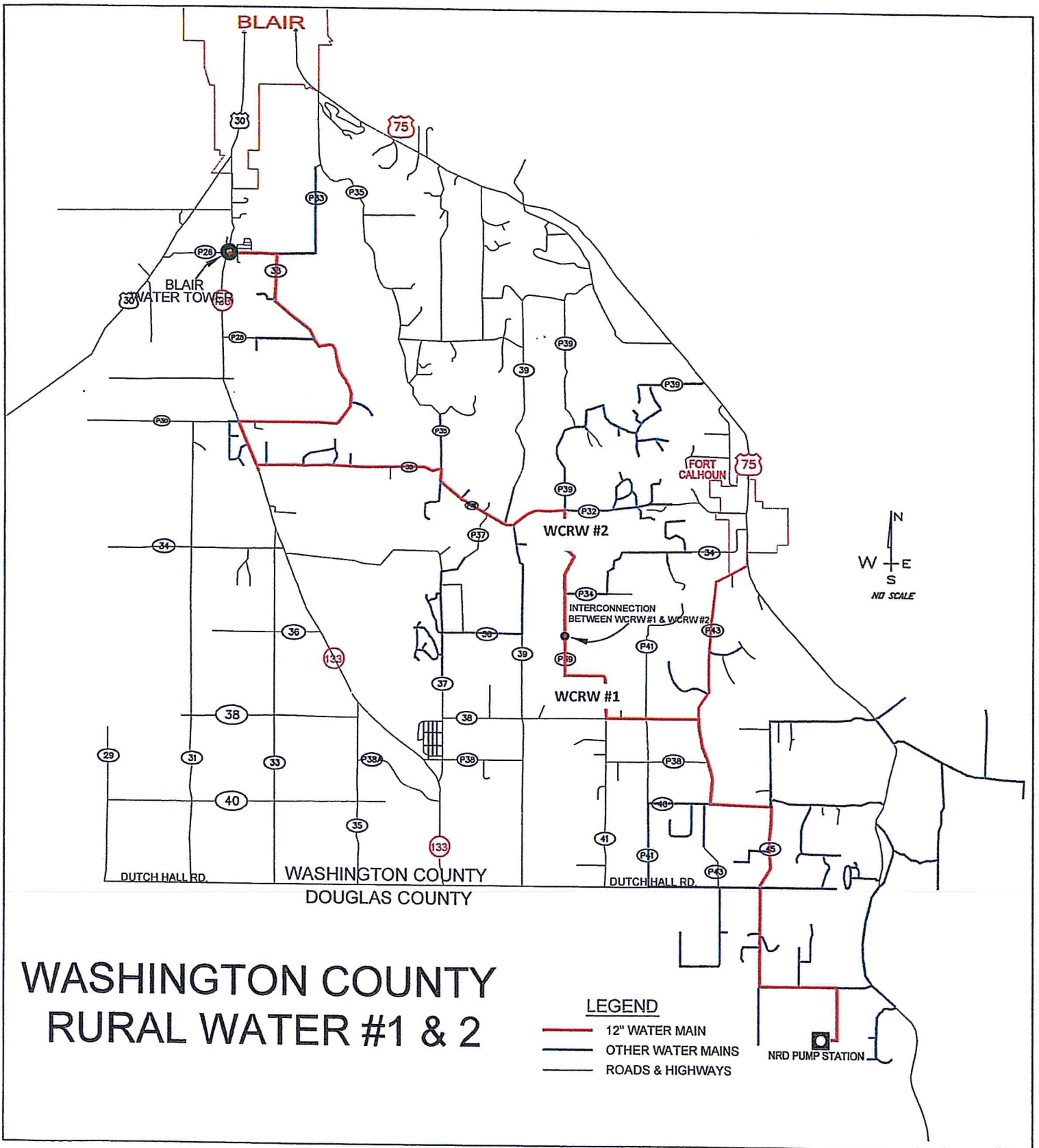
A second alternative could be for the District to use general fund monies for providing a loan to WCRW#2 for an extended period of time. Repayment terms would need to be determined by the Board of Directors.

#### **SUMMATION:**

Historically, the District has had success in the development and operation of rural water systems for over 30 years. Unfortunately, optimism on Washington County Rural Water #2 was short lived due to a number of factors. Most likely it will take several years before this system is capable of standing on its own two legs. It is hoped that in the coming years financial stability will be achieved when new housing starts are in the upswing in this area. The financial merger of WCRW#1 with WCRW#2 will provide that additional time. If this is not successful, refinancing of existing debt service after 2016 may be necessary once again. Failure to provide capital for WCRW#2 in the very near future will result in default of the loan and revenue bonds, resulting in subsequent higher interest rates for the District on any future loans, revenue bonds and general obligation bonds.

**Management recommends that the Subcommittee recommend to the District's Board of Directors that a financial merger of Washington County Rural Water #1 and Washington County Rural Water #2 be implemented commencing in Fiscal Year 2014.**





PROJECTED DRAFT BUDGET FOR F.Y. 2014 -2017  
Washington County Rural Water #2

| REVENUES                                 |    | F.Y. '14   | F.Y. '15       | F.Y. '16        | F.Y. '17        |
|------------------------------------------|----|------------|----------------|-----------------|-----------------|
| CASH ON HAND                             | \$ | 400,000.00 | \$ 171,878.00  | \$ (54,045.00)  | \$ (363,819.00) |
| Water Sales                              | \$ | 140,000.00 | \$ 143,000.00  | \$ 157,440.00   | \$ 161,040.00   |
| Hookup Fees                              | \$ | 17,500.00  | \$ 17,500.00   | \$ 18,500.00    | \$ 18,500.00    |
| Late Charges                             | \$ | 1,750.00   | \$ 1,800.00    | \$ 1,800.00     | \$ 1,850.00     |
| Interest Income                          | \$ | 1,000.00   | \$ 750.00      | \$ 500.00       | \$ 250.00       |
| Misc. Income                             | \$ | 350.00     | \$ 350.00      | \$ 350.00       | \$ 350.00       |
| City/County Reimbursement                | \$ | 357,632.00 | \$ 352,734.00  | \$ -            | \$ -            |
| TOTAL INCOME                             | \$ | 918,232.00 | \$ 688,012.00  | \$ 124,545.00   | \$ (181,829.00) |
| EXPENDITURES                             |    |            |                |                 |                 |
| Vehicle Repairs/Maint.:                  | \$ | 3,500.00   | \$ 4,000.00    | \$ 4,500.00     | \$ 4,500.00     |
| Customer Contract:                       | \$ | 15,000.00  | \$ 15,000.00   | \$ 15,500.00    | \$ 16,000.00    |
| Water Purchase:                          | \$ | 24,000.00  | \$ 24,500.00   | \$ 25,000.00    | \$ 25,500.00    |
| Expenses/Personnel:                      | \$ | 100.00     | \$ 100.00      | \$ 100.00       | \$ 100.00       |
| Information & Education:                 | \$ | 200.00     | \$ 200.00      | \$ 250.00       | \$ 250.00       |
| Bonds Payable:                           | \$ | 345,000.00 | \$ 345,000.00  | \$ 95,000.00    | \$ 95,000.00    |
| Interest Expense:                        | \$ | 94,844.00  | \$ 87,647.00   | \$ 80,189.00    | \$ 75,679.00    |
| Public/Legal Notices:                    | \$ | 100.00     | \$ 100.00      | \$ 100.00       | \$ 100.00       |
| Misc. Expenses:                          | \$ | 500.00     | \$ 500.00      | \$ 500.00       | \$ 500.00       |
| Office Supplies:                         | \$ | 1,000.00   | \$ 1,000.00    | \$ 1,050.00     | \$ 1,050.00     |
| Postage:                                 | \$ | 160.00     | \$ 160.00      | \$ 175.00       | \$ 175.00       |
| Prof. Services/Legal:                    | \$ | 1,500.00   | \$ 1,500.00    | \$ 1,500.00     | \$ 1,500.00     |
| Professional Services:                   | \$ | 4,000.00   | \$ 4,000.00    | \$ 4,100.00     | \$ 4,100.00     |
| Equipment Rental:                        | \$ | 100.00     | \$ 100.00      | \$ 100.00       | \$ 100.00       |
| Proj. Maint. Materials:                  | \$ | 3,400.00   | \$ 3,600.00    | \$ 3,800.00     | \$ 3,800.00     |
| Contract Work:                           | \$ | 15,000.00  | \$ 15,500.00   | \$ 16,000.00    | \$ 16,500.00    |
| Salaries:                                | \$ | 40,000.00  | \$ 41,200.00   | \$ 42,500.00    | \$ 44,000.00    |
| Bad Debts:                               | \$ | 250.00     | \$ 250.00      | \$ 300.00       | \$ 300.00       |
| Bond & Interest Reserve                  | \$ | 197,700.00 | \$ 197,700.00  | \$ 197,700.00   | \$ 197,700.00   |
| TOTAL EXPENSE                            | \$ | 746,354.00 | \$ 742,057.00  | \$ 488,364.00   | \$ 486,854.00   |
| Excess Revenue Over (Under) Expenditures | \$ | 171,878.00 | \$ (54,045.00) | \$ (363,819.00) | \$ (668,683.00) |

TABLE 1

COMBINED DRAFT BUDGET  
FOR WASH. COUNTY. RURAL WATER #1 & #2

**REVENUES**

| ITEM                       | ACCT. # | F.Y. '14        | F.Y. '15        | F.Y. '16        | F.Y. '17        | F.Y. '18      | F.Y. '19      |
|----------------------------|---------|-----------------|-----------------|-----------------|-----------------|---------------|---------------|
| Cash On Hand               | 3000    | \$ 1,100,000.00 | \$ 913,893.00   | \$ 727,485.00   | \$ 462,302.40   | \$ 222,589.40 | \$ 25,083.08  |
| Water Sales                | 3091    | \$ 468,000.00   | \$ 476,580.00   | \$ 523,286.40   | \$ 532,646.00   | \$ 584,617.68 | \$ 593,977.00 |
| Hookup Fees                | 3092    | \$ 45,500.00    | \$ 45,500.00    | \$ 48,100.00    | \$ 48,100.00    | \$ 48,100.00  | \$ 50,700.00  |
| Late Charges               | 3093    | \$ 5,800.00     | \$ 5,900.00     | \$ 6,000.00     | \$ 6,100.00     | \$ 6,200.00   | \$ 6,300.00   |
| Interest Income            | 3110    | \$ 4,500.00     | \$ 2,000.00     | \$ 1,500.00     | \$ 1,000.00     | \$ 750.00     | \$ 500.00     |
| Contrib./Reimb./Cost Share | 3120    | \$ 357,632.00   | \$ 352,734.00   | \$ -            | \$ -            | \$ -          | \$ -          |
| Misc. Income               | 3130    | \$ 1,100.00     | \$ 1,100.00     | \$ 1,100.00     | \$ 1,100.00     | \$ 1,100.00   | \$ 1,200.00   |
| Total Income               |         | \$ 1,982,532.00 | \$ 1,797,707.00 | \$ 1,307,471.40 | \$ 1,051,248.40 | \$ 863,357.08 | \$ 677,760.08 |

**EXPENDITURES**

|                                          |      |                 |                 |               |               |               |                 |
|------------------------------------------|------|-----------------|-----------------|---------------|---------------|---------------|-----------------|
| Vehicle Repair/Maint.                    | 4052 | \$ 7,500.00     | \$ 8,000.00     | \$ 9,000.00   | \$ 9,000.00   | \$ 9,500.00   | \$ 9,500.00     |
| Customer Contract Costs                  | 4080 | \$ 70,000.00    | \$ 70,000.00    | \$ 71,000.00  | \$ 71,000.00  | \$ 72,000.00  | \$ 72,000.00    |
| Water Purchase                           | 4090 | \$ 145,000.00   | \$ 147,000.00   | \$ 149,000.00 | \$ 151,000.00 | \$ 153,000.00 | \$ 155,000.00   |
| Dues & Memberships                       | 4130 | \$ 250.00       | \$ 250.00       | \$ 250.00     | \$ 250.00     | \$ 250.00     | \$ 300.00       |
| Staff Travel & Expenses                  | 4171 | \$ 700.00       | \$ 700.00       | \$ 700.00     | \$ 700.00     | \$ 700.00     | \$ 750.00       |
| Information Programs                     | 4217 | \$ 375.00       | \$ 400.00       | \$ 400.00     | \$ 400.00     | \$ 400.00     | \$ 450.00       |
| Bond Principal Payments                  | 4280 | \$ 345,000.00   | \$ 345,000.00   | \$ 95,000.00  | \$ 95,000.00  | \$ 100,000.00 | \$ 100,000.00   |
| Bond Interest Payments                   | 4290 | \$ 94,844.00    | \$ 87,647.00    | \$ 80,189.00  | \$ 75,679.00  | \$ 71,794.00  | \$ 65,144.00    |
| Public Notices                           | 4311 | \$ 100.00       | \$ 100.00       | \$ 100.00     | \$ 100.00     | \$ 100.00     | \$ 150.00       |
| Misc. Expense                            | 4330 | \$ 1,100.00     | \$ 1,100.00     | \$ 1,100.00   | \$ 1,100.00   | \$ 1,100.00   | \$ 1,300.00     |
| Office Supplies                          | 4331 | \$ 2,000.00     | \$ 2,100.00     | \$ 2,200.00   | \$ 2,200.00   | \$ 2,200.00   | \$ 2,300.00     |
| Photocopier Lease                        | 4334 | \$ 2,900.00     | \$ 2,900.00     | \$ 3,000.00   | \$ 3,000.00   | \$ 3,000.00   | \$ 3,200.00     |
| Postage                                  | 4370 | \$ 420.00       | \$ 450.00       | \$ 480.00     | \$ 480.00     | \$ 480.00     | \$ 500.00       |
| Legal Fees                               | 4392 | \$ 3,000.00     | \$ 3,000.00     | \$ 3,000.00   | \$ 3,000.00   | \$ 3,000.00   | \$ 3,000.00     |
| Professional Services                    | 4400 | \$ 8,000.00     | \$ 8,100.00     | \$ 8,200.00   | \$ 8,200.00   | \$ 8,200.00   | \$ 8,400.00     |
| Equip. Rental                            | 4475 | \$ 100.00       | \$ 100.00       | \$ 100.00     | \$ 100.00     | \$ 100.00     | \$ 150.00       |
| Maintenance Materials                    | 4477 | \$ 8,700.00     | \$ 8,900.00     | \$ 9,100.00   | \$ 9,100.00   | \$ 9,100.00   | \$ 9,300.00     |
| Contract Work                            | 4479 | \$ 24,000.00    | \$ 24,500.00    | \$ 25,000.00  | \$ 25,000.00  | \$ 25,000.00  | \$ 26,500.00    |
| Telephone                                | 4520 | \$ 1,700.00     | \$ 1,750.00     | \$ 1,800.00   | \$ 1,800.00   | \$ 1,800.00   | \$ 1,900.00     |
| Remote Elec. Utilities                   | 4530 | \$ 400.00       | \$ 425.00       | \$ 450.00     | \$ 450.00     | \$ 450.00     | \$ 5,000.00     |
| Pump Station Utilities                   | 4531 | \$ 7,000.00     | \$ 7,250.00     | \$ 7,500.00   | \$ 7,500.00   | \$ 7,500.00   | \$ 8,000.00     |
| Salaries                                 | 4550 | \$ 147,000.00   | \$ 152,000.00   | \$ 159,000.00 | \$ 165,000.00 | \$ 170,000.00 | \$ 175,000.00   |
| Building Maint.                          | 4630 | \$ 250.00       | \$ 250.00       | \$ 250.00     | \$ 250.00     | \$ 250.00     | \$ 3,000.00     |
| Auto & Truck Purchase                    | 4803 | \$ -            | \$ -            | \$ 20,000.00  | \$ -          | \$ -          | \$ 20,000.00    |
| Bad Debt Expense                         | 4900 | \$ 600.00       | \$ 600.00       | \$ 650.00     | \$ 650.00     | \$ 650.00     | \$ 700.00       |
| Bond & Interest Reserve                  | 4998 | \$ 197,700.00   | \$ 197,700.00   | \$ 197,700.00 | \$ 197,700.00 | \$ 197,700.00 | \$ 197,700.00   |
| Total Expense                            |      | \$ 1,068,639.00 | \$ 1,070,222.00 | \$ 845,169.00 | \$ 828,659.00 | \$ 838,274.00 | \$ 869,244.00   |
| Excess Revenue Over (Under) Expenditures |      | \$ 913,893.00   | \$ 727,485.00   | \$ 462,302.40 | \$ 222,589.40 | \$ 25,083.08  | \$ (191,483.92) |

**TABLE #2**