



Sewer Discussion

DATE: Thursday, April 19, 2018

TIME: 7:30 P.M.

LOCATION: Curtis Hall, 1250 Church Road, Wyncote, PA 19095



Agenda

- I. Background and Process
- II. The Results of the Competitive Bid Process
- III. Considerations
- IV. Summary

I. Background and Process



Background & Rationale

- The condition of the Township's sewer infrastructure dictated two things to the Board of Commissioners and Administration:
 - Significant, ongoing and unrecoverable investments were needed to repair or replace aging and inefficient sewage processing across the Township which has resulted in sewage back-up and surcharging along with escalating costs and problems
 - Creative and responsible efforts are needed to reduce growing sewer debt, facilitate necessary inceptor and pipeline repair/replacement and protect the operational and fiscal integrity of the system as well as the community and sewer rate-payers



Background & Rationale

- Since 2014, the Board of Commissioners and Township Administration explored solutions that would mitigate current system shortfalls and position the Township to address expected sewer related operational and fiscal challenges
 - With existing sewer related debt of approximately \$30mm; considering immediate Interceptor repair costs and with substantial anticipated additional infrastructure costs, Cheltenham Township is compelled to pursue a more aggressive, most likely external set of alternative solutions



Process & Result of the Outreach

- Expert outside engineering, financial and legal counsel was enlisted to provide an objective assessment of the options
- Potential buyers/investors were solicited via a Request for Qualification based on industry established criteria for the possible execution of an Asset Purchase Agreement
- Three bidders emerged and participated in a rigorous vetting, full disclosure and collaborative assessment process
- A Request for Bid due March 23, 2018 was issued by the Township

II. The Results of the Competitive Bid Process



Results of the Request for Bid

- After a very thorough and competitive bid process, the Township received a bid from Aqua Pennsylvania Wastewater
 - Bid amount - \$50,250,000
- Aqua's bid is significantly higher than valuations provided by Township Consultants
 - Valuations ranged from \$38mm to \$44mm
- Other potential bidders involved in the process included Bucks County Water and Sewer Authority and Pennsylvania American Water



Highlights - Aqua Bid

- Aqua:

- Provides synergies since Aqua currently provides Township water service
- Believes system-wide replacements of private laterals may be avoided which may provide future savings for rate payers
- Actively supports HB 2075 - allows regulated utilities to replace private laterals
- Has long standing working relationships with Philadelphia Water Department (PWD) and Department of Environmental Protection (DEP)
- Has a plan to reduce flow volume caused by I&I (Infiltration and Inflow) issues and offers timely resolution of the DEP Corrective Action Plan (plan to reduce overflows and backups)
- Indicates that timely capital improvements will result in Cheltenham's ability to add customers thereby enabling growth
- Will adopt Township rates upon closing
- Will now provide one bill for both water and sewer (monthly)



Highlights - Aqua Bid (cont'd)

- Expected that existing base rates will remain unchanged until next rate case (effective in 2022) and can only be modified with PUC approval
 - However, Aqua may impose a surcharge for capital expenditures (DSIC-Distribution System Improvement Charge) prior to 2022 (capped at 5% of bill)
- PUC makes all final determinations of rates through the regulated rate process
- The Office of the Consumer Advocate (OCA) provides another layer of protection for rate paying customers and will intervene on their behalf in Aqua's rate cases. Residents may also file protests with PUC.

III. Considerations



Critical Considerations – Capital and Debt

- Unknowns of future capital costs
 - Current estimates include \$50 million for sewer over the next five years and \$10 million in 2018 for General Improvements, but could deviate significantly based on future mandates and change orders & assumes no additional non-sewer related borrowings
 - Assuming 30 year level annual payments, each new \$10 million bond issue adds approximately \$700,000 of additional annual cost to the Township
- Debt capacity constraints for future sewer and non-sewer capital projects
 - Township near borrowing max as illustrated below
 - Township currently has approximately \$55,750,000 of outstanding debt (up to \$10mm more expected to be issued in 2018)
 - Approximately \$30 million of this is allocable to sewer. No prepayment penalties to pay off, but may require escrows

	1	2	3	4	5	6
State law prescribes borrowing limits	Actual 2018	Projected 2019	Projected 2020	Projected 2021	Projected 2022	Projected 2023
Remaining Borrowing Capacity	35,857,092	29,369,858	22,887,382	16,194,027	9,738,762	3,641,603

- Credit rating – impact to borrowing costs
 - Currently Township has rating of Moody's Aa2
 - High debt levels & borrowing base constraints may cause stress on the rating – lower rating can result in higher borrowing costs



Critical Considerations – Laterals, Synergies, Outside Parties

- Unknowns of future treatment costs from Philadelphia Water Department
 - Approximately 85% of the Township's sewer operating expenditures are determined by Philadelphia Water Department so any PWD changes and mandates will have a large impact on Cheltenham rates
- Sewer laterals
 - If needed to be replaced, estimated average impact to homeowner = \$6,000/house
 - Aqua's proposal mentions potentially being able to avoid system-wide replacement of laterals
- Synergies and economies of scale with same operator coordinating water and sewer for both Aqua and the Township
 - Residents will now receive one water and sewer bill which will be paid monthly
 - Aqua currently has near term plans to replace over 20 miles of water mains in the Township,
 - With Aqua's project management experience, they can coordinate with needed sewer repairs where applicable which results in limited road interruptions and newly paved roads curb to curb when complete
 - Coordinate sewer repair efforts with water main replacements and coordinate with Township on storm sewer inspections while Aqua has street opened doing work



Critical Considerations – Liability Shifting and Oversight

- Reallocation of Township administrative staff to focus on other key initiatives of the Township
- Environmental liabilities shifted to Aqua (unless problem existed prior to closing)
- Shifting all Department of Environmental Protection & Philadelphia Water Department negotiations/issues/demands to Aqua
- Township water has been provided by Aqua for very long period of time
 - Provides performance track record
- Aqua performance oversight
 - PUC, DEP, EPA and other regulatory bodies oversee various aspects of Aqua's performance
 - PUC rate process lasts up to 9 months
 - PUC evaluates Aqua's performance in areas other than rates (response times, etc.)



Critical Considerations – Financial Projections

- Township has been working on long range financial modeling to assist with fiscal planning
- Lack of growth in assessed value is a key contributor to future fiscal challenges
 - Economic development initiatives in the Township are critical but are progressing slowly
 - Limited EDUs are available presently
 - Resolving DEP’s Corrective Action Plan is also critical
- Significant budget deficits could come to fruition in the near term if significant changes are not made
 - High level projection summary below assumes the Township keeps the system illustrating that there will ongoing future financial challenges. However, the Township still faces financial challenges even if the sewer system is sold

1	2	3	4	5	6	7	8
	Final Unaudited:	Budgeted	Projected	Projected	Projected	Projected	Projected
	2017	2018	2019	2020	2021	2022	2023
Total Revenues	41,793,611	44,202,961	43,355,594	44,657,033	45,922,366	47,302,721	49,324,324
Total Expenses	41,716,726	44,202,961	46,534,239	48,743,075	51,029,304	53,589,554	56,170,453
Surplus/(Deficit)	76,885	-	(3,178,645)	(4,086,043)	(5,106,938)	(6,286,833)	(6,846,129)



Critical Considerations — Financial Projections

- For analysis purposes Township and Consultants developed models assuming the Township would keep the system as well as the Township selling the system
- If sold, Township able to payoff all sewer debt –approximately \$30mm
- Due to known future capital investments sewer rates will increase with or without a sewer sale
- If sold, after payoff of all sewer debt, Township will have approximately \$20mm to be used for other purposes such as:
 - Pay off non sewer debt, pension and OPEB funding, or fund budgeted capital projects the Township would otherwise have to borrow for.
 - Further analysis will be completed create a plan to optimize the use of those funds
- If sold, there will be no layoffs of sewer staff. Reallocation within the Highway Department of Public Works will be evaluated

IV. Summary



Summary

- Years of thorough and exhaustive due diligence process undertaken by the Township
- Very competitive process undertaken by the Township
- Aqua owns the Township's water system and has a long proven track record with the Township and,
 - Many synergies will could be realized by the Township with their Project Management experience
 - Major future capital unknowns, PWD issues, environmental issues (DEP issues will now be shifted to a well-qualified operator)
- PUC/OCA governance will add a substantial amount of accountability and oversight
- The Township is facing significant future financial challenges
 - Decision based on quantitative and qualitative perspectives
 - Qualitative – benefits of shifting of risks and refocus of Township priorities (economic dev)
 - Quantitative – impact to resident
 - Careful and thorough evaluation by Township management with input from consultants, Commissioners and public, further public input will be forthcoming
- Township wants to provide the highest quality of life to its residents



Sewer Discussion Supplement #1

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Est. Net Proceeds Calculation

- Bid Price approx. \$50 million
- Est. Sewer Debt Payoff and Transaction Costs approx. \$30 million
- Est. Net Available to be Redeployed approx. \$20 million
- If the sewer transaction is approved, extensive planning and analysis will occur to determine the optimal deployment of the proceeds based on the Township's long term goals and objectives



Current Sewer Budget

- Based on 2018 budget:
 - Total Sewer Revenues approx. \$9 million
 - Total Sewer Expenses approx. \$7 million
 - Sewer Surplus approx. \$2 million



Critical Considerations – Capital and Debt

- Unknowns of future capital costs

- Current capital plan attempts to bring system in compliance with mandate to reduce flows to 18 CSF
- Potential need to do additional major capital repairs beyond the current capital plan if the actions taken are not sufficient
- Options might include an equalization tank and/or new sewer service line to PWD to bring system in compliance
- Costs could be an additional \$50 to \$100 million depending on the outcome of the current capital plan
- Township increasing debt service and repair/replacement costs substantially expected to exceed the traditional sewer surplus



Retain the System— Fiscal Considerations

Status Quo

2018
Current Sewer Debt:
Approx. \$30 million

2018-2019
Committed sewer
repairs/replacements
\$7-\$15 million

2018
Sewer surplus
Approx. \$ 2 million

Moving Forward with Mandated Corrections

2018
Current Sewer Debt:
Approx. \$30 million

PWD cost increases of
5%-10% equate to
\$200,000-\$400,000 of
additional operating costs
annually

2018-2019
Committed sewer
repairs/replacements
\$7-\$15 million

Potential need for \$30
million equalization tank
and/or new line to PWD

Sewer rate increases
necessary to meet
additional cost burden

2019-2024
Required
repairs/replacements
\$35-\$50 million
& associated debt service

Need to commit to
ongoing annual pay go
maintenance which is not
currently happening



Sale to Aqua— Fiscal Considerations

~~2018
Current Sewer Debt:
Approx. \$30 million~~

2018-2019
Committed sewer
repairs/replacements
\$7-\$15 million

~~2018
Sewer surplus
Approx. \$ 2 million~~

Moving Forward
with Sale

Approx \$20 million of
net proceeds to be
redeployed for other
purposes

2019-2024
Shift Required
repairs/replacements
\$35-\$50 million
to Aqua

Shift obligation for
potential need for \$30
million equalization tank
and/or new line to PWD to
Aqua

Rates determined via
PUC process



Summary

- Maintain Township ownership

- Cheltenham Township burdened with sizable growing costs
 - System maintenance
 - Debt service
 - PWD treatment costs
 - Costs expected to exceed the traditional surplus

- Sell system to Aqua

- Steady but controlled (via PUC) sewer rate increases
- Expectation for residents to have reduced lateral replacement costs based on Aqua representations
- Township relieved of sewer fiscal burdens & shifts risks to Aqua
- Township fiscal health and creditworthiness positioned for stabilization