



Town of Oak Island

2014 Water and Sewer Fund Budget, Review of Budget
Balancing Strategies and Long-Term Financial Plans

June 25, 2013

Introduction and Presentation Outline

DEC Associates - Firm Background and Experience

Presentation Overview

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Presentation Overview

The Utility System Has Major Challenges Requiring Significant Change in Both the Short and Long-Term Financial Plan and Capital Maintenance of the System

Town Management Professionals Are Currently Pursuing Alternatives to Meet the 2014 Budget Needs and Set New Directions for Council Approval of Future Plans and Strategies

Solutions for the System Challenges Are Available; However, Consistency and Evenness in Implementing the New Financial Plan Is Essential

Communication and Interchange of Questions and Answers Will Provide Needed Information to Town Council, Management and the System Rate Payer

History of Sanitary Sewer Project and Creation of Significant Long-term Debt



- Overall Project Cost and Project Budget Changes Have Created a Level of Debt Requiring Adjustment to System Finances
 - First Capital Project Ordinance Reflected a Project Cost of Approximately \$57 Million, Current Cost Estimates Approximate \$130 Million, an Increase of Over 128%
 - Multiple Bond Issuance and Other Sources of Funds Created Additional Cost and Concern Over Capital Projects Planning and Execution
- Changing Conditions Have Made Prior Financial Planning and Rate Changes Inadequate to Sustain Required Revenue Bond Coverage Without Significant Rate Changes in the Future and Constant Monitoring to Meet Bond Covenants
 - Increased Reliance on Assessment Revenues in the Past Created “Accumulated Need” for User Fee Rate Changes
 - 2010 Bond Covenants Were Not Fully Met Creating Essentiality of Future Full Compliance
- Sanitary Sewer Assessments Based Upon Much Lower Capital Cost Producing Lower Revenue Than if Based Upon Much Larger Final Project Cost - Higher Revenue Could Have Created Potential to Call Debt Early

History of Sanitary Sewer Project and Creation of Significant Long-term Debt



- Levels of Outstanding Debt Create Little Capacity for Future New Money Issuance
- Future Capital Improvements Funding Source Needed to Implement a Capital Improvement Plan
 - Without New Debt Capacity Paygo or Grant Funding (if available) Will be Primary Source for Capital Improvements
 - Current Financial Model Projects Some Cash Flow Available for Capital in Future Years - With Projected Rate Increases - Amount Projected as Available Likely Not the Full Amount Needed

Changes to Capital Funding Sources Leaves an Approximate \$3.5 Million Funding Source Need That Must be Addressed in the 2014 Capital Project Budget - Methods to Meet the Need Could Impact User Rates and Charges in 2014 Significantly Without Innovative Solution

Conditions Creating Current Financial Challenges and Need for Solutions



- Capital Project Cost Increases Resulting in Large Debt Payments
- Delayed Project Completion, Customer Connections and User Charge Revenue Generation Produced Larger Use of Wastewater Assessments Sooner Than Anticipated
- Decreasing Water Usage and Inadequate Account Growth
 - Original Projected Build Out in 2017
 - 2008 Estimate 370,000,000 to 380,000,000 Annual Gallons
 - 2014 Estimate 280,000,000
 - Usage Measurement Issues Remain and Are Being Worked On
- Economic Downturn and Potential for Second/Retirement Home Real Estate Market Recovery as a Means to Increase Usage
- Assessment Revenue Lower Than Final Capital Cost Would Have Permitted

All of the Forgoing Challenges Created Assumptions in the FFEs That Have Not Been Achieved

Conditions Creating Current Financial Challenges and Need for Solutions



- Need for Policies and Means to Improve Collections of User and Other Fees
- Staffing Changes and Need for Improved Technology and System Software
- New City Management
- Need to Find the Final Funding Source for the Capital Budget - Fill the Capital Funding Gap
- Funding Future CIP Needs Have Not Been Defined With Paygo Sources a Likely Solution

Solutions for Financial Challenges Exist - Now the However; Within a Planning and Execution Framework Consistent With Borrowing Covenants and Sound Business Practices to be Outlined Later in the Presentation

2014 Operating Budget Revenue Raising Options



- Assessment Revenues Currently Accumulated Are Needed as Operating Revenues for 2014 to Temporarily "Abate" Other User Charge Increases for 2014
 - Prior Year User Rate Increases Were Not Planned at a Level to Diminished Current Need for Assessment Revenues, a Source That Will End in 2020, and
 - Future Plans Must Address How Assessment Revenues Will Be Replaced as Collections Become Less in the Future
- Assessment Revenues Cannot be Used as the Source to Fill the Gap for the Capital Budget Replacement Funding Source Without Increasing Other User Charges Dramatically
- Borrowing Is Not Available as the Replacement Funding Source for the Capital Budget Due to the High Current Level of Outstanding Debt

Temporarily Lending Cash from the Occupancy Tax Fund Creates a Method to Fill the Capital Funding Gap and Reduce the Impact on 2014 User Fee Increases

2014 Operating Budget Revenue Raising Options



- Three Scenarios Have Been Identified to Address the Capital Funding Gap and Meet Coverage Requirements for the 2014 Budget
 - Fund the Capital Funding Gap from Currently Accumulated Assessment Revenues - Requires an Across the Board User Fee and Sewer District Fee (SDF) Rate Increase of Approximately 36%
 - Fund the Capital Funding Gap from a Temporary Cash Loan from Occupancy Tax Fund and Repay Temporary Loan Over an Approximate Seven Year Period from 2.5 Cents of Property Tax Not Reduced in the General Fund Budget for 2014 - Requires an Across the Board User Fee and SDF Rate Increase of Approximately 10%
 - Fund the Capital Funding Gap from a Temporary Cash Loan from Occupancy Tax Fund and Repay Temporary Loan Over a Ten Year Period from an Increase in User Fees - Requires an Across the Board User Fee and SDF Rate Increase of 11.75%
- These Scenarios Will Meet Only 2014 Budget Needs and Future Rate Increases Will Be Necessary

Even With an 11.75% Rate Increase the 2014 Budget Will be Balanced by Non Operating Revenues that Total Over 36% of Total Revenues, a Level Not Sustainable into the Future

At This Rate Increase Level the Rate Covenant Test Will be Approximately 1.05 Times With 1.00 Times the Minimum to Meet Bond Rate Covenants

Need for On-Going Revenue Monitoring and Rate Adjustments to Meet Coverage



- Due to the "Thin" Revenue Bond Coverage After the Planned 2014 Rate Increases Revenue Collections Compared to Plan Will Have to be On-Going
 - Quarterly Monitoring is Recommended for Both Revenue Collections and Consumption Billed
- To the Extent Actual Collections Are Below Projections Mid-Year Rate Increases Could Become Necessary in Future Years
 - Bond Covenants Must be Met and the Debt Service Covenant Is Heavily Impacted by Collections
 - Since Debt Service Cannot Currently be Lowered Collections Have to Provide the Cash Flow Variable
- As Previously Addressed, Assessment Revenues Have Bridged the Gap on User Charges in the Past, Less Revenue Will be Available for Future Years and in 2020 Current Assessment Revenue Ends - Hence the Need for User Fees to Meet Annual Projections
- System Fund Balance Levels Need to Grow to Provide for Coverage
- Other

Future Actions and Events Potentially Improving the Financial Status of the Fund



- Increase Usage and Improved Community Economics, Especially Tourism and Real Estate Economies
- Potential for Bond Refunding - Likely Several Years Away
- Extraordinary Sources to Retire Debt?
- Continued Prudent Budgeting and Spending for Operating Costs
- Others Actions/Events

Future Actions or Events Can Have Meaningful Impacts on the System Finances, a Number Are Outside the Control of the Town and May Require Assistance of Others

Long-Term Solution Planning



- Move to Next Level of Financial Planning
- Create Plans and Strategies to Implement Some of the Previously Addressed Measures
- Evaluate Assessment Process and Ability to Implement Changes
- Other Elements of Planning

Conclusion

- Final Questions
- Next Steps?