

**State Water Infrastructure Authority
 Viable Utility Reserve Committee
 June 25, 2020 Meeting
 Agenda Item D – Distressed Criteria**

The Division is presenting to the Viable Utility Reserve Committee the draft distressed unit criteria. These criteria will be used to better target assistance to those that are non-viable or most at risk of becoming non-viable. In addition, should the viable utility reserve grant program be realized, the criteria could be used, in conjunction with the criteria developed by the Local Government Commission, to work with distressed units.

Criteria development includes financial criteria that, if the viable utility reserve grant program becomes law, the Authority has agreed to defer to the Local Government Commission. However, staff are providing some financial criteria for context. Note that the criteria will be used for outreach and/or the distressed unit processes and in those efforts, additional information may indicate a unit is viable or is a higher priority for assistance.

In this version of the criteria, weighting has been added to certain parameters and as a result points are used in lieu of a binary system (Yes or blank). Certain changes also reflect the statutory language (e.g., transfers out). The following table list the criteria in the staff’s working draft:

Criteria	Weight	Notes
Service Population	1	One of five required criteria in the proposed viable utility reserve legislation. System serves less than 10,000 customers based on population (actual service population may be slightly different).
Transfers Out in last five years	1	One of five required criteria in the proposed viable utility reserve legislation. Legislation includes qualifications on the transfers out of the enterprise fund – two or more of the preceding five fiscal years without maintaining a reserve fund sufficient to provide for <ul style="list-style-type: none"> • operating expenses, • capital outlay, and • debt service. The draft criterion uses whether there is a transfer out in 2 of last 5 years <u>AND</u> the following data points to meet the legislative language: <ul style="list-style-type: none"> • Surplus < 0 <u>OR</u> • DSCR < 1.1 for existing debt or a test project if the unit has no debt
Transfers In last five years	1	One of five required criteria in the proposed viable utility reserve legislation. Transfers into Enterprise Fund in 2 of last 5 years
Operations and Maintenance		One of five required criteria in the proposed viable utility reserve legislation. Several parameters are used for this including <ul style="list-style-type: none"> • DW Compliance • WW Compliance • Moratoria These parameters and weighting are discussed in more detail below.

Criteria	Weight	Notes
Annual debt service disproportionate to annual revenue	1	One of five required criteria in the proposed viable utility reserve legislation. Debt Service Coverage Ratio (DSCR) of less than 1.1 is used to meet this aspect. $(\text{Operating revenues} - \text{operating expenses excluding depreciation}) / (\text{principal} + \text{interest payments}) < 1.1$
Unit Assistance List	3	When considering the Unit Assistance List (UAL), only internal control issues are used to reflect organizational capacity. UAL issues related strictly to financial issues are not considered as they are likely redundant to other financial criteria considered.
Revenue Outlook	6	In previous discussions with the Committee, population change was discussed as a secondary parameter. In the draft criteria it is used in combination with high rates to give an indication of the utility's ability to raise revenue in the future. The criterion is met when both rates are high (meets high rates criteria) and population growth is low or negative. Population change to trigger the criterion is proposed to be <0%; however, note that the state average is 4.4%.
Affordability	1	In the Committee meeting on May 21 st , there was a desire to include overall economic condition of the area served by the utility. The criteria now include use of the existing affordability parameters. The criterion is exceeded if the area served exceeds ≥ 4 of the 5 affordability parameters (for state grants it is exceeded at least 3 of 5).
DW Compliance	1	5 years of Public Water Supply Section data evaluated. Criteria is <ul style="list-style-type: none"> > 4 MCL violations over 5 years, or >0 Open Treatment Technology Violations
WW and CS Compliance	1	5 years of data evaluated including NPDES, non-discharge facilities, and collection systems. A change from the last version is that all wastewater compliance is combined into one criterion. Systems with the greatest number of the following indicators were identified as at risk based on compliance: <ul style="list-style-type: none"> Number of Limit violations over 5 years (top 20%), or % of inspections that resulted in violations (>50% violations) # of SSO violations over 5 years (top 20%) #SSOs/mile of collection system (top 20%)
Flow Moratorium	2	Currently on Division of Water Resources Moratorium list for <ul style="list-style-type: none"> Statutory moratorium 90% rule
Rates	1	Rates are considered when considered very high. <ul style="list-style-type: none"> The bill for 5,000 gallons for both water and sewer service is > \$100 The bill for 5,000 gallons for water service is > \$50 for water-only providers The bill for 5,000 gallons for sewer service is > \$60 for sewer-only providers

Criteria	Weight	Notes
Density - Water Distribution System	1	Infrastructure criteria that reflects ability to operate as an enterprise system when the system has few customers per unit of infrastructure. The threshold is < 100 service population / mile of pipe.
Density - Sewer Collection System	1	Infrastructure criteria that reflects ability to operate as an enterprise system when the system has few customers per unit of infrastructure. The threshold is < 100 service population / mile of pipe.
Revenue sufficient to cover expenditures (including debt service)	1	This is a financial indicator for context at this time. This parameter examines whether the utility generates sufficient revenue to cover operating expenditures and debt service. The criterion is exceeded when the utility does not generate any surplus revenue. Surplus (Deficit) = Operating Revenues - ((Operating Expenses-Depreciation)+Long-term Debt Service) < \$0
Debt Service Coverage Ratio for test debt service	1	This is a financial indicator for context at this time. Similar to DSCR but covers systems <u>that do not have debt</u> and whether revenue is sufficient to finance a basic project (debt service for a \$1 million project over 20 years). The same DSCR threshold is used for this criterion as the DSCR above.
Operating Margin	1	This is a financial indicator for context at this time. Similar to surplus revenue above but it includes depreciation but not debt service. A negative operating margin is the threshold.
Percent Depreciation	1	This is a financial indicator for context at this time. The provides some indication of the remaining useful life of the infrastructure and the scale of potential needs in the system.