

Lehigh County Authority & City of Allentown
July 20, 2020 – LCA Board of Directors Meeting



Allentown Water & Sewer Lease: A Renewed Partnership Approach

Our Water, Our Future!

Public Comments / Questions

Email: info@lehighcountyauthority.org

- Include your name and where you live
(municipality only – street address not necessary)
- Comments will be read out loud after the presentation!

Live (in meeting) – after presentation

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Presentation Overview

- Lease Background & History (2013-2018)
- Components of a Renewed Partnership
- Partnership Details
- Anticipated Results
- Next Steps



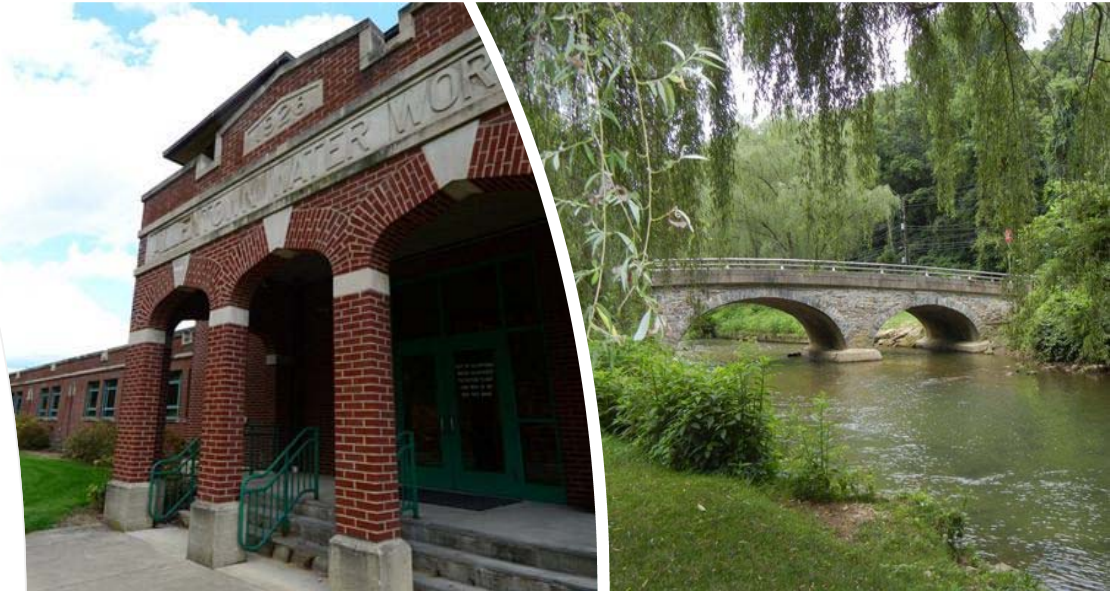
Lease Background: 2012-2013

- City's desire to address its financial concerns
- Competitive bidding process
- Upfront payment + ongoing Annual City payment
- 50-year lease to operate water & sewer systems
- City operating standards and ongoing oversight
- Rate control throughout the lease term



LCA's Core Principles for Getting Involved

- Lease would have to stand on its own merits due to heavy debt burden
- Protect existing LCA existing assets and customers
- Work toward realizing regional approach / economies of scale
- Leverage system interconnections & working relationship with City staff
- LCA's non-profit status & local focus will bring value in the long run!



Bid Results & Resulting Bonds

- LCA and 7 other for-profit bidders
 - LCA's bid: \$220 million upfront plus \$500,000 annually
 - Next highest bid: within 5%

 - LCA Bond Issue: \$308 Million to pay for...
 - Upfront payment
 - Initial operating reserve
 - Required bond reserves
 - First block of capital funding
 - Transaction & transition costs
-

LCA's First Five Years (2014-2018)

- Lease revenues miss the target
- City system capital improvement needs are higher than expected
- Legal disputes compound problems



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Impact of Lease Challenges

- Decreased ability to fund system improvements
- Increased risk to system operations
- Aging infrastructure issues unresolved
- Risk of lowered service standards
- Lease's financial viability at risk
- Deteriorating relations between LCA & City
- Outlook: Customers will pay even more if challenges aren't resolved!


Important to remember... The public's health, the quality of our local waterways, and our region's economic future all depend on having a sustainable water and sewer system!

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Despite Challenges, Positive Outcomes!

- Top priority system improvements have been completed
 - LCA continuing City's tradition of operational excellence
 - Many examples of City / LCA collaboration on new challenges and regulatory changes
 - Enhanced regional collaboration on sewer capacity / wet-weather issues
 - Agreement that system improvements are needed to address aging infrastructure
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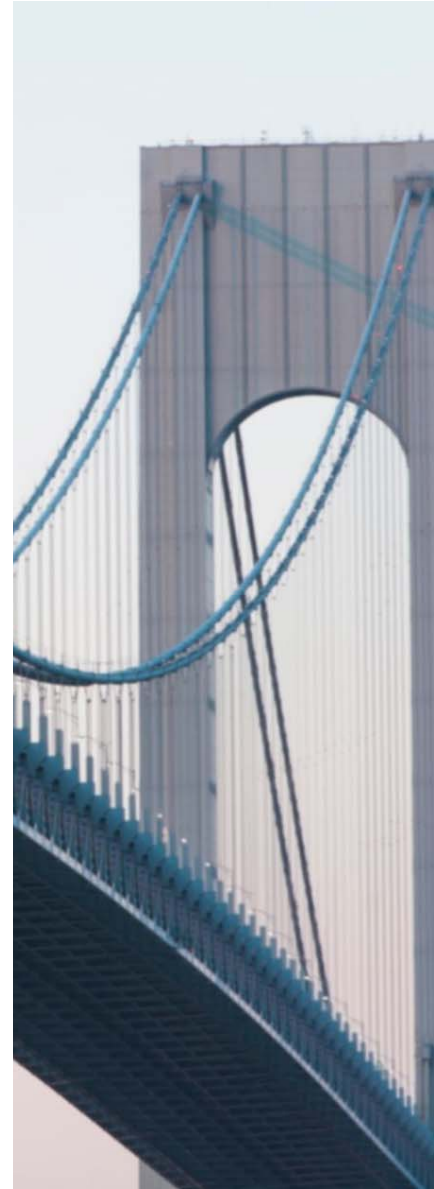


City Water / Sewer System Upgrades Needed (10-Year Outlook – 2021-2030)

- Water Filtration Plant = \$47M
- Wastewater Treatment Plant = \$39M
- Water Main Replacements = \$49M
- Sewer System Rehab = \$15M
- **Total System Need = \$150M**



2019:
Allentown &
LCA agree to
seek solutions



Negotiating Solutions: Overarching Goals



Financial sustainability of LCA



Permanent solutions to avoid future disputes



Financial capacity to fund system improvements when they are needed



Long-term rate stability for Allentown customers



Renewed partnership approach between LCA and the City

Major Building Blocks of New Agreement

Meeting Revenue Requirements	Upgrading the Water & Sewer System	Enhancing our Partnership
City Rates & Future Rate Relief	Capital Improvements & Funding Approaches	Dispute Resolution
Water Supply & Treatment: Equitable Cost-Sharing	Sewer System Rehabilitation	Additional Mutual Support

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First Building Block: Meeting Revenue Requirements

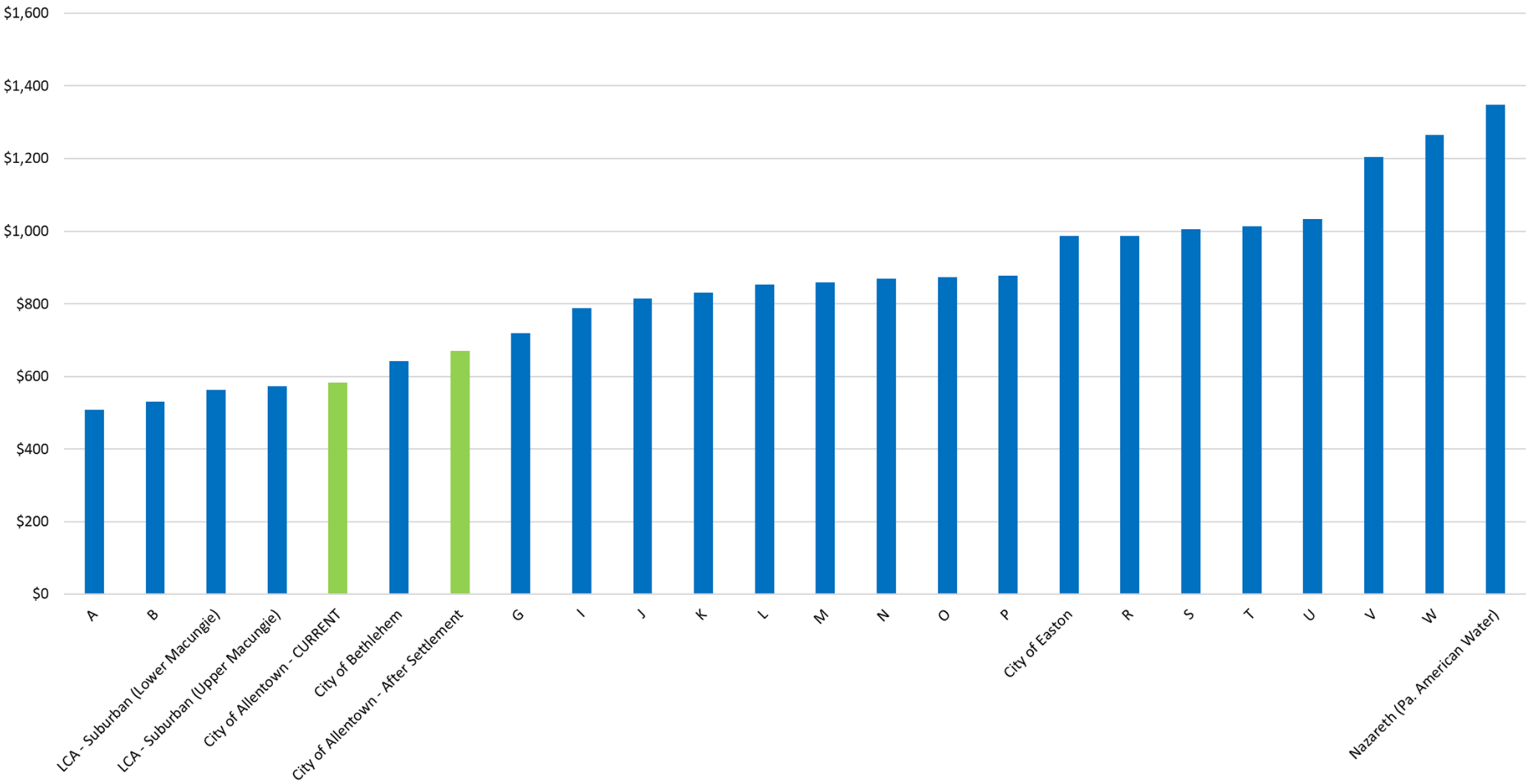


City Rates – Phased Increases, Future Relief

Part 1 – Phased Rate Increases

- Using tiered fixed charge included in Lease agreement
 - Phase in higher fixed charge over 4-year period
 - First phase begins October 1, 2020 → \$88 per year impact
 - By 2024 → \$176 per year total impact, plus normal inflationary increases
 - Annually → Normal inflationary & project cost increases
 - January 1, 2022 → Increase of \$44 per year
 - January 1, 2024 → Increase of \$44 per year
 - No change in billing cycle / frequency during transition
 - If future change to monthly billing is desired, no additional cost to City customers
-

Lehigh Valley Water & Sewer Rate Comparison (Data from 2019-2020)
 24 communities in Lehigh Valley - average annual residential water & sewer bill (5000 gallons per month)



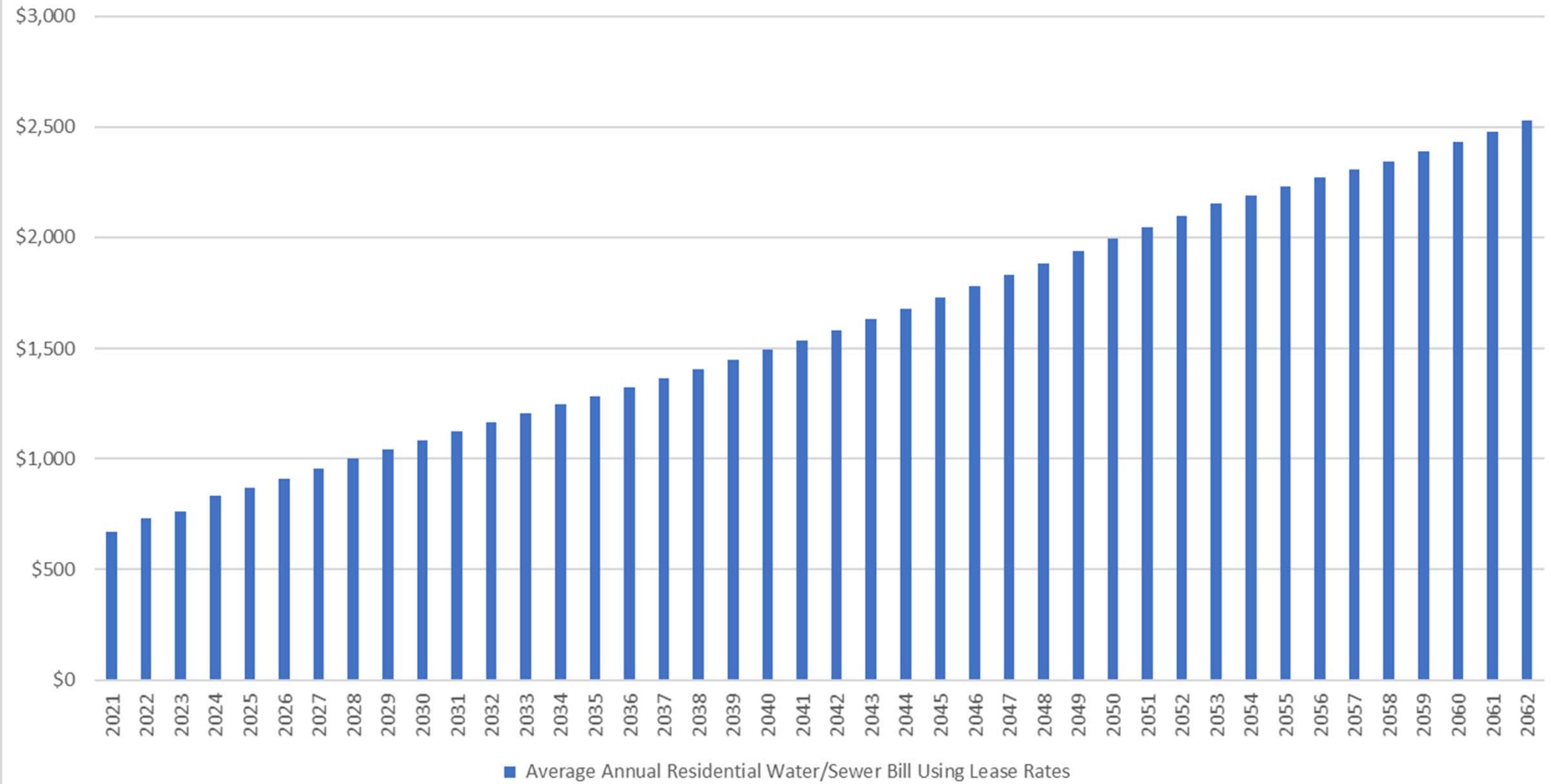


City Rates – Phased Increases, Future Relief

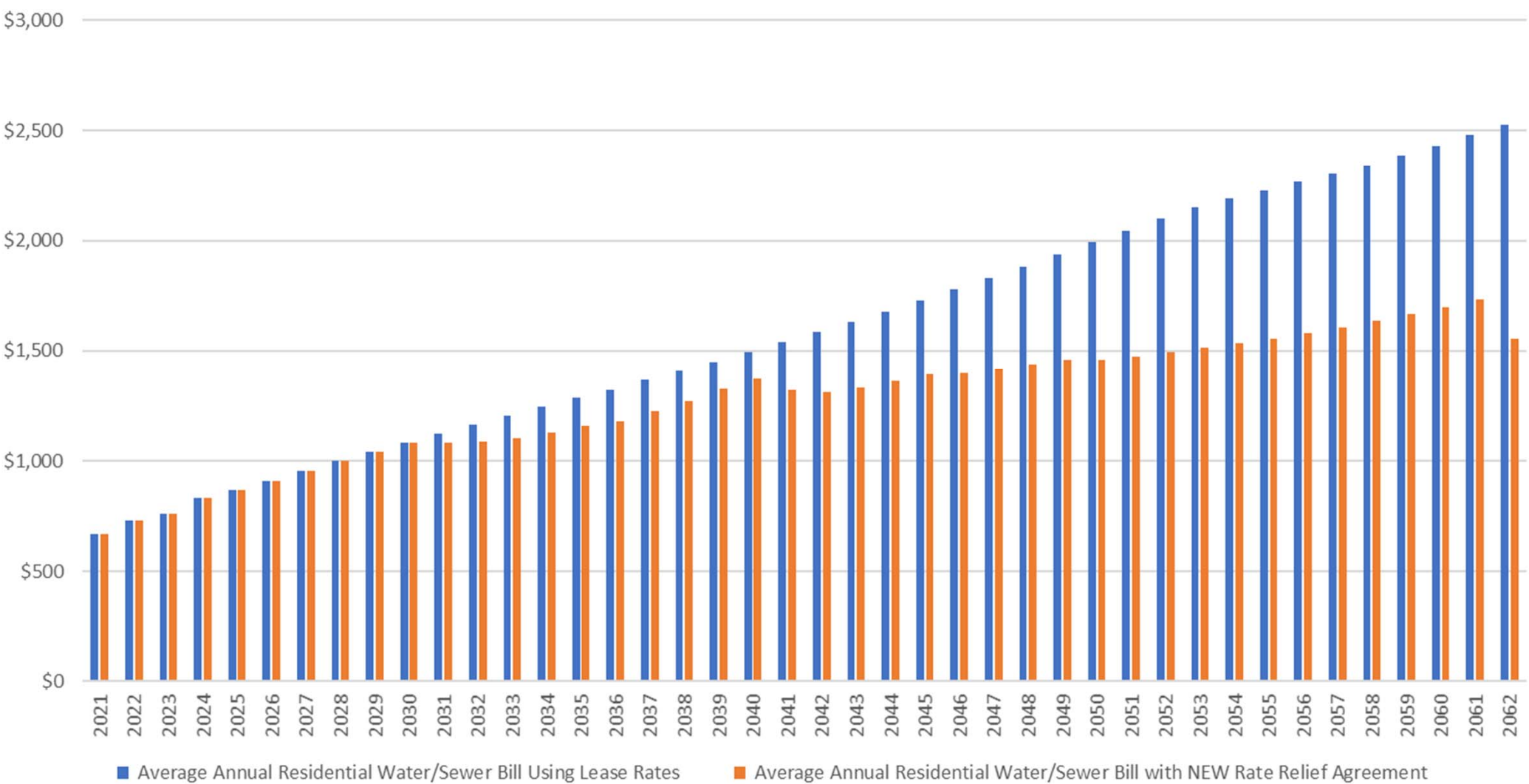
Part 2 – Future Rate Relief

- NEW term of agreement between LCA and Allentown!
 - Rates to City customers will be frozen or reduced after LCA hits key financial targets:
 - Adequate capacity to complete future system improvements (based on then-current plans)
 - Enhanced bondholder protection achieved (debt service coverage ratio ≥ 1.70)
 - When? Depends on economic conditions & project costs
 - Bond refinancing may allow rate relief to happen sooner
 - City and LCA will review together annually
-

Projected Customer Water / Sewer Bill Using Lease Rates

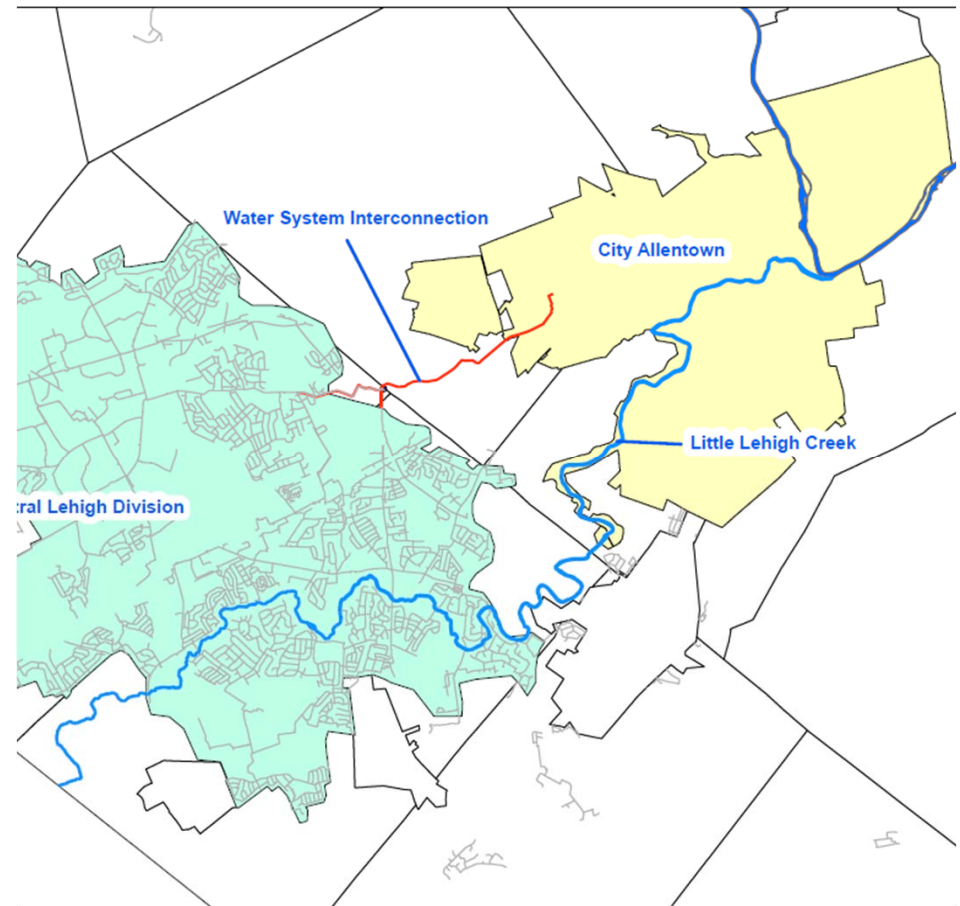


EXAMPLE ONLY - Possible Customer Impact with NEW Rate Relief Agreement



2009 LCA Bulk Water Supply Agreement Updated

- Key Principles:
 - Water supply costs shared by all users
 - Supports watershed-based approach to supply management
- New bulk rate for LCA's Suburban water purchase based on...
 - All water treatment costs
 - Proportionate share of capital costs
 - Lease debt **not** included
- Rate impact to LCA Suburban customers TBD in future budgets
- Agreement extended to end of Lease



Expected Results:
2009 LCA Bulk
Water Supply
Agreement
Update

- Equitable cost-sharing = increase in LCA's City Division revenues
- Revenue increases = earlier implementation of rate relief is possible
- Proportionate cost-sharing for water treatment plant improvements = lower capital cost recovery charges to City customers
- Long-term watershed approach to supply management!

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Second Building Block: Upgrading the Water & Sewer System



Adjustments to Capital Improvements Program

- Small adjustments to support alternative financing approaches
- Language clarified to help avoid future disputes about cost recovery
- LCA will set aside up to \$2 million to be available to address future regulatory changes
- **Cost recovery for major projects no longer based on PUC “equity rate of return” (currently 9.75%) – LCA will use current bond rate of 5.45%**
- **Four-year reduction in water main replacements, increase in leak detection**
- **Collaboration and commitment to complete sewer system rehabilitation**

Deeper Dive: Review of Cost Recovery for Capital Projects

- Lease structured to build cash through rate increases to support capital improvements
- As cash is used, rates are increased to recover the cost of projects, so new projects can be completed
- Lease includes a “rate of return” equal to Pa. Public Utility Commission allowable charge for private, for-profit utilities (currently 9.75%)
- LCA will cap the “rate of return” at 5.45% for all future projects
- ***Remember, these charges can be frozen / eliminated when Rate Relief kicks in!***

Example: Hypothetical Major Capital Project

Project Cost: \$10,000,000 Cost Recovery Period: 20 Years

Lease Terms:

- PUC Rate of Return = 9.75%
- Annual Charge to City Customers: \$1,155,000
- Impact to Average Customer: \$19 per year
- 20-Year Impact: \$380

NEW Terms:

- LCA Rate of Return = 5.45%
- Annual Charge to City Customers: \$833,000
- Impact to Average Customer: \$14 per year
- 20-Year Impact: \$280

A \$5 per year rate reduction may seem small, but the savings will compound as more projects are completed!

Deeper Dive: Main Replacement Projects & Leak Detection



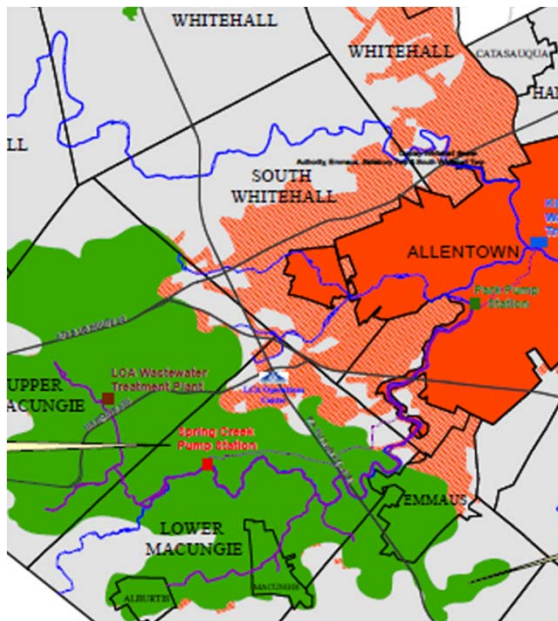
During four-year phase-in period for new rates (2021-2024):

- Water main replacements reduced to 1 mile per year
- LCA leak detection activity will increase to 165 miles per year

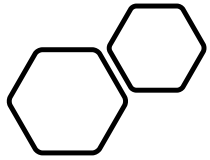
Impact:

- Supports phasing in of new rates over time by lowering LCA costs
- Lower capital improvement costs added to City customer bills
- Water system fully evaluated for leaks more frequently
- Short-term reduction in main replacements, then reverting back to normal 2 miles per year to address aging infrastructure

Deeper Dive: Commitment to Sewer System Rehabilitation



- Allentown’s Kline’s Island Wastewater Treatment Plant provides service to 15 municipalities.
- City of Allentown and LCA are the two largest “customers” of the treatment plant – making up about 75% of the sewer flows in the system
- Lease requires City to complete work committed to EPA and DEP to address wet-weather concerns that were subject to Administrative Order (projects details in the Regional Flow Management Strategy)
- **LCA agrees to continue the City’s progress after the City’s obligations are complete**
- LCA and City will continue to be partners to lead regional efforts to address wet-weather issues and long-term sewer capacity needs



Impact of Sewer System Rehab Agreement



**ADDRESSES AREAS OF THE LEASE
THAT ARE UNCLEAR ABOUT THE EPA
ADMINISTRATIVE ORDER**



**REMOVING LEAKAGE FROM THE CITY
SEWER SYSTEM WILL SUPPORT
ECONOMIC DEVELOPMENT IN THE
CITY AND REDUCE FUTURE COSTS**



**ANNUAL PROJECTS WILL BE SIZED TO
REDUCE RATE IMPACTS TO CITY
CUSTOMERS**

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Third Building Block: Enhancing our Partnership



Dispute Resolution

- All legal disputes withdrawn & resolved
- Allows LCA and City to focus on system operation and improvements
- Recognizing value our partnership brings to the region!



Additional Mutual Support



Cost-sharing for retiree health benefits (LCA pays \$306,000 per year for 2021-2024 to cover City's future liability)



LCA contributes \$400,000 per year to help defray City's water and sewer administrative and regulatory expenses



Agreement on options we will explore together before the Lease ends in 2063 (Lease is currently silent on this issue)

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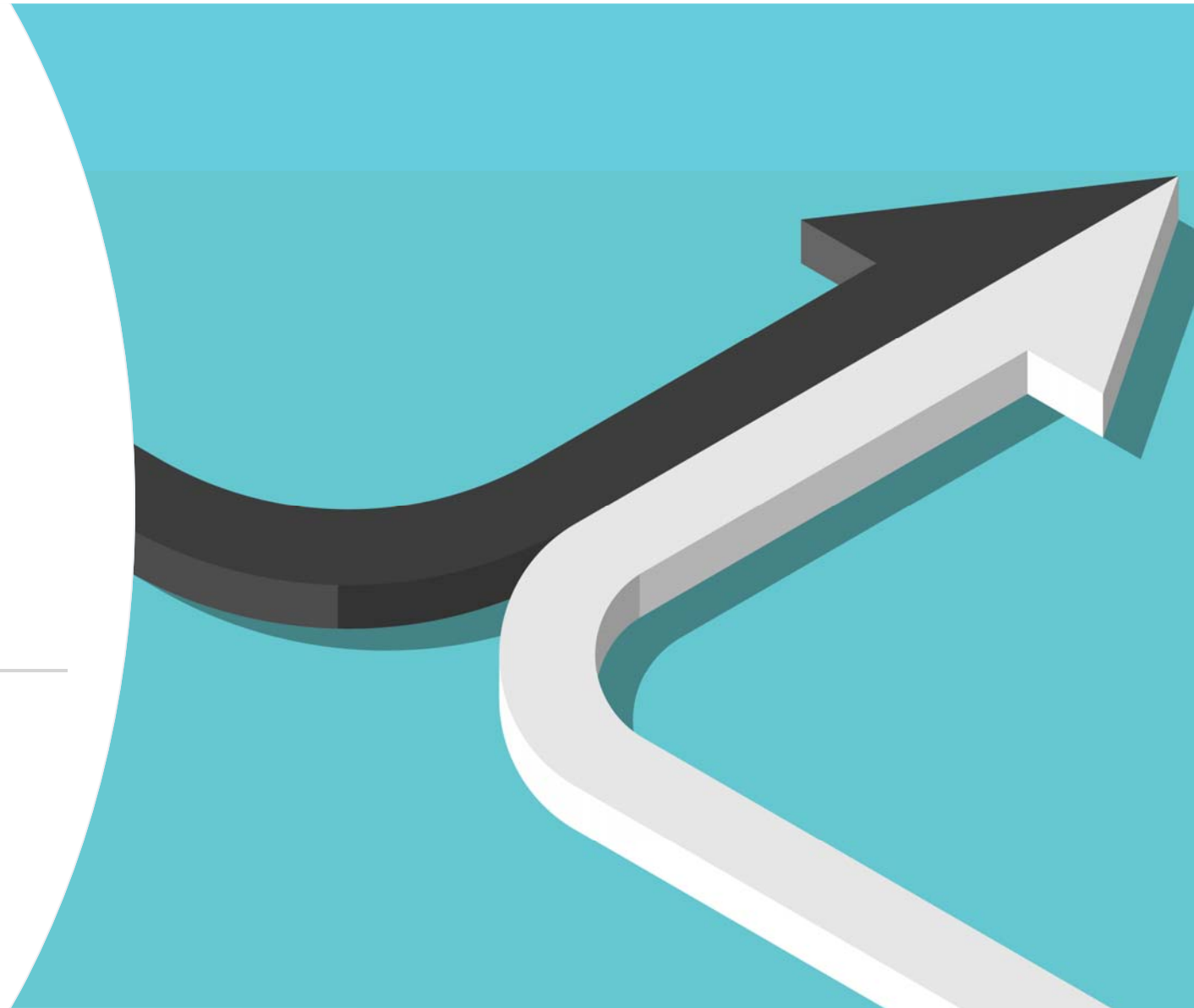
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Results of Renewed Partnership



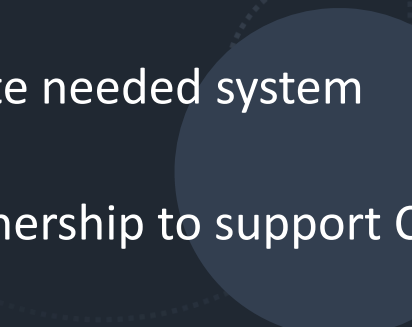


Summary of Expected Results



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- Customer rate impact phased in over 4-year period
 - Significant opportunity for future rate relief
 - Equitable distribution of water treatment costs to all users
 - Regional approach to water supply and sewer capacity management
 - Financial capacity to complete needed system improvements
 - City and LCA working in partnership to support City customers!
- 

Anticipated Lease Financial Performance (2021-2030)

Allentown Water / Sewer Lease - Lehigh County Authority Cash Flow (2021-2030)

Utilizing terms of renewed partnership agreement between LCA and the City of Allentown

	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
Operating Revenues (1)	\$ 42,316,027	\$ 45,147,658	\$ 46,562,232	\$ 50,020,030	\$ 51,505,800	\$ 53,997,355	\$ 56,209,379	\$ 58,354,889	\$ 60,369,437	\$ 62,511,341
Operating Expenses	\$ (19,398,000)	\$ (19,973,000)	\$ (20,565,000)	\$ (22,037,643)	\$ (21,932,766)	\$ (22,585,943)	\$ (23,258,211)	\$ (23,947,608)	\$ (24,655,174)	\$ (25,383,950)
Non-Operating Revenues	\$ 775,600	\$ 787,400	\$ 800,200	\$ 813,000	\$ 826,800	\$ 840,600	\$ 854,600	\$ 868,600	\$ 882,600	\$ 896,600
Non-Operating Expenses (2)	\$ (1,225,400)	\$ (1,234,600)	\$ (1,243,940)	\$ (1,253,320)	\$ (956,842)	\$ (966,504)	\$ (976,208)	\$ (986,054)	\$ (995,943)	\$ (1,005,974)
Debt Service Payments (3)	\$ (15,566,468)	\$ (12,604,779)	\$ (14,733,030)	\$ (15,471,639)	\$ (15,986,764)	\$ (16,519,514)	\$ (17,069,889)	\$ (17,637,652)	\$ (18,227,802)	\$ (18,840,102)
Reserve Deposit Requirements (4)	\$ (792,700)	\$ (801,300)	\$ (1,241,622)	\$ (452,961)	\$ (332,089)	\$ (341,634)	\$ (350,299)	\$ (359,383)	\$ (370,088)	\$ (381,714)
Capital Improvement Project Expenses (5)	\$ (8,951,000)	\$ (7,539,000)	\$ (10,312,760)	\$ (12,042,295)	\$ (15,924,242)	\$ (16,878,507)	\$ (17,925,677)	\$ (13,024,791)	\$ (14,225,887)	\$ (11,729,004)
Capital Funding from Reimbursements & New Borrowing (6)	\$ 4,245,000	\$ 2,545,000	\$ 3,780,000	\$ 3,670,000	\$ 650,000	\$ -	\$ -	\$ -	\$ -	\$ -
Net Cash Flows	\$ 1,403,059	\$ 6,327,379	\$ 3,046,081	\$ 3,245,172	\$ (2,150,103)	\$ (2,454,147)	\$ (2,516,305)	\$ 3,268,001	\$ 2,777,144	\$ 6,067,196
Debt Service Coverage Ratio (1.20 Required)	1.44	1.96	1.73	1.78	1.84	1.89	1.92	1.94	1.95	1.96
Cumulative Cash*	\$ 1,403,059	\$ 7,730,438	\$ 10,776,519	\$ 14,021,690	\$ 11,871,587	\$ 9,417,441	\$ 6,901,136	\$ 10,169,137	\$ 12,946,280	\$ 19,013,477

* Cumulative Cash excludes prior cash balances and all reserves. For purposes of this statement, Cumulative Cash is shown to represent the cushion available for additional capital improvements or future rate relief.

Notes:

- (1) Operating Revenues includes increased revenue from City rate increases, phased in over 4 years, plus additional revenue from the LCA bulk water purchase beginning in 2021.
- (2) Non-Operating Expenses includes Annual City Payment, City Water/Sewer Fund Payment, and cost-sharing on retiree health benefits.
- (3) Debt Service Payments includes estimated bond payments after refinancing in 2020, plus additional borrowing for capital improvements (see note 6).
- (4) Reserve Deposit Requirements includes pre-funding of "event-driven" capital improvements, plus additional bond reserve requirements.
- (5) Capital Improvement Project Expenses includes sewer system rehabilitation, all critical projects outlined in current water/sewer master plan documents, and a 4-year reduction in water main replacements.
- (6) Capital Funding from Reimbursements & New Borrowing includes City reimbursement for remaining obligations for sewer system rehabilitation and loan funding for approximately \$10.3 million in critical projects.



Next Steps: Making it Happen

Legal Agreements – Integrated Approach

1

Concession Lease Agreement:
Amendment

(primary agreement with most changes captured)

2

Capital Cost Recovery Charge MOU:
Amendment

(specific updates to capital cost recovery process)

3

LCA Water Supply Agreement:
Amendment

(cost-sharing for water treatment costs, extended term of agreement)

4

NEW Settlement Agreement

(specific dispute resolution items as stand-alone terms, not tied to other agreements)

Plus: Update to LCA water and sewer rate schedules to implement the changes to City customers.



LCA Lease Bonds: Another Important Step

- Changes to Lease Agreement will require bondholder consent
 - Refinancing a portion of LCA's Lease Bonds may provide additional benefits
 - Required to achieve consent or refinancing before implementing changes in the new LCA-Allentown agreements

 - **More info on this step to be provided to LCA Board in August.**
 - **Target to begin implementation: October 1, 2020**
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Discussion & Questions

Thank you!



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