



# LONG-TERM FINANCIAL PLAN

2023

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**Presented to the Board of Directors  
On June 14, 2023, by:**

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# Highlights

- The Sacramento Area Sewer District (SacSewer) is in excellent financial condition and is expected to remain so throughout the ten-year forecast period, as evidenced by its AA+ credit rating.
- SacSewer continues to maintain healthy cash reserves with over \$42 million in designated reserves and approximately \$80 million in additional unreserved cash, which is available to offset cost increases without putting pressure on rates.
- About one-third of the outstanding debt was retired ahead of schedule in 2015, reducing average annual debt service expense by up to \$8 million per year over the subsequent ten years. This helps defer the need for rate increases and helps finance the Capital Improvement Program without the need for new debt. Refunding and restructuring of the Series 2015 Bonds may provide additional debt service savings in 2025 and beyond. At present, total district indebtedness stands at \$161 million principal, with annual debt service payments averaging \$13.6 million over the ten-year period.
- SacSewer should be able to finance all capital project needs over the next ten years with ongoing revenues and accumulated cash and thereby avoid the issuance of new debt.
- In January 2023, SacSewer began to invest a portion of its reserves outside of the Sacramento County Pooled Investment Fund to better align with the investment objectives and liquidity needs of SacSewer.
- In March 2023, the Board of Directors (Board) received a report from the District Engineer regarding the various financial pressures affecting SacSewer. The Board was receptive to the fact that rate increases may be needed sooner than expected with the implementation of new rates projected in fiscal year (FY) 2025-26.

# Introduction

SacSewer is in excellent financial condition as evidenced by healthy cash reserves, low debt levels, and a history of balanced budgets. This excellent financial health is reflected in the high and stable AA+ credit ratings that SacSewer has maintained for many years. Details of SacSewer's financial condition are available in the audited Annual Comprehensive Financial Reports (ACFR) along with annual budget documents on SacSewer's website at [sacsewer.com/financial-reports](http://sacsewer.com/financial-reports).

The Long-Term Financial Plan (LTFP) is an important component of the SacSewer strategy for building and maintaining a financially sound and sustainable sewage utility. The plan incorporates a ten-year financial forecast and the Capital Funding Projection. The LTFP includes a review of critical issues and risks facing SacSewer that could impact the financial forecast. The plan also includes a review of the financial environment and regional economy that SacSewer must operate in. Finally, the LTFP provides some recommended long-term action plans for debt management, asset management, reserve building, and other financial issues facing SacSewer over a term longer than the next annual budget cycle.

## Profile of SacSewer

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SacSewer is a county sanitation district organized under the laws of the State of California. It is also a contributing agency of the Sacramento Regional County Sanitation District (Regional San). SacSewer was formed in 1978 by consolidating ten smaller districts to provide a common service rate structure for customers in the affected areas. Consolidation brought savings through efficiencies and economies of scale due to operating one district instead of ten.

SacSewer is governed by a ten-member Board of Directors comprised of the Sacramento County Board of Supervisors, plus a member of each of the city councils of Sacramento, Folsom, Citrus Heights, Elk Grove, and Rancho Cordova.

SacSewer is the largest sewage collection utility in the Sacramento region and is responsible for operating and maintaining the sewer system that collects sewage from homes and businesses.

SacSewer serves 1.2 million people in its 281-square-mile service area made up of the urban unincorporated area of Sacramento County; the cities of Citrus Heights, Elk Grove, and Rancho Cordova; portions of the City of Sacramento; a small area in the City of Folsom; and the communities of Locke, Walnut Grove, Courtland, and Freeport. SacSewer serves approximately 306,000 sewer service connections and maintains/operates 3,100 miles of main line pipes, 90 miles of force mains, 1,600 miles of lower lateral pipes, 68,000 manholes, and 106 pump stations—all vital components of the region's sewer infrastructure.

## Purpose of the Long-Term Financial Plan

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The LTFP is a tool to assist policymakers in identifying the financial challenges and opportunities facing SacSewer and determining the impact of various policies and decisions that might be implemented to meet those challenges and opportunities. The LTFP includes a set of well-reasoned assumptions that provides a foundation upon which a variety of policies and decisions can be formulated for the annual operating and capital budgets, debt management program, reserves management, rate and fee setting, and other ongoing financial processes. The LTFP includes a recommendation section with some specific recommended action items to be considered over the long-term horizon to address expected financial challenges and opportunities.

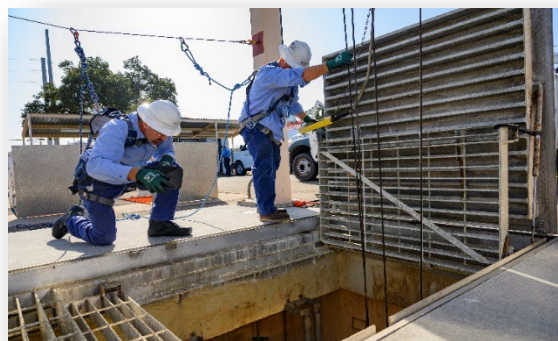
## The Planning Process

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The LTFP process involves gathering information from managers and staff related to the long-term operating and capital needs of SacSewer. The planning process includes reviews of various planning documents produced by SacSewer, Regional San, and other agencies. The LTFP does not repeat or replace other planning processes or documents but works in conjunction with them. Those plans include, but are not limited to, the SacSewer Five Year Strategic Plan 2017-2022, the SacSewer annual budget, the SacSewer staffing plans, the SacSewer Sewer System Capacity Plan, and the SacSewer Asset Management Plan.

Research and analysis of economic data and trends affecting SacSewer are also included. The process involves discussions and collaborations with management, staff, legal counsel, regulators, and outside financial advisors to determine critical issues and opportunities SacSewer may face over the next ten years. Finally, the process culminates in a presentation to the Board of Directors to receive public and elected officials' input and guidance on what they feel is important to consider in the future of SacSewer.

The LTFP will be updated and brought back to the Board at least once each fiscal year. Any action items outlined in the plan will be brought back to the Board for approval at appropriate times in the future, as conditions and opportunities warrant.



## The Mission, Vision, Values, and Guiding Financial Principles

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The SacSewer mission is ***“To protect public health and the environment by efficiently and effectively collecting sewage for our community.”*** The vision of SacSewer is ***“Setting the bar for essential sewage collection services.”*** The goal of the Long-Term Financial Plan is to support the SacSewer mission and provide a long-term sustainable financial foundation for achieving and sustaining the vision.

More specific financial principles and goals guiding this plan include:

1. Growth pays for growth. Sewer impact fees will be set at a level necessary to assure that new connections finance all capital costs associated with expanding the system.
2. Monthly service rates should be smoothed to avoid spikes and coordinated with other utility rates to minimize the total burden on ratepayers. Undesignated reserves may be used to smooth rates and mitigate rate increases.
3. Required annual maintenance and scheduled asset replacement should not be deferred to minimize current rates at the expense of future rates.
4. Budget surpluses will be applied to the General Reserve, Asset Replacement Reserve, and unreserved cash balances to mitigate future rate increases.
5. One-time money should only be used for one-time capital-related expense or debt reduction and should not be relied upon to cover ongoing expenses.
6. Use and cost of debt should be minimized. SacSewer should look for opportunities to pay off debt early.
7. Financing recurring capital projects (rehabilitations and equipment replacements) should be on a pay-go basis (cash) to avoid the added expense of debt in the future, if it can be accomplished without rate spikes.

### Core Values



# Financial Environment

## The Economy – Financial Markets and Trends

Regional, state, national, and global economies and financial markets have a significant impact on SacSewer operations and, therefore, have a significant effect on SacSewer financial strategies and decisions. Because SacSewer is an integral part of the Sacramento regional economy, conditions and trends here have a significant influence on SacSewer's financial outlook, particularly in the area of revenue projections.

**Development Growth** – Regional economic conditions have the most direct effect on SacSewer's growth. Customer growth fuels revenue growth from rates by adding new ratepayers. In addition, new customers also pay impact fees to cover the cost of added infrastructure necessary to support growth. The average annual growth rate for the past ten years was 0.63%. Since the construction boom peaked in 2007, SacSewer has experienced limited new construction, and SacSewer customer growth declined to less than 0.25% in 2015. Development in the Sacramento area has shown recent signs of improvement with customer growth in 2022 above 1%. Over the past five years, the average annual ESD growth has been 0.81%. The table below shows the growth SacSewer has experienced over the past 10 years as measured by Equivalent Single-Family Dwellings (ESDs), as reported in SacSewer's ACFRs:

**Table 1**  
**Sacramento Area Sewer District**  
**ESD Development Trends\***

	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
<b>ESDs</b>	402,705	404,647	405,997	407,502	410,689	413,809	417,027	420,297	423,244	427,549
<b>New ESDs</b>	1,300	1,942	950	1,905	3,187	3,120	3,218	3,270	2,947	4,305
<b>% Change</b>	0.32%	0.48%	0.23%	0.47%	0.78%	0.76%	0.78%	0.78%	0.70%	1.02%

\* For comparability across different land uses, ESD Development Trends are measured in equivalent single-family dwellings (ESDs).

**Interest Rates** – Market interest rates went from all-time highs in the 1980s to all-time lows over the past decade, as the Fed cut the federal funds rate in response to the Great Recession and more recently the COVID-19 pandemic. The Fed began raising the federal funds rate to help contain rising inflation, which recently hit a near 40-year high. Beginning in March 2022, the Fed aggressively raised the federal funds rate throughout 2022 and in the first and second quarters of 2023 from 0% to a target range of 5.0% to 5.25% as of May 2023.

Low interest rates have both good and bad effects on SacSewer’s financial outlook. Low interest rates over the last decade meant that SacSewer was able to refund (refinance) debt at a lower cost. This, in turn, reduces the financing cost of capital projects and reduces the impact of the capital program on SacSewer rates and fees. On the negative side, with low interest rates, SacSewer is unable to earn a good return on invested cash balances. Because the majority of SacSewer’s cash is invested in the Sacramento County Pooled Investment Fund, SacSewer is limited by State law and local policy to investing in securities with maturities of five years or less. For the past two years, SacSewer has averaged 1% in the County Pool. Since March 2020, when the Fed lowered the federal funds rate to 0% in response to the economic impact of the COVID-19 pandemic, short-term interest rates have precipitously declined to very low levels, and below the rate of inflation experienced by SacSewer, which has resulted in a loss of value over time for cash balances. With the Fed’s change in policy direction in response to rising inflation, interest rates have now risen to over 5%. This will improve the investment performance of SacSewer’s portfolio but will mean higher debt financing costs, making it imperative to minimize the issuance of new debt.



## Critical Issues

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SacSewer continues to hold a financially stable position where revenue, costs from customer growth, and operational costs have grown moderately in the past few years. The District has developed and implemented a rate and fee structure that provides long-term financial stability and maintains reserves to mitigate a variety of financial risks. However, a number of potential issues and unforeseen events could have a significant impact on the financial position of SacSewer, as described below:

- 1. Regulatory requirement changes** – Changes in regulatory requirements that govern SacSewer operations can cause costs to rise. The State Water Resources Control Board adopted new Sanitary Sewer State Wastewater Discharge Regulations on December 6, 2022. SacSewer actively participated in the review of the update. The new order becomes effective on June 5, 2023. No significant-capital and/or operating costs beyond our projected levels are expected at this time.
- 2. Lawsuits and settlements** – Legal challenges are an ever-present hazard in the sewage utility business. In late 2020, litigation was filed regarding one of SacSewer’s pump station sites. In 2023, SacSewer entered into a settlement agreement with the California Coastkeeper Alliance for violations of the Clean Water Act for sanitary sewer overflows. Defending the current litigation and any other potential legal issues can result in settlement costs that are not included in the current projections.
- 3. Board approved service levels** – Future rate increases may be necessary if more resources are needed to meet service level targets. SacSewer has met all of its service level targets for the last four years.
- 4. Economic Conditions** – Adverse changes in macroeconomic conditions, such as rising interest rates and inflation, may negatively impact the financial performance of this plan. On the one hand, since SacSewer has no plans to issue new debt to finance its capital projects, rising interest rates are not expected to directly impact project financing costs. On the other hand, rising inflation may result in higher construction costs that could significantly exceed engineers’ cost estimates, which may result in the need to issue new debt. Rising interest rates would, however, benefit SacSewer by providing additional interest income from higher returns on invested cash balances.
- 5. Natural Disasters, Climate Change, Pandemics, or Other Emergencies** – The potential for natural disasters, such as earthquakes or floods, are issues that SacSewer considers in its emergency planning. An increase in extreme weather events may result in the need for additional capital spending to enhance system capacity or resiliency. A general reserve of 25% of projected annual operating costs is funded and will continue to be maintained to cover additional costs that could be incurred during times of emergency.

6. **Water Fluctuations** – Reduced or increased sewage could have an impact on utilities in the future. As sewage flows decline in SacSewer’s collection system due to mandated water conservation or drought, potential issues may arise that will increase the costs of maintenance in the system. Lower sewage flows increase the potential for debris stoppages and may also result in odor issues. There is also a higher risk of root intrusion in the sewer collection system. Conversely, intense storm events can cause system surcharging and increased sanitary sewer overflows.
7. **Aging infrastructure** – In order to adequately address emerging aging infrastructure issues, SacSewer has developed asset sustainability strategies for main lines, pump stations, force mains, lower laterals, and reinforced concrete pipe. Estimates of cost increases and appropriate reserve levels associated with the sustainability strategies are evaluated annually and included in financial projections and budgets. The North Area Corporation Yard (NACY) is nearing the end of its design life, and renewal costs will be incurred over several years as specified in the ten-year Capital Funding Projection.



# Ten-Year Financial Forecasts

## Financial Performance Targets

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One of the primary objectives of the SacSewer Board and management is to maintain a financially sound and sustainable sewage utility capable of delivering the high-quality service at the lowest long-term cost. Some financial benchmarks and performance targets are used to determine and maintain financial health. Those targets include cash balances, annual cash flow needs, and debt coverage ratios. The forecast model is designed to maintain total cash on hand equal to at least eight months of operating expenses net of depreciation. Currently, SacSewer has about 21 months of operating cash on hand which is above the industry median of 18 months for Water and Sewer Retail districts, AA+ rated. The forecast model shows how the cash balances are allocated between designated reserves and the unreserved cash balance. The current Debt Service Coverage Ratio of 4.8x is above the industry median of 2.3x in 2022, for water and sewer retail districts, AA+ rated as reported by Fitch Ratings.<sup>1</sup>

When projected revenues or cash flow needs cause any of these metrics to fall below these target levels, a rate increase should be considered to return these benchmarks to their target levels. Under the baseline forecast, which has an annual growth assumption of 0.5% per year, SacSewer may need to consider increasing rates in FY 2025-26 to keep the debt service coverage ratio at 2.00x. The 2.00x is a target of the forecast model. This is above the bond covenant requirements of 1.20x for senior coverage and 1.10x for total debt coverage. Projected coverage is higher than the covenant requirements and the targets.

## Financial Forecast Tables

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The following two pages contain the ten-year financial forecast tables for SacSewer. The forecast includes two tables showing actuals for two prior years, the projected year-end estimates for the current budget year, and a ten-year forecast to FY 2032-33, with the first year reflecting the final adopted budget for FY 2023-24. The first table, Table 2, is a pro-forma statement of operations showing revenues, expenditures, and debt coverage projections. Table 3 shows cash flows and cash balance projections, including cash in reserve funds. These tables reflect a baseline growth rate assumption that ESDs will be added at a rate of 0.5% in each fiscal year from FY 2024-25 through FY 2032-33. This is a conservative growth assumption given the past ten-year average annual growth rate for SacSewer has been 0.63%.

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<sup>1</sup> Fitch Ratings 2022 U.S. Water and Sewer Peer Review.

**Table 2: SacSewer Pro Forma as of June 14, 2023**

	Audited Actual	Year End Estimate	Proposed Budget	Forecast								
(\$000s unless noted otherwise)	FY 2021/22	2022/23	2023/24	2024-25	2025-26	2026-27	2027-28	2028-29	2029-30	2030-31	2031-32	2032-33
<b>Revenues</b>												
ESD Growth Rate	4.46%	0.52%	1.04%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%
Average ESDs (estimated)	427,384	429,625	434,090	436,260	438,442	440,634	442,837	445,051	447,277	449,513	451,761	454,019
<b>Operating Revenues</b>												
Monthly rate per ESD*	\$ 19.85	19.85	19.85	19.85	20.85*	21.85*	22.35*	22.85*	23.85*	24.85*	25.85*	26.35*
Residential/Commercial revenue	101,803	102,337	103,400	103,917	109,698	115,534	118,769	122,033	128,011	134,045	140,136	143,561
Industrial revenue	301	300	320	321	323	324	326	328	329	331	333	334
<i>Total revenue from service charges</i>	<u>102,104</u>	<u>102,636</u>	<u>103,720</u>	<u>104,238</u>	<u>110,021</u>	<u>115,859</u>	<u>119,095</u>	<u>122,361</u>	<u>128,340</u>	<u>134,376</u>	<u>140,469</u>	<u>143,895</u>
Impact fee revenue	7,548	7,000	5,000	6,000	6,181	6,367	6,559	6,756	6,960	7,170	7,386	7,608
Subtotal operating revenue	<u>109,652</u>	<u>109,636</u>	<u>108,720</u>	<u>110,238</u>	<u>116,202</u>	<u>122,226</u>	<u>125,654</u>	<u>129,117</u>	<u>135,300</u>	<u>141,545</u>	<u>147,854</u>	<u>151,503</u>
Fed./State Grants (With BAB Subsidy)	2,229	2,312	2,251	2,251	2,251	2,251	2,251	2,251	2,251	2,251	2,251	2,251
Interest earnings	768	1,736	2,400	2,413	1,840	1,609	1,446	1,423	1,555	1,639	1,767	1,949
Other revenue	<u>9,093</u>	<u>10,170</u>	<u>12,569</u>	<u>12,820</u>	<u>13,077</u>	<u>13,338</u>	<u>13,605</u>	<u>13,877</u>	<u>14,155</u>	<u>14,438</u>	<u>14,726</u>	<u>15,021</u>
<b>Total revenue</b>	<u>\$ 121,742</u>	<u>\$ 123,855</u>	<u>\$ 125,939</u>	<u>\$ 127,722</u>	<u>\$ 133,369</u>	<u>\$ 139,423</u>	<u>\$ 142,955</u>	<u>\$ 146,668</u>	<u>\$ 153,260</u>	<u>\$ 159,872</u>	<u>\$ 166,598</u>	<u>\$ 170,723</u>
<b>Expenditures</b>												
<b>Operating expenses</b>												
Salaries & Benefits	\$ 42,852	48,272	53,691	55,839	58,072	60,395	62,811	65,323	67,936	70,654	73,480	76,419
Services & Supplies	<u>28,910</u>	<u>39,857</u>	<u>44,209</u>	<u>45,536</u>	<u>46,902</u>	<u>48,309</u>	<u>49,758</u>	<u>51,251</u>	<u>52,788</u>	<u>54,372</u>	<u>56,003</u>	<u>57,683</u>
Operating expense (Net of depr/amort.)	71,762	88,129	97,900	101,374	104,974	108,704	112,569	116,574	120,725	125,026	129,483	134,102
Non-operating expense	<u>0</u>	<u>0</u>	<u>3,659</u>	<u>3,873</u>	<u>4,086</u>	<u>4,200</u>	<u>4,314</u>	<u>4,328</u>	<u>4,343</u>	<u>4,457</u>	<u>4,373</u>	<u>4,388</u>
<b>Total expense</b>	<u>71,762</u>	<u>88,129</u>	<u>101,560</u>	<u>105,247</u>	<u>109,060</u>	<u>112,904</u>	<u>116,883</u>	<u>120,902</u>	<u>125,067</u>	<u>129,483</u>	<u>133,856</u>	<u>138,490</u>
<b>Net revenue</b>	<u>49,980</u>	<u>35,726</u>	<u>24,379</u>	<u>22,475</u>	<u>24,309</u>	<u>26,519</u>	<u>26,072</u>	<u>25,766</u>	<u>28,192</u>	<u>30,389</u>	<u>32,742</u>	<u>32,233</u>
<b>Net revenue for coverage test</b>	<u>\$ 49,980</u>	<u>\$ 35,726</u>	<u>\$ 28,039</u>	<u>\$ 26,348</u>	<u>\$ 28,395</u>	<u>\$ 30,719</u>	<u>\$ 30,386</u>	<u>\$ 30,094</u>	<u>\$ 32,535</u>	<u>\$ 34,846</u>	<u>\$ 37,115</u>	<u>\$ 36,621</u>
 Senior Debt Service	 \$ 10,459	 10,461	 10,456	 10,464	 13,641	 13,626	 13,590	 13,562	 13,521	 13,492	 16,792	 16,674
Total Debt Service (All Senior)	\$ 10,459	10,461	10,456	10,464	13,641	13,626	13,590	13,562	13,521	13,492	16,792	16,674
Senior debt coverage (must be at least 1.20x)	4.78x	3.42x	2.68x	2.52x	2.08x	2.25x	2.24x	2.22x	2.41x	2.58x	2.21x	2.20x
Total debt coverage (must be at least 1.10x)	4.78x	3.42x	2.68x	2.52x	2.08x	2.25x	2.24x	2.22x	2.41x	2.58x	2.21x	2.20x

\* Assumed rate increases for planning purposes only. Actual future rate increases will be set by the Board and may differ significantly from planning assumption shown above.

**Table 3: SacSewer Cash Flow Projection as of June 14, 2023**

(\$'000s unless noted otherwise)	Audited Actual	Year End Estimate	Proposed Budget	Forecast								
	FY 2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29	2029-30	2030-31	2031-32	2032-33
Beginning Cash	\$126,267	\$125,526	\$125,446	\$125,385	\$112,541	\$ 99,021	\$ 87,454	\$ 79,317	\$ 78,190	\$ 84,762	\$ 88,948	\$ 95,369
Cash Inflow												
Impact Fees	7,548	7,000	5,000	6,000	6,181	6,367	6,559	6,756	6,960	7,170	7,386	7,608
Monthly Service Charges	102,104	102,636	103,720	104,238	110,021	115,859	119,095	122,361	128,340	134,376	140,469	143,895
Interest/Other	9,861	11,906	14,969	15,233	14,917	14,947	15,051	15,300	15,709	16,076	16,493	16,969
Federal BAB Subsidy & State Grants	2,229	3,272	7,546	28,685	6,313	2,251	2,251	2,251	2,251	2,251	2,251	2,251
<i>Subtotal Cash In</i>	<i>121,742</i>	<i>124,815</i>	<i>131,234</i>	<i>154,157</i>	<i>137,431</i>	<i>139,423</i>	<i>142,955</i>	<i>146,668</i>	<i>153,260</i>	<i>159,872</i>	<i>166,598</i>	<i>170,723</i>
Cash Outflow												
Operating Expenses	71,762	88,129	97,900	101,374	104,974	108,704	112,569	116,574	120,725	125,026	129,483	134,102
Non-Operating Expenses	0	0	3,659	3,873	4,086	4,200	4,314	4,328	4,343	4,457	4,373	4,388
Capital Expenses	40,262	26,304	19,280	51,290	28,250	24,460	20,620	13,330	8,100	12,710	9,530	6,480
Debt Service	10,459	10,461	10,456	10,464	13,641	13,626	13,590	13,562	13,521	13,492	16,792	16,674
<i>Subtotal Cash Out</i>	<i>122,483</i>	<i>124,894</i>	<i>131,296</i>	<i>167,001</i>	<i>150,951</i>	<i>150,989</i>	<i>151,093</i>	<i>147,794</i>	<i>146,688</i>	<i>155,686</i>	<i>160,178</i>	<i>161,644</i>
Ending Cash	\$125,526	\$125,446	\$125,385	\$112,541	\$ 99,021	\$ 87,454	\$ 79,317	\$ 78,190	\$ 84,762	\$ 88,948	\$ 95,369	\$ 104,448
Unreserved cash	83,920	79,056	82,941	68,450	53,898	41,265	32,023	29,756	35,147	38,113	43,271	51,043
Reserves												
General (target=25% of Operating Expenses)	20,092	20,549	20,549	24,475	25,344	26,244	27,176	28,142	29,144	30,181	31,256	32,371
Upper Lateral Loan Revolving Fund	500	500	500	500	500	500	500	500	500	500	500	500
Metro Airpark	2,744	2,799	2,854	2,912	2,970	3,029	3,090	3,152	3,215	3,279	3,344	3,411
Confluence Program (New in 2018)	3,000	8,000	8,000	8,000	8,000	8,000	8,000	8,000	8,000	8,000	8,000	8,000
McClellan Airpark	1,689	1,723	0	0	0	0	0	0	0	0	0	0
Asset Replacement (funded by monthly rates)	9,581	8,820	6,541	4,204	4,309	4,417	4,527	4,641	4,757	4,876	4,997	5,122
Rate Stabilization	4,000	4,000	4,000	4,000	4,000	4,000	4,000	4,000	4,000	4,000	4,000	4,000
Total Reserves	41,606	46,391	42,444	44,091	45,123	46,190	47,293	48,434	49,615	50,836	52,098	53,405
Ending Cash Total	\$125,526	\$125,446	\$125,385	\$112,541	\$ 99,021	\$ 87,454	\$ 79,317	\$ 78,190	\$ 84,762	\$ 88,948	\$ 95,369	\$ 104,448

## Forecast Assumptions

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1. **Rate Revenue** – The monthly rate per ESD is projected to remain at the current amount of \$19.85 through the next two years. Natural rate revenue growth is based on ESD growth, which is estimated to remain at the 0.5% growth rate throughout the ten-year forecast period.
2. **Impact Fee Revenue** – Increased impact fees were adopted effective July 1, 2023, (\$786/ESD for relief areas and \$4,067/ESD for expansion areas), July 1, 2024, (\$790/ESD for relief areas and \$4,067/ESD for expansion areas), and July 1, 2024 (\$790/ESD for relief areas and \$4,374/ESD for expansion areas). We do not expect the new fees to negatively impact construction activity and new service connections. The fee revenue forecast reflects the same ESD growth assumptions used for rate revenues.
3. **Non-operating Revenue** – The main variable in this revenue category is interest income on invested cash balances. This revenue category decreased by about 10% in FY 2019-20 and another 65% in FY 2020-21 due to decreases in market interest rates for short-term securities. After 2021-22, as the Fed continues to raise the federal funds rate to curb inflation, we expect non-operating revenue to increase moderately at 2% each year through the remainder of the forecast period.
4. **Operating Expenses: Salaries and Benefits** – This cost category is projected to increase between 3% and 4% annually throughout the forecast period. These increases reflect expected cost-of-living adjustments negotiated in labor agreements, rising retirement and health benefit costs, and additional staff to meet projected program growth.
5. **Operating Expenses: Services and Supplies** – This expenditure category is projected to increase between 2% and 4% per year based on program needs and maintenance schedules throughout the forecast period.
6. **Non-Operating Expenses** – This expenditure category is projected to increase 2% annually throughout the forecast period.
7. **Debt Service** – Debt service is based on total outstanding bonded debt of approximately \$161 million as of June 30, 2022. In 2015, the Series 2005 Bonds were refunded and approximately \$72 million of the bonds were retired up to 20 years early. Early retirement of a portion of these bonds, along with lower interest rates on the remaining refunded bonds, resulted in savings in the annual debt service costs. Debt service coverage stays at, or above, the target level of 2.00x throughout the ten-year forecast period. Under the current assumptions for growth not exceeding 0.5% annually, rate increases would be needed in FYs 2025-26 and beyond to maintain this level of debt coverage and to keep a positive unreserved cash balance.

**8. Reserves** – The designated reserve levels are projected to decrease from \$46.4 million as of June 30, 2023, to \$42.4 million by the end of FY 2023-24. Below is a description of each reserve fund, including the purpose, size, and forecast assumptions:

- **General Reserve (\$20,549,000)** – Covers emergency costs and other unexpected expenditures, or offsets temporary fluctuations in revenues. This reserve is targeted at a level equal to 25% of operating expenditures and provides protection from rate increases that might result from short-term cost spikes from emergencies, regulatory changes, or legal (lawsuit) settlements.
- **Upper Lateral Loan Revolving Fund Reserve (\$500,000)** – Was established in FY 2016-17 to provide a base revolving loan fund for low-interest loans for customers that need to replace failing upper lateral sewer pipes on their property.
- **Metro Airpark Reserve (\$2,854,484)** – Was developer funded at this level by agreement between SacSewer and the developer of Metro Airpark to cover additional future maintenance and repair expenditures expected in this area. This reserve will be increased each year by a 2% general inflation factor to cover cost increases resulting from inflation.
- **Asset Replacement Reserve (\$6,541,000)** – Is funded from monthly rates and will be used to finance replacement of pipelines, buildings, and equipment assets as they reach the end of their useful lives. The changes in this reserve are based on asset replacement needs identified annually in the SacSewer Asset Management Plan and may be drawn down in years where the Capital Funding Projection total costs exceed \$25 million.
- **Rate Stabilization Reserve (\$4,000,000)** – Is available to make sure debt coverage ratios of at least 1.20x, as required by bond agreements, are met if revenues decline without requiring an immediate increase in rates. As debt gets paid off, the need for the reserve declines.
- **Reserve for Confluence Program (\$8,000,000)** – Was first set aside in FY 2018-19 to manage the program’s funding annually through non-rate/non-fee revenues. This reserve provides a funding buffer to ensure long-term programs can continue during years of low non-rate/non-fee revenues.
- **Unreserved Cash** – This is defined as all of the cash balances not designated for a specific purpose by the Board and provides an additional cushion for unexpected expenses or revenue loss. Unreserved cash also provides a flexible source of funding to take advantage of opportunities to maximize long-term economic benefits for ratepayers. In this plan, unreserved cash provides financing for the capital projects and offsets the need for additional debt.

9. **Capital Costs** – The cost estimates for capital project expenditures are from the SacSewer Asset Management Plan that has replacement schedules for all major assets of SacSewer. Larger than normal capital expenditures occurring in 2023 through 2028 can be covered by unreserved cash balances and the Asset Replacement Reserves. More detail on the capital projects is included in the following Capital Funding Projection section.



## Capital Funding Projection

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Table 4 below lists the SacSewer capital projects already in progress or projects that are expected to begin within the ten-year projection timeframe. The projects are shown in a summary format and have been updated to reflect the most current cost and timing information available. About \$194 million in capital project costs are anticipated over the next ten years. The capital program will be financed with grants, rate revenue, and available cash, and will not require any debt issuance. SacSewer has sufficient reserves to handle the large capital outlays for the years of FY 23-24, FY 24-25, FY 25-26, FY 26-27, and FY 27-28, where more than \$20 million is needed. More than 90% of Septic Conversion Focus Areas (Projects #19-#22 in Table 4) costs are expected to be reimbursed by State and federal grants and Regional San contributions from the Confluence Program.

The ten-year Capital Funding Projection (CFP) in the SacSewer 2015 forecast totaled about \$142 million. Since then, the CFP has increased to the current forecast level of over \$194 million (37% increase over these eight years). Due to improved financial metrics, mainly from the early retirement of debt in 2015 and a surplus property sale in 2019, SacSewer is able to devote more financial resources to the CFP. The additional resources address major relief projects and expanded system rehabilitation without increasing rates sooner and without issuing new debt.

The capital projects listed in Table 4 are organized into the following five project types:

**Relief Projects** – Projects #1 through #10 listed in Table 4 are major relief projects that address capacity deficiencies and risks at specific locations in existing facilities.

**Pump Station Rehab Projects** – Projects #11 through #13 are for rehabilitation of existing pump stations throughout the service area.

**Ongoing Multiple Location Projects (System Rehabilitation)** – Projects #14 through #17 are ongoing projects at numerous locations throughout the service area that replace or rehabilitate various components of the sewer system.

**Vehicles, Mobile Equipment, and Facilities** – Project #18 is an estimate of the cost to renovate the North Corporation Yard. This facility is nearing the end of its functional life and will undergo significant renovations in the planning period.

**Focus Area Septic Conversions** – Projects #19 through #22 provide funding for converting septic systems to the sewer system in specific communities. These conversions are completed with construction contracts managed by SacSewer in concert with the property owners and regulatory agencies. A significant portion of the cost for each area project will be covered by grant programs and Regional San non-rate/non-fee revenues (Confluence Program).

**Table 4: SacSewer Ten-Year Capital Funding Projection 2023-24 to 2032-33 (in thousands)**

<b>Project # / Project Name</b>	<b>10-Year Totals</b>	<b>FY 23/24</b>	<b>FY 24/25</b>	<b>FY 25/26</b>	<b>FY 26/27</b>	<b>FY 27/28</b>	<b>FY 28/29</b>	<b>FY 29/30</b>	<b>FY 30/31</b>	<b>FY 31/32</b>	<b>FY 32/33</b>
1-Highlands ARD 4&5 (Pump Stations S015 & S016)	\$1,040	1,040									
2-System Capacity Project - ARD-24	\$2,100		1,790	310							
3-System Capacity Project - ARD-10	\$6,400			340	1,620	3,810	630				
4-System Capacity Project - ARD-21	\$6,800				380	1,020	5,400				
5-System Capacity Project - MCL-1	\$3,810						190	620	2,250	750	
6-System Capacity Project - SEA-20	\$4,340							1,000	1,670	1,670	
7-System Capacity Project - RIO-3	\$6,500	300	360	2,360	3,480						
8-System Capacity Project - WG-1	\$710	570	140								
9-System Capacity Project - NEA-51	\$2,500	120	410	1,480	490						
10-System Capacity Planning	\$900	90	90	90	90	90	90	90	90	90	90
11-RCCC Pump Station Rehabilitation - S012	\$14,450	3,980	6,980	3,490							
12-Landis Pump Station Rehabilitation - S067	\$460	220	240								
13-Other Pump Station Rehabilitation Projects	\$13,020	420	2,730	1,050	420	2,730	1,050	420	2,730	1,050	420
14-Creek Crossing/Main Line Rehabilitation	\$4,930	2,600	2,330								
15-Main Line Cured-In-Place Pipe	\$24,000	2,400	2,400	2,400	2,400	2,400	2,400	2,400	2,400	2,400	2,400
16-Lower Lateral Replacements	\$33,000	3,300	3,300	3,300	3,300	3,300	3,300	3,300	3,300	3,300	3,300
17-Lower Lateral Cured-In-Place Pipe	\$2,700	270	270	270	270	270	270	270	270	270	270
18-North Area Corporation Yard Rehab (NACY)	\$31,740	730	860	11,140	12,010	7,000					
19-Linda Manor Septic Conversion Project	\$5,080	630	3,360	1,090							
20-Old Florin Town Septic Conversion Project	\$8,780	870	7,590	320							
21-Franklin Septic Conversion Project	\$6,200	600	5,330	270							
22-Hood Septic Conversion Project	\$14,680	1,230	13,110	340							
<b>Totals</b>	<b>\$194,140</b>	<b>\$19,370</b>	<b>\$51,290</b>	<b>\$28,250</b>	<b>\$24,460</b>	<b>\$20,620</b>	<b>\$13,330</b>	<b>\$8,100</b>	<b>\$12,710</b>	<b>\$9,530</b>	<b>\$6,480</b>

# Debt Management Plan

## Debt Policies and Goals

The policy of SacSewer is to ensure debt is issued and managed in a manner that benefits ratepayers, protects the credit ratings, maintains access to the credit market, and provides financial flexibility. The primary objectives of the SacSewer debt management plan are to minimize financial risk, reduce debt service costs, maintain or improve credit ratings, and reduce the complexity and administrative cost of maintaining the portfolio.

SacSewer debt policy includes the following elements:

1. SacSewer should try to avoid issuing additional debt to fund the capital program.
2. If excess cash is available, it should be used to pay off existing debt early to reduce debt service costs.

## Existing Debt

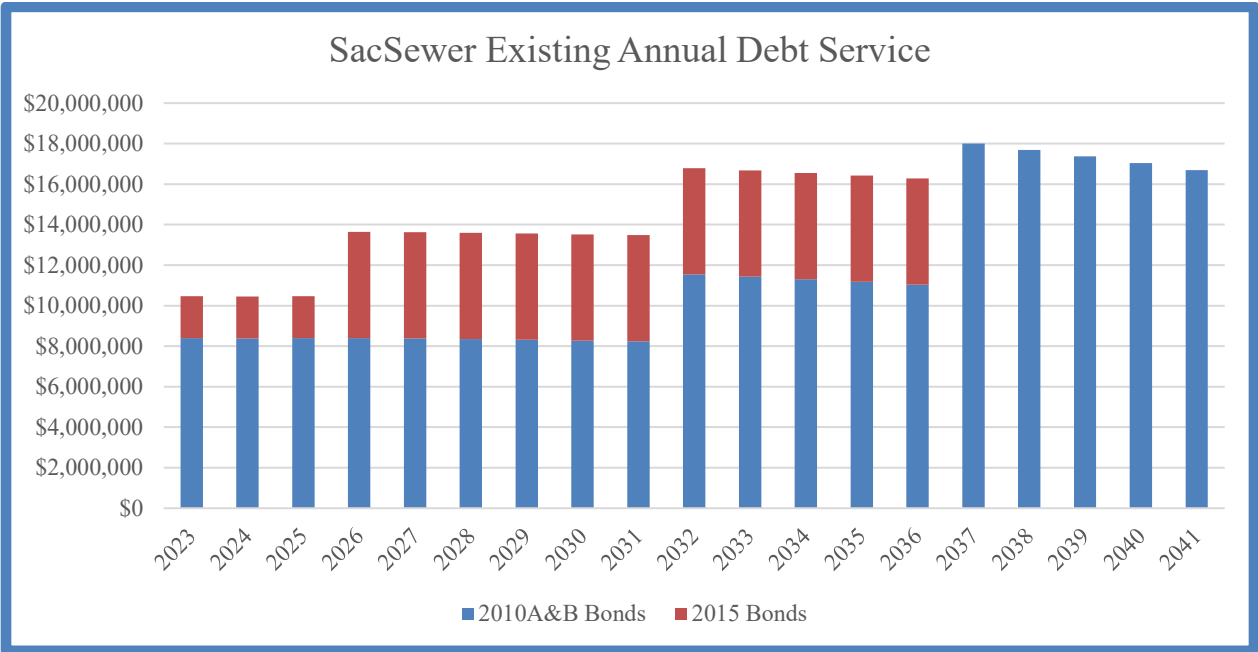
SacSewer has about \$161.4 million of outstanding revenue bond debt in three issues as of June 30, 2022. All of this debt is fixed rate senior lien debt. The following table shows the details of each of these debt issues.

**Table 5**

Issue	Par Amount (\$)	Call Date	Final Maturity	Comments
Series 2015	45,435,000	8-1-2025	8-1-2035	Refunding Bonds
Series 2010A	110,690,000	Make whole call	8-1-2040	Taxable BABs
Series 2010B	5,225,000	8-1-2020	8-1-2025	Tax Exempt
<b>Total</b>	<b>161,350,000</b>			

This debt portfolio is 100% fixed rate debt that has a low level of risk. Annual debt service (principal and interest payments) total about \$10.5 million, of which approximately \$2.25 million is subsidized by the federal government under the Build America Bond (BAB) program. Debt service net of the BAB subsidy currently consumes a manageable 8% of the \$19.85 per month rate per ESD paid by SacSewer ratepayers. As the chart on the next page illustrates, the SacSewer annual debt service remains level at about \$10 million for the next three years. Then the debt service steps up as outstanding principal begins to be paid off. With expected customer growth, debt service should remain manageable at between 10-12% of monthly

service rates. After 2025, some of the outstanding debt could be refunded and restructured to reduce annual debt service if necessary.



## Strategies for Specific Debt Issues

**Series 2015 Revenue Bonds** – These fixed rate, tax-exempt bonds have an outstanding par amount of \$45,435,000. They have a final maturity date of August 1, 2035, and bear interest at rates ranging from 3% to 5%. These bonds were issued on May 1, 2015, to refund the Series 2005 Revenue Bonds. Also at that time, approximately \$72 million of excess cash was used to pay off a portion of the Series 2005 Revenue Bonds up to 20 years early. This refunding and early payoff of debt will save SacSewer about \$125 million over those 20 years.

These bonds can be called at par in early 2025 and refunded with tax-exempt bonds for savings at that time. If SacSewer has any excess reserves at that time, a small cash contribution (\$5-10 million) can provide additional restructuring savings by eliminating some of the longer maturities. This would help reduce the need for rate increases beyond 2025.

**Series 2010A&B Revenue Bonds** – These bonds were issued for SacSewer on August 11, 2010, to provide new money proceeds to finance SacSewer capital projects including the Goethe Road Facility. The Series 2010A Bonds are \$110.7 million of federally taxable direct subsidy Build America Bonds (BABs) with an average taxable interest rate of about 6.25% and a final maturity in 2040. These bonds have a low net debt service cost due to the BABs subsidy from the federal government that covers 35% of their interest costs. This results in a net interest rate of 4.1% with the subsidy. The Series 2010B Bonds were initially \$15.9 million of fixed rate tax-exempt bonds with an average interest rate of about 3.7% and a final maturity in 2026.

SacSewer has been receiving about \$2.25 million annually from this subsidy to offset the debt service costs of the Series 2010A Bonds. These bonds have a make-whole call provision that gives SacSewer the right to call the bonds at any time but requires the future interest to be paid at a discounted present value along with the outstanding principal. This generally makes it uneconomical to call these bonds before they get close to maturity. The Series 2010A Bonds also have a provision that allows for a better discount rate for a make-whole call if an extraordinary event occurs. Elimination of the subsidy may qualify as an extraordinary event. That may give SacSewer an opportunity to call and restructure the Series 2010A Bonds at a reduced cost. Even though a restructuring transaction may not generate net present value savings, it may give SacSewer the opportunity to reschedule the payment of debt service to be lower in FYs 2025-26 through 2040-41. This may allow SacSewer to avoid or reduce monthly service rate increases in some of those years.



# Recommendations and Action Items

This section of the Long-Term Financial Plan is divided into strategic recommendations that are general in nature and specific action items that could be undertaken to achieve the recommendations. All action items will be brought to the SacSewer Board for separate approval at future dates as required by existing ordinance or Board policy.

## **Recommendation #1**

Continue pay-go financing for the SacSewer capital program. All capital projects can be financed with current rate revenue and reserves over the next ten years. With a well-managed asset replacement schedule that provides for some asset replacement or refurbishing every year, large replacements that need to occur in a short timeframe that might require debt financing can be avoided. The current level of rates and fees can support the level of maintenance and capital expenditures needed and build reserves to handle the few years where capital expenditures may be higher than normal. Due to the steady nature of replacement spending and long life of most SacSewer assets, there should be no need to build very large reserves for asset replacements.

**Action Item #1:** Continue the robust Capital Funding program necessary to preserve and maintain SacSewer capital assets.

## **Recommendation #2**

Continue to monitor the municipal bond market to look for opportunities to refund and restructure SacSewer debt issues to lower costs and level the annual debt service costs to help reduce the need for rate increases in the future.

**Action Item #1:** If short-term interest rates continue to trend higher while long-term rates trend lower, SacSewer, along with the District's financial advisor, will explore a taxable refunding transaction for the Series 2015 Revenue Bonds to lower debt service costs or restructure future principal payments to help achieve a better level annual debt service cost profile to help reduce the need for rate increases.

# Investment Management

SacSewer currently has about \$120 million in cash and invested reserve balances as of March 31, 2023. Interest income earned on these balances is non-rate/non-fee income that can be used to support incentive and assistance programs (Confluence Program).

A total of \$105 million of the District's cash is deposited in the Sacramento County Treasury and is part of the Sacramento County Pooled Investment Fund (Pool). Annually, the SacSewer Board approves an investment policy that mirrors the policy approved by the County Board of Supervisors for the Pool. SacSewer earned 3.97% on its reserve balances for the fiscal quarter ended March 31, 2023. State law and the County Investment Policy limit the Pool to investments in securities with maturities of five years or less. Due to its need to preserve invested principal and provide liquidity for all participants in the Pool, it has a weighted average maturity of less than one year. As of March 2023, the weighted average maturity of the Pool was 289 days, which reflects the Pool's need for liquidity.

In January 2023, \$15 million of the District's cash was transferred out of the County Pool and was invested with Chandler Asset Management (Chandler), which serves as the District's investment advisor and manager. SacSewer earned 4.37% as of March 2023 and has a weighted average maturity of 2.81 years. Because the District's cash flow is relatively constant throughout the year, the need for liquidity is less important for the District than the Pool as a whole. Investing in securities with an average maturity longer than the Pool earns higher interest income and better serves the investment objectives and liquidity needs of SacSewer.

