

City of Wilkes-Barre



Status Update on City's Financial Situation & Potential Sewer Monetization

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Prepared by:

✓Scott Shearer, Managing Director

✓Gordon Mann, Director

✓Ben Kapenstein, Senior Analyst

PFM Financial
Advisors LLC

213 Market Street
Harrisburg, PA 17101

717.232.2723
pfm.com



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Update on City's Financial Situation



Multi-year financial planning: Thinking about the big picture

The PA Department of Community and Economic Development has given the City of Wilkes-Barre grant funding to develop and implement a multi-year year financial plan through the Early Intervention Plan (now the Strategic Management Plan or STAMP) program. The City has been working with PFM Group Consulting on this engagement since 2016.

The multi-year plan released in 2017 described the importance of achieving financial stability in three ways:

- **Cash stability:** Does the City have enough cash to pay its obligations when they are due throughout the year?
- **Budgetary stability:** Can the City balance its revenues and expenditures on an annual basis?
- **Structural stability:** Can the City balance recurring expenditures against recurring revenues, without reliance on one-time or short-term fixes?

These are important components to achieving service stability where City government can provide the services that residents and businesses need and want at a price they are willing and able to afford. We have provided the City with periodic updates on the cash flow, budgetary performance and the multi-year projections since 2017.



2020 Budget gap closing measures

Mayor George's introduced budget closes the \$3.6 million baseline deficit mostly by making changes on the revenue side. The difference between the 2020 budget and baseline projection is less than 1.0 percent for expenditures. Here are the major differences on the revenue side

2020 Revenue projections (\$ Millions)

	2020 Budget	2020 Baseline	Difference	Explanation
Building/plumbing/electrical permits	\$2.5	\$0.7	\$1.8	City projects revenues will be 345% higher in 2020 because of projects
Earned income tax	\$14.6	\$14.2	\$0.5	City projects more growth in EIT revenues
Sale of City owned property	\$0.5	\$0.0	\$0.5	Assumed property sale not in baseline
WVSA Contribution	\$0.4	\$0.1	\$0.3	Authority payment for storm sewer repairs
General fund revenues	\$52.7	\$49.6	\$3.1	

The 2020 budget has the same risk that we highlighted in the 2018 and 2019 budgets. It relies on one-time revenues to close a structural deficit (permits and property sales). Sometimes those revenues don't materialize (asset sales in 2018) but, even when they do, they only help you for one year and the deficit is even larger the next year.



How does the sewer system fit into this?

The 2017 multi-year plan described the City's multi-year deficits in three pieces:

- **Structural deficit** where regular spending grows faster than regular revenues
- **Increase in debt service:** The 2017 debt refinancing prevented the costly jump in payments. Those payments are stable at \$4.8 million but they could be lower if the City can pay off debt ahead of schedule
- **Increase in pension payments:** The pension problem was described in the 2017 plan, referenced again in our March 2018 update to Council, quantified again in the multi-year projection included in the 2018 application for Act 47, and has now arrived as projected. The actuary advocated for the City to change its pension assumptions to more realistic levels which would increase the City's contributions from \$7.1 million in 2020 to \$9.9 million in 2021 (\$5.6 million in 2019).

The City should not try to use the sewer system process "solve the structural deficit." The worse thing the City can do is to use any proceeds to temporarily cover its deficit for a couple years. That sets the City up for a massive deficit when the proceeds are gone.

But it could **use any proceeds to either pay down debt ahead of schedule or increase the pension funding levels and reduce the required contributions to those pension plans.** That was the concept we recommended exploring in the 2017 multi-year plan.



Sewer system: Mitigating risk

There's another consideration in evaluating the sewer system, beyond how any potential proceeds might be used.

Unlike other Pennsylvania municipalities, Wilkes-Barre includes the sewer related revenues and expenditures in its General Fund. They are not segregated in an enterprise fund. In recent years the sewer-related revenues have covered the sewer-related costs as reported, though the City does not separately budget labor costs related to system maintenance.

	2015 Actual	2016 Actual	2017 Actual	2018 Estimate	2019 Budget
Sewer charge revenues	\$1,318,021	\$1,307,664	\$1,402,892	\$1,314,250	\$1,300,400
Sewer repair expenditures (w/out labor)	\$928,680	\$1,298,970	\$790,741	\$948,939	\$900,000
Surplus / (Deficit)	\$389,341	\$8,694	\$612,151	\$365,311	\$400,400

If the sewer system has a large or emergency need, the City does not have a separate reserve to address it. It would have to draw on its limited cash reserves in the near term, issue debt to pay for the project, and then likely increase the sewer rates or real estate taxes to repay the debt.



Update on Potential Sewer Monetization



Process to Date

- PFM conducted limited-scope valuation of the system in late 2017 and early 2018

- In 2018, competitive procurement process began with three entities being shortlisted to continue the process
 - Aqua Pennsylvania Waste Water Inc
 - Pennsylvania-American Water Company
 - Wyoming Valley Sanitary Authority

- Management meetings held and considerable due diligence was conducted during the second half of 2018



Process to Date - Continued

- In early 2019, the process was suspended to allow time to enter into sole discussions with WVSA
 - After a period of time, WVSA proposed some non-binding ideas illustrating the relationship between rates and estimated proceeds
 - After receipt of that analysis, the City decided to re-initiate the process with just Aqua and American Water
- For months after the process was re-initiated, the City and WVSA worked together to collaborate on various agreements that ultimately a buyer would need to enter into
- In Fall of 2019, a Request for Indicative Bids was sent to Aqua and PA American
- Indicative offers were received in November but included various conditions



Regulatory and Rate Process

- Both prequalified bidders are regulated by the PUC (Pa Public Utility Commission)
 - Meaning all rates and acquisitions are reviewed and approved by the PUC
- If sale occurs, Buyer will adopt the City's rates at closing
- PUC must approve customer rates
 - Meaning expenditures must be ***prudent***
- Rates can only be changed as a result of an extensive legal rate process which includes
 - Public hearings
 - Review by Office of Consumer Advocate and other advocates
 - Analysis of expenditures to ensure prudence



Current Sewer Rates

- The City currently charges residential customers \$50/year for sewer collection
 - These bills are sent by WVSA and funds are remitted to the City
- WVSA also bills City residents \$55/quarter or \$220 annually for sewer treatment
- In summary, a resident in the City pays \$270/year which is equivalent to \$22.50/month for both collection and treatment



Highlights of Indicative Offers

- ◆ Both bidders submitted multiple offers assuming different purchase prices and estimated rates for the next eight years
- ◆ Both bidders need to conduct additional due diligence on the system including more conversations with WVSA and their various agreements in order to fine tune the proposal
- ◆ **Goal – Assuming the City wants to continue a process, the Team will negotiate a price that represents a fair value of the assets and rates that are also fair and reasonable**
- ◆ **Bottom line – regardless of which entity or which option....sewer rates will be increasing**



Next Immediate Considerations

- ◆ City Stakeholders have very important financial decisions to make in the near term
- ◆ Significant budget deficits are projected for the foreseeable future
- ◆ Sustainable revenue sources or sustainable expenditure reductions need to be thoroughly vetted including:
 - Tax increases providing new sustainable revenue sources
 - Some form of monetization of the sewer system to provide sustainable expenditure reductions to items like pension contributions and debt service
 - Again, sewer rates and/or taxes (i.e. real estate) will need to be increased



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