

**State Water Infrastructure Authority
Viable Utility Reserve Committee
November 13, 2020 Meeting
Agenda Item D – Distressed Criteria Updates**

Division of Water Infrastructure Staff Report

Background

Session Law 2020-79, entitled in part “An Act to Improve the Viability of the Water and Wastewater Systems of Certain Units of Local Government...”, authorizes the State Water Infrastructure Authority (Authority) and Local Government Commission (Commission) to develop criteria to assess and review local government units, and to utilize the assessment and review process to identify distressed units.

At the Special Joint meeting of the Authority and Commission held on October 14, 2020, the staffs of the Division of Water Infrastructure (Division) and the Commission presented the Authority and Commission with proposed Assessment Criteria. The Division and Commission staffs then developed criteria for identifying distressed units (Identification Criteria). At its meeting on October 30, 2020, the Viable Utility Reserve Committee (Committee) of the State Water Infrastructure Authority reviewed and approved the Assessment Criteria and the Identification Criteria shown below.

Note that the Commission adopted the Assessment Criteria and adopted the Identification Criteria at its meeting on November 10, 2020.

Assessment Criteria

The Commission adopted the Assessment Criteria for assessing and reviewing local government units as shown in the table below, entitled “Viable Utility Reserve Assessment Criteria.”

Identification Criteria

The Commission adopted the Identification Criteria used to identify distressed units as follows:

1. A unit whose fiscal affairs are under the control of the Commission pursuant to its authority granted by G.S. 159-181 (“under Commission fiscal control”), or
2. A unit that has not submitted its annual audits for the last two (2) fiscal years to the Commission as required by G.S. 159-34, or
3. A unit with a total Assessment Criteria score that:
 - a) Equals or exceeds 9 for units providing both drinking water and wastewater services, or
 - b) Equals or exceeds 8 for units providing only one service, either drinking water or wastewater, or
4. A unit for which other information is available to or known by the Authority or Commission that reflects and is consistent with, but does not expressly appear in, the Assessment Criteria to account for situations in which the Assessment Criteria score does not wholly or accurately reflect a system’s level of risk due to the limitations of available data.

Viabie Utility Reserve Assessment Criteria

Parameter	Weight	Description	Formula / Other	Data Source
Criteria Required by Statute				
Service Population	1	Identifies smaller systems (less than 10,000 people served).		Varied
Transfers Out	1	Point scored when money is transferred out of the system's dedicated utility fund in 2 or more of the last 5 fiscal years if the system also has a negative surplus in the fiscal year of the transfer, or if the system has no debt and there is a negative surplus with debt service for a \$1 million "test" project. This indicates that money generated by the utilities is not being put back into the system for improvements.		Calculated from LGC data
Transfers In	1	Indicates that the system is not generating enough money to cover expenses. Point scored when money is transferred into the primary water/sewer fund from other sources in 2 or more of the last 5 years.		Calculated from LGC data
Debt Service Coverage Ratio (DSCR)	1	Measures unit's ability to cover loan payments by looking at revenue, expenses, and loan payments (principal and interest). Threshold value is less than 1.1.	(Operating revenues - operating expenses excluding depreciation) / (principal + interest payments)	Calculated from LGC data
Established, operational, and adequately funded program for repair, maintenance, and management		This criterion is measured by other parameters that are identified by an asterisk (*) including compliance, flow moratorium, and UAL control issues.		
Infrastructure/Organizational Criteria				
DW Compliance (*)	1	Point scored for more than 5 MCL violations in a 5-year period or for ongoing treatment technique violations.		NC DEQ-DWR
WW / CS Compliance (*)	1	<ul style="list-style-type: none"> • WW: Point scored if either in the top 10% for number of violations in a 5-year period, or a combination of in the top 20% for number of violations in a 5-year period and more than 50% of inspections document violations for wastewater treatment operations. • CS: Point scored if either the following occur: <ul style="list-style-type: none"> ○ The system is in the top 10% of systems for the number of SSO violations in a 5-year period and the top 20% for the number of SSOs per mile of collection system, or ○ The system is in the top 20% of systems for the number of SSO violations in a 5-year period and the top 10% for the number of SSOs per mile of collection system. 		NC DEQ-DWR

Parameter	Weight	Description	Formula / Other	Data Source
Infrastructure/Organizational Criteria (continued)				
Flow Moratorium (*)	4	Points scored when the system is under a moratorium preventing service expansion due to inability to treat wastewater or because the system has reached 90% of permitted capacity.		NC DEQ-DWR
Revenue Outlook	4	Reflects service unit's ability to generate income in the future. Points scored when the system has high rates AND declining population.		EFC rates; source of population varies
Affordability	1	Identifies economically disadvantaged communities by comparing the service area's population change rate, poverty rate, median household income (MHI), unemployment rate, and property valuation per capita to established state benchmarks. Point scored if 4 or 5 of these indicators are worse than the state benchmark. Note that the benchmark values are updated every year.	<u>Current Benchmarks:</u> Population change: 4.42% Poverty rate: 14.0% MHI: \$52,413 Unemployment rate: 4.0% Property valuation per capita: \$107,620	Developed by DWI/SWIA
Rates	1	Point scored when rates are already high. Indicates that the system is unlikely to be able to increase rates to improve revenue. High rates thresholds are: > \$100/month for combined water and sewer service; > \$50/month for water service only; and > \$60/month for wastewater service only.	2019 inside rate for 5,000 gallons used	EFC
DW Pop / Mile	1	Evaluates population density. Lower density areas tend to face more service challenges. Threshold value is less than 100.	Service Population/ Miles of drinking water pipe	LWSP (see above for population)
Sewer Pop / Mile	1	Evaluates population density. Lower density areas tend to face more service challenges. Note that there is a significant lack of data on miles of sewer line for small systems. Threshold value is less than 100.	Service Population/ Miles of sewer pipe	NC DEQ-DWR
UAL Control Issues - W/S only (*)	3	Points scored for systems that have been identified as medium risk (2) or high risk (1) of accounting control issues associated with water and/or sewer systems based on annual audits.		LGC
Financial Criteria				
UAL Missing Audit	3	If audit not submitted, then treat as if on the UAL for control issues (for FY 19 audits)		LGC
Surplus (deficit) w/ Debt	2	Identifies systems that are not generating enough revenue to cover expenses, asset depreciation, and debt payments. Threshold value is less than or equal to \$0.	Operating Revenues- ((Operating Expenses- Depreciation)+Long-term Debt Service)	Calculated from LGC data
No Debt DSCR Test	1	Similar to the DSCR calculated above but includes \$1 million "test" project if system has no debt to allow evaluation of the ability to finance a simple project. Threshold value is 1.1.		Calculated from LGC data

Parameter	Weight	Description	Formula / Other	Data Source
Financial Criteria (continued)				
% Depreciated	1	Evaluates the financial impact of depreciation of water and sewer assets as they age. Threshold value is greater than 50%.		Calculated from LGC data
Operating Margin	1	Point scored if the system is not generating enough revenue to cover operating expenses. Threshold value is less than 0.	(Operating Revenue - Operating Expenses) / Operating Revenue Includes depreciation	Calculated from LGC data
Quick Ratio	1	Evaluates a system's ability to meet short-term financial obligations with cash or easily accessible funds. Threshold value is less than 1.1.	Current assets (excluding inventories and prepaids) / current liabilities	Calculated from LGC data
Receivables Ratio	1	Measures how well the system is collecting money from customers. Point scored for 3-year average greater than or equal to 2.3 or if there is an increase of greater than or equal to 0.2 in each of the last two years which demonstrates a declining trend in bill payment.	Days Receivables / billing period Days receivables=Net Customer Accounts Receivable/Charges for services /365	Calculated from LGC data

List of Acronyms		
CS = Collection System	DWR = Division of Water Resources	SSO = Sanitary Sewer Overflow
DEQ = Dept. of Environmental Quality	EFC = Environmental Finance Center	SWIA = State Water Infrastructure Authority
DSCR = Debt Service Coverage Ratio	LGC = Local Government Commission	WW = Wastewater (sewer)
DW = Drinking Water	LWSR = Local Water Supply Plan	UAL = Unit Assistant List generated by LGC to identify communities that may have problems with accounting procedures identified through audits
DWI = Division of Water Infrastructure	MCL = Maximum Contaminant Level	

Staff Recommendation

Staff recommends that the Viable Utility Reserve Committee approve the Assessment Criteria and the Identification Criteria as presented above. This action would parallel the action taken by the Local Government Commission on November 10, 2020. If approved by the Committee, this Committee recommendation will be presented to the full Authority at its meeting on November 18, 2020.
