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TO: COUNCIL MEMBERS

FROM: David Whitaker, Director 
Legislative Policy Division Staff

DATE: July 8, 2020

RE: Second Report on the Fiscal Review of DWSD

Council President Brenda Jones and Council Member Janee Ayers requested that the Legislative Policy Division (LPD) prepare reviews of the fiscal operations of the Detroit Water and Sewerage Department (DWSD), and its financial relationship with Great Lakes Water Authority (GLWA). To report on such a complex request, this is the second report of several that we will prepare on the finances of DWSD.

We thank the DWSD Director, Gary Brown and his staff, the GLWA CEO, Sue McCormick and her staff, for their assistance as we prepared this report. We must especially commend the DWSD Director, Gary Brown and his staff for some of the excellent work that they have accomplished over the past three and a half years in several areas. They took a system with billions of dollars in debt, survived through a difficult bankruptcy, a bifurcation with GLWA, and continued providing clean water and safe disposal of sewage.

One of our long-range objectives in providing this report is to make every effort to ensure that our children, grandchildren and future generations have access to safe, clean and affordable water, and safe disposal of waste water including drainage.

We will address the Flow of Funds requirement in the agreement with GLWA and the Master Bond Ordinances, and then we will present questions to DWSD management and the Office of the Chief Financial Officer on DWSD financial activity.

A requirement of the Master Bond Ordinances (MBO), relating to the assumption by GLWA of all the outstanding debt related to the regional and DWSD's local water supply and sewage disposal systems, was the establishment of the Flow of Funds. DWSD, however, continues to be required

to pay the debt service (principal and interest payments) on the outstanding debt associated with DWSD's local water supply and sewage disposal systems. However, part of GLWA's annual \$50 million lease payment to DWSD over the next 40 years under the terms of the lease agreement between GLWA and DWSD is used to pay DWSD's debt service on the outstanding debt associated with local system improvements, debt service on the outstanding debt associated with the City of Detroit's share of common-to-all system improvements, and local system improvements.

Both GLWA and DWSD have a Water Master Bond Ordinance and a Sewer Master Bond Ordinance. The Ordinances provide additional security for payment of the bonds. All revenues of the systems (GLWA and DWSD) were pledged and are deposited into Revenue Receipts Funds, which are held in trust by a trustee, U.S. Bank National Association. GLWA and DWSD both have Receipt Funds for Water and Sewer.

Each month, the budgeted amount for the wholesale charges for water and sewerage DWSD is purchasing from GLWA is deducted from the Revenue Receipts Fund, then the transfers of cash according to the MBO are as follows:

(As Council reviews the information below, LPD suggests that you also review Attachment I, which represents a flowchart labeled 'Master Bond Ordinance Flow of Funds')

Order of transfers according to the MBO Flow of Funds

First - Operation & Maintenance (O&M) expenses based on 1/12th of the current year's budget. Also, O&M Legacy Pension Allocation (includes administrative fee) and Accelerated Legacy Pension Allocation (includes B&C notes obligation). This fund is held outside the trust, it is held by DWSD for monthly operating and maintenance expenses based on the current years' approved budget. It is for the maintenance of the water and sewer systems as may be necessary to preserve the systems in good repair and working order. This transfer of funds based on 1/12 of the current year's budget has led to cash flow problems with the sewer fund. This will be explained more in detail later in this report.

Second - Senior Lien Bond Interest & Redemption Fund - Debt Service Account and Bond Reserve. This is determined by the trustee to provide the cash for the debt payments on the due dates.

Third - Second Lien Bond Interest & Redemption Fund - Debt Service Account and Bond Reserve. This is determined by the trustee to provide the cash for the debt payments on the due dates.

Fourth - State Revolving Fund (SRF) Junior Lien Bond Interest & Redemption Fund based on SRF requirements, if any.

Fifth - If Pension Junior Lien Bonds are issued, Pension Junior Lien Bond Interest & Redemption Fund based on requirements.

Sixth - If Pension Junior Lien Bonds are not issued, Pension Obligation Payment Fund contributions equal to 1/12th of the Required Annual GRS Payment and 1/12th of the BC Note Obligation are required.

Seventh - Water Residential Assistance Program (WRAP) based on 1/12th of a percentage of budgeted revenue – currently 0.5%.

Eighth - Budget Stabilization Fund based on 1/12th of the annual budget. For fiscal years 2019 and 2020, there are no required budget transfers.

Ninth - Extraordinary Repair & Replacement Reserve Fund based on an amount needed to bring the balance up to the Maximum Requirement of the Fund.

Tenth - Improvement & Extension (I&E) Fund Local Account, at the written direction of an Authorized Officer to the Trustee, an amount that GLWA deems advisable for Local Water and Sewer systems, provided that no amount shall be deposited in either such account for so long as a withdrawal from the Fund remains unpaid. The lease payment from GLWA and any other cash receipts are transferred to this fund.

Eleventh - Surplus Fund - this Fund has never had any deposits made into it.

For Council’s edification, Attachment II represents a DWSD forecast of Water and Sewer net cash flows from trust receipts and disbursement for FY 2020. This forecast also shows the individual transfers from the trust as depicted in the MBO flow of funds schedule above. The following shows the results of the first five (5) years of the MBO Flow of Funds for DWSD Water and Sewer.

DWSD Water Net Cash Flows from Trust Receipts & Disbursements for Fiscal Years 2016-2020

	Total FY 2016	Total FY 2017	Total FY 2018	Total FY 2019	Total FY 2020 9 Mos YTD
WATER					
Adjusted Receipts	44,647,981	96,451,105	101,233,147	99,868,219	74,995,005
Disbursements	(47,809,552)	(93,066,144)	(93,049,457)	(97,694,600)	(73,876,869)
Improvement & Extension Trans	-	-	-	(8,407,080)	-
Net Change (for Fiscal Year)	(3,161,571)	3,384,961	8,183,690	(6,233,461)	1,118,136
Ratio of Receipts to Disbursements	93%	104%	109%	102%	102%

The above figures may not add and/or subtract as prior year adjustments and rounding occur.

In the above table for water, the Ratio of Receipts to Disbursements, DWSD Water has adjusted receipts greater than required disbursements in four of the five fiscal years (104%, 109%, 102% and 102%). These percentages are shown in the above table in the shaded area. For fiscal year 2019, net cash flow was \$2.2 million sans transfer to Imp. & Ext. Fund. This means that DWSD has met all of the requirements of the MBO, and after 4-3/4 fiscal years, has a positive balance.

DWSD Sewer Net Cash Flows from Trust Receipts & Disbursements for Fiscal Years 2016-2020

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	<u>Total</u> <u>FY 2016</u>	<u>Total</u> <u>FY 2017</u>	<u>Total</u> <u>FY 2018</u>	<u>Total</u> <u>FY 2019</u>	<u>Total FY 2020</u> <u>9 Mos YTD</u>
SEWER					
Adjusted Receipts	121,011,834	233,723,367	242,104,791	271,866,997	201,385,204
Disbursements	(122,297,300)	(261,963,973)	(266,217,825)	(271,018,306)	(206,100,693)
Net Change (for Fiscal Year)	(1,285,466)	(28,240,606)	(24,113,034)	848,691	(4,715,489)
Shortfall advance from GLWA	1,285,466	28,014,534	24,113,034	-	-
Ratio of Receipts to Disbursements	99%	89%	91%	100%	98%

The above figures may not add and/or subtract as prior year adjustments and rounding occur.

In the above table for sewage, the Ratio of Receipts to Disbursements, DWSD Sewage has not had adjusted receipts equal to, or greater than required disbursements in each of the first three fiscal years (99%, 89%, and 91%). This is reflected in the above table in the shaded area as percentages. In addition, FY 2020 could end up with required disbursements being greater than adjusted receipts.

In fiscal years 2016 and 2017, adjusted receipts were less than required disbursements by \$1,285,466 and \$28,014,534 (as depicted in the table above), for a total of \$29,300,000. This amount was not recorded until June 30, 2018, when it was recorded as a loan from GLWA, as GLWA advanced the necessary funds to make the required disbursements. In the lease agreement with GLWA and the Master Bond Ordinance, augmented by the June 2018 MOU between GLWA and DWSD, any shortfall by DWSD must be paid by GLWA, at an interest rate to be repaid by DWSD, based on the three-year U.S. Treasury rate (2.63%), plus 150 basis points. This interest rate over a three-year repayment plan, at an interest rate of 4.13% means that DWSD must pay \$866,683 per month from July 1, 2018 until June 30, 2021, and this will have to be built into future budgets. The principal balance has been paid down to \$13,469,975 as of February 29, 2020.

Also, in the above table, the shortfall by DWSD for sewage in fiscal year 2018, \$24,113,034 was also made up, or paid, by GLWA, resulting in another loan due GLWA. This amount will also be charged at 4.13%, and the monthly payments for the 36-month period from July 1, 2019 until June 30, 2022 has been calculated to be \$703,460. This amount has been paid since 7-1-2019, and the balance at February 29, 2020 is down to \$18,953,111.

In summary, GLWA advanced DWSD funds in fiscal years 2016, 2017 and 2018 for shortfalls in net cash flows per the Sewer Fund. Since that time, in fiscal year 2019 DWSD has balanced their receipts and their disbursements, and has been making the required payments per the MBO and the lease agreement.

LPD respectfully requests that representatives of DWSD respond to following questions/requests:

1. According to the DWSD's net cash flows through March 2020, a \$4.7 million shortfall in the Sewer Fund is projected. What are the main drivers causing this shortfall?
2. Please provide any preliminary cash flow numbers for the Sewer Fund for the months of April through June 2020, if available.

3. What plans have been implemented by DWSD to resolve the potential \$4.7 million shortfall, and any projected shortfalls in the months of April through June 2020, by June 30, 2020?
4. What funds are being used to repay the Sewer Fund \$29.3 million and \$24.1 million shortfalls due to GLWA over a three-year period plus interest in accordance with the June 2018 MOU agreement between GLWA and DWSD?
5. What is the projected cash balance as of June 30, 2020 in the Sewer Fund? Could any this cash be used to pay down the shortfall balances due GLWA?

Attachments

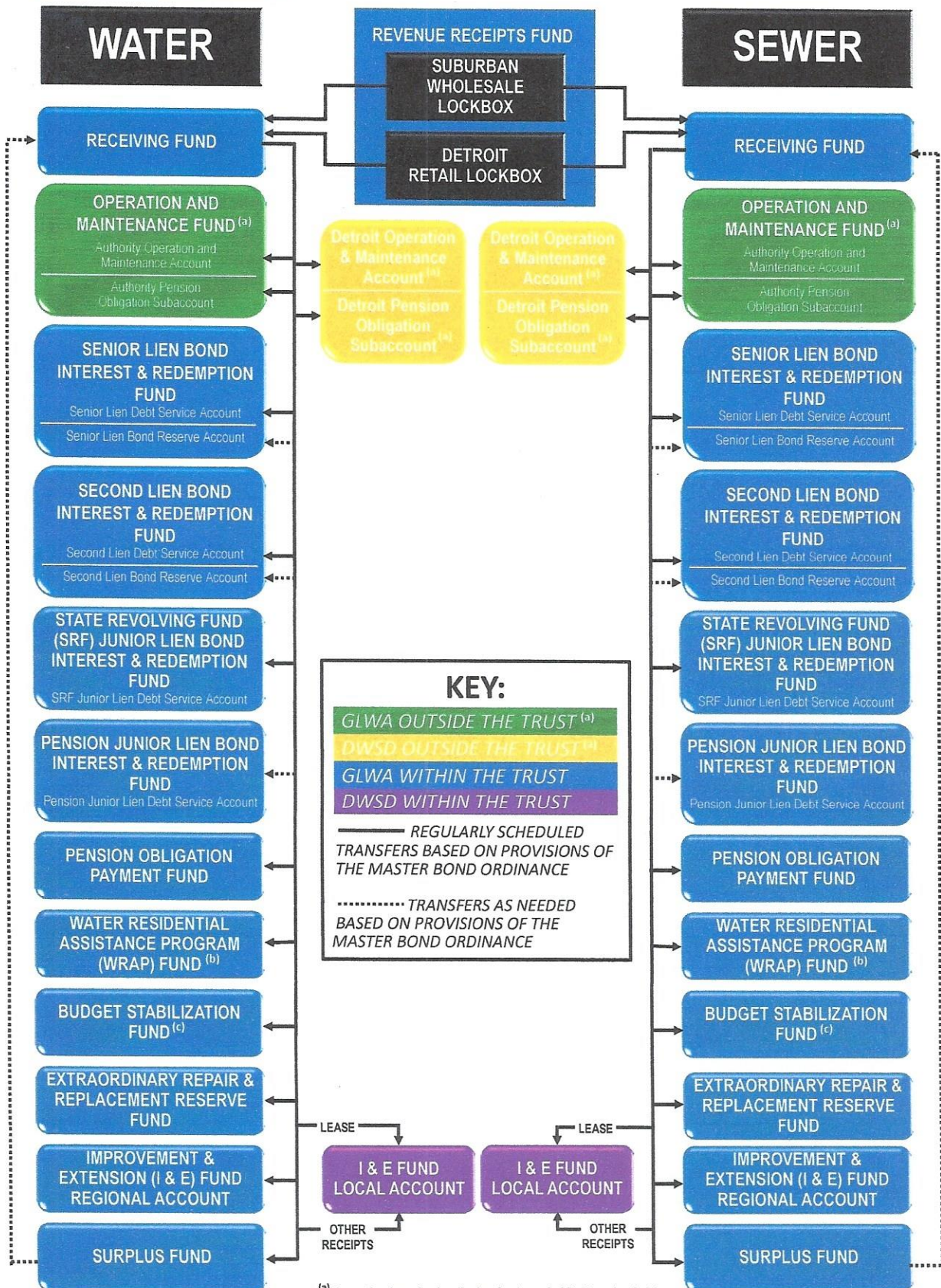
cc: Gary A. Brown, Director, DWSD
Thomas Naughton, DWSD Chief Financial Officer
Dave Massaron, Chief Financial Officer
Auditor General's Office
Tanya Stoudemire, Budget Director
Avery Peoples, Mayor's Office

Attachment I

Flowchart of Master Bond Ordinance Flow of Funds for both GLWA and DWSD
In Accordance with the Master Bond Ordinances

Master Bond Ordinance Flow of Funds

Note: This chart is a summary of the Master Bond Ordinance Flow of Funds and is for illustrative purposes only. For a more complete and comprehensive description of the flow of funds, reference is made to each Master Bond Ordinance, a copy of which is available at glwater.org.



(a) Except for these funds, all other funds are held in Trust by the Trustee.

(b) Disbursing fund for WRAP

(c) For the Detroit Local Systems per Section 515 of the Master Bond Ordinance.

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Attachment II

DWSD's forecast of Water and Sewer net cash flows from trust receipts and
disbursement for FY 2020

THE UNIVERSITY OF CHICAGO
DEPARTMENT OF CHEMISTRY

The Cash @ GLWA deficit is expected to approximate \$19 million by June 30



	ACTUALS						FORECAST		
	Six Months Ended Dec-19	Month Ended Jan-20	Month Ended Feb-20	Month Ended Mar-20	Month Ended Apr-20	Month Ended May-20	Month Ended Jun-20		
Deposits									
Retail Receipts	\$ 186,507	\$ 32,589	\$ 30,965	\$ 26,262	\$ 22,575	\$ 22,575	\$ 22,575	\$ 22,575	\$ 22,575
Wayne Metro CARES Allocation	-	-	-	-	1,000	1,000	1,000	1,000	1,000
Trust Interest	35	4	4	5	5	5	5	5	5
DWSD Lease Deposit (Debt Service)	4,290	715	715	715	715	715	715	715	715
Transfer Budget Savings (incl. Covid-19)	2,600	-	4,500	-	2,484	3,112	2,156	2,156	2,156
Total Deposits	193,432	33,308	36,184	26,982	25,779	26,407	25,451	25,451	25,451
Transfers from Trust									
GLWA Wholesale	(103,551)	(17,259)	(17,259)	(17,259)	(17,259)	(17,259)	(17,259)	(17,259)	(17,259)
DWSD IWC	(712)	(116)	(124)	(124)	(124)	(124)	(124)	(124)	(124)
DWSD O&M	(51,003)	(7,667)	(7,667)	(7,667)	(7,667)	(7,667)	(7,667)	(7,667)	(7,667)
DWSD Debt Service	(34,380)	(5,730)	(5,730)	(5,730)	(5,730)	(5,730)	(5,730)	(5,730)	(5,730)
DWSD Pension O & M	(3,564)	(594)	(594)	(594)	(594)	(594)	(594)	(594)	(594)
DWSD Non-Operating Pension	(3,747)	(625)	(625)	(625)	(625)	(625)	(625)	(625)	(625)
DWSD WRAP	(383)	(64)	(64)	(64)	(64)	(64)	(64)	(64)	(64)
Total Transfers	(197,342)	(32,054)	(32,062)	(32,062)	(32,062)	(32,062)	(32,062)	(32,062)	(32,062)
Increase (Decrease) in Trust	(3,910)	1,254	4,122	(5,080)	(6,283)	(5,655)	(6,611)	(6,611)	(6,611)
Balance at Beginning of Period	2,796	(1,113)	140	4,262	(817)	(7,101)	(12,755)	(12,755)	(12,755)
Balance at End of Period	\$ (1,113)	\$ 140	\$ 4,262	\$ (817)	\$ (7,101)	\$ (12,755)	\$ (19,367)	\$ (19,367)	\$ (19,367)

(Amounts in 1,000's)

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