

Edgemont Ranch Metro District Public Rate Hearing: Water & Sewer Enterprise Funds
October 17, 2024
Recommendations to the Board of Directors

This year ERMD staff have reported the District is incurring significantly higher operating and maintenance costs. The most recent example is the repair to a broken water main near Victoria Village. Our engineer estimate for the repair was approximately \$350,000 (which took into account very large recent cost increases for asphalt, pipes, valves, and labor). However, the lowest bid we received came in at \$550,000. A 57% increase over expectation. The District is experiencing similar cost increases across material, equipment and services in all of our operations.

ERMD's Board of Directors engaged the services of a Reserve Analysis firm to help us understand the future costs for the District to provide for adequate cash reserves that will properly maintain our capital assets. A summary of the report by Association Reserves (AR) of Golden Colorado is attached in Appendix I. AR's Reserve Study generally recommends that Metro Districts maintain reserves in the range of 70% to 100% of expected full replacement costs of its capital assets in order to avoid significant special assessments.

Taking into account the recent inflationary trends and our existing reserve levels, the Reserve Study recommended a one-time special assessment of \$4,100,000 (\$3.5mm for the General Account and \$0.6mm for the Water Account) and increasing our **annual** cash transfers to reserves by \$820,000 to bring our reserve levels to 100% of fully funded replacement costs. A Special Assessment of \$4.1mm would cost each owner of a property in the District approximately \$4,775.00 However, we do not recommend the Board pursue a Special Assessment as outlined below.

The following issues should be considered prior to the Board taking action on ERMD's reserve situation:

1. General Account Reserves, Roads: The Reserve Study findings includes full reserving for our 13.2 miles of roads, a significant portion of which are more than 25 years old. We recommend a different approach for dealing with road reserves. Paved roads generally have a 20 to 30-year life. Requiring current District residents to pay for fully funding road replacement costs is neither realistic nor fair. A long-term borrowing to finance roads that spreads the cost among future residents over the life of the road is more appropriate. Much like the 30-year bond that financed the initial road work when Edgemont was established. The bond was fully repaid in May 2024 and residents will no longer pay property taxes for this road related bond).
2. Adjusting AR's Recommendations for Road Reserves: Approximately 90% of AR's reserve recommendations are related to road resurfacing and repair, all of which reside in the General Account. We recommend long term borrowings to meet the District's major road needs.
3. Water System Reserves: The \$550,000 cost of the Victoria Village water main repair will completely exhaust Water Reserves. The portion of the \$550,000 cost related to the road expenses should be paid out of the General Account Roads. The Water reserves should be replenished as soon as possible with transfers from the General Account and from excess reserves in the Sewer Fund.

Taking into consideration the above issues and ERMD's current unallocated cash and its existing cash reserves, we recommend the following actions by the Board to meet higher operating costs and increase our annual rate of cash transfers to our various reserve accounts:

1. No special one-time assessment to be established at this time. No increase in road or snow fees.
2. Prior to Year-end, allocate up to \$325,000 of our existing unallocated cash into General Fund reserves.
3. Allocate 100% of the unallocated cash (approximately \$325,000) in the Water Account into Water Reserves. Prior to year-end allocate the amount necessary to replenish Water Reserves to a level not less than \$15,000 from the Sewer Fund. That amount should be less than 10% of current Sewer Fund Reserves and cash.

4. Approve an increase of **\$8.00 per month** to the Water Maintenance Fee, no increase to Water Base Fees. Annual total Water Fees increase to \$788.00. Such increase to be effective January 1, 2025.
5. Approve an increase of **\$4.00 per month** to the Sewer Maintenance Fee, no increase in Sewer base Fees, bringing the yearly total Sewer Fees to \$1,188.00. Such increase to be effective January 1, 2025. The total monthly fee increase for both water and sewer would equal \$12 per month, an increase of 7.2%.
6. In general, adopt a reserving policy to maintain total overall reserves at a level between 70% to 90% of recommended fully funded capital asset reserve levels for all District non-road assets.

Below is a summary of ERMD’s 10-year financial forecast showing revenues, expenses, cash flow and reserve levels. The key element is that Edgemont will not be able to rely on the rapid growth in lots and homes experienced in the past. Absent a rate increase our revenue growth would stop while inflation and replacement of aging infrastructure would deplete our cash reserves. The first forecast below is our best estimate of cash flow and reserves if we do nothing. The District would go cash flow negative in two years and our reserve levels would drop below 20% of recommended levels within 10 years. Note that in this scenario it is estimated the Sewer Fund would have a negative balance of -\$133,000 at the end of the period.

| ERMD Forecasted Cash Flow & Cash Reserves With No Monthly Fee Increase | | | | | | | | | | |
|---|------------------|------------------|------------------|------------------|-------------------|-----------------|-----------------|-----------------|----------------|-----------------|
| | 2025 | 2026 | 2027 | 2028 | 2029 | 2030 | 2031 | 2032 | 2033 | 2034 |
| Total Revenues | 2,172,283 | 2,158,302 | 2,170,584 | 2,180,300 | 2,190,166 | 2,205,185 | 2,218,645 | 2,231,089 | 2,243,694 | 2,256,466 |
| Total Expenses | 1,903,581 | 2,038,160 | 2,298,442 | 2,309,369 | 3,638,754 | 2,322,991 | 2,355,024 | 2,348,600 | 2,313,265 | 2,415,069 |
| Net Cash Flow | 268,702 | 120,142 | -127,858 | -129,069 | -1,448,588 | -117,806 | -136,379 | -117,511 | -69,571 | -158,603 |
| Beginning Reserves | 2,284,671 | 2,553,373 | 2,673,515 | 2,545,657 | 2,416,588 | 968,000 | 850,193 | 713,814 | 596,303 | 526,732 |
| Change | 268,702 | 120,142 | -127,858 | -129,069 | -1,448,588 | -117,806 | -136,379 | -117,511 | -69,571 | -158,603 |
| Ending Reserves | 2,553,373 | 2,673,515 | 2,545,657 | 2,416,588 | 968,000 | 850,193 | 713,814 | 596,303 | 526,732 | 368,128 |

Applying the recommended monthly rate increases of \$8.00 and \$4.00 in the Water and Sewer Funds respectively, as summarized in the table below, is forecasted to keep the District cash flow positive for at least the next 5 years and maintain reserves at a 70% to 90% level for our non-road assets.

| ERMD Forecasted Cash Flow & Cash Reserves With Proposed Monthly Fee Increase: Water + \$8 and Sewer + \$4 | | | | | | | | | | |
|--|------------------|------------------|------------------|------------------|-------------------|------------------|------------------|------------------|------------------|------------------|
| | 2025 | 2026 | 2027 | 2028 | 2029 | 2030 | 2031 | 2032 | 2033 | 2034 |
| Total Revenues | 2,292,942 | 2,283,948 | 2,296,509 | 2,306,225 | 2,316,091 | 2,331,110 | 2,344,571 | 2,357,014 | 2,369,620 | 2,382,391 |
| Total Expenses | 1,903,508 | 2,038,009 | 2,298,206 | 2,309,043 | 3,638,332 | 2,322,466 | 2,354,389 | 2,347,847 | 2,312,387 | 2,414,057 |
| Net Cash Flow | 389,434 | 245,939 | -1,697 | -2,818 | -1,322,241 | 8,644 | -9,819 | 9,167 | 57,233 | -31,666 |
| Beginning Reserves | 2,284,671 | 2,674,105 | 2,920,044 | 2,918,347 | 2,915,529 | 1,593,288 | 1,601,932 | 1,592,114 | 1,601,280 | 1,658,513 |
| Change | 389,434 | 245,939 | -1,697 | -2,818 | -1,322,241 | 8,644 | -9,819 | 9,167 | 57,233 | -31,666 |
| Ending Reserves | 2,674,105 | 2,920,044 | 2,918,347 | 2,915,529 | 1,593,288 | 1,601,932 | 1,592,114 | 1,601,280 | 1,658,513 | 1,626,847 |

The key assumptions in these forecasts are for 3% annual inflation while new lot development stops in 2027. The District’s interest income is forecasted to drop as interest rates fall and our cash balances drop. Finally, it will be necessary to use some of our cash reserves to pre-pay a portion of our new sewer plant debt by 2029. The known large future capital expenses are new water tanks, water treatment plant filter replacement, phosphorus filter installation in the sewer plant, vehicle replacement, new water meters and road sealing.

Although we would be pleased if this were the last fee increase needed over the next 10 years, it must be understood that these forecasts are based on estimates and assumptions that may not become reality. Inflation may be higher or lower, equipment may need to be repaired and replaced at a faster pace and a higher cost. The future Board should review our financial position and outlook on a regular basis to ensure that our cash reserves are sufficient to maintain our assets and services at an appropriate level. Finally, we recommend the Board consider implementing progressive water usage fees in the future to better align residents water usage habits with the realities of the Southwest.

Appendix I. Reserve Study Summary Tables

| ERMD Reserve Analysis of Association Reserve Study | | | | | |
|---|-------------------------|------------------|-----------------|---------------------|--------------------|
| Based on ERMD Financial Numbers as of 01.01.2024 | | | | | |
| | General Fund + Roads | Water Fund | Sewer Fund | Unallocated Cash | Total ERMD |
| Current Reserves 01.01.2024 | 574,970 | 16,899 | 836,077 | | 1,427,946 |
| Unallocated Cash | | 326,786 | 536,329 | 364,424 | 1,227,539 |
| Reserves + Cash | 574,970 | 343,685 | 1,372,406 | 364,424 | 2,655,485 |
| Recommended Reaerves: 100% | 7,616,414 | 905,809 | 411,799 | 0 | 8,934,022 |
| Difference | (7,041,444) | (562,124) | 960,607 | 364,424 | (6,278,537) |
| % Difference | 7.5% | 37.9% | 333.3% | N/A | 29.7% |
| Recommended Special Assessment | 3,500,000 | 600,000 | 0 | 0 | 4,100,000 |
| Current Annual Reserving Rate* | 177,000 | 102,395 | 29,910 | 0 | 309,305 |
| Recommended Reserving Rate | 915,000 | 90,000 | 124,000 | 0 | 1,129,000 |
| Difference | (738,000) | 12,395 | (94,090) | 0 | (819,695) |
| % Difference | 19.3% | 113.8% | 24.1% | N/A | 27.4% |

Based on the District's financial statements as of January 1, 2024, the reserve study recommended we increase General Account Reserves by \$7,041,444 to \$7,616,414 (of which \$7,085,414 relate to Roads – most of which are > 25 years old). They recommend Water Reserves to increase \$562,124 to \$905,809 and that Sewer Reserves are in excess by \$960,607. However, by year-end 2024 the \$560,000 Victoria Village water main repair is forecasted to reduce Water, Sewer and General Account reserves and cash to the levels outlined below.

| Actual ERMD Annual Reserve Rate vs Recommended Annual Rate Per Reserve Study* | | | | | | |
|--|----------------------------|-------------------------------|-----------------|------------------|--------------------|---------------------------------|
| | General Account - Roads | General Account - Nonroads | Water Fund | Sewer Fund | Total Reserve Rate | Total Reserve Rate Non Roads |
| Current ERMD Rate | 110,000 | 68,900 | 102,395 | 29,910 | 311,205 | 201,205 |
| Recommended Rate | 803,000 | 112,000 | 90,000 | 124,000 | 1,129,000 | 326,000 |
| Difference | -693,000 | -43,100 | 12,395 | -94,090 | -817,795 | -124,795 |
| * Note: Sewer Fund Reserving and excess Cash Flow has been adjusted for sewer debt repayment. | | | | | | |
| ERMD ACTUAL CASH + RESERVE BALANCES vs RECOMMENDED RESERVE BALANCES per Reserve Study* | | | | | | |
| | GA - Roads | GA - Non Roads | Water Fund | Sewer Fund | Unallocated Cash | Total Reserves |
| Reserve Balances Year End 2024 | 490,000 | 260,000 | 17,000 | 940,000 | 250,000 | 1,957,000 |
| Fully Funded Reserve Balance Year End 2024* | 7,085,414 | 531,000 | 905,000 | 411,800 | 0 | 8,933,214 |
| Difference | -6,595,414 | -271,000 | -888,000 | 528,200 | 150,000 | -7,226,214 |
| Available Cash YE 2024 | 200,000 | 160,000 | 375,000 | 500,000 | 150,000 | 1,385,000 |
| Difference | -6,395,414 | -111,000 | -513,000 | 1,028,200 | 150,000 | -5,841,214 |

Once we adjust for the Roads component, our reserve and cash balances are forecasted to end the year within 80% of fully funded status. However, Association Reserves, and District staff dealing with cost increases, recommend ERMD increase our Reserving rates by ~\$124,750 per year. The recommended \$8.00 monthly increase in water fees and \$4.00 monthly increase in sewer fees beginning in 2025 is forecasted to raise approximately \$121,650. Which we believe is sufficient for the near future in light of current conditions.