



Financial Benchmarking
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Financial Benchmarking

What Does This Mean and How is it Used?

- Benchmarking: The process of comparing the Business Practices and performance standards of your organization to that of other organizations within the same industry
- Benchmarking attempts to determine the best practices of other organizations in the same industry to improve the practices in your own organization



Benchmarking

The Joint Action Agency Perspective

- The purpose of the Benchmarking Program is to incorporate publicly available metrics utilized by the three major credit rating agencies to achieve and maintain the highest possible bond ratings for Joint Action Agency “JAA” projects.
- Higher bond ratings result in lower borrowing costs and subsequently lower cost of power for all participants.
- Ultimately, investors in JAA debt as well as power supply counterparties and financial institutions look to the Member Municipalities’ credit when they evaluate the creditworthiness of JAA.
- The JAA is only as strong as its weakest member.

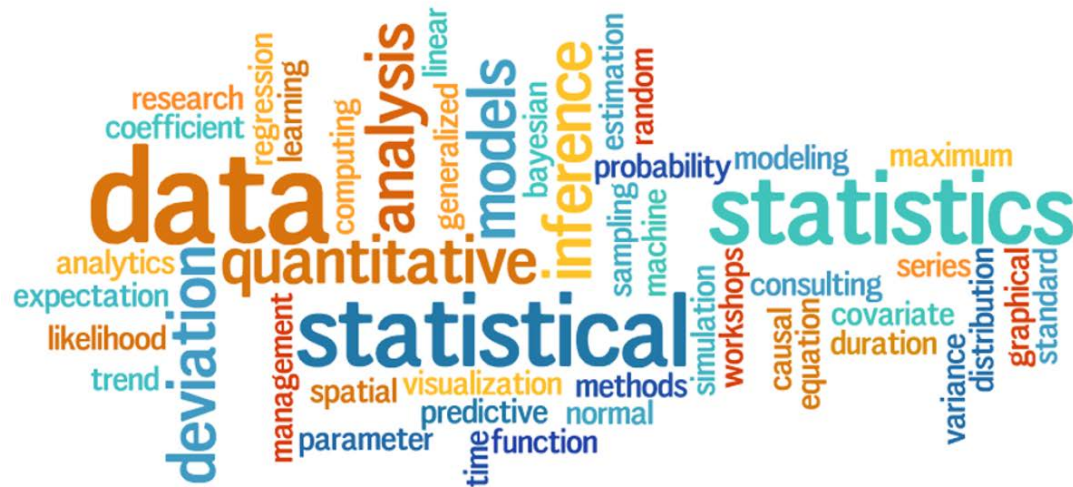


Benchmarking

Use of Statistics in Benchmarking

The following is a short introductory clip about the use of Statistics to tell the story of your organization

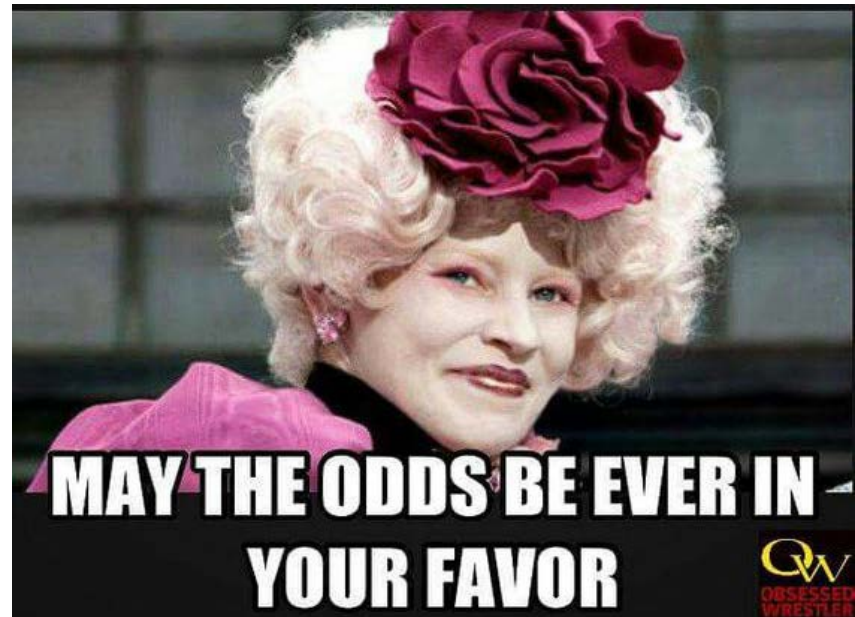
- https://www.youtube.com/watch?v=UASWcDsH_nM&t=11s



What Criteria is Used to Assess Member Financial Health?

QUANTITATIVE METRICS

- A. Covenant Compliance Ratios
- B. Ratio Analysis
- C. Income & Expense Ratios
- D. Cash Reserves
- E. Rate Analysis



What Criteria is Used to Assess Member Financial Health?

QUALITATIVE MEASURES

- Policy Review and Development
- Rate Setting Studies
- Power Supply Planning Practices



"Not everything that counts can be counted, and not everything that can be counted counts."

- Albert Einstein

What Criteria is Used to Assess Member Financial Health?

QUANTITATIVE METRICS

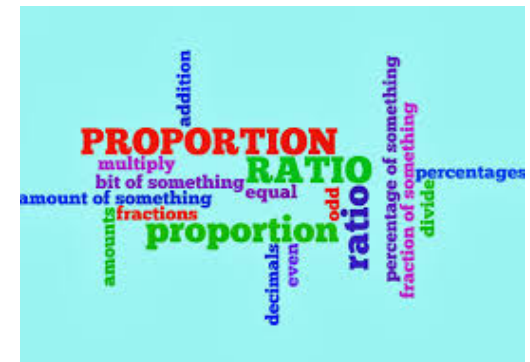
A. Covenant Compliance Ratios

1. Debt Service Coverage

- Net Revenues-O&M + Depr./Total Debt Service
- Key ratio in all bond covenant documents
- Rating Agencies like no less than 1.1X coverage
- Look Back at the previous 3 years

2. Fixed Obligation Charge Coverage

- Includes debt service & fixed costs embedded in JAA generation projects
- Includes fixed expense embedded in Purchase Power Contracts
- Includes Pension Expense



What Criteria is Used to Assess Member Financial Health?

QUANTITATIVE METRICS

Nuances of JAA Fixed Charge Coverage calculations

Fixed Obligation Charge Coverage

S&P- Will treat 50% of the JAA's Purchase Power expenses as a fixed cost

Fitch- Will treat 30% of the JAA's Purchase Power expenses using a 8.0X multiple to create a debt- equivalent figure. (this can be adjust based on provision of documentation the indicated no fixed component to a PPA)

Moody's- does not assess a debt equivalent to JAA PPA's although there is much talk on the subject

S&P Global
Ratings

MOODY'S

FitchRatings

What Criteria is Used to Assess Member Financial Health?

B. Ratio Analysis

Utility Debt Ratios

These ratios compare the individual member ratio to the collective average ratio of members with debt.

Good way to compare members to each other regardless of organizational size or structure

- Debt per KW of Demand
 - Uses the system peak load in the calculation

Debt as % to Total Revenue

- Speaks to utility's ability to manage debt and make its payments



What Criteria is Used to Assess Member Financial Health?

B. Ratio Analysis- Cont'd

Utility Debt Ratios

- Total Debt per Customer
 - Looks at the impact # of customers makes on the utility's ability to pay its debts.
 - Judges the impact of customer loss on debt servicing
- Total Debt per KWh Sold
 - Judges the impact of a large customer on the utility's ability to pay its debts.



What Criteria is Used to Assess Member Financial Health?

Income & Expense Ratios

These ratios look at the overall effectiveness of the Utility's operations.

Compares the costs to operate a utility versus the income it generates

These Ratios compare the member ratio to the industry median based on municipal size (APPA Financial and Operating Ratio Survey)

- Operating Ratio (O&M/Revenue)
- Net Income per Revenue Dollar
- Total O&M Expense per KWh Sold
 - Are you generating at an effective cost?
- Uncollectible Accounts per Revenue Dollar
 - Also look at "days to collect"- should be under 30 days



What Criteria is Used to Assess Member Financial Health?

C. Cash Reserves

- Months of O&M in Unrestricted Cash
 - 90 days minimum for A rated debt
- Depreciation Funding
 - Exhibiting a net operating income BEFORE adding back depreciation
 - Zero or Breakeven is acceptable
 - Demonstrates planning for future capital improvements



What Criteria is Used to Assess Member Financial Health?

D. Competitiveness Ratio

- How do your rates compare to the competitors (IOUs/Co-ops) in your State/Territory
 - Residential
 - Commercial
 - Industrial
- If your rates are higher than your local IOU's, you need to look at what is wrong.....



What Criteria is Used to Assess Member Financial Health?

QUALITATIVE MEASURES

These measures are more textual in nature.

Policy and procedural driven

Demonstrates well organized planning and execution strategies

- Cash reserves policy
 - Do you have a WRITTEN policy for the maintenance of cash reserves?
 - Are the reserves for the Electric fund and the Water/Sewer fund kept separately?



What Criteria is Used to Assess Member Financial Health?

QUALITATIVE MEASURES Cont'd

- Capital Spend Policy
 - Do you have a FORMAL Capital Outlay Plan that has been passed by your Council/Board?
 - Board approval increases your chances of successful implementation.
 - Is that written Capital Outlay Plan detailed for AT LEAST the next 5 years? And summarized for a total of 10 years?



What Criteria is Used to Assess Member Financial Health?

QUALITATIVE MEASURES Cont'd

B. Regular Rate Studies & Rate Setting

- Has the Municipality conducted an independent **COMPREHENSIVE** cost of service study within the previous 5 years?
- Were the recommendations from the study implemented?
- Were rate increases necessary to meet debt covenant obligation, capital needs and cash reserve goals implemented?
- Were those rate studies conducted at the individual class level? (i.e. residential, commercial, industrial etc)
- Does the municipality require approval at the state level to change rates?



What Criteria is Used to Assess Member Financial Health?

QUALITATIVE MEASURES Cont'd

- Power Sales Cost Recovery (PSCR) Adjustment
 - Are all Purchased Power and market based fuel expenses recovered within 12 months of being incurred?
- General Fund Health of the Member Municipal
 - What is the balance in the General fund of the City?
 - A low or negative balance in the General Fund means your city may be looking to the robust balances in the Utility fund as a source of cash flow.



What Criteria is Used to Assess Member Financial Health?

QUALITATIVE MEASURES Cont'd

- Electric Fund Transfers (PILOT or other)
 - Are the transfers made according to a RESTRICTED formula, resolution or ordinance of municipality's Council/Board leaving 3 or more months of cash reserves at the electric utility?
- Debt Rating- G/O and Revenue based
 - For the utility AND the total municipality

What Criteria is Used to Assess Member Financial Health?

QUALITATIVE MEASURES Cont'd

Power Supply Planning- Written policy including:

Diversification structure: Nat gas, Wind, Solar, Hydro

Risk Mitigation structure: Layering of energy and capacity purchases over a defined period of time

Risk Management Policy: Authority over products, purchasers, counterparties, volumes etc.



What's your score???

Every question whether quantitative or qualitative is assigned points along a sliding scale of acceptability.

Critical Metrics such as DSCR and Days Cash are assigned higher points than other metrics (debt/KW demand, Debt per customer)

Total scoring points divided into total possible points determines a scoring percentage.

| <u>Scoring Scale %</u> | <u>Grade</u> | <u>Description</u> |
|------------------------|--------------|-----------------------|
| 85-100 | A | Excellent Performance |
| 70-84 | B | Good Performance |
| 60-69 | C | Average Performance |
| 59 ↓ | D | Under Performance |

What does MPPA do with this information???

- MPPA will provide a Credit Report Card to each member utility within 3 months of the utility's published financial audit report.
- For utilities that score in the Under Performance category or below, the CFO and/or CEO will schedule a visit with the utility to discuss the Agency's concern with the credit score of the utility and offer suggestions and assistance with improvements.
- For utilities who fail to improve their scores year over year, the utility may be limited in its ability to transact with MPPA or may have to post additional collateral as security against default.



Practical Results

MPPA Started its report card scoring program in 2016.

MPPA is in the process of reviewing 2018 performance results for its member utilities

Score Improvements over the first 2 years:

Average Score Year 1: 82%

Average Score Year 2: 93%

Percentage of Member Utilities that improved their overall score= 94%

QUESTIONS?