



City and Borough of Sitka

100 Lincoln Street • Sitka, Alaska 99835

MEMORANDUM

To: Mayor Paxton and Assembly Members
Keith Brady, Municipal Administrator

From: Jay Sweeney, Chief Finance and Administrative Officer

Date: February 6, 2019

Subject: Effect of Extending Seasonal Electric Rates on Debt Coverage Ratio Covenants for Electric Revenue Bonds

Issue

Extending low seasonal electric rates by one month, from March 31 to April 30, 2019, may place the Municipality at risk of a technical default on its debt service coverage ratio in fiscal year 2019 unless a subsidization transfer to the Electric Fund is accomplished by June 30, 2019.

Facts

1. The loan agreements with the Alaska Municipal Bond Bank Authority (AMBBA) governing the Electric Fund's outstanding revenue bonds stipulate that the City and Borough of Sitka will annually meet a debt service coverage ratio ("Rate Covenant") equal to 125% of the annual debt service of all revenue bonds.
2. If the 125% debt service coverage ratio is not met, the Municipality would be in a technical event of default. The Municipality's bond ordinances detail the lender's remedies in instances of an event of default.
3. An event of default due to failure to meet the minimum Rate Covenant can be cured if, within 180 days after the end of the fiscal year, the Municipality:
 - a. Employs a consultant to recommend changes in the Electric System rates that are estimated to produce Revenue of the System sufficient to satisfy the rate covenant, and
 - b. Imposes Electric System rates at least as high as those recommended by the consultant that will become effective at the time or times so recommended.
4. Even if an Event of Default is avoided through engagement of a consultant and imposition of electric rate increases, disclosure may still be required in the Municipality's Comprehensive Annual Financial report (CAFR).
5. An Event of Default, whether cured or uncured, will impact the Municipality's ability to issue future revenue bonds through the Alaska Municipal Bond Bank Authority.

6. For fiscal year 2018, the Electric Fund met the Rate Covenant by achieving a debt service coverage ratio of 126.87%, with excess revenue of the system of \$136,544 above the minimum requirement of \$9,127,141. In fiscal year 2019, with user fees not being increased and some elements of operating costs increasing due to inflation and wage increases, the Electric Fund is projected to achieve the bare minimum 125% debt service coverage ratio.
7. To avoid an Event of Default, the Municipality may subsidize the Electric Fund by transferring in funds from another source, such as the General Fund. If this is accomplished before June 30, the end of the fiscal year, an event of default will not occur. If the seasonal electric rate is extended for one additional month as proposed, and, staff projects that the minimum Rate Covenant will not be met, staff will recommend to the Assembly that a subsidization transfer be made.
8. Finance Department analysis projects that extending seasonal low electric rate charges for one additional month, through April 30th, would result in a shortfall of \$497,300 from planned electrical user fee revenue for FY19. This estimate is based on 8,673,500 kWh projected to be sold during April, 2019 at an average low season user fee of \$0.1246/kWh versus the planned average high season user fee of \$0.1819/kWh. The exact amount of a shortfall would be dependent on weather and electricity usage and could vary from the Finance staff estimate.

Analysis

If the Finance staff analysis of the potential revenue shortfall due to extending seasonal low electric rate charges for one additional month prove to be valid, the Municipality will likely not meet the minimum Rate Covenant of 125% and, unless the Electric Fund receives significant subsidization from another source before June 30, 2019.