Tacoma Water Budget Overview & Strategy

Presented by Scott Dewhirst and Heather Pennington for the Public Utility Board on May 22, 2024
Operating costs continue to rise despite stable demand.
State of the Utility: Customers

We have a broad, diverse customer base with opportunities for growth.

Top Customers by Revenue and Usage for 2023

<table>
<thead>
<tr>
<th>No.</th>
<th>Customer</th>
<th>Revenue</th>
<th>% of Total Revenue</th>
<th>Usage</th>
<th>% of Total Usage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>WESTROCK CP LLC</td>
<td>$5,538,296</td>
<td>6.1%</td>
<td>6,086,337</td>
<td>25.2%</td>
</tr>
<tr>
<td>2</td>
<td>CITY OF FIRE</td>
<td>$1,299,615</td>
<td>1.2%</td>
<td>826,485</td>
<td>3.4%</td>
</tr>
<tr>
<td>3</td>
<td>METRO PARKS DISTRICT</td>
<td>$1,219,759</td>
<td>1.1%</td>
<td>257,159</td>
<td>1.1%</td>
</tr>
<tr>
<td>4</td>
<td>FREDERICKSON POWER</td>
<td>$1,184,838</td>
<td>1.1%</td>
<td>509,648</td>
<td>2.1%</td>
</tr>
<tr>
<td>5</td>
<td>NIAGARA BOTTLING LLC</td>
<td>$781,991</td>
<td>0.7%</td>
<td>336,744</td>
<td>1.4%</td>
</tr>
<tr>
<td>6</td>
<td>TACOMA SCHOOL DISTRICT</td>
<td>$780,756</td>
<td>0.7%</td>
<td>138,684</td>
<td>0.6%</td>
</tr>
<tr>
<td>7</td>
<td>US OIL &amp; REFINING</td>
<td>$569,757</td>
<td>0.5%</td>
<td>279,562</td>
<td>1.2%</td>
</tr>
<tr>
<td>8</td>
<td>TEHALEH OWNERS ASSOCIATION</td>
<td>$548,262</td>
<td>0.5%</td>
<td>94,163</td>
<td>0.4%</td>
</tr>
<tr>
<td>9</td>
<td>JAMES HARDIE BLDG PRODUCTS INC</td>
<td>$453,900</td>
<td>0.4%</td>
<td>136,904</td>
<td>0.6%</td>
</tr>
<tr>
<td>10</td>
<td>MULTICARE HEALTH SYSTEMS</td>
<td>$355,524</td>
<td>0.3%</td>
<td>71,743</td>
<td>0.3%</td>
</tr>
<tr>
<td>11</td>
<td>SUNRISE MASTER ASSOCIATION</td>
<td>$310,726</td>
<td>0.3%</td>
<td>53,196</td>
<td>0.2%</td>
</tr>
<tr>
<td>12</td>
<td>PORT OF TACOMA</td>
<td>$306,452</td>
<td>0.3%</td>
<td>33,681</td>
<td>0.1%</td>
</tr>
<tr>
<td>13</td>
<td>UNIVERSITY PLACE SCHOOL DISTRICT</td>
<td>$295,811</td>
<td>0.3%</td>
<td>51,243</td>
<td>0.2%</td>
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<tr>
<td>14</td>
<td>ST JOSEPH MEDICAL CENTER</td>
<td>$279,959</td>
<td>0.3%</td>
<td>50,905</td>
<td>0.2%</td>
</tr>
<tr>
<td>15</td>
<td>CITY OF BLACK DIAMOND</td>
<td>$257,239</td>
<td>0.2%</td>
<td>67,993</td>
<td>0.3%</td>
</tr>
<tr>
<td>16</td>
<td>PIERCE COUNTY FACILITIES MANAGEMENT</td>
<td>$252,015</td>
<td>0.2%</td>
<td>54,604</td>
<td>0.2%</td>
</tr>
<tr>
<td>17</td>
<td>CITY OF BONNEY LAKE</td>
<td>$233,306</td>
<td>0.2%</td>
<td>70,743</td>
<td>0.3%</td>
</tr>
<tr>
<td>18</td>
<td>UNIVERSITY OF PUGET SOUND</td>
<td>$220,764</td>
<td>0.2%</td>
<td>51,866</td>
<td>0.2%</td>
</tr>
<tr>
<td>19</td>
<td>WESTRIDGES APPTS PROPERTY OWNER LLC</td>
<td>$205,723</td>
<td>0.2%</td>
<td>50,381</td>
<td>0.2%</td>
</tr>
<tr>
<td>20</td>
<td>FAIRWAYS TIC IV LLC</td>
<td>$186,821</td>
<td>0.2%</td>
<td>51,139</td>
<td>0.2%</td>
</tr>
</tbody>
</table>

- WestRock shut down removes biggest customer risk
- Customer base more diversified
- Potential to market excess contracted wholesale capacity
- Residential growth outside of Tacoma
- Customer inside vs outside: 60% vs 40%
State of the Utility: Financial

**Sound financial stewardship reflected in strong credit ratings.**

S&P upgraded Tacoma Water and Regional Bonds to AA+ in 2022 and affirmed the ratings in 2024, emphasizing financial strength and planning:

- **Despite the loss of its largest customer, the utility has implemented necessary rate increases to maintain a healthy financial profile.**
- **Further support for the rating is provided by the system’s stable customer base and robust long-range planning.**

Moody’s upgraded Tacoma Water and Regional Bonds to Aa1 in 2024:

- **Excellent rate-setting record which was demonstrated following the recent closure announcement by its largest customer, with rate increases to maintain financial metrics, as well as equitable and affordable customer rates.**
- **Sophisticated management of regulatory compliance and ten-year capital program.**
- **Strong system characteristics, including ample capacity and water resources (high-quality, long-lived water supply).**
- **Broad and diverse customer base, served by a local system larger than the city and augmented by a regional second water supply.**

**Tacoma Water Bond Ratings**

<table>
<thead>
<tr>
<th>Rating</th>
<th>S&amp;P Global Ratings</th>
<th>Moody’s Ratings</th>
</tr>
</thead>
<tbody>
<tr>
<td>AAA</td>
<td>AAA</td>
<td>Aaa</td>
</tr>
<tr>
<td>AA+</td>
<td></td>
<td>Aa1</td>
</tr>
<tr>
<td>AA</td>
<td></td>
<td>Aa2</td>
</tr>
<tr>
<td>AA-</td>
<td></td>
<td>Aa3</td>
</tr>
<tr>
<td>A+</td>
<td></td>
<td>A1</td>
</tr>
<tr>
<td>A</td>
<td></td>
<td>A2</td>
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<tr>
<td>A-</td>
<td></td>
<td>A3</td>
</tr>
<tr>
<td>BBB+</td>
<td></td>
<td>Baa1</td>
</tr>
<tr>
<td>BBB</td>
<td></td>
<td>Baa2</td>
</tr>
<tr>
<td>BBB-</td>
<td></td>
<td>Baa3</td>
</tr>
</tbody>
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**Outlook**

<table>
<thead>
<tr>
<th>Rating</th>
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<tr>
<td></td>
<td>Stable</td>
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**Tacoma Water Bond Ratings**

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<td>Aa3</td>
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<td>A+</td>
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<td>A1</td>
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<td>A2</td>
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<td>A-</td>
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<tr>
<td>BBB-</td>
<td></td>
<td>Baa3</td>
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<td>Stable</td>
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</table>
State of the Utility: Financial

Lean budget and forecasting closer to reality, with additional reductions due to mill closure.

Quarterly Outlook
Budget planned to be closer to actual spending

- Realistic budget
- Personnel vacancy factor
- Capital carryforward factor
- Smaller variances pre-mill closure

Reductions due to loss of WestRock revenue

- Capital outlay variance due to:
  - $9M deferred due to loss of WestRock
  - $1.8M ARPA grant for main project
- More cost savings stories on later slide

Projected 2023/24 Biennium Performance at Q1 2024

<table>
<thead>
<tr>
<th>Category</th>
<th>Performance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash on Hand</td>
<td>416 days</td>
</tr>
<tr>
<td>Debt Service Coverage</td>
<td>2.21x</td>
</tr>
<tr>
<td>Total Revenue</td>
<td>$6.7M over budget*</td>
</tr>
<tr>
<td>Total Expenditures</td>
<td>$5.2M under budget</td>
</tr>
<tr>
<td>Capital Outlay</td>
<td>$9.5M under budget</td>
</tr>
</tbody>
</table>

*Includes $2.7M interest earned on cash and investments, could see reductions due to fair market value adjustment at year-end.
State of the Utility: Ongoing Impacts

**Increased Expenses**
- Technology projects (SAP Now!)
- Supplies and services
- Transportation / fuel prices
- Fleet replacement
- Staff turnover
- Construction inflation
- Commodities (insurance, utilities)
- Regulatory mandates (lead and copper, PFAS, Pipeline 1)

**Balancing Efforts**
- Financial management
- Long-term planning
- Expense prioritization
- Project & process management
- Operational efficiencies
- Strategic alignment
- FTEs / professional services
- Revenue expansion
- Recycling and salvaging efforts

**Managing Expenses**
- Hiring
- Delaying projects
- Debt management
- Meetings, travel, and trainings
- Cost savings categories (infrastructure investment offset, grants and loans, innovative thoughts around projects)
Using our strategic plan to help inform our budget.

- Alignment with TPU strategic plan
- Vision for next biennium
- Connecting to Board Guiding Principles
- Division Objectives:
  - Providing customer value
  - Prepared workforce
  - Operational improvements
<table>
<thead>
<tr>
<th>External Commitments</th>
<th>Blended Commitments</th>
<th>Internal Commitments</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Assessments</td>
<td>- Capital Investment Plan (CIP)</td>
<td>- Strategic initiatives</td>
</tr>
<tr>
<td>- Taxes</td>
<td>- Wholesale water sales</td>
<td>- Workforce development</td>
</tr>
<tr>
<td>- Debt service</td>
<td>- Climate action pledge</td>
<td>-</td>
</tr>
<tr>
<td>- SAP Now!</td>
<td>- Emergency management</td>
<td>-</td>
</tr>
<tr>
<td>- Equity</td>
<td>- Safety</td>
<td>-</td>
</tr>
<tr>
<td>- Safety</td>
<td>- Strategic initiatives</td>
<td>-</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>External Drivers</th>
<th>Blended Drivers</th>
<th>Internal Drivers</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Personnel expenses</td>
<td>- Fleet investments</td>
<td>- FTE count</td>
</tr>
<tr>
<td>- Cost of commodities</td>
<td>- Purchasing regulations / contract constraints</td>
<td>-</td>
</tr>
<tr>
<td>- Regulatory requirements</td>
<td>- Technology investments</td>
<td>-</td>
</tr>
<tr>
<td>- Inflation</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>
Water will not request additional for 2025-2026, asking to repurpose existing project positions.

- Tacoma Water currently has 7 positions that were added as project positions of limited duration based on AMI resolution.
- The personnel expense related to these positions is assumed in the financial modeling.
- We would like to repurpose these positions for sustainment and to fill prioritized needs across the organization.
- We expect to see a reduction in the personnel expense vacancy factor with more filled positions.
Water is a Capital Intensive Utility

**Renewal & Replacements**
- Main replacement program
- Hydrants, valves, blowoffs
- Water services and meters
- Fleet vehicles and equipment

**Environmental Stewardship**
- Additional Water Storage Project (AWSP)
- Fish Passage
- Fish habitat and mitigation
- Watershed projects

**Supply and Treatment Facilities**
- Prairie Ridge reservoir
- Wells Master Plan
- Ozone system replacement
- Cascadia reservoir and pump station

**Infrastructure / Facilities**
- Water Operations Warehouse
- Smart Water Program
- Electrical improvements
- Major communication and SCADA

**Regulatory**
- Pipeline 1 Pressurization Program
- PFAS treatment (South Tacoma wells)

**Technology**
- SAP Now!
- Enterprise asset management solution
- GIS utility network migration
System Growth/Complexity Requires Personnel to Protect

Plant Assets vs Employees
% change since 2004

- Second Supply Project
- Regulatory Mandates
  - Covering Reservoirs
  - Green River Filtration Facility (GRFF)
- Advanced Meters

- Plant-in-Service (Original Cost)
- Full-Time Employees (FTEs)
Project & Process Management Improvement

Budget Decision-Making
- Personnel: Hiring Action Form
- Capital: Business Case Evaluations / Charters
- Decision-Making Framework

Forecasting
- Adaptive Insights for financial forecasting
- Capital Improvement Plan
- Developing a phased approach

Project and Process Documentation
- Capital intake and prioritization tools
- Business process documentation
- Project management training
- Data, technology intake, prioritized list
# Cost Savings Stories

**Efficiencies, reductions, and deferrals.**

<table>
<thead>
<tr>
<th>Description</th>
<th>Category</th>
<th>Type</th>
<th>Duration</th>
<th>2023 Actual</th>
<th>2024 Estimate</th>
<th>Total Est Savings</th>
</tr>
</thead>
<tbody>
<tr>
<td>Refinanced 2013 Water &amp; Regional Bonds</td>
<td>Refinancing</td>
<td>Reduction</td>
<td>20 years</td>
<td>$0</td>
<td>$710,000</td>
<td>$7.83M NPV</td>
</tr>
<tr>
<td>Earned Revenue from Recycling and Surplus Scrap Sales</td>
<td>Recycling &amp; Salvage Efforts</td>
<td>Increase</td>
<td>Ongoing</td>
<td>460,000</td>
<td>160,000</td>
<td>$100,000/year</td>
</tr>
<tr>
<td>Reduced and Deferred Investments in Infrastructure after the WestRock Mill Closure</td>
<td>WestRock Reset</td>
<td>Deferral Reduction</td>
<td>Ongoing</td>
<td>0</td>
<td>9,000,000</td>
<td>Additional $10M cancelled on CIP</td>
</tr>
<tr>
<td>Offsets to Capital Infrastructure Costs</td>
<td>Funding Opportunities</td>
<td>Reduction</td>
<td>20 years</td>
<td>46,000</td>
<td>2,400,000</td>
<td>$150,000/year</td>
</tr>
<tr>
<td>Cost Avoidance/Savings for Water AMI Project Expenses</td>
<td>Innovation</td>
<td>Reduction</td>
<td>5 years</td>
<td>100,000</td>
<td>100,000</td>
<td>Over $10M avoided</td>
</tr>
<tr>
<td>New Material for GRFF Chemical Feed Lines Replacement</td>
<td>Innovation</td>
<td>Reduction</td>
<td>Ongoing</td>
<td>0</td>
<td>200,000</td>
<td>$200,000 also saved in 2034</td>
</tr>
<tr>
<td>Credit for Steel Pricing for Pinnacle Ridge Tank</td>
<td>Operational Efficiency</td>
<td>Reduction</td>
<td>One-time</td>
<td>150,000</td>
<td>0</td>
<td>One-time $150,000</td>
</tr>
<tr>
<td>Watershed Stakeholder Engagement and Cost Sharing</td>
<td>Revenue Expansion</td>
<td>Increase</td>
<td>Ongoing</td>
<td>15,000</td>
<td>15,000</td>
<td>At least $30,000 each biennium</td>
</tr>
<tr>
<td>Consolidated Cellular Devices</td>
<td>Operational Efficiency</td>
<td>Reduction</td>
<td>Ongoing</td>
<td>0</td>
<td>27,000</td>
<td>$27,000/year</td>
</tr>
</tbody>
</table>
AMI and Smart Water

Taking advantage of the automated meter infrastructure project

Meter Example

- Currently installing flow meters in the 251 PZ to better understand how water flows through that zone following the shutdown of WestRock

Smart Water

- Provides operators and staff with more tools
  - Proactive, know about problems before customers call

Access to Data for better analysis

- Understanding monthly demand
- Revenue shaping
Supporting our Customers

- Customer Assistance (Discount, BCAP)
- Water Grant and Loan Program

New Services-Related Improvements

- Responding directly to feedback from the development community
- Recommended TMC updates for water service construction charges
  - Extend incremental fixed fee escalation (ends in 2025)
  - Add fixed fee for service sizes up to 2” and a la carte option for paving
    - To improve predictability and reduce staff time and delays
  - Improve process for selling fire/domestic combination meters
  - Align with Home in Tacoma minimum lot width

<table>
<thead>
<tr>
<th>Water Service Construction Charges on Existing Mains</th>
<th>1/1/2020</th>
<th>1/1/2021</th>
<th>1/1/2022</th>
<th>1/1/2023</th>
<th>1/1/2024</th>
</tr>
</thead>
<tbody>
<tr>
<td>1&quot; Service with 5/8&quot; Meter</td>
<td>$3,600</td>
<td>$3,800</td>
<td>$4,010</td>
<td>$4,230</td>
<td>$4,460</td>
</tr>
<tr>
<td>1&quot; Service with 3/4&quot; Meter</td>
<td>$3,675</td>
<td>$3,900</td>
<td>$4,140</td>
<td>$4,400</td>
<td>$4,670</td>
</tr>
<tr>
<td>1&quot; Service with 1&quot; Meter</td>
<td>$3,825</td>
<td>$4,040</td>
<td>$4,270</td>
<td>$4,510</td>
<td>$4,760</td>
</tr>
<tr>
<td>Meter Exchange from 5/8&quot; to 3/4&quot;</td>
<td>$700</td>
<td>$720</td>
<td>$740</td>
<td>$760</td>
<td>$790</td>
</tr>
<tr>
<td>Meter Exchange from 5/8&quot; to 1&quot;</td>
<td>$700</td>
<td>$720</td>
<td>$740</td>
<td>$760</td>
<td>$790</td>
</tr>
<tr>
<td>Meter Exchange from 3/4&quot; to 5/8&quot;</td>
<td>$325</td>
<td>$330</td>
<td>$340</td>
<td>$360</td>
<td>$370</td>
</tr>
<tr>
<td>Meter Exchange from 3/4&quot; to 1&quot;</td>
<td>$700</td>
<td>$720</td>
<td>$740</td>
<td>$760</td>
<td>$790</td>
</tr>
<tr>
<td>Meter Exchange from 1&quot; to 5/8&quot;</td>
<td>$200</td>
<td>$210</td>
<td>$210</td>
<td>$220</td>
<td>$230</td>
</tr>
<tr>
<td>Meter Exchange from 1&quot; to 3/4&quot;</td>
<td>$200</td>
<td>$210</td>
<td>$210</td>
<td>$220</td>
<td>$230</td>
</tr>
</tbody>
</table>
• **Budget Development is well underway**
  - Water preliminary capital budget and CIP nearly completed
  - O&M budget is in progress for Tacoma Water cost centers
  - Labor and benefit expense assumptions are being developed by GG
  - Revenue at existing rates and miscellaneous revenue assumptions nearly complete
  - Internal assessments, including SAP Now!
    - GG costs allocated based on City-wide budgets and FTE counts
    - TPU costs are allocated based on various factors
• **Long-Range Financial Plan (LRFP) updated base case and scenario development**
  - Incorporate revenue requirement and assumptions
• **Public Utility Board feedback and questions**
Budget vs Actual Trends: Water Sales Revenue

Budgeted water sales have an average increase of 5.3% per year, while actual revenue has an averaged increase of about 5.5% per year.
**Budget vs Actual Trends: Personnel**

- **Budgeted expenses has an average increase of 6.1% per year, while actual spending in this category has an averaged increase of about 6.3% per year.**
Budget vs Actual Trends: Other O&M

Budgeted expenses have an average increase of 5.1% per year; while actual spending in this category has an averaged increase of about 6.3% per year.
Budget vs Actual Trends: Capital

Budgeted expenses have an average increase of 5.0% per year, while actual expenses have an average increase of about 1.0% per year.
Tacoma’s share of the 2nd Diversion is approximately 41.7%. Expenses in 2013-2016 include the Green River Filtration Facility. Since 2017, budgeted expenses for the RWSS have been relatively flat.
Tacoma Water Long-Range Financial Plan

Presented by Jodi Collins for the Public Utility Board on May 22, 2024
2023-2024 Base Case Comparison

2023-2024 Base Case (Post WestRock) Projections

System Average Rates

- 2024: 9.0%
- 2025: 9.0%
- 2026: 5.0%
- 2027: 2.5%
- 2028: 2.5%
- 2029: 3.0%
- 2030: 3.0%
- 2031: 3.0%
- 2032: 3.0%
- 2033: 3.0%
- 2034: 3.0%

Debt Service Coverage

- 2024: 1.41
- 2025: 2.22
- 2026: 2.33
- 2027: 1.89
- 2028: 1.31

Fund Balances

- 2024: $1,021M
- 2025: $960M
- 2026: $840M
- 2027: $822M
- 2028: $811M
- 2029: $800M
- 2030: $795M
- 2031: $786M
- 2032: $776M
- 2033: $767M
- 2034: $621M

2023-2024 Base Case (Pre WestRock) Projections

System Average Rates

- 2024: 4.0%
- 2025: 3.0%
- 2026: 3.0%
- 2027: 3.0%
- 2028: 3.0%
- 2029: 3.0%
- 2030: 3.0%
- 2031: 3.0%
- 2032: 3.0%
- 2033: 3.0%
- 2034: 3.0%

Debt Service Coverage

- 2024: 1.41
- 2025: 2.22
- 2026: 2.33
- 2027: 1.89
- 2028: 1.31

Fund Balances

- 2024: $955M
- 2025: $621M
- 2026: $776M
- 2027: $755M
- 2028: $736M
- 2029: $723M
- 2030: $695M
- 2031: $671M
- 2032: $601M
- 2033: $586M
- 2034: $551M
Our LRFP plan is based on the revenue requirement, will incorporate our capital and O&M budgets

**Updated**
- Preliminary capital budget and CIP
- Short-term demand forecast

**Awaiting More Information**
- Internal service assessments which includes SAP Now!
- Labor and benefits assumptions are still being developed by GG
- O&M budget is in progress for Tacoma Water cost centers
- Miscellaneous revenue
- Taxes
- Capital funding plan and new debt issuance
What’s Changed for Our New Draft Base Case

**Continued Impact from Previous Biennia**
- Deferred spending
- **Higher personnel expenses**
  - Delayed class & comp adjustments
  - Wage inflation
- **Higher assessments**
  - Also impacted by higher personnel expenses

**Impact Since the WestRock Base Case**
- **Higher capital budget and CIP**
  - $120 million increase from last base case
  - Construction inflation
  - Regulatory mandates (P1 and PFAS)
  - Additional Water Storage Project (AWSP)
  - Water Operations Warehouse
- **Ongoing impacts from mill closure**

**What’s Beyond the Planning Period**
- Water Operations Building (Phase 2)
- Wells improvement & treatment
- McMillin Reservoir 3rd cell
- Transmission system replacements
- Pump and PRV station rehab
- Headworks Master Plan and site expansion
- New regulatory requirements?
# 10-Year Capital Improvement Plan (CIP)

## 2025-2026 Tacoma Capital Improvement Plan (Proposed)

<table>
<thead>
<tr>
<th>Year</th>
<th>Water Operations Warehouse</th>
<th>Pipeline 1 Pressurization</th>
<th>AWSP, Fish Passage &amp; Mitigation</th>
<th>Cascadia Reservoir &amp; PS</th>
<th>Treatment</th>
<th>Source &amp; Transmission</th>
<th>General &amp; Fleet</th>
<th>Distribution</th>
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## 2025-2026 RWSS Capital Improvement Plan (Proposed)

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## Summary

- **Total Capital Budget**:
  - Water Only (Not Shared): $78M
  - RWSS 1st Diversion: $55M
  - RWSS Tacoma: $120M
  - RWSS Other Partners: $14M
  - 25/26 Capital Budget: $107 6M

## Allocation by Year

- **2025/2026**: $24,700,000
- **2026/2027**: $4,000,000
- **2027/2028**: $12,400,000
- **2028/2029**: $11,200,000
- **2029/2030**: $17,500,000
- **2030/2031**: $17,500,000
- **2031/2032**: $15,400,000
- **2032/2033**: $200,000

**Note:** The allocations are subject to change and are based on proposed plans.
Projected Range of System Average Rates

We build our base case based on our expected revenue requirement and then develop scenarios based on possible risks and opportunities. This analysis provides ‘bookends’ for our rate projections.

This initial range of rate projections builds upon the base case developed during the WestRock discussions along with updates from the preliminary capital budget and CIP.