National Strategy Council

Financial Strategy Playbook

National Strategy Council for Local Government Public Utilities

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Preamble To All Strategy Playbooks

This section provides the common context for National Strategy Councils and their Strategy Playbooks.

Who This Playbook Is For

We are creating several distinct Playbooks, each with a specific focus audience. This Financial Strategy Playbook has been created by CFOs for CFOs, providing guidance and strategy intended to inform long-term financial planning. Key points include measuring and monitoring key metrics for success, contemporary best practices, and how to institutionalize them for the long-term benefit of communities and future generations. We live in times dependent on technology, connectivity, and data. Transformation is necessary, but bad decisions made today can result in disastrous and costly implications in the future. These decisions revolve around a common set of Grand Challenges playing out in communities across the US right now.

Despite the gravity and immediacy of the situation, these GRAND CHALLENGES often receive less attention than they should, due in no small part to the uncertainty we face daily in our newsfeeds. Left unaddressed, the challenges continue to mount. The overarching goal of this Playbook is to address these challenges and inform the way forward.

The Infrastructure Crisis

Infrastructure deficit threatens to undermine most communities' vision of a vibrant future. The American Society of Civil Engineers (ASCE) estimates the current infrastructure deficit at over $2 trillion, with a significant portion of that in public works and utilities.

Much of America's infrastructure is over 50 years old and has exceeded its intended lifespan.Intergenerational equity is at risk if we continue to wear down infrastructure in the present without contributing to its renewal. As a result, we effectively rob future generations of comfort, convenience, and reliability by saddling them with excessive infrastructure liabilities.

> *We still have pipes in the ground that are over 110 years old.*
>
> Anthony Moggio

Underfunding, limited resources, and ongoing wear and tear of infrastructure are at the heart of the matter, further compounded by rapid population growth, urbanization, and extreme weather patterns that place additional stress on public works. Rising sea levels, more frequent and severe storms, and prolonged droughts strain water systems, which must adapt to these changing conditions to remain effective. New regulations, compliance, and security are also imminent concerns, as are determining which costs can be included in rate design, environmental protections, and ensuring public health and safety. Compliance with newly enacted state or federal regulations often introduce additional capital and operating costs, which may place untenable strain on budgets.

The infrastructure deficit crisis directly impacts the economy, public health, and quality of life for millions of Americans. Wide-ranging consequences include reduced access to safe drinking water, increased traffic congestion, higher cost of goods and services, and decreased competitiveness in the global market—factors we are already experiencing. These issues not only affect the present but also impact our future economy. Failure to address it will lead to unaffordability, lost productivity, and missed opportunities, resulting in an estimated $4 trillion GDP shortfall in the next two decades. Managing the infrastructure problem is crucial and immediate, lest we find ourselves in an impossible situation.

> *We were putting off everything: expansion projects, critical replacement & repair projects... because our revenues were barely covering operating costs and existing debt service. We had to make some changes.*
>
> Wes Smith

The Grand Challenges

Factors precipitating the infrastructure crisis manifest as three distinct challenges every community must contend with:

01

Financial Sustainability

Pertains to the local government's ability to manage financial resources to ensure long-term viability, stability, and resilience.

02

Affordability

Refers to the ability of citizens to comfortably manage the costs of the services without undue financial burden or hardship.

03

Intergenerational Equity

Addresses the principle of fairness that considers the rights, needs, and interests of both present and future generations.

The National Strategy Council And Strategy Playbooks

The complexity of the task at hand, the absence of a well-defined solution, and the fact that every community must tackle these issues independently creates additional obstacles.

The overarching goal of the National Strategy Council is to assemble tight, focused teams of civic leaders to meet these challenges head-on. Institutionalizing these fundamental goals ensures that all citizens, present and future, will continue to have access to safe and reliable infrastructure and the services and utilities it supports.

Each council reviews a tight set of the most pressing challenges to innovate actionable strategies—viable and sustainable approaches that can be handed off to local agencies for adaptation to local realities. With a well-mapped plan, these organizations can focus on execution, knowing that it was conceived by a strategic council of peers who understand every aspect of their challenges. Each council group captures its work, including research, long-term strategy, and pragmatic action plans, in a Strategy Playbook.

The Strategy Playbook is a medium to facilitate accelerated learning the adoption of effective strategies by communities. Through this, it is hoped that the current trajectory, steering society toward the vibrant future we all envision for our communities.

Visionary Thinking In Finance

The Finance Objective

The National Strategy Council on Local Government Public Utilities presents the Financial Strategy Playbook, a practical guide developed by CFOs for CFOs. The Playbook offers valuable guidance that progressive CFOs can adopt around long-term financial plans, measuring and monitoring key metrics for success, practicing contemporary best practices, and ultimately institutionalizing them for the long-term benefit of communities and future generations.

> *Why? Because government copies itself! This financial strategy playbook will be an important resource for finance officers to refer to that convinces elected officials, the community, and executive staff that continuous utility rate management is a financial best practice!*
>
> Bret Prebula

Framing The Role Of Finance Leadership

The CFO or finance director in local governments plays a critical role in addressing the infrastructure deficit crisis in America. They are responsible for ensuring their communities have a safe, reliable infrastructure by guaranteeing financial sustainability. The following four tenets describe the CFO role in more detail.

Responsibilities	Operational CFO	Strategic CFO
Preserving Value Asset and liability management, managing risk in relation to setting and achieving the organization's objectives, and implementing and monitoring effective internal control systems.	✓	✓
Reporting Value Ensuring relevant and useful internal and external business reporting.	✓	✓
Enabling Value Supporting the governing body and senior management in making decisions and facilitating the understanding of performance of organizational functions or units.	✗	✓
Creating Value Developing policies and strategies for sustainable value creation.	✗	✓

All too often, CFOs find themselves stuck in a cycle of addressing only two of these features: preserving value and reporting value. These are indispensable for the basic day-to-day requirements of running of government from one fiscal year to another, but from a long-term strategic perspective, enabling and creating value are also critical. Sustainability is at risk if any of the above tenets are overlooked and neglected.

What's The Solution?

A long-term approach is essential, as focusing on near-term goals is akin to an endless game of whack-a-mole. The NSC has identified three strategies representing complementary approaches that, taken together, result in a whole greater than the sum of its parts. These three strategic pillars are the focus of this Strategy Playbook.

> *Our 20-year asset management plan informs the budget of the annual required contribution for asset replacement*
>
> Anthony Moggio

Values , Vision & Priorities

Grand Challenges + Community Goals

01 Long-term Strategic Planning

A financial plan to support infrastructure realities not limited to a short-term CIP. It must deliver on the community's Vision, Values, and Priorities and inform the annual budgeting process.

02 Metrics-guided Execution

A small set of indisputable, undeniably critical measures that all stakeholders can use as their North Star to align efforts and always make the right decisions for the community.

03 Continuous Rate Management

A data-driven, integrated approach to managing revenues (rates, debt, and grants) favoring immediate small adjustments to stay on top of changing realities and protect the community from sudden or monumental rate increases.

Budgeting & Accounting

Operations + Execution

01. Long Term Strategic Planning

Why It's Important

A long-term public utility infrastructure investment plan is critical to ensuring communities have sustainable systems for future generations. A long-term plan addresses immediate infrastructure needs and helps utilities to anticipate and plan for future challenges such as population growth, climate change, and aging infrastructure. The key benefit of long-term strategic planning is enabling a proactive rather than a reactive approach to utilities financial management

The Anticipated Result Translates To The Following Wins

1. Smart Capital Investment

Identifying and prioritizing critical infrastructure needs in advance enables smarter capital investments leading to improved cost-effectiveness, cost-efficiency, and more judicious leveraging of debt to achieve specific objectives.

2. The Right Foundation For Budgeting

Long-term planning should inform the annual budgeting process to ensure the budget reflects key priorities for sustainability and help affirm financial resources are being applied efficiently and effectively.

3. Values Alignment

The long-term plan must reflect the community's values and priorities. By engaging with the community during the planning process, utilities can better understand end-user needs and concerns and win public trust by communicating how plans would deliver on those needs.

4. Institutionalization

Data and analytics enable informed decisions driving full use of the toolbox available to finance leaders. Such tools include thoughtful rate design, prudent debt management, and leveraging grant and other funding options to ensure long-term financial sustainability.

Best Practices

Best Practices	What This Is And What It Does For You
Real Time Sync With Capital Plans	Assumes a long term Master Infrastructure Plan informed by both the Community Strategic Plan and an Asset Replacement Schedule in the domain of Public Works and Utilities. Synchronize these elements into the long term financial plan so that whenever some thing changes in the Master Plan, the Long Term Financial Plan is always up to date. This practice ensures that as CFO, you are always ahead of funding implications within the scope of infrastructure planning.
Ferocious Pursuit Of Grants	Leverage Long Term Financial Plan scenarios to tell powerful stories that build a rationale for grants and loan forgiveness.
Optimize The Use Of Debt Financing	Financing with debt facilitates big projects without up front cash outlay. It's also a fairness mechanism that allows distributing the infrastructure cost evenly over time to align cost with use. Despite interest costs a positive result justifies the added expense.
Align Rate Design With Sustainability, Affordability, And Equity	Align rate design with long-term financial sustainability, based on the anticipated capital investment needs and the cost of service. This is not just about increasing rates to generate more revenue but also restructuring rates to shift the cost burden around to improve fairness, equity, and affordability. This means that utilities must consider the needs of low-income and vulnerable populations and must work to minimize the impact of rate increases on these groups.
Collaborate And Iterate With Key Stakeholders	The Master Plan inputs into the Long-Term Financial Plan might place demands on rates that are not immediately acceptable. It may be necessary to renegotiate with public works to shift projects around and buy some time to build up funding capacity. This might result in adjustments to the Capital Improvement Plan. Make use of scenario exploration to facilitate efficient conversations and iterations until a workable solution is attained.

Best Practices

Best Practices	What This Is And What It Does For You
Integrate The Current Year Of The Long-term Plan Into Annual Budgeting	The current year of the long-term strategic planning process should inform the annual budget, and it should be reviewed and updated annually to ensure that it remains relevant and aligned with current needs and priorities. This process ensures that the budgeting exercise is not done in isolation, but rather informed by a thorough updating of the long-term strategic plan.
Track Year To Date Budget To Actuals And Feedback Into Long-term FinancialPlan	As a fiscal year unfolds, what actually happens often deviates from the original budgeted plan. It's important to track this to make sure the overall approved budget amount is not exceeded (by transferring between accounts) but also to project to year end and to update the Long-Term Financial Plan as needed, in much the same way that a changing Master Plan should be synched to the Long-Term Financial Plan.
Modernize By Adopting Technology	Several best practices are challenging to adopt without using technology. Specialized software can help to address these problems and improve efficiency, accuracy, and transparency. Software can free up staff time for other higher-value activities. Additionally, software can provide real-time data and insights for better decision-making and respond more quickly to changes in the market. Smartly chosen software can deliver benefits that are a huge multiple over the costs incurred.
Cost Savings And Efficiency Improvements	Utilities should continually look for ways to reduce costs and improve efficiency to keep rates as low as possible. This can involve investing in new technology, reducing energy consumption, and exploring new revenue streams.

02. Metrics To Guide Execution

The Need For Community Alignment

While there is almost always an intent to collaborate, the divergent priorities of different divisions mean perspectives can differ significantly, resulting in departmental silos. These divergent perspectives can be even more pronounced between the city and elected officials, although both groups want to serve the community as best as possible.

> *We have three bubbles: the community, the elected officials, and staff. The community wants low rates, the elected officials acquiesce to the community. Why, because staff has not done a good enough job communicating the necessity of the infrastructure needs*
>
> Bret Prebula

> *By tracking key metrics, we can make sure that we are setting affordable rates, maintaining adequate liquidity, and planning for sufficient capital expenditures. We can also ensure that we are meeting our debt service obligations and that the community is investing enough in infrastructure to maintain the quality of life for current and future generations.*
>
> Luis Pedroza

As a result, well-meaning, competent people are tethered, left without a shared frame of reference, priorities, or even a language to make the best decisions on important issues affecting the community. There is an urgent need to agree on and rally around a common set of goals that all stakeholders value.

Recognizing the adage that “if you can’t measure it, you can’t improve it,” it follows that, rather than being vague, these ideas must be quantitatively measurable.

Strategic Metrics For Finance

1. Liquidity

Water utilities are essential, life-critical systems. Utility operators must be ready to address every risk and contingency swiftly to ensure uninterrupted service. Adequate cash reserves must cover ongoing operations, proactive maintenance, and emergency outflows.

Liquidity is a measure of preparedness and is expressed as the number of days a utility has unrestricted cash to ensure uninterrupted service. Poor liquidity results in an inability to handle sudden stressors, putting constraints on essential work and potentially delaying infrastructure projects.

> *Although the City of Bryant has an ordinance that mandates an annual internal review of utility rates, more frequent, even quarterly updates would better keep the elected officials and the community more aware of the requirements to keep our systems sustainable.*
>
> Joy Black

DCOH

Days Cash on Hand = $\left(\frac{\text{Cash and Cash Equivalents}}{\text{Daily Operating Expenses}} \right)$

Minimum Threshold: 90 days
Target Range 150-180 days
Optimal Range: 200-300 days

2. Credit

Debt gives utilities versatility by performing two crucial functions:

Cash Flow Regulator:

Utilities often cannot fund infrastructure from reserves built up from previously accrued rates. The urgency of infrastructure investments means they must borrow to get work done on time, infusing cash flow in the short term while allowing rates to fund Debt Service outflows in the long term.

Fairness Mechanism

Utility infrastructure is long-lived. It could be untenable for today's residents to bear all the burden for infrastructure that would benefit the community over a long period. Using debt distributes a large outflow into smaller outflows over a long period of time spreading the cost burden over the life of the asset. This ensures that the people benefitting from the infrastructure are contributing to its cost.

Debt Service Coverage Ratio is a popular measure of a utility's available cash flow to pay its debt obligations. It indicates the borrowing headroom available to fund strategic infrastructure projects using debt. Significant headroom means the utility can more easily access bond markets to fund projects that rates can support.

DSCR

$$\text{Debt Service Coverage Ratio} = \left(\frac{\text{Net Operating Income (NOI)}}{\text{Total Debt Service}} \right)$$

Minimum Threshold: DSCR = 1
Target Range: DSCR = 1.2 to 1.5
Optimal: DSCR > 1.5

3. Operating Ratio

Compares total operating expenses to net revenue. It measures the organically available strategic surplus that can be provisioned toward essential capital infrastructure outflows. It directly measures the efficiency of core utility operations. A high-performance utility generates revenues while keeping costs low.

The smaller the operating ratio, the more efficient the utility generates revenue vs. total expenses, and the greater the operating surplus. A high ratio indicates a community that would be unable to invest in infrastructure. It's a proverbial 'canary in the coalmine' and often an early warning of serious trouble to come.

OR

$$\text{Operating Ratio} = \left(\frac{\text{Operating Expenses}}{\text{Net Sales (or Revenue)}} \right) \times 100$$

Minimum Threshold: 85% to 90%
Target Range: 75% to 85%
Optimal Range: 60% to 75%

03. Continuous Rate Management for Public Utilities

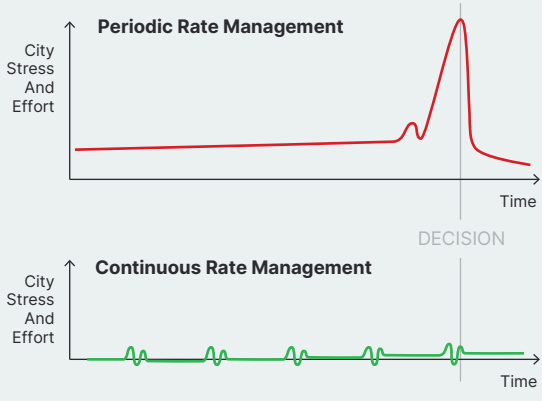
What is Continuous Rate Management?

In many cases, utility rates are only periodically and often infrequently reviewed. When it's time to review rates, the process proceeds with an intensive RFP process for a rate study with a report as a deliverable.

Reports are static. They may consider the next five years, but their recommendations are often out-of-date within weeks or months of completion due to rapid external and often unexpected changes. Recent examples include the pandemic, new regulations (such as for Per-and-poly-fluoroalkyl substances (PFAS), microplastics, lead, and copper), and increased inflationary periods requiring planned projects to be re-priced.

> *An important outcome of the Strategy Playbook is to have a set of tangible best practices for continuous utility rate management*
>
> Bret Prebula

Other factors include growth, changes in demand patterns (perhaps due to climate or economic shifts), and unplanned capital projects. Today's world is changing rapidly. Using static tools like infrequent rate study reports does not represent success in managing such changes. Agility is essential. To address these issues, municipal utilities are increasingly adopting and institutionalizing the practice of continuous rate management. This involves ongoing analysis of costs and revenues, analysis of trends and other factors that may impact the utility's financial position, and importantly keeping a long-term financial model up to date. By continuously adjusting long-term financial plans according to these ever-changing factors and trends, managers can stay on top as well as keep all stakeholders informed of these changes. This is accomplished by regularly informing stakeholders of changes, and how those changes are likely to impact rate payers.



Frequent engagement helps decision makers become more familiar with the process, building trust in the Long Term Financial Plan. Future conversations around rate changes become easier and more efficient when information flows and remains transparent.

Practicing Continuous Rate Management

Continuous rate management requires deviation from the traditional approach. We've identified six best practices below

Best Practices	What This Is And What It Does For You
Stay On Top	Commit to being disciplined about adjusting the Long-Term Financial Plan whenever something substantial changes. This likely is an organizational discipline rather than on just one individual. Finance, public works, and city management need to work together to stay on top.
Analyze Early And Often	Analyze past trends in customer usage and other factors, such as population growth, economic trends, and weather patterns. Compare actuals to budget throughout the year and determine early on if some variations to the approved budget will persist beyond the current year thereby impacting the Long-Term Financial Plan.
Review With Stakeholders Regularly	We know advertising works through repetition. The more often an ad is seen, the more likely the audience will respond. The same principle works with managing rates: many, brief engagements with policy-makers prepare them by softening the tough issues, giving them a chance for early input and time to reflect on the matter.
Engage And Explore With Visuals	Policy-makers need to be engaged if they are to be efficient and productive. Static reports are hard to read and don't lend well to engagement. It's much more effective to have the ability to explore scenarios together interactively, in a way that involves visuals and an ability to explore options easily.
Keep Affordability And Equity In Mind	Any changes to a plan will always be met with the question: "How does this impact ratepayers, particularly vulnerable households?" By maintaining a live, up-to-date model that links revenue requirements to rates, this question can be answered easily at any time.
Modernize With Technology	Practicing continuous rates management requires integration of existing systems, such as budget and accounting along with the Long-Term Financial Plan. It also requires close and frequent collaboration. All this can be challenging. Seek to modernize by adopting technology that can insulate from these challenges and make the practice of continue rates management more seamless and therefore achievable.

The Final Thoughts

Let's recap the primary themes and recommendations of this Financial Strategy Playbook. We hope we have provided good food for thought in these areas and that our research will inform the way forward.

> *We implemented a predictive analytics tool for long term financial planning and continuous rate management. We monitor the impact on rates, of operating expenses and capital budget outlays. The continual calibration of our plan results in better data driven evidence for rate setting. And also enhances communications with elected officials, residents, and external stakeholders such as rating agencies, bond investors, regulators. And best of all we feel good knowing we've institutionalized all processes for succession planning.*
>
> Wes Smith

01

Long-term Strategic Planning addresses the infrastructure deficit crisis while ensuring sustainability and intergenerational equity. Done successfully, the Plan must balance community priorities while charting a roadmap for sustainable infrastructure investment.

02

The Metrics identified in this Playbook—Liquidity, Credit, and Operating Ratio—are intended to align stakeholders, guide financial decision-making on critical matters, and gain public trust.

03

Continuous Rate Management requires frequent stakeholder engagement. It is a low-effort approach to adjusting rates in a way that reassures elected officials, protects affordability, and averts sudden rate shocks while safeguarding the community's long-term interests.

National Strategy Council

Learn more about us

nationalstrategycouncil.org