

Washington Suburban Sanitary District, Maryland

The 'AAA' bond rating considers Washington Suburban Sanitary District's (WSSD) very strong utility fundamentals, as reflected in its revenue defensibility and operating risk profiles, both assessed at 'aa'. The financial profile, also assessed at 'aa', reflects Fitch Ratings' expectations for continued financial profile improvement leading to a trend of declining leverage (measured as net adjusted debt to adjusted funds available for debt service [FADS]) to about 8.0x over the next five years. This trend is dependent upon continued healthy rate adjustments over the five-year horizon generating FADS in support of ongoing capital spending and increasing operating costs.

The district's financial performance improved into fiscal 2022 (ended June 30) and continued into fiscal 2023 with leverage of 8.9x and 8.1x, respectively. Improved leverage reflects rate adjustments and improved collections along with curbs on the rate of expenditure growth. Liquidity also improved, although it remains neutral to the financial profile assessment.

Fitch also considers the district's financial profile in the context of the service area's (Prince George's and Montgomery counties) resource base. From this vantage, its long-term obligations approximate 2.8% of total personal income (2022 data) of the service area. When combined with the district's authority to levy taxes to pay debt service and operations, this expanded view of the resource base supports the 'AAA' bond rating.

However, Fitch notes that ad valorem taxes are not currently levied, and the authority to do so is subject to a process that, while serving to prevent default, limits the benefit of this additional resource at the current rating level. Fitch's view regarding the incremental benefit of the district's authority to levy taxes would be unlikely to support the current rating if the trend of declining leverage is interrupted or reversed.

Security

Debt service is expected to be paid from revenues generated by district fees, charges, rates and assessments and other available funds. In the event of a deficiency of such revenues, the bonds are payable from ad valorem taxes levied within the district (Montgomery County and Prince George's County).

Rating

Long-Term Issuer Default Rating AAA

New Issue

\$299,310,000 Consolidated Public Improvement Bonds of 2024 AAA
\$29,930,000 Consolidated Public Improvement Bonds of 2024 (Second Series) (Green Bonds) AAA

Sale Date

Feb. 8, 2024, competitively

Outstanding Debt

Consolidated Public Improvement Bonds AAA
Consolidated Public Improvement Bonds (Green Bonds) AAA
Consolidated Public Improvement Refunding Bonds AAA
General Obligation Multi-Modal Bond Anticipation Notes AAA

Rating Outlook

Stable

Applicable Criteria

[U.S. Public Sector, Revenue-Supported Entities Rating Criteria \(January 2024\)](#)
[U.S. Water and Sewer Rating Criteria \(March 2023\)](#)

Related Research

[Fitch Rates Washington Suburban Sanitary District, MD's GO Bonds 'AAA'; Outlook Stable \(January 2024\)](#)

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Key Rating Drivers

Revenue Defensibility — 'aa'

Very Favorable Service Area, Affordable Rates for the Vast Majority of the Population

WSSD serves an expansive and very favorable service area that encompasses portions of Prince George's and Montgomery counties. The district retains the legal authority to adjust rates as needed without external oversight. Using Prince George's County as proxy, Fitch considers the monthly residential water and sewer bill affordable for approximately 87% of the service area population based on standard monthly usage of 7,500 gallons for water and 6,000 gallons for sewer.

The very favorable service area is characterized by stronger income levels, a moderate unemployment rate relative to the nation and midrange customer growth. Customer growth registered a five-year CAGR of 0.5% as of fiscal 2023; the district's customer base is primarily residential and there is no customer concentration.

Operating Risk — 'aa'

Very Low Operating Cost Burden, Moderate Investment Needs

In fiscal 2023, the system's operating cost burden was very low at \$5,470 per million gallons (mg) of flows, consistent with the operating risk assessment. The life cycle ratio was very low at 32% in fiscal 2023. Annual capital spending relative to depreciation has been robust, posting a five-year average of 205% for the five years ended in fiscal 2023. Planned capital spending for the next five years should generally outpace historical depreciation, supporting a continued very low life cycle ratio.

The district's anticipated capital spending for fiscal years 2024 through 2028 approximates \$3.0 billion. The estimated spending includes approximately \$2.1 billion of bond proceeds, including those from prior sales, as well as \$746.3 million of pay-as-you-go funds. The remaining sources are primarily derived from grants and capital contributions. The district continues to refine its capital plan to improve efficiencies and execution.

Financial Profile — 'aa'

Leverage to Decline, Neutral Liquidity

The district had very low leverage of 8.1x as of fiscal 2023. As noted, leverage has been on a declining trend in recent years, largely driven by improving FADS, and is down from the peak of 11.1x in fiscal 2020. The liquidity profile is neutral to the overall assessment with current days cash on hand of 229 and coverage of full obligations (COFO) of 1.8x. Fitch-calculated total debt service coverage for fiscal 2023 was 1.9x, which excludes fixed service expense.

The Fitch Analytical Stress Test (FAST) considers the potential trend of key ratios in a base case and stress case over a five-year period. The stress case is designed to impose capital costs 10% above expected base case levels and evaluate potential variability in projected key ratios. The FAST reflects Fitch's view of a reasonable scenario, which is generally informed by publicly available and/or management-provided information with respect to capex, user charges and rate of revenue and expenditure growth.

In the base case scenario, the leverage ratio is projected to increase to 9.4x in fiscal 2024, then decrease to 7.5x through fiscal 2028. In the stress case, the leverage ratio is expected to increase to 9.5x in fiscal 2024, before declining to 7.9x through fiscal 2028. Liquidity is expected to remain neutral to the assessment over the five-year horizon.

Asymmetric Additional Risk Considerations

No asymmetric additive risk considerations affected this rating determination.

Sensitivities

Factors that could, individually or collectively, lead to negative rating action/downgrade

- Failure to maintain leverage comfortably below 10.0x through the five-year horizon.
- Failure to secure rate increases that satisfactorily support operations and continued robust capital investment, including progress toward consent decree milestones.
- Contraction in the economic base that no longer supports an enhancement to the ratings.

Factors that could, individually or collectively, lead to positive rating action/upgrade

- The rating is at the highest level on Fitch's scale and cannot be upgraded.

Profile

The district provides retail water and sewer services to Montgomery and Prince George's counties along the northern and eastern borders of Washington, D.C. In addition to utility charges, the district has the authority to levy ad valorem taxes without limit for debt service. The district's very favorable service area includes a broad and economically diverse customer base that spans nearly 1,000 square miles and serves over 1.9 million residents through approximately 479,000 water and 449,000 sewer customer accounts.

The commission consists of six members (three from each county, all of whom are district residents), who are appointed by respective county executives. The commission's responsibilities include, but are not limited to, planning for operating and capital improvements of the district; establishing water and sewer usage rates, connection charges and other charges and fees; causing ad valorem taxes to be levied; and approving new debt.

Water production at the district's two treatment plants averages in excess of 160 million gallons per day, well below the district's available supply. The district's sewer conveyance and treatment capacity are also ample. Treatment is shared among the district's six plants and the Blue Plains Advanced Wastewater Treatment Plant (owned and operated by the District of Columbia Water and Sewer Authority; IDR: AA/Stable) with whom the district maintains a cost-sharing agreement.

Revenue Defensibility

Revenue Source Characteristics

All of the district's revenues are derived from the monopolistic provision of water and wastewater services. While WSSD's taxing authority and capacity are considered in the district's ratings, to date no taxes have been levied nor required to pay debt service.

Service Area Characteristics

The district's bi-county economic base is very strong, characterized by considerable diversity, high resident income levels and low unemployment.

Montgomery County's economy is supported by a significant U.S. government presence, including significant employment by the U.S. Department of Health and Human Services and the U.S. Department of Defense. Depth and diversity added by an expanding biomedical sector, driven in large part by the presence of the National Institutes of Health. Prince George's County's economic base also includes an important U.S. government presence and institutions of higher education, including Andrews Air Force Base and the University of Maryland.

The median household income (MHI) of both counties is strong relative to that of the nation and the unemployment rate in both counties approximates or trends below that of the nation.

Rate Flexibility

The district retains independent rate-setting authority and significant rate flexibility. Rate increases of 6.0%, 5.9%, 6.5% and 7.0% were implemented for fiscal years 2021 through 2024, respectively. The district's long-term plans include a proposed rate adjustment of 8.5% in fiscal 2025, for which the district indicates it has the counties' support. Continued adjustments are anticipated to support the capital plan and increasing operating expenditures. Rates that fail to support the anticipated trend of declining leverage and, in the absence of offsetting actions, may negatively impact the rating.

The Public Utilities Article, Annotated Code of Maryland (the Act), Section 22-111 requires the commission to determine rates sufficient to meet debt service, as well as the cost of system service. In the event that, during its budgeting process, the commission projects a budgetary revenue shortfall, it must notify the counties of the need to levy a tax, which is available for debt service only. The receipt of the entire levy may take up to a year depending on the time of notice to the counties. Section 22-106 of the Act authorizes the commission to "impose against the assessable property that is in the sanitary district a tax sufficient to pay the principal of and interest on the bonds, as and when due and until paid in full." Voter approval to access the unlimited taxing authority (in the event of a revenue shortfall) is not required.

Rates include increasing block, tiered volumetric charges and fixed charges. In fiscal 2023, the typical customer charge based on Fitch's standard measurement of 7,500 gallons and 6,000 gallons per month of water consumed and sewer usage, respectively, totaled \$116.19, considered affordable for the vast majority of the population (around 87%). This is based on Prince George's County demographics, the rate base for which comprises about 47% of the service area population. As Montgomery County income levels are stronger, overall affordability is likely stronger.

Asymmetric Factor Considerations

No asymmetric factor considerations affected the revenue defensibility assessment.

Operating Risk

Operating Cost Burden

The district's operating cost burden remains consistent with the operating risk assessment, averaging \$5,257 for the five fiscal years ended in fiscal 2023. While sewer flows have fluctuated, water produced has remained relatively stable. The district's expenditures have increased an average of 2.8% from fiscal 2019 through fiscal 2023, reflecting constrained expenditures during fiscal 2021 and reduced expenditures into fiscal 2022.

Costs are likely to continue to rise over time, especially given increased treatment costs at Blue Plains. While not included in the calculation of operating cost burden, pension and other post-employment benefit (OPEB) expense are likely to show continued volatility as market fluctuations continue, contributing to some variability in financial results.

Capital Planning and Management

Average annual capital spending over the past five years has exceeded 200% of depreciation costs, resulting in a low life cycle ratio of 32% in fiscal 2023. Estimated capital spending for fiscal years 2024–2028 continues to focus on renewal and replacement and totals about \$3.0 billion. New debt issuance of approximately \$1.9 billion (inclusive of the current sale), along with \$230 million of proceeds on hand, will fund about 70% of capital projects; alternative funding sources may replace the use of bond proceeds as available. The district has increased its planned use of pay-as-you-go funds to an estimated \$746 million, from \$300 million in the previously provided plan, which will require rate increases to support.

Asymmetric Factor Considerations

No asymmetric factor considerations affected the operating risk assessment.

Financial Profile and FAST Analysis

The district's financial profile is very strong and assessed at 'aa'. Between fiscal years 2017 and 2019, leverage rose steadily amid ongoing debt issuance and heightened capex. Pandemic-related pressures contributed to further weakening in fiscal 2020, with modest improvement in fiscal 2021, when leverage was 11.1x and 10.9x, respectively, reflecting generally flat revenues and reserve adjustments despite approved rate increases. Leverage declined to 8.9x in fiscal 2022, as revenue collections improved and cost containment measures were realized. A further decline into fiscal 2023 to 8.1x reflects continued revenue gains but also the impact of the pension expense adjustment on FADS.

The liquidity profile has also improved, remaining neutral to the financial profile assessment, with a liquidity cushion of 229 days cash on hand and COFO of 1.6x in fiscal 2023, excluding capital contributions.

Fitch Analytical Stress Test

The FAST base case assumptions reflect information provided by the district that includes estimates of operating revenues and expenses through 2028, including revenue adjustments adopted for fiscal 2024 and anticipated for fiscal 2025. The base case also includes an anticipated \$3.0 billion of capital spending and associated funding sources.

Leverage peaks in fiscal 2024 at 9.4x and 9.5x in the base and stress cases, respectively. Thereafter, leverage gradually declines through fiscal 2028, approximating 7.5x in the base case and 7.9x in the stress case, remaining consistent with the financial profile assessment. However, the district's historical financial performance has made financial results, and Fitch-calculated leverage, susceptible to fluctuations due to modest changes in underlying assumptions. Liquidity and COFO are expected to remain at least stable with current levels and neutral to the financial profile assessment.

Fitch considers the district's leverage in the context of its authority to levy both utility charges and taxes, which lend support to the rating despite the leverage ratio and financial profile assessment of 'aa'. Absent the anticipated improvement in leverage through the five-year horizon, the benefit of the authority to levy taxes may not sufficiently offset elevated leverage at the current rating level.

Asymmetric Additive Risk Considerations

No asymmetric additive risk considerations affected this rating determination.

ESG Considerations

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, due to either their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit <https://www.fitchratings.com/topics/esg/products#esg-relevance-scores>.

Financial Summary

(\$000, Audited Fiscal Years Ended June 30)	2019	2020	2021	2022	2023
Revenue Defensibility					
% of Total Revenue from Monopolistic Services	100	100	100	100	100
Service Area Characteristics					
Service Area Population	911,562	967,201	956,254	946,971	—
Total Customer Count	909,659	913,598	918,020	922,000	928,000
5-Year Total Customer Count CAGR	0.8	0.7	0.7	0.6	0.5
Service Area Median Household Income (\$)	84,920	86,994	91,124	97,935	—
Service Area MHI/U.S. Median Household Income (%)	135	134	132	130	—
Service Area Unemployment Rate (%)	3.6	7.8	6.8	3.5	—
Service Area Unemployment Rate/U.S. Unemployment Rate (%)	97	96	128	97	—
Rate Flexibility					
Total Monthly Bill (\$) (7,500 Gallons Water/6,000 Gallons Sewer)	79.31	98.18	103.42	109.17	116.19
% of Population with Unaffordable Bill	11	13	13	13	—
Operating Cost Burden (\$/mg)	4,646	5,430	5,260	5,481	5,470
Capital Planning and Management					
Life Cycle Ratio (%)	30	31	31	31	32
Annual Capex/Depreciation (%)	251	194	192	177	203
5-Year Average Capex/Depreciation (%)	340	294	249	219	203
Financial Profile					
Current Unrestricted Cash/Investments	188,811	139,391	164,278	247,819	321,569
Current Cash Available	188,811	139,391	164,278	247,819	321,569
Available Cash	188,811	139,391	164,278	247,819	321,569
Total Debt	3,570,057	3,670,501	3,889,142	4,102,918	4,330,375
Capitalized Fixed Charges	133,937	162,501	159,456	163,736	200,787
Adjusted Net Pension Liability	335,068	230,142	237,804	136,653	370,477
Available Cash	188,811	139,391	164,278	247,819	321,569
Net Adjusted Debt	3,850,250	3,923,753	4,122,123	4,155,488	4,580,070
Total Operating Revenues	742,817	749,758	749,606	837,663	889,472
Purchased Water/Sewer Services	54,668	66,327	65,084	66,831	81,954
Other Operating Expenses	391,273	429,315	424,160	409,671	430,796
EBITDA	296,876	254,116	260,362	361,161	376,722
Investment Income/(Loss)	13,324	3,840	1,420	1,218	26,304
Other Cash Revenues/(Expenses)	4,451	-17,067	28,531	28,590	28,238
Capital Contributions	82,829	67,816	63,067	62,416	59,042
Funds Available for Debt Service	397,480	308,705	353,380	453,385	490,306
Fixed Services Expense	19,134	23,214	22,779	23,391	28,684
Pension Expense	39,950	21,899	764	-8,652	49,034
Adjusted Funds Available for Debt Service	456,564	353,818	376,923	468,124	568,024
Net Adjusted Debt/Adjusted Funds Available for Debt Service (x)	8.4	11.1	10.9	8.9	8.1
Funds Available for Debt Service	397,480	308,705	353,380	453,385	490,306
Fixed Services Expense	19,134	23,214	22,779	23,391	28,684
Adjusted Funds Available for Debt Service for Coverage of Full Obligations	416,614	331,919	376,159	476,776	518,990
Total Annual Debt Service	236,856	239,061	263,706	289,726	263,543
Fixed Services Expense	19,134	23,214	22,779	23,391	28,684
Adjusted Debt Service (Includes Fixed Services Expense)	255,990	262,275	286,485	313,117	292,227
Coverage of Full Obligations (x)	1.63	1.27	1.31	1.52	1.78
Coverage of Full Obligations Excluding Connection Fees (x)	1.30	1.01	1.09	1.32	1.57

Financial Summary

(\$000, Audited Fiscal Years Ended June 30)	2019	2020	2021	2022	2023
Current Days Cash on Hand	155	103	123	190	229
Liquidity Cushion Ratio (Days)	155	176	123	190	229
All-In Debt Service Coverage (x)	1.68	1.29	1.34	1.56	1.86

Note: Fitch may have reclassified certain financial statement items for analytical purposes.
Source: Fitch Ratings, Fitch Solutions, Washington Suburban Sanitary District

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