



Memorandum

To: Board of Selectmen
Martha White, Town Administrator

From: Michael Walters Young, Deputy Town Administrator
Ted Jankowski, Treasurer/Collector

Date: Thursday, April 18, 2013

Re: Water and Sewer Rate Setting for FY 2014

Introduction

The Board of Selectmen serve as the Water & Sewer Commissioners for the Town of Natick. Among the various duties assigned to you in this role, perhaps none is more important than the annual setting of Water & Sewer rates. This memorandum introduces (or re-introduces) commissioners to the process involved in rate setting, recent changes witnessed by the fund and ratepayers over the last couple of fiscal years, provides pertinent financial information of the water & sewer enterprise fund and finally a summary of rate recommendations, which will be presented to you during the formal rate hearings of May 6th and May 20th.

Water & Sewer Rates: Process

Ideally, water and sewer rates are set once a year in Natick. This is to ensure not only stability in the rates and the revenue stream, but more importantly so end-users can reliably and predictably budget for how much they have to pay for water & sewer services. In order for rate changes to correspond to the Town's fiscal year, rates must be set by June 1st, or very shortly thereafter, to meet bill production deadlines and billing cycles.

Therefore, staff works to begin the process so that it ends with the affirmative action of the Board no later than June 1st. This requires that the Board review the expenses - both operational and capital - *before* setting rates so that sufficient revenues can be raised to support the level of expenses requested and then appropriated through Town Meeting in April. Thus, the rate setting process actually begins January 1st when the Town Administrator unveils her recommended operational and capital budgets for the Water & Sewer Enterprise Fund.

The Selectmen then review and approve both budgets during February and March and they are advanced to the Finance Committee for their recommendations to Town Meeting in April.

Town Meeting will approve the budget in late April or early May, at the same time that the Selectmen are considering rate proposals and eventually setting rates.

The annual rate setting process is summarized below in Figure 1.

Annual Water & Sewer Rate Setting Process					
January	February	March	April	May	June
Water & Sewer Budget Unveiled by Town Administrator	Water & Sewer Budget (Operating & Capital) Reviewed and Approved by Selectmen; forwarded to Finance Committee for Subsequent Recommendation to Town Meeting		Rate Setting Begins @ BOS Town Meeting Hears & Approves Water & Sewer Budget	BOS Approves Rates for Next Fiscal Year	Bills with New Rates Produced & Distributed

Water & Sewer Rates: Timeline

As mentioned above, staff proposes that the formal rate setting process for FY 2014 take place in three sessions – April 22nd, May 6th and May 20th. The formal public hearing to set the rates would start on May 6th and end on May 20th. The proposed timeline and what is to be discussed when is presented below:

Session #1: April 22, 2013

- Introduction to the Rate Setting Process
- Solicitation of additional input from Commissioners on rate proposals
- Review of Water/Sewer Draft Rates
- Review of Water/Sewer Proposed Financial Management Policies
- Review of Public Comment Received to Date

Session #2: May 6, 2013

- Open Public Hearing
- Receive Rate Proposal(s) & Comprehensive Rate Packet
- Receive Additional Analysis (as requested by BOS)
- Take Public Input

Session #3: May 20, 2013

- Finish Public Hearing
- Set Rates

Immediately afterwards:

- First bills go out for FY 2014

Water & Sewer Rates: A brief review of changes & issues over the last several years

Since FY 2009, ratepayers have witnessed significant changes in both the structure of rates and the actual amount billed.

In FY 2009, the inclining block rate structure used by the Town was modified a) to accommodate for an 23% increase (on average) in people's bills (to accommodate for unprecedented declines in available retained earnings, increased capital spending and lower usage amounts) and b) elongated so that the differences between tiers were greater. Translated, this means that those who used less would see very little increase in their rates, whereas average users would see a 23% increase, and heavy water users would see between 40-49% increases in their rates. Finally, the first category of multi-unit dwellings – condominiums – was averaged in order to more accurately reflect the individual dwelling units cost of water & sewer services in buildings serviced by a master meter.

In FY 2010, the practice of averaging multi-unit dwellings was expanded to include all multi-unit residential dwelling units (apartment buildings, and multi-plex (2, 3, 4, etc.) unit dwellings that were served by master meters), as well as non-Natick residential properties served by master meters.

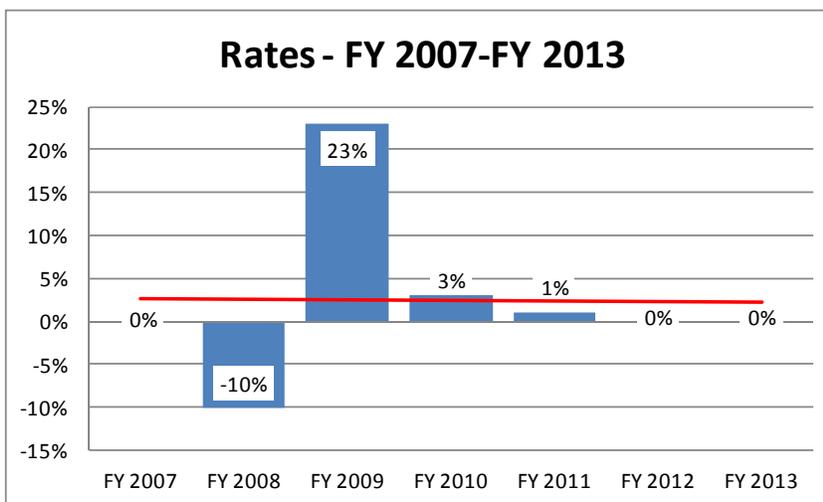
In FY 2011, FY 2012 and FY 2013, no major changes in rate structures were made by the Water & Sewer Commissioners. Water and sewer rates have remained unchanged for the last two years.

The combination of all of these actions over the last five-years has been to a) stabilize the fund and b) make the overall billing structure more fair to all residential properties while c) maintaining our commitment to encourage water conservation.

Unfortunately, revenues did not keep pace with estimates in FY 2012 as a result of decreased usage due to weather conditions, increased water conservation, and averaging of condominiums and apartments. Because of this shortfall, we have had to request that certain capital projects be placed on hold and \$375,000 worth of projects be rescinded to ensure that the Water & Sewer Enterprise Fund will end FY 2013 in a stable and sustainable financial position.

To ensure that a similar circumstance does not occur in the future, a rate increase in FY 2014 is unavoidable.

Figure 2: Rates from FY 2007-2013 are shown below. The 7-year average is an increase year-over-year of 2.43%.



Water & Sewer Rates: Proposals for FY 2014

Staff has worked to minimize expenses in the Water & Sewer Enterprise Fund with the goal of keeping rate increases as low as possible for FY 2014. To that end, the table below summarizes the Water & Sewer Enterprise budget for FY 2014. Mathematically speaking, the forecasted increase in rates would be 1.36%, or around \$165,000 for FY 2014 when compared to FY 2013.

Figure 3: FY 2011-2014 Water & Sewer Enterprise Fund Revenue/Expense Summary

	2011 Actual	2012 Actual	2013 Appropriated	2014 Recommended	2013 vs. 2014	
					\$	%
Water/Sewer Enterprise Fund						
Revenues						
User Charges	12,353,351	11,127,657	12,143,096	12,307,879	164,783	1.36%
Connection Fees	104,470	71,064	114,290	70,000	(44,290)	-38.75%
Other Departmental Income	758,698	1,100,812	1,120,000	1,100,000	(20,000)	-1.79%
Investment Income	66,356	19,980	25,000	20,000	(5,000)	-20.00%
Capital Article Closeouts	150,000	-	-	-	-	#DIV/0!
I & I Fund	-	-	39,369	-	(39,369)	-100.00%
Retained Earnings	-	410,000	1,291,746	147,000	(1,144,746)	-88.62%
Total Revenues	13,432,875	12,729,513	14,733,501	13,644,879	(1,088,622)	-7.39%
Expenses						
Water & Sewer Operations	7,021,847	7,743,788	7,798,124	7,971,946	173,822	2.23%
Utility Billing	167,179	224,318	233,568	237,383	3,815	1.63%
Fringe Benefits	627,467	675,431	652,593	682,834	30,241	4.63%
Debt Service	2,287,229	1,800,816	2,096,702	2,082,138	-14,564	-0.69%
Reserve Fund	0	200,000	200,000	200,000	0	0.00%
Indirects (included in G/F)	2,449,757	2,535,885	2,581,514	2,323,579	-257,935	-9.99%
Capital	312,000	410,000	1,171,000	147,000	-1,024,000	-87.45%
Total Expenses	12,865,480	13,590,238	14,733,501	13,644,879	-1,088,622	-7.39%

Given the need to rescind capital appropriations to ensure adequate fund balance at year-end, we do not recommend a rate increase of 1.36%, but **rather 3.5% for water & sewer rates for FY 2014**. This increase, coupled with minor modifications to the averaging of apartments and condominiums, we believe would result in sufficient resources to adequately fund the operational and capital needs of the Water & Sewer Enterprise Fund in FY 2014.

Staff will develop a comprehensive rate package which leaves the tiers, groupings and existing averaging of multi-unit dwellings in place, but raises all tiers by 3.5 %. In addition, we recommend the introduction of a vacancy rate for multi-unit dwellings of 5% that will more accurately reflect the actual amount of usage or multi-unit dwelling units serviced by a master meter. This will result in a fair and equitable revenue stream from these developments to the community.

As you consider these and any other proposals, we have attached the adopted Water & Sewer Enterprise Fund Financial Policies.

Public Commentary: Additional Requests/Changes Requested by Users

Over the last several years, we have made great strides to hear and recommend changes where applicable and advisable to the Water & Sewer rate structure. This has included both changes to the rates themselves (via the implementation of averaging for all multi-unit residential dwellings), and to the presentation materials – both during the rate setting process and the creation of more informative water & sewer bills and rate summaries after the rate setting process. We have also in the past received comments regarding the water rates and their impact upon laundromats and irrigation users.

The only comments received from individuals by the Finance Department is a request to eliminate the Administrative Fee of \$5.00/bill, designed to offset the cost of the production of the bills to ratepayers. We do not advise the elimination of this fee, as it accurately captures the costs of producing the over 52,000 bills for the Water & Sewer Enterprise Fund annually and was put in place in-lieu-of a minimum bill in FY 2009. Staff believes this does this more accurately and fairly than the prior minimum bill charge.

Requested Action:

Administration is asking that the Water & Sewer Commissioners take no action on April 22nd, other than:

Calling for the posting of a public hearing to commence on May 6th and ending on May 20th for the purpose of setting water & sewer rates for the Fiscal Year beginning July 1, 2013.

AND

Determining how many rate proposals staff should develop in advance of the public hearing.

Staff will develop rate recommendations as summarized above for your meeting of May 6th. Staff needs to know, however, if there are other requests, rate scenarios or analysis that the Board desires for that next meeting. This can include the questions & concerns raised by water users and discussed herein. In order for staff to complete this on-time and still have the Board vote rates on May 20th, *we need to know at least a week ahead of time.* Please e-mail (myoung@natickma.org) or call (505) 647-6404 the Deputy Town Administrator/ Finance Director with any requests or suggestions you may have **by Monday, April 29th.**

Please let us know if you have any questions.

Attachments

- Adopted Water/Sewer Enterprise Fund Financial Policies (*circa May 2011*)



Town of Natick, Massachusetts

Water/Sewer Enterprise Fund Financial Policies – Approved by Board of Selectmen – 05/23/2011

To protect the Water & Sewer Enterprise Fund’s financial stability and to ensure the availability of adequate financial resources in times of emergency, it is essential that policies regarding the enterprise fund’s financial management be adopted and adhered to in the preparation and implementation of the operating and capital budgets.

1) Reserves

Maintaining adequate reserves is a fundamental principle of sound financial management. Although there is no standardized reserve policy guidance for enterprise funds in Massachusetts, industry practice would suggest the following:

- a) Retained Earnings (as certified by the Mass. Department of Revenue *eff. July 1* of each fiscal year) shall serve as the principle reserves for the Water & Sewer Enterprise Funds.
- b) Retained Earnings balance should be at least 10% of the gross revenues of the Water & Sewer Enterprise Fund after accounting for planned draws in any fiscal year (e.g. capital purchases).
- c) Reserves can be used for any lawful purpose, but serve primarily to provide financial security in case of catastrophic and unforeseen events, or capital and asset renewal and replacement.
- d) Reserves should not be used to subsidize ongoing operations, whenever possible.

2) Capital

In order to preserve the Town’s fixed asset base and ensure that Water and Sewer facilities, and equipment efficiently and effectively support the Town’s programs and operations, the Town should provide consistent and stable funding sources for the timely and periodic renewal and/or replacement of water/sewer infrastructure, vehicles and equipment. To that end:

- a) **Methods of Financing:** Generally, the Town should finance all vehicles, equipment and infrastructure with a useful life less than 10 years out of its Retained Earnings. For those vehicles, equipment and infrastructure with a useful life greater than 10 years, the town should consider borrowing as per the regulations set forth under M.G.L. Ch. 44 Sec. 7 & 8 and/or any other applicable laws, if sufficient Retained Earnings are not available.
- b) **Debt Management:** When borrowing is necessary to finance a capital improvement, the Town Finance Director shall seek to issue bonds in such way as to minimize issuance and interest costs while achieving the best terms for the financial betterment of the Enterprise Fund.
- c) **Capital Planning:** All capital projects funded through the Enterprise Fund must be part of the agreed to and adopted 5-year Capital Improvement Plan.
- d) **Roadway Improvement:** Any disruption caused of a paved surface as a result of Water & Sewer Infrastructure Improvements shall be restored as part of the Water & Sewer project and paid for out of revenues of the Water & Sewer Enterprise Fund.

3) Rate Structures

- a) The Town of Natick should continue its established practice of ascending or inclined block rates for water usage in order to promote conservation.
- b) Rates should be proposed and adopted sufficient to cover all costs incurred during the fiscal year with the exception of catastrophic events. Mid-year rate modifications should be avoided whenever possible.

4) Indirect Costs

- a) Indirect costs shall be reviewed at regular intervals to ensure that they are reasonable to the services being provided by the General Fund in support of Water & Sewer Operations.

These policies should be reviewed at regular intervals for their effectiveness and continued improvement.