



Memorandum

To: Board of Selectmen

From: Martha White, Town Administrator
Michael Walters Young, Deputy Town Administrator

Date: Friday, April 23, 2010

Re: Water and Sewer Rate Setting for FY 2011

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 formally be presented to you during the formal rate hearings of May 10th and May 24th.

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.

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 2011 take place in three sessions – April 26th, May 10th and May 24th. The formal public hearing to set the rates would start on May 10th and end on May 24th. The proposed timeline and what is to be discussed when is presented below:

Session #1: April 26, 2010

- 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

Session #2: May 10, 2010

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

Session #3: May 24, 2010

- Finish Public Hearing
- Set Rates

Immediately afterwards:

- First bills go out for FY 2011

Water & Sewer Rates: Changes & Issues

Since FY 2008, 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.

The combination of all of these features 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.

Water & Sewer Rates: Proposals for FY 2011

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 2011. To that end, the table below summarizes the Water & Sewer Enterprise budget for FY 2011. The forecast increase in rates is .07%, or just under \$120,000 for FY 2011 when compared to FY 2010.

	2008 Actual	2009 Actual	2010 Appropriated	2011 TA Proposed	Change from 2010	
					\$	%
Revenues						
User Charges	\$ 9,992,305	\$ 13,068,730	\$ 12,314,366	\$ 12,433,778	\$ 119,412	0.97%
Connection Fees	\$ 94,291	\$ 95,193	\$ 95,000	\$ 170,000	\$ 75,000	78.95%
Other Departmental Income	\$ 739,814	\$ 1,000,186	\$ 700,000	\$ 750,000	\$ 50,000	7.14%
Investment Income	\$ 81,930	\$ 48,798	\$ 45,000	\$ 45,000	\$ -	0.00%
Capital Article Closeouts/Trans.	\$ -	\$ -	\$ 162,304	\$ 150,000	\$ (12,304)	-7.58%
Retained Earnings	\$ 2,675,000	\$ -	\$ 213,696	\$ -	\$ (213,696)	-100.00%
Total Revenues	\$ 13,583,340	\$ 14,212,907	\$ 13,530,366	\$ 13,548,778	\$ 18,412	0.14%
Expenses						
Sewer	\$ 4,743,775	\$ 4,823,607	\$ 5,218,449	\$ 5,253,221	\$ 34,772	0.67%
Water	\$ 1,649,681	\$ 1,830,313	\$ 2,013,391	\$ 2,077,341	\$ 63,950	3.18%
Utility Billing	\$ 231,116	\$ 172,061	\$ 219,282	\$ 221,648	\$ 2,366	1.08%
Fringe Benefits	\$ 604,816	\$ 610,046	\$ 607,776	\$ 636,395	\$ 28,619	4.71%
Debt Service	\$ 1,888,392	\$ 2,177,270	\$ 2,415,052	\$ 2,398,416	\$ (16,636)	-0.69%
Reserve Fund	\$ -	\$ -	\$ 200,000	\$ 200,000	\$ -	0.00%
Indirects (included in G/F)	\$ 2,379,592	\$ 2,546,346	\$ 2,506,416	\$ 2,449,757	\$ (56,659)	-2.26%
Capital	\$ 1,100,000	\$ 746,635	\$ 350,000	\$ 312,000	\$ (38,000)	-10.86%
Total Expenses	12,597,373	12,906,278	13,530,366	13,548,778	\$ 18,412	0.14%

Staff will prepare for the Board's consideration three detailed rate proposals in advance of your next meeting. The rate proposals at this time are:

- 1) **Status quo:** All rate tiers, groupings and averaging would remain the same; gross increase in revenue would be .97%
- 2) **Leveling of the Tiers:** Current tiers would be "leveled"; in other words, high users would pay less where low-end users would pay more in order to "level" out the extreme differences between tiers; gross increase in revenue would be .97%
- 3) **Surplus building:** All rate tiers, groupings and averaging would remain the same; gross increase in revenue would be between 3%- 5% for the purpose of building reserves and retained earnings for use in future years.

In addition, staff would like to revisit the formal adoption of formal financial management policies for the Water & Sewer Enterprise Fund. These have been included as an attachment to this memorandum; we welcome your questions at this and subsequent meetings but request that the board consider adopting these policies prior to the close of the hearing.

Requested Action:

Staff will develop rate recommendations as summarized above for your meeting of May 10th. Staff needs to know, however, if there are other requests, rate scenarios or analysis that the Board desires for that next meeting. In order for staff to complete this on-time and still have the Board vote rates on May 24th, we need to know over the next week and one half what those are. Please e-mail (myoung@natckma.org) or call (505) 647-6404 the Deputy Town Administrator with any requests or suggestions you may have by Wednesday, May 5th.

Please let us know if you have any questions.

Attachments

- Proposed Water/Sewer Enterprise Fund Financial Policies

Town of Natick, Massachusetts

Water/Sewer Enterprise Fund Recommended Financial Policies

The Town of Natick has adopted policies governing the use and administration of its general fund finances, but not for its enterprise funds. The list of proposed policies below is not a complete list, and is intended for discussion purposes only. Any adoption of policies for one entity of the Town should be done in concert with a comprehensive set of policies for all fiscal matters.

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) Operating Reserve: Maintain 30-60 days of operating reserve in retained earnings or a specialized stabilization fund at all times. The Natick equivalent to this in FY 2009 would be approximately \$1,000,000-\$2,000,000. This reserve could be used to stabilize rates in the event of unforeseen significant budgetary impacts, (e.g. unpredicted mid-year MWRA Assessments).

b) Capital Reserve: Maintain an appropriate capital reserve for two purposes: a) to mitigate those pieces of the Town's infrastructure which pose a moderate to immediate risk and require immediate resolution, and b) to fund items which regularly need to be replaced (i.e. Vehicles, Equipment and Small Infrastructure). The recommended amount for Natick would be approximately \$750,000.

c) Asset Renewal & Replacement Reserve (Stabilization Fund): In order to augment debt issuance and repayment costs, the Town should establish and regularly fund an Asset Renewal & Replacement Fund for the purpose of partially or completely funding capital improvements.

2) Capital Financing

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 shall finance all vehicles, equipment and infrastructure with a useful life under 10 years out of its Capital Reserve. For those vehicles, equipment and infrastructure with a useful life greater than 10 years, the town shall borrow as per the regulations set forth under M.G.L. Ch. 44 Sec. 7 & 8 and/or any other applicable laws.

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.

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.

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