

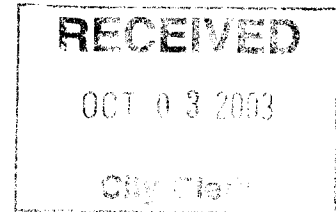
# MEMORANDUM

CITY/BOROUGH OF JUNEAU  
Public Works Department  
5433 Shaune Drive, Juneau, Alaska 99801

DATE: October 1, 2003

TO: Mayor & Assembly Members

FROM: Joe Buck, PE  
Public Works Director



SUBJECT: Response to Assembly Concerning Mr. Gregg's Email dated Saturday September 27, 2003.

In light of Mr. Gregg's email to the Assembly concerning the proposed utility rate increases, I felt that a detailed response was appropriate. Mr. Gregg presented some very good questions on how our utilities are run. I have highlighted the key issues in Mr. Gregg's email and have provided additional information for your consideration.

**"They involve abandoning our historic funding mechanisms; restructuring our utilities as business enterprises suitable for privatization; four separate rate increases; and as yet unspecified bonding activity. There has been no meaningful public notice regarding these drastic changes in policy"**

Historic funding mechanisms: It was the "historic funding mechanism" that has put the CBJ in this uncomfortable situation of having to drastically increase our water and sewer rates. The CBJ has historically under-funded its utilities by collecting insufficient revenues from its customers. Shortfalls in revenues needed for major capital repair work have been made up by diverting funds from other sources on an "emergency" basis, and in some cases having Streets Sales Tax funds pay for replacement and repair of distribution or collection systems within the roads. We have also relied heavily on low interest loans, borrowed from the State which need to be paid back. These "historic funding mechanisms" have not been sufficient to meet the needs of either utility to assure the ongoing sustainability of the operations, and were not consistent with the directive of operating the utilities as enterprise funds.

Restructuring our utilities as business enterprises suitable for privatization: To the best of my knowledge, the CBJ has always considered the water and sewer utilities to be enterprise fund operations. It has been the intent of our community and the Assembly that these two operations be fully supported through the revenues received from their customers. Unfortunately, this has not been the practice due to the difficulty of actually asking our customers to pay the costs. The recent cost allocation and rate study conducted on each utility is not an effort to restructure the enterprise. It is simply sound business practice to determine what the rates need to be and to insure the financial stability and sustainability of the utilities.

With respect to privatization, I do not support privatizing our utilities. My personal opinion is that water is one of the most basic of human needs and should not be controlled by private business. The people of Juneau should always own and control their water resources and systems. In addition, the mission of the wastewater utility is to collect our community's sewage so that it can be safely treated to protect our public's health and the health of our natural environment. Again, in my opinion this is too important a mission to turn over to private enterprise.

On a side point, if the utilities are managed efficiently enough for privatization then that means we are doing a good job for our customers. But remember, privatization will likely cost even more as private enterprise needs to make a profit. If they don't raise the cost of service, then they must cut corners on an already efficient operation. This means potentially putting the safety of our community's water, our health, and the natural environment at risk.

Four separate rate increases: This is correct, the cost allocation and rate design study looked at a nine-year study period and determined that four increases would be necessary to meet the financial needs of the utilities. The analysis first looked at increases at three year intervals, but a management decision was made with the concurrence of the Assembly's Public Works and Facilities Committee to have future rate adjustments coincide with the city's biennial budget process. As part of the consultant contract, a computer model for analyzing future utility rates will be provided to the city. The utility management will reanalyze the revenue needs annually and make recommendations to the Assembly for future rate adjustments and revenue bond sales.

Part of the reason for the significant increase that we are facing is that rates have not been adjusted regularly for inflation, or to meet the increasing maintenance needs of the utilities. In addition, we have borrowed money to pay for system improvement needed to comply with ongoing unfunded mandates from state and federal governments without adequately increasing our revenues to cover debt costs or the related increase in operational, maintenance, and replacement costs that go with the improvements.

Unspecified Bonding Activity: The bonding activity is outlined in the Capital Financing Plan for each utility. For the Water Utility, it is shown on page 9 of the Rate Study Results document, and for the Wastewater Utility it is shown on page 14. The analyses indicates that the Water Utility will require revenue bond sales starting in FY2007 and the Wastewater Utility will require revenue bond sales much earlier in FY2005. This bond sales projection is based on the current rate increase proposal being passed by the Assembly.

A lower utility rate increase will likely result in higher revenue bonds being needed at a sooner date. Although if the rate increase is not adequate, the utilities may lose their ability to sell revenue bonds due to insufficient revenues necessary to meet the debt service recovery requirements for bonding.

Revenue bond packages will be put together for three-year capital improvement programs instead of doing small annual bond sales. Each revenue bond package will be detailed and presented to the Assembly for their review and approval.

No meaningful Public Notice regarding these drastic changes in policy: As confirmed by the City Attorney, adequate public notice has gone out. The cost allocation and rate design study has taken approximately one year to complete. During that time there have been multiple Assembly sub-committee presentations to the Public Works and Facilities Committee and the Committee of the Whole. All standing Assembly committee meetings are advertised on the Web, in the newspaper, and on the television; the same as the regular Assembly meetings. In addition, the City Manager has discussed the need for rate increases twice on the local Capital Chat radio program, and the Juneau Empire headlines on Thursday September 4, 2003 read "Water, sewer fees may rise 32 – 37%".

**“The report on which you are relying is not even available to the public”**

While the final report is currently being prepared, all the financial material is contained in the Rate Study Results, dated August 18, 2003, as presented to the Assembly Committee of the Whole and provided in their meeting packet. The study results are also listed on the Web, as Mr. Gregg has pointed out in his summary of on-line references. The final report will be available next week, but it is unlikely to provide any significant additional information to what is already presented.

**“The race to adopt the proposed rates is clearly premature”**

Mr. Gregg refers to a portion of a memorandum I submitted to the Public Works and Facilities Committee which requested additional funds for FCSG to do the cost allocation and rate design study for the Wastewater Utility. My statement was based on my understanding of how rate increases had been planned for the FY2003 and FY2004 budget. An increase was planned by staff for each year of that budget cycle to cover two State loans. A \$2.00 per sewer service increase in both fiscal years was assumed adequate.

During the rate study process, it was determined that not only could the Wastewater Utility not cover the an additional loan in FY2004, it would not have sufficient customer revenues to meet our cost of operations, maintenance, or our current debt service load due to our declining reserves. FCSG has provided an independent analysis of the financial management of our utilities and the resulting rate study indicates that the \$2.00 increase that staff had planned for back in 2002 is not sufficient.

**“ An inaccurate public record”**

Mr. Gregg is correct that there was an error in the Juneau Empire concerning the scheduled public hearing on the proposed rate increase ordinance. The newspaper mistakenly stated the next Assembly meeting to be October 6, 2003 instead of the actual date of October 13, 2003. While this mistake was unfortunate, I don't really see it as being detrimental to the public process. Also, I don't really think it appropriate to place the responsibility on the Juneau Empire as being the city's "newspaper of record" and therefore responsible for the public record. Unfortunately, mistakes do happen now-and-then.

**“A missing \$71,440 Report”**

The report is not missing, it just has not been completed as of yet. The contract with FCSG required completion of the report once the material had been presented to the Assembly and the rate increase ordinance had been introduced. The final report will mirror the material presented to the Assembly in the Rate Study Results presentation, dated August 18, 2003. The final report is expected to be available the week of October 6, 2003.

**“Unreasonably Short Public Notice”**

The ordinance before the Assembly to increase the utility rates is not based on the pending report, but on the material presented to the Assembly Public Works Committee on May 28, 2003, the Assembly Committee of the Whole (COW) on August 18, 2003, and again on September 3, 2003. The September 3, 2003 COW meeting was specifically intended for a public hearing. This is four months of various forms of public notice.

**“An incomplete public record”**

The rate study assesses the financial picture of the utilities over next nine years ( FY2004 to FY2012). The Capital Financing plan, Revenue Requirements plan, and the Fund Balance plan developed in the study look in detail at the need for multiple rate increases and revenue bonds. The cost to repay existing loans and revenue bond debt, as well as the estimated interest earnings on those bonds, are calculated into the proposed rate increases.

All of this information has been presented multiple times to the Assembly Public Works and Facilities Committee and the Committee of the Whole and is of public record.

**“Switching to user fees without reducing taxes presently used to fund the utilities may effectively be an unauthorized tax increase”**

There are currently no tax revenues dedicated to supporting either of the utilities.

Both utilities have historically been supported by their customer service fees. Street sales tax has been used to pay for replacement of the water and sewer system at times when it was necessary to replace the infrastructure as part of the entire street reconstruction process. Part of the reason for the rate increase is to provide the necessary revenues to the utilities to carry their share of cost of these major public improvements. The rate increase provides the utilities with the revenues they need to repair and replace the aging water and sewer systems when needed.

The Rate Study Results presented to the Assembly identifies significant outside funding for both utilities for FY2004. The outside fund sources for FY2004 are as follows:

- \$1,500,000 in General Obligation (GO) bonds approved by the votes in the fall of 2002 for water and sewer system replacement in Third Street Douglas;
- \$2,200,000 in GO bonds (2002) for the expansion of the water system out to North Tee Harbor;
- \$750,000 ADEC grant for Third Street Douglas utility replacement;
- \$415,000 ADCE grant for JDWWTF incinerator repairs;
- \$500,000 Legislative Re-appropriation of ADEC grant (Lena Reservoir to N. Tee Harbor Extension)

The rate study does not assume future outside revenues, as these sources are not dependable. Furthermore, we already have a considerable number of loans that need to be paid back. Both utilities will continue to seek grant funding, when appropriate and necessary, for repair and replacement of infrastructure to minimize future water and sewer rate increases. But, as there are no guarantees of these future revenue sources, they cannot be correctly figured into a financial analysis for organizational needs.

Due to insufficient revenues received by the Wastewater Utility for FY2004, the utility asked the Assembly to consider authorizing a one time use of \$880,000 of Street Sales Tax and \$195,000 of Marine Passenger Fees to cover some emergency repairs that were necessary. The Marine Passenger Fee request and \$220,000 of the Streets Sales Tax request were to fund major repairs to the JDWWTF

incinerator. The Assembly denied the incinerator repair request and other grant sources were sought and received from the State Legislature.

The following two wastewater projects were funded under the FY2004 CIP using Streets Sales Tax:

- Wastewater Facilities/Deferred Maintenance @ \$510,000
- Bayview Subdivision Sewer Outfall @ \$150,000

These were presented as a one-time funding request. It is the intent of the utilities to fund future major repairs through increased customer revenues.

No Liquor Tax or Tobacco Tax is used to subsidize either utility.

In the past the utilities have essentially "begged" for funds from other municipal revenue sources to respond to emergency repairs. This has been necessary because adequate customer revenues have not been collected to cover the needs of the infrastructure. Raising customer service rates does not equate to lowering other program revenues as Mr. Gregg implies. These other programs have essentially provided an emergency grant to the utility in these cases.

**"When did the public vote to convert our public utilities to business enterprise?"**

The Water Utility and Wastewater Utility have always been run as an enterprise fund. In review of the City and Borough of Juneau Biennial Budget for Fiscal Years 2003 and 2004 you will find both the Water Utility and the Wastewater Utility listed as enterprise funds. In review of Section 9.16 Enterprise Funds from the CBJ Charter you will find the following definition:

***Section 9.16. Enterprise funds.***

*Revenues from an enterprise, whether established before or after July 1, 1970, shall be first used for debt retirement, construction, acquisition, operation, maintenance, repair, and capital improvement of the enterprise.*

The basic definition of an enterprise fund is that it should be self-sustaining and pay for itself through user revenues.

As previously mentioned, it is unwise to count on undependable outside funding sources when defining our utilities' revenue requirements. If outside funding is obtained, then that revenue will be figured into future consideration of rate increases and/or lower revenue bond levels. It is not something that should be considered when the utilities are first trying to "get on their feet" financially.

**"Is it equitable to force residential customers to subsidize large business users?"**

This is a municipal policy question not uncommon with respect to water and sewer utility rate adjustments. As was stated by the consultant, the Cost-of-Service rate structure relates customer use to actual costs to provide that service. If the utilities had been doing regular rate adjustments to keep up with increasing cost of operation and repair, the Cost-of-Service rate structure alternative would likely be appropriate and already enacted.

In our current situation, the utilities have not sufficiently kept up with rate increases and the jump from current rates to Cost-of-Service rates is very significant and may have major financial impacts on our business community. For this reason, the recommendation is to implement the Across-the-Board rate structure for the first three to five years and to assess a transition over to Cost-of-Service method as part of future utility rate increases.

I see this as a question of value and not something that is either yes or no. The residential customers and the business community are dependent on each other. Is it equitable right now? Probably not. But it's not the business community's fault. If the business community is to pay significantly higher rates at first, these increased costs will likely be passed on to the citizen in some form. Will it cause some of our businesses to become unprofitable and thus result in fewer job opportunities in Juneau and fewer business related services? I can't answer this yes or no. I see the Across-the-Board rate increase method as a logical solution to get us to where we need to be financially.

**“Are the unfinished study's assumptions even correct?”**

Zero growth is conservative but reasonable for this kind of study. The State Demographer indicates that Juneau's projected growth over the study period is less than one-percent. The high population projections used by other agencies to support their new construction projects are turning out to be significantly off.

By assuming zero growth we have a conservative analysis that assures adequate revenues are received to operate the utilities. If there is community growth and additional customers are connected, that is great. The utilities annual model analysis will show this increased number of customers and should result in lower future rate increases and/or smaller revenue bond sales.

**“For the sake of completeness, let's not forget the issue I first raised – is it equitable for single people in one-bath homes with water conserving appliances to pay the same rate as large residences with multiple baths and undeclared apartment?”**

This is an issue of economics. To implement an areawide-metering program, the Water Utility would be looking at a \$5 to \$6 million capital project. If the utility were to sell a 20-year revenue note for this work, we would be looking at approximately a 36-percent increase in our FY2004 water rates instead of 19-percent. Also, we would be looking at increasing the Water Utility's annual operations and maintenance expenses by approximately \$300,000, an approximate 13-percent in O&M, to cover the manpower, materials, equipment, and administrative costs of the additional meters.

The Water Utility will be considering an areawide metering program in the future and making a presentation to the Assembly concerning this program. It is not considered “affordable” at this time though. If funding sources other than customer service fees were identified to pay capital cost of meter implementation then it would make more sense financially.

Response to Mr. Gregg's Email dated 9/27/03

October 1, 2003

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**“Summary. At this stage, the so-called “study” raises more questions than it answers.”**

**“The smaller amount (\$2.00) may not meet the utility's long term needs, but future assemblies can deal with that.”**

**“Please consider implementing the minimum increase necessary and taking more time to consider the long-term alternatives. Thank you.”**

I do not believe that the study raises more questions than it answers. The three phases of the study, (1) the rate revenue analysis, (2) the cost allocation phase, and (3) the rate design phase have been quite thorough and were done by an independent consultant; the work was not done by utility staff. The process was comprehensive and was not rushed to a conclusion. It is unfortunate that financial analysis efforts such as this do not receive the public's attention until the first bill shows up in the mail, but the utility staff has tried to keep this as open and public as possible.

The \$2.00 increase that was planned for in 2003/2004 biennial budget is not applicable now, based on what we know from the current rate study. This increase would not even cover the Wastewater Utility debt service costs.

A significant part of the problem that we are now having to deal with is that the past city administration failed to address this uncomfortable, and unpopular, necessity of increasing utility rates. The necessary cost allocation and rate analysis just kept getting put off until the operations were reaching the point of not being financially viable and potentially putting their revenue bond capacity in jeopardy.

The purpose of this rate study process was to address the long-term alternatives. Putting off the needed utility rate adjustments will only:

- Result in unstable financial condition for the utilities;
- Place the utilities' revenue bonding and loan capability at risk;
- Result in the lack of necessary funding to make major system repairs necessary to meet the utilities' service missions;
- Result in the utilities' inability to react to increasing unfunded mandates by State and Federal agencies pertaining to operational permits;
- Increases the risk of serious legal fines for not meeting utility permit conditions;
- Places the public and our environment at risk if our utilities are not provided adequate revenues to allow proper operation, maintenance, and replacement of the systems.

I do not believe it is in the best interest of our community's health and well being, nor the safety of our natural environment, to delay the implementation of this necessary rate adjustment for the Water Utility and the Wastewater Utility.

cc. Rod Swope, City Manager  
Donna Pierce, Deputy City Manager  
Scott Jeffers, Wastewater Superintendent  
Grant Ritter, Water Utility Superintendent  
Craig Duncan, Finance Director