Homer City Hall
491 E. Pioneer Avenue
Homer, Alaska 99603
www.cityofhomer-ak.gov

City of Homer
Agenda

City Council Worksession
Monday, August 22, 2022 at 4:00 PM
In Person at City Hall Cowles Council Chambers and Zoom Webinar
https://cityofhomer.zoom.us/j/96586314135?pwd=WTdvVHdDVmxxZHJwaC9ZNmFYYlZ3dz09
Dial: (669) 900 6833 or (253) 215 8782 or Toll Free (888) 788 0099 or (877) 853 5247
Webinar ID: 965 8631 4135 Password: 792566

CALL TO ORDER, 4:00 P.M.

AGENDA APPROVAL (Only those matters on the noticed agenda may be considered, pursuant to City Council's Operating Manual, pg. 6)

DISCUSSION TOPIC(S)

a. Water and Sewer Rates

COMMENTS OF THE AUDIENCE (3 minutes)

ADJOURNMENT NO LATER THAN 4:50 P.M.
Next Regular Meeting is Monday, September 12, 2022 at 6:00 p.m., Committee of the Whole at 5:00 p.m. All meetings scheduled to be held in the City Hall Cowles Council Chambers located at 491 E. Pioneer Avenue, Homer, Alaska.

Unpacking Water and Sewer Rates and other mysteries – Decision Time

AUGUST 22, 2022

Questions for 2022 – How should the CARMA Accounts be replenished?

- ***Recommendations:***
  - Use Utility Asset Management Plan to develop a 5-year CIP, based on need.
  - Include CARMA expense as "input" in Rate Model.
  - Apply part of existing Fund Balance to maintain CARMA

Other CARMA Recommendations

- Explore loans for larger projects
- Set floor for each CARMA Fund – $500,000
- Set cap for each CARMA Fund – $1,500,000

Question for 2022 – How should the Fund Balance be managed?

- ***Recommendations for existing Fund Balance:***
  - Use ¼ to start building 3-month Op. Reserve
  - Use ¼ to start replenishing CARMA
  - Use ½ to buy down rate increase

Question for 2022: How should future Fund Balances be managed?

- ***Recommendations for future Fund Balances:***
  - Maintain 3-month Operating Reserve
  - Maintain CARMA floor
  - Buy down future rate increases

Questions for 2022 – How should administrative fees be charged?

- ***Recommendations:***
  - Starting with FY 24/25 – Add cost of 1 FTE for Fin. Admin. as Input to "Rate Model"
  - Approx. $90,000 direct & indirect costs

Question for 2022 – How can we do better forecasting?

- ***Recommendations:***
  - Base Rates on the two-year Budget cycle
  - Start with FY 24/25

Question for 2022: When should rates be effective

- ***Recommendation:***

  2022 – November 1, 2022

  Future – match Budget cycles

Proposed Rate Setting Schedule

- August 8 — Introduction & present decisions
- August 22 — Proposed Rate Schedule
- September 12 — Introduce supporting legislation
- September 26 — Public Hearing for legislation
  Adopt rates
- October — Public notice
- November 1 — Rates effective

City of Homer
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Memorandum

TO: Mayor Castner and Homer City Council

THROUGH: Rob Dumouchel, City Manager

FROM: Elizabeth Walton, Finance Director

DATE: August 18, 2022

SUBJECT: Water and Sewer Rate Model

The purpose of this memo is to provide an overview of the model used to generate the water and sewer rates.

Introduction:

The basic principles and assumptions of this model were developed by the most recent Water and Sewer Task Force. The purpose of this model is to generate a utility rate that is a product of budget assumptions and the backing out of fixed fee components. The intent was to provide the City with a mechanism that connected the water and sewer rates to the actual costs to maintain the infrastructure.

The format of the rate model has changed from the one the Water and Sewer Task Force generated, but the basic principles and assumptions remain the same. These changes were made to more accurately reflect the City's budget structure.

City staff has spent substantial time this year to further connect this rate model to the operating budget and the financial worksheet that HDR helped us to develop. This allows for the rate model to more precisely fund the operating expenses as well as urgent capital project needs for the upcoming fiscal year.

Water Rate Model:

This model generates a rate based on water revenues and consumption.

Revenues

The revenue inputs are defined as follows:

- FY23 Operating Revenue Required – This amount is pulled directly from the amended budget. This amount represents the budgeted operating expenses for FY23.
- CARMA Transfer Requirement – This amount is pulled directly from the financial worksheet that details the future capital needs.

- Deduct Operating Fund Balance – This amount represents the amount of Utility Operating Fund Balance to be used for rate buyback.
- Deduct Portion Collected through Service Fee – This input has been removed this year, as the Admin Fee was waived for FY23.
- Hydrant Rents – This is related to the costs associated with maintaining the water hydrants and is budgeted at 10% of total water revenue required and the costs are shared 50/50 between the General Fund and the Water/Sewer Fund.
- Surplus Water Sales (Bulk) Surcharge Only – This amount is determined by applying the bulk surcharge (0.004/gallon) to the prior fiscal year total gallons consumed by bulk users. This is backed out because these expenses are captured by the separate rate for bulk users.
- Revenue Required for Commodity Rate Calculation – Summation of revenue required less deductions. This represents the amount of revenue necessary to generate to meet operating and capital budget needs for upcoming fiscal year.

Consumption

The water consumption line is determined by prior fiscal years gross meters water sales (in gallons). The water usage at the Sewer Treatment Plant has been backed out of this figure, as it has been determined to be an operational cost. The model rounds up to the nearest million for ease of reporting.

Rates

The water rates are broken into three categories. The commodity rate (per gallon) is generated by dividing the total revenue required by the estimated water sales. This ensures that the whole population of water users are contributing to an equal share of costs. The bulk rate (per gallon) is applying a surcharge of 0.004 per gallon to the set commodity rate. The monthly fees is determined by dividing the budgeted administrative costs by the current number of water meters. As of the most recent billing, there were a total of 1,904 meters. This fee has been waived in this model as the admin fee was waived in FY23.

The included rate comparison sheet illustrates the proposed rate change between calendar years 2022 and FY23. Also included in this comparison sheet is an analysis of the variances between proposed scenarios.

Sewer Rate Model:

This model generates a rate based on sewer revenues and usage.

Revenues

The revenue inputs are defined as follows:

- FY23 Operating Revenue Required – This amount is pulled directly from the amended budget. This amount represents the budgeted operating expenses for FY23.
- CARMA Transfer Requirement – This amount is pulled directly from the financial worksheet that details the future capital needs.

- Deduct Operating Fund Balance – This amount represents the amount of Utility Operating Fund Balance to be used for rate buyback.
- Fixed Fee Components
    - Lift Stations Costs - These costs are pulled straight from the current operating budget. These costs are backed out because the users on the lift station bear the complete costs associated with maintaining this infrastructure.
    - Pumping Fee - The City RFP's the pumping contract every three years and the costs of the contract is divided up amongst the number of Kachemak City users. As of most recent billing, there are currently 142 users.
    - Dumping Station Fee - These costs come directly from the current operating budget. This fee has been determined to be an operational cost and, as such the fee is not forwarded along to customers.
    - Multi-Units and Kachemak City meters - This is an additional fee charged to help offset added costs associated with maintaining such infrastructure. It might be worth revisiting this fee now that the monthly fees for all users have been waived this year.
- Revenue Required for Commodity Rate Calculation – Summation of revenue required less deductions. This represents the amount of revenue necessary to generate to meet operating and capital budget needs for upcoming fiscal year.

Usage

The sewer usage is determined by the by the number of gallons actually billed for in the prior fiscal year. The model rounds up to the nearest million for ease of reporting.

Rates

The sewer rate is broken into two categories (non-lift and lift station). The non-lift rate is generated by dividing the total revenue required by the projected billable volume for non-lift. The lift station rate is generated by dividing the total revenue required by the projected billable volume for only the lift zone.

The included rate comparison sheet illustrates the proposed rate change between calendar years 2021 and 2022. Also included in this comparison sheet is an analysis of the variances between proposed scenarios.

Recommendation:

Review the model and approve the rates set forth in Scenario 3 (fund emergency balance at 25%, fund CARMA replenishment at 25%, and fund rate buyback at 50%).

Rate Calculations
Scenario 1

WATER Rate Model		
Revenues		
FY23 Operating Revenue Required - Water	$	2,013,046
CARMA Transfer Requirement*		593,196
Deduct Operating Fund Balance		0
Deduct Portion Collected through Service Fee		0
Hydrant Rents (10% of Total)		(100,652)
Surplus Water Sales (Bulk) surcharge only		(67,796)
Revenue Required for Commodity Rate Calculation	$	2,437,794
Water Consumption (Gallons)		
Total Estimated Water Sales		131,000,000
Water Rates:		
Commodity Rate (per gal)	**$**	**0.0186**
Bulk Rate (per gal)	**$**	**0.0226**
Monthly Fees	**$**	**-**
Consumption Additional Information:		
FY22 Gross Meters Water Sales (Gallons)		130,971,800

SEWER Rate Model		
Revenues		
FY23 Operating Revenue Required - Sewer	$	1,754,682
CARMA Transfer Requirement*		275,834
Deduct Operating Fund Balance		0
Lift Stations Costs		(225,231)
Pumping Fee		(10,224)
Dumping Station Fees		(5,986)
Multi-Units and K-city ($5/unit/mo.)		(76,020)
Revenue Required for Commodity Rate Calculation	$	1,713,055
Sewer Usage (Gallons)		
Projected Billable Volume		77,000,000
Projected Billable Volume - Lift Zone Only		20,000,000
Total Projected Billable Volume		97,000,000
Sewer Rate		
Non-Lift Station Rate	**$**	**0.0177**
Lift Station Rate	**$**	**0.0289**
Lift Station Additional Information:		
FY 22 Actually Billed Gallons (Lift-Station Zone Only)		19,581,500

*CARMA Transfer Requirement - Fund FY23 capital projects in financial model less operating budget transf[illegible]ARMA. For Water, also back out grant funding to cover reimburseme[illegible]roject.

Rate Calculations
Scenario 2

WATER Rate Model		
Revenues		
FY23 Operating Revenue Required - Water	$	2,013,046
CARMA Transfer Requirement*		593,196
Deduct Operating Fund Balance		(225,000)
Deduct Portion Collected through Service Fee		0
Hydrant Rents (10% of Total)		(100,652)
Surplus Water Sales (Bulk) surcharge only		(67,796)
Revenue Required for Commodity Rate Calculation	$	2,212,794
Water Consumption (Gallons)		
Total Estimated Water Sales		131,000,000
Water Rates:		
Commodity Rate (per gal)	**$**	**0.0169**
Bulk Rate (per gal)	**$**	**0.0209**
Monthly Fees	**$**	**-**
Consumption Additional Information:		
FY22 Gross Meters Water Sales (Gallons)		130,971,800

SEWER Rate Model		
Revenues		
FY23 Operating Revenue Required - Sewer	$	1,754,682
CARMA Transfer Requirement*		275,834
Deduct Operating Fund Balance		(225,000)
Lift Stations Costs		(225,231)
Pumping Fee		(10,224)
Dumping Station Fees		(5,986)
Multi-Units and K-city ($5/unit/mo.)		(76,020)
Revenue Required for Commodity Rate Calculation	$	1,488,055
Sewer Usage (Gallons)		
Projected Billable Volume		77,000,000
Projected Billable Volume - Lift Zone Only		20,000,000
Total Projected Billable Volume		97,000,000
Sewer Rate		
Non-Lift Station Rate	**$**	**0.0153**
Lift Station Rate	**$**	**0.0266**
Lift Station Additional Information:		
FY 22 Actually Billed Gallons (Lift-Station Zone Only)		19,581,500

*CARMA Transfer Requirement - Fund FY23 capital projects in financial model less operating budget transf[illegible]ARMA. For Water, also back out grant funding to cover reimburseme[illegible]roject.

Rate Calculations
Scenario 3

WATER Rate Model		
Revenues		
FY23 Operating Revenue Required - Water	$	2,013,046
CARMA Transfer Requirement		450,000
Deduct Operating Fund Balance		(305,998)
Deduct Portion Collected through Service Fee		0
Hydrant Rents (10% of Total)		(100,652)
Surplus Water Sales (Bulk) surcharge only		(67,796)
Revenue Required for Commodity Rate Calculation	$	1,988,600
Water Consumption (Gallons)		
Total Estimated Water Sales		131,000,000
Water Rates:		
Commodity Rate (per gal)	**$**	**0.0152**
Bulk Rate (per gal)	**$**	**0.0192**
Monthly Fees	**$**	**-**
Consumption Additional Information:		
FY22 Gross Meters Water Sales (Gallons)		130,971,800

SEWER Rate Model		
Revenues		
FY23 Operating Revenue Required - Sewer	$	1,754,682
CARMA Transfer Requirement		285,000
Deduct Operating Fund Balance		(305,998)
Lift Stations Costs		(225,231)
Pumping Fee		(10,224)
Dumping Station Fees		(5,986)
Multi-Units and K-city ($5/unit/mo.)		(76,020)
Revenue Required for Commodity Rate Calculation	$	1,416,223
Sewer Usage (Gallons)		
Projected Billable Volume		77,000,000
Projected Billable Volume - Lift Zone Only		20,000,000
Total Projected Billable Volume		97,000,000
Sewer Rate		
Non-Lift Station Rate	**$**	**0.0146**
Lift Station Rate	**$**	**0.0259**
Lift Station Additional Information:		
FY 22 Actually Billed Gallons (Lift-Station Zone Only)		19,581,500

CIty of Homer
Water and Sewer Rates Comparison
Presented August 18, 2022

	Average Volume				High Volume				Lift-Station (Year-Round)			
	City Hall				Library				Port & Harbor - Maintenance			
	Existing	Scenario 1	Scenario 2	Scenario 3	Existing	Scenario 1	Scenario 2	Scenario 3	Existing	Scenario 1	Scenario 2	Scenario 3
Consumption	3800	3800	3800	3800	6600	6600	6600	6600	1800	1800	1800	1800
Water Rate	0.0107	0.0186	0.0169	0.0152	0.0107	0.0186	0.0169	0.0152	0.0107	0.0186	0.0169	0.0152
Sewer Rate	0.0143	0.0177	0.0153	0.0146	0.0143	0.0177	0.0153	0.0146	0.0243	0.0289	0.0266	0.0259
Charges:												
Water	40.66	70.68	64.22	57.76	70.62	122.76	111.54	100.32	19.26	33.48	30.42	27.36
Sewer	54.34	67.26	58.14	55.48	94.38	116.82	100.98	96.36	43.74	52.02	47.88	46.62
Service	14	0	0	0	14	0	0	0	14	0	0	0
Total Bill	**$ 109.00**	**$ 137.94**	**$ 122.36**	**$ 113.24**	**$ 179.00**	**$ 239.58**	**$ 212.52**	**$ 196.68**	**$ 77.00**	**$ 85.50**	**$ 78.30**	**$ 73.98**
Impact		**$ 28.94**	**$ 13.36**	**$ 4.24**		**$ 60.58**	**$ 33.52**	**$ 17.68**		**$ 8.50**	**$ 1.30**	**$ (3.02)**

Scenario 1: Utilitize existing operating fund balance to fully fund emergency balance (3 months operating)
Scenario 2: Split utility operating fund balance (50% to emergency balance; 50% to offset necessary transfer to CARMA)
Scenario 3: Split utility operating fund balance (50% to rate buyback; 25% to emergency fund balance; 25% to CARMA) - Staff Recommendation

Revenues & Expenses - Utility Operations Fund

	FY 22 Budget	FY 22 Actual	FY 23 Budget
Water			
Meter Sales	1,779,324	1,845,903	1,779,324
Other Revenue	143,678	46,796	142,348
Hydrant Transfer	91,418	91,418	91,734
Water Operations Fund - Total Revenue	**2,014,420**	**1,984,117**	**2,013,406**
Salaries, Wages & Benefits [1]	1,017,210	920,515	1,107,332
Maintenance & Operations [2]	731,711	766,835	781,295
Transfers to:			
Reserves	247,542	247,542	106,804
Other	17,957	17,957	17,976
Water Operations Fund - Total Expenses	**2,014,420**	**1,952,849**	**2,013,406**
Revenues over Expenses	**0**	**31,268**	**0**
Sewer			
Meter Sales	1,731,174	1,761,570	1,731,174
Other Revenue	31,090	43,349	23,508
Sewer Operations Fund - Total Revenue	**1,762,264**	**1,804,919**	**1,754,682**
Salaries, Wages & Benefits [1]	812,036	725,362	881,138
Maintenance & Operations [2]	647,672	563,291	634,290
Transfers to:			
Reserves	297,484	297,484	234,166
Other	5,073	5,073	5,088
Sewer Operations Fund - Total Expenses	**1,762,264**	**1,591,210**	**1,754,682**
Revenues over Expenses	**0**	**213,709**	**0**
Utility Operations Fund Total	**0**	**244,977**	**0**

[1] *Includes leave cash out*

[2] *Includes GF admin fees (overhead costs) - waived in FY22 and FY23*

Utility Fund
Unaudited Fund Balance Summary
Presented 8/10/22

Utility Operations Fund (200)					
	FY18	FY19	FY20	FY21	FY22
Beginning Fund Balance	$ 3,291,818	$ 3,325,819	$ 673,608	$1,030,917	$ 979,016
Ending Fund Balance	$ 3,325,819	$ 673,608	$ 1,030,917	$ 979,016	$1,223,993
Net Change	$ 34,001	$(2,652,211)	$ 357,309	$ (51,901)	$ 244,977

Water CARMA Fund (256-0378)						
	FY18	FY19	FY20	FY21	FY22	FY23
Beginning Fund Balance	$ 2,593,246	$ 2,650,270	$ 2,615,008	$2,555,103	$2,360,100	$2,002,880
Ending Fund Balance	$ 2,650,270	$ 2,615,008	$ 2,555,103	$2,360,100	$2,002,880	$2,002,110
Net Change	$ 57,024	$ (35,262)	$ (59,905)	$ (195,003)	$ (357,220)	$ (770)

Encumbered	$ 838,236
Current Balance Available	$1,163,874
FY23 Budgeted CARMA Transfer	$ 106,804

Sewer CARMA Fund (256-0379)						
	FY18	FY19	FY20	FY21	FY22	FY23
Beginning Fund Balance	$ 2,153,985	$ 1,979,619	$ 2,065,381	$1,929,114	$1,823,338	$1,662,656
Ending Fund Balance	$ 1,979,619	$ 2,065,381	$ 1,929,114	$1,823,338	$1,662,656	$1,661,886
Net Change	$ (174,366)	$ 85,762	$ (136,267)	$ (105,776)	$ (160,682)	$ (770)

Encumbered	$1,288,587
Pending Encumbrance (ORD 22-43)	$ 51,000
Balance Available	$ 322,299
FY23 Budgeted CARMA Transfer	$ 234,166

Sewer CARMA 8-8-22

City of Homer
Water and Sewer Financial Plan
Sewer Capital Improvement Plan
Exhibit 7

			Year 1 - July 2020 - June 2021	Year 2 July 2021- June 2022	Year 3 July 2022- June 2023	Year 4 July 2023- June 2024	Year 5 July 2024- June 2025				
CARMA-Funded Projects	**CY 2019**	**CY 2020**	**CY 2021**	**FY 2022**	**FY 2023**	**FY 2024**	**FY 2025**	**FY 2026**	**FY 2027**	**FY 2028**	**FY 2029**
Future Unidentified Projects	$118,039	$0	$0	$0	$225,000	$225,000	$225,000	$225,000	$225,000	$225,000	$225,000
1/2 of Utility Financial Mgmt.			12,907								
Beluga Lift Station - conceptual design			4,463								
Betterments of East Hill			49,000								
Launch Ramp Lift Station Enclosure			13,674								
Replace Deep Shaft Air Compressor			85,000								
Upgrade SCADA for 7 Lift Stations			210,900								
WWTP Digester Blowers			145,750								
Fuel Island - sewer share			7,200								
Influent Station Backup Pump				16,136							
Safety Hoist for Lift Station & Other Underground				10,282							
Sewer Inspection Camera				57,320							
Repair Pond Liner at Sewer Treatment Plant				25,000							
Replacement of E-170 ToolCat				21,667							
Replacement of E-161 CAT Loader				158,333							
Replacement of E-131 W/S Truck				15,000							
Replacement of E-130 Service Truck				26,667							
Replacement of E-114 PW Truck				10,000							
PW Campus Mitigation Plan				16,667							
East Hlll Road Paving Project "Betterments" - Sewer share				64,477							
East Hill Road Paving Project - Manhole repairs				150,000							
Update Design Criteria Manual & Standard Specs				5,000							
Computerized Maintenance Management System				23,333							
Clarifer belts				472,000							
Aerators - 3 each				50,000							
Replace UV System- lamps & control panel					10,000	10,000	10,000	10,000	10,000		
WWTP MCC Spare Parts					30,000						
Replace Cracked Incinerator					75,000						
Beluga Lift Station - Final Design & Construction					20,000	20,000	20,000	20,000	20,000		
Lagoon liner					25,000						
Replace Lift Station access hatch on Bay Ave as part of road project					50,000						
Sludge Drying Beds					25,000						
Fleet Replacement (50-50 split with Water)					50,000	50,000	25,000	25,000	25,000		
Lift Station upgrades						50,000	50,000	50,000	50,000		
Total CARMA-Funded Projects	**$118,039**	**$0**	**$528,894**	**$1,121,882**	**$510,000**	**$355,000**	**$330,000**	**$330,000**	**$330,000**	**$225,000**	**$225,000**
Transfer to Cash Reserve	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Total CARMA-Funded Projects	**$118,039**	**$0**	**$528,894**	**$1,121,882**	**$510,000**	**$355,000**	**$330,000**	**$330,000**	**$330,000**	**$225,000**	**$225,000**

Water CARMA 8-8-22

City of Homer
Water and Sewer Financial Plan
Water Capital Improvement Plan
Exhibit 5

CARMA-Funded Projects	CY 2019	CY 2020	Year 1 - July 2020 - June 2021 CY 2021	Year 2 July 2021-June 2022 FY 2022	Year 3 July 2022-June 2023 FY 2023	Year 4 July 2023-June 2024 FY 2024	Year 5 July 2024-June 2025 FY 2025	FY 2026	FY 2027	FY 2028	FY 2029
Future Unidentified Projects	$406,754	$25,620	$0	$0	$300,000	$300,000	$300,000	$300,000	$300,000	$300,000	$300,000
1/2 of Utility Financial Mgmt.			12,907								
Betterments on East Hill			49,000								
Raw Water Transmission Line			33,185								
Commercial Meter Replacement			80,000								
Dredge for WTP			10,000								
Million Gallon Water Tank Aeration System			172,624								
Tesoro Water Vault Upgrade			100,000								
Raw Water Line Replacement Design			202,222								
Raw Water Line Replacement - Construction					1,470,000						
PRV Replacement West Trunk Line			25,000								
Fuel Island - water share			7,200								
Water Share of Ocean Drive SAD				52,506							
DR 6000 uV VIS Spectrophotometer w/ RFID				9,276							
Mlox Chlorine Generator Cell Replacement				30,000							
PR Station Hatch Improvement				35,279							
Water Treatment Plant HVAC Control System Upgrade				55,955							
East Trunk FPI Mag Flow Meter				9,000							
Replacement Flow Meters at Main and Danview PR Station and East Rd Monitor				15,000							
Replacement of E-170 ToolCat				21,667							
Replacement of E-161 CAT Loader				158,333							
Replacement of E-131 W/S Truck				15,000							
Replacement of E-130 Service Truck				26,667							
Replacement of E-114 PW Truck				10,000							
PW Campus Mitigation Plan				16,667							
East Hill Road Paving Project - Betterments - water share				64,477							
Update Design Criteria Manual & Standard Specs				5,000							
Computerized Maintenance Management System				23,333							
WTP Filter Media Train - 1 each/year					100,000	100,000	100,000	100,000	100,000		
Balance motor/shaft at RWP-1					50,000						
Hydrant Replacement (100 need to be replaced, plan for 10 per year with road projects)					100,000	100,000	100,000	100,000	100,000	100,000	100,000
Fleet Replacement (Split 50-50 with sewer)					50,000	50,000	25,000	25,000	25,000		
Renovate Morning Glory, etc. at Dam					100,000						
Total CARMA-Funded Projects	**$406,754**	**$25,620**	**$692,138**	**$548,160**	**$2,170,000**	**$550,000**	**$525,000**	**$525,000**	**$525,000**	**$400,000**	**$400,000**
Transfer to Cash Reserve	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Total CARMA-Funded Projects	**$406,754**	**$25,620**	**$692,138**	**$548,160**	**$2,170,000**	**$550,000**	**$525,000**	**$525,000**	**$525,000**	**$400,000**	**$400,000**

City of Homer Water and Sewer
Water and Sewer Utility
Financial/Rate Setting Policies

Introduction

Financial policies are an important tool for maintaining a financially healthy and sustainable utilities while also maintaining required and/or mandated measures. The Government Finance Officers Association (GFOA), bond rating agencies, and other industry organizations (e.g., the American Water Works Association (AWWA), the Water Environment Federation (WEF)) recommend written financial/rate setting policies to provide clear policy direction and guidance.

The establishment of written financial policies is intended to:

- Institutionalize sound financial practices
- Clarify strategic intent
- Define boundaries
- Support bond ratings
- Promote long range strategic thinking
- Manage risk
- Adhere to established best practices

Financial Policy Goals and Objectives

The goals of the City's financial policies are to:

1. Maintain sufficient revenues for operating and capital needs,
2. Maintain sufficient reserves, and,
3. Provide rate stability. Notwithstanding (1) and (2) above, rates will be set to provide rate/revenue stability and avoid major periodic increases.

A detailed set of financial policies have been adopted to establish consistency in utility financial planning and rate setting decision-making for the City Council and City management team.

This framework provides recommendations that take into consideration the typical or median reserve levels for a "AAA" versus a "AA" rated utility. This framework will also enable the City Council to make more informed decisions in establishing the financial targets contained within the financial policies.

Review and Discussion of the City's Financial/Rate Setting Policies

The Utility Financial Plan will take into consideration the following financial policies. The financial planning period will be for a minimum of five years to determine overall trends and impacts to reserves and rates over a long-term horizon. The Utility Financial Plan is an integral component of the City's approach to effectively managing the utilities at a sustainable level to support the service levels of the community.

1. Reserve Funds

Reserve funds shall be established for the City to properly account for the City's funds, but to also provide adequate reserve levels to address the different types of funding requirements of the City. The City's reserve policies shall be as follows:

1.1 Operating Reserve – The City's operating reserve is an unrestricted reserve. The minimum operating reserve shall be established at 90 Days of annual O&M expenses (approximately 25% of annual O&M for both the Water and Sewer Funds) as outlined in Exhibits 4 and 6 in the Utility Financial Planning models for water and sewer.

1.2 Capital Reserve – The City currently has two different capital reserves for the water and sewer utilities. The first is the Homer Accelerated Water and Sewer Program (HAWSP). HAWSP is funded through a portion of the voter approved sales tax and assessments levied on benefited properties. The second is the Capital Asset Repair and Maintenance Allowance (CARMA). CARMA is funded annually through a rate surcharge equal to 15% of water and sewer costs and collected through the water and sewer rates. In general, HAWSP is intended to provide seed money to support expanded access to the City water and sewer system while CARMA is intended to support improvements, repairs, and replacements of the City's existing infrastructure, and may also be used for Capital Contingencies or Infrastructure Replacement. CARMA and HAWSP funds may be used jointly to fund a project where applicable. The development of the projection of CARMA and HAWSP funds is provided in Exhibits 8 and 9 respectively of the Utility Financial Plan.

1.2.1 Homer Accelerated Water and Sewer Program (HAWSP) – Voters in the City of Homer established the HAWSP fund to improve the Health and Welfare of the community by funding capital improvements to the City's water and sewer system. The HAWSP is funded by a voter approved dedicated sales tax, and assessments levied on benefited properties. (See HCC 9.16.010(b).) Specifically, the HAWSP Fund is built from a levy of ¾ of a percent on the retail sales tax. This tax was established by voters and can only be modified through another ballot measure. The key objectives of the HAWSP fund are as follows:

- Provide for water/sewer improvements without placing a heavy financial burden on individual property owners. (Resolution 99-53.)
- Increase the number of users to the system(s), thereby increasing revenues to

the Water and Sewer Enterprise Funds. (Resolution 99-53.)

- Promote construction of additional improvements to the City water and sewer systems. (See Ordinance 99-14(S)(A).)
- Protect public health. (2016 HAWSP Policy Manual.)

The HAWSP is generally intended to provide "Seed Money" for major projects (projects that exceed $1.1 million). The target HAWSP fund value is to be maintained at a level to provide sufficient funding for current long-term debt obligations and annual funding needs as outlined in the Utility Financial Plan. The HAWSP fund may additionally be used to pay off HAWSP-project debt, subject to City Council approval, and may furthermore be used in conjunction with CARMA for project funding, especially where an element of the project involves extension of service, expansion of capacity, or promotion of public health.

1.2.2 Capital Asset Repair and Maintenance Allowance (CARMA) – The CARMA reserve was established to fund improvements, repairs, and replacements to the City's existing water and sewer systems. The level of CARMA funding can be adjusted by the City Council. "The amount of the CARMA funds shall be established by City Council in the biennial budget based on the projected maintenance and repair needs of the City." (Ordinance 19-35(S)(A)). CARMA shall be funded as an element of the rates at a sufficient level to fund capital improvements as identified in the Utility Financial Plan.

The intent of the City of Homer Water and Sewer CARMA Fund is "for appropriation and expenditure for equipment replacement, fleet replacement, engineering or planning services, major maintenance of city facilities, or any other purpose as identified and recommended by the City Manager and authorized by the City Council…and to extend the life and use of taxpayer funded assets, facilities and infrastructure." (See Ordinance 19-35(S)(A)). The Water and Sewer Utilities - which operate independently - use CARMA Funds for improvements, repairs, and replacements to the City's existing water and sewer systems. CARMA Funds may additionally be used for capital contingencies or infrastructure replacement and can be used in conjunction with HAWSP to jointly fund a project.

1.3 Bond Reserve – A bond reserve fund is a restricted reserve. A bond reserve fund shall be established, as required and in accordance with anticipated bond covenants for specified projects where the City Council intends to pursue bond funding. The minimum fund balance of the bond reserve shall be equal to bond reserve requirements set by applicable bond covenants.

2. Debt Issuance and Debt Management

The City, during the course of normal operations, may issue long-term debt to fund certain capital projects. The establishment of policies related to debt issuance and debt management are intended to minimize the overall long-term costs of the City and utilize long-term debt to the benefit of the City's customers. Provided below are the debt issuance and debt management policies.

2.1 Funding of Annual Renewal and Replacement Capital Projects – The City will not need to issue long-term debt to fund annual renewal and replacement capital projects, as it will use rate funding, through CARMA, to properly and adequately fund the City's

annual renewal and replacement capital projects. Accordingly, the minimum annual funding from rates shall be at least equal to or greater than the City's annual renewal and replacement needs as determined in the Utility Financial Plan.

2.2 Long-Term Debt as a Funding Mechanism for Capital Projects – The City can consider the use of long-term debt to fund significant non-reoccurring capital projects. The policy objective when issuing long-term debt is to minimize the financial and rate impacts of significant non-reoccurring capital projects. When structuring such long-term debt, the City shall consider the following factors as:

- Current interest rates (costs)
- Current amount of the utility's outstanding debt levels
- Consistency with the City's debt policy and overall debt level

The City shall avoid an over-reliance upon debt by considering the debt service coverage ratios of rating agencies to measure whether the City's debt to capitalization or debt to operating revenue ratios are appropriate. Specifically, the City should maintain a debt/equity ratio which is less than 50% for utility financial planning. In certain circumstances the City may need to exceed this target to fund critical infrastructure projects. In these cases, the City Council will provide guidance on the appropriate target debt/equity ratio. For each debt issuance, the City will identify the funding source for annual principal and interest payments, prior to the approval issuing the debt.

2.3 Types of Long-Term Debt – To minimize the overall costs of debt, the City shall strive, at all times, to utilize the lowest and best available cost option for issuing debt.

2.4 Bond Covenants – The City, at all times, shall adhere to and meet any bond covenants put forth by bonds issued by the City. Bond covenants are legal obligations placed upon the City. If the City is not in compliance with bond covenants, the City's management team shall inform the City Council and appropriate action will be taken.

2.5 Debt Service Coverage Ratio – At all times, the City shall meet the minimum debt service coverage (DSC) requirements associated with bond covenants. For financial planning and rate setting purposes, the City shall target a minimum DSC of 1.25 times annual debt service on all outstanding debt.

2.6 Debt Funding Through Assessment Revenues – For certain capital improvements the City may use Assessment District's to fund improvements to provide service to these areas. In these circumstances the City will establish specific criteria for each assessment to ensure the adequate repayment of the assessment to reimburse the funding of the infrastructure providing service. When structuring debt the funding sources will be identified prior to approving the Assessment District.

3. Balanced Operating Budget

3.1 Self-Supporting – The water and sewer utility shall be self-supporting, where current revenue fully funds current operating and capital expenditures on an annual basis.

3.2 Adequate Funding to Preserve System Assets – The City's assets shall be properly operated and maintained to provide for a long life. Annual operating expenditures will be budgeted and funded at a level that promotes the efficient operation of and preservation of assets through the asset's useful life.

3.3 Evaluation and Monitoring of Cost – Costs will be monitored monthly to ensure the utility is operated in a cost effective and economically prudent manner and reported to the City Council on a quarterly basis.

3.4 Positive Annual Net Income – The City shall plan for annual net income (total revenue less O&M, taxes or transfers, debt service, and capital projects funded from rates) greater than or equal to zero (positive balance of funds).

3.5 Strive for Rate Stability – The City's rates should be stable over time while generating sufficient revenue. As a part of the annual budgeting process, the City shall review the rates to confirm the adequacy of the current rates.

3.6 Disposition of "One-Time" Revenue – In instances of large one-time revenues (e.g., legal settlement), if not specifically earmarked, the funds will be transferred to an appropriate reserve(s) (operating, capital, or rate stabilization).

3.7 Alternative Funding/Revenue Diversification – To minimize overall rates, the City should explore alternative revenue sources such as grants and direct developer contributions.

4. Establishing Rates and Fees

The City shall establish rates utilizing industry recognized "generally accepted" rate setting methodologies. This will provide the City with consistency in their ratemaking process, while also establishing rates which are legally defendable. The City's policies on establishing the water and sewer rates and fees, and the general methodologies to be utilized, are as follows:

4.1 Revenue Requirement Analysis

The revenue requirement analysis provides a projection of the City's revenues and expenditures for a defined time period. The revenue requirement analysis shall provide the City Council with the information and cost-basis to determine the size and timing of any proposed rate adjustments. The City's revenue requirement analysis methodology shall consider the following:

4.1.1 The revenue requirement (financial plan) analysis will be developed for a minimum projected five-year time period.

4.1.2 Revenue requirements will be established using the "cash basis" methodology. The "cash basis" methodology includes O&M expenses, taxes/transfer payments, debt service (P+I) and capital improvements (renewal and replacement) funded from rates. The revenue requirements may include a component for change in working capital/rate stabilization funds to manage reserve balances and mitigate rate impacts.

4.1.3 Costs shared across utilities shall be allocated to each utility based an equitable allocation method. These may include, but not be limited to, labor ratios, number of customers, revenues, usage etc. The allocation method should be whichever method most equitably allocates the specific cost.

4.1.4 Any wholesale increases imposed upon the City by a water supplier or wastewater treatment agency will be reviewed for financial/rate impacts.

4.1.5 The City's revenue requirement analysis shall fully incorporate the City's reserve, debt and budgeting policies.

4.2 Cost of Service Analysis

A cost of service analysis provides an equitable method to allocate the City's water and sewer revenue requirements to the customers utilizing the service. The City's cost of service analysis for the water utility shall use generally accepted cost of service methodologies as defined by the American Water Works Association (AWWA) and the analysis developed for the City's sewer utility shall use cost of service methodologies as defined by the Water Environment Federation (WEF). The City's water and sewer cost of service shall be developed to provide an equitable allocation of costs by taking into consideration a customer group's (e.g. residential, commercial) facility requirements and usage characteristics. The City's specific cost of service policies are as follows:

4.2.1 The cost of service shall be developed for a projected one-year time period or the period over which rates will be set, utilizing the revenue requirements as developed in 4.1.

4.2.2 The cost of service analysis shall be designed and developed to consider the unique and specific circumstances of the City's water and sewer system.

4.2.3 The City shall allocate costs to customer class of service based upon facility requirements and usage characteristics.

4.2.4 When necessary, the City may phase-in the cost of service results to transition to fully-cost based rates.

4.3 Rate Design Analysis

The development of cost-based rate designs concludes the City's rate setting process. The development of rate designs utilizes the results from the revenue requirement and cost of service analysis to establish the target level of revenues for each customer class of service (rate schedule). The City's rate design analysis is primarily focused on the structure of the rates. The City's rate design analysis policies are as follows:

4.3.1 The City shall utilize the results of the revenue requirement analysis and cost of service analysis in the development of final proposed rate designs.

4.3.2 Rates shall be designed to collect the overall target level of revenues for each customer class of service.

4.3.3 The City's rate designs shall be reflective of the City Council's rate design goals and objectives, while also being reflective of the greater public purpose (e.g., economic development, conservation, etc.).

4.3.4 The City shall take into consideration both fixed and variable costs in the development of final proposed rates. The average unit costs calculated within the cost of service analysis provides the cost-information related to fixed and variable costs.

4.3.4 Bill comparisons shall be developed for all proposed rate designs to illustrate the general impacts to customers across a range of consumption.

4.3.5 In establishing the final water and sewer rates, the City's Council may take into consideration neighboring utility rates, but not to the financial detriment of the City.

4.4 Other Rate Setting Considerations

Provided below are other policies related to the City's rate setting process.

4.4.1 At a minimum, the City shall conduct a comprehensive rate study every five (5) years to update assumptions and determine financial sustainability.