

March 21, 2016

To the Honorable, the City Council:

RECOMMENDATIONS

The City administration and City Council continue to recognize the importance of minimizing increases in water and sewer rates. I recommend that the City Council approve a 0% increase in the water consumption block rate and a 3.2% increase in the sewer use block rate, resulting in a 2.4% increase in the combined rate for the period beginning April 1, 2016 and ending March 31, 2017. This is the sixth consecutive year that the City has been able to produce a 0% increase in the water rate.

In last year's recommendation, the projected FY17 rate increases for water, sewer, and combined were 3.1%, 7.7%, and 6.4%, respectively, based on March 2015 consumption rates and projected budgets. We have been able to produce rates lower than estimated due primarily to lower operating budget projections in the Water Budget, and lower projected Massachusetts Water Resources Authority (MWRA) assessments in the Sewer Budget. The MWRA provides annual updates to their projected assessments.

In March of each year, the City Council establishes water and sewer rates, which determine water and sewer revenues for the next fiscal year. Because of the timing requirements, water and sewer rates are set prior to the adoption of both the Cambridge budget and MWRA budget; therefore, revenue needs are based upon estimated expenditures. Historically, water and sewer rates have been established so that revenues generated by them, when combined with other related revenue sources, cover projected annual costs.

WATER

Two major factors determine the rate necessary to generate sufficient revenues: water consumption and the budget. The total FY17 Water Budget reflects a \$108,815 increase from FY16. Water is able to offset costs related to cost-of-living allowances, pensions, and health benefits in the salaries and wages portion of the operating budget with a decrease in debt service payments.

The planned FY17 capital allocation is \$5,000,000 using pay-as-you-go capital funding based on current revenues (\$3,500,000) and fund balance (\$1,500,000). The major project in the FY17 budget is the second phase of the installation of variable frequency drives (VFDs) to the raw water pump system. An additional \$1,000,000 million has been included for the replacement of existing VFDs on the finished water pumps. Installation of the VFDs will substantially improve energy efficiency at the water treatment plant. The total project cost is \$5,000,000 over two years, of which \$3,000,000 was funded from fund balance. The remainder of the FY17 capital allocation will be used for improvements to the distribution and transmission system, treatment plant equipment replacement, consulting services, and improvements to the watershed. Table 4 on page 5 indicates the details of water fund projected revenues and expenditures for FY16-21. Table 7 on page 8 shows actual water fund balances for FY11-15 and the projected balance for FY16.

To support a 0% water rate increase for the sixth year, \$350,000 from fund balance will be used in FY17, bringing the total fund balance used to \$1,850,000. We expect to eliminate the use of the fund balance in FY18, as decreases in debt service continue and as long as water consumption remains constant.

Water and sewer charges are directly linked to water consumption, with sewer costs comprising approximately 71.2% of total water and sewer expenditures. When consumption declines, revenues are negatively impacted. In the current fiscal year, water is being consumed at a rate similar to the previous fiscal year. If this trend continues, this would be the second year in which consumption has not decreased.

SEWER

The FY17 sewer budget reflects a 6.0% increase from FY16. This includes the MWRA assessment, debt service payments, and the sewer component of the Public Works budget. Debt service on sewer bonds and the MWRA assessment account for 90.2% of the total Sewer Budget.

FY17 estimated sewer revenues will cover the FY17 estimated MWRA assessment, which is scheduled to increase by \$639,184 from the FY16 final assessment. The MWRA rate increase projected for the City is subject to change based on the MWRA budget, which is adopted later in spring 2016. These changes have typically been minor in past years. Unlike the water budget, sewer revenues are credited to the general fund and not to a separate proprietary fund that can be drawn upon if the need arises.

Included in the sewer budget are debt service increases attributable to the \$12,740,000 general obligation bonds issued in February 2016 and the February 2016 SRF loan for Concord Avenue for \$14,000,000.

The following sewer projects were included in the February 2016 bond issue: Cherry Street / South Massachusetts Avenue; Alewife Watershed; and Harvard Square projects.

The FY17 capital allotment of \$1,000,000 in sewer revenues will continue to finance the remedial reconstruction program and development.

The City Council has authorized significant investments in the water and sewer systems to ensure Cambridge continues to benefit from a healthy and environmentally sound water and sewer system. In addition to the projects currently under way, the City's five-year capital plan (FY17-21) calls for an additional investment of approximately \$135,663,000 (primarily sewer, \$114,663,000) in the water and sewer systems. The City carefully monitors the issuance of debt to fund authorized sewer projects and makes adjustments to ensure that debt service cost increases, which impact the sewer rate, are moderate.

Subsidies from the SRF loan program will cover only \$44,240 or 0.2% of the total debt service of \$19,942,737 for all FY17 sewer projects. The City will continue to receive state subsidies on existing debt. The FY18-21 capital plan includes other projects that may be eligible for subsidized loans from the state. As in past years, it is not certain that these projects will receive state subsidies and the debt service on these projects has been calculated based on funding through general obligation bonds. If state subsidies become available to the City, they will be used to lower the sewer rate in future years. Table 5 on page 6 shows the detail of sewer-related expenditures and revenues for FY16-21.

COMBINED WATER & SEWER

The table below reflects the projected combined water and sewer metered revenue requirements needed to cover water and sewer expenditures.

TABLE 1

	FY16 Projected	FY17 Budget	% Change
Water	\$17,135,000	\$17,137,015	0.0%
Sewer	\$46,350,000	\$47,844,595	3.2%
Combined Water / Sewer Revenue	\$63,485,000	\$64,981,610	2.4%

FY17 projected revenues are based on FY16 projected collections and reflect our practice of conservative revenue projections.

The table below reflects the FY16 actual and FY17 proposed water and sewer rates.

TABLE 2

	Annual Consumption*	FY16 Water Rate	FY17 Proposed Water Rate	FY16 Sewer Rate	FY17 Proposed Sewer Rate
Block 1	0 – 40 CcF	\$3.02	\$3.02	\$9.21	\$9.50
Block 2	41 – 400 CcF	\$3.24	\$3.24	\$9.74	\$10.05
Block 3	401 – 2,000 CcF	\$3.44	\$3.44	\$10.46	\$10.79
Block 4	2,001 – 10,000 CcF	\$3.65	\$3.65	\$11.26	\$11.62
Block 5	Over 10,000 CcF	\$3.96	\$3.96	\$11.97	\$12.35

*All rates are per CcF. CcF is an abbreviation of 100 cubic feet. One CcF is approximately 750 gallons.

The table below reflects the average change to combined water and sewer residential bills.

TABLE 3

Residential Type	FY16 Average	FY17 Projected	Annual Variance	% Change
Single Family	\$766	\$784	\$18	2.4%
Two Family	\$1,070	\$1,096	\$26	2.4%
Three Family	\$1,553	\$1,590	\$37	2.4%

SENIOR DISCOUNT PROGRAM

There are currently 2,620 homeowners who qualify for the age 65+ water/sewer 15% discount (not to exceed \$90 annually), which is not tied to the homeowner's income.

There are also 80 elderly homeowners who qualify for an income-based discount of 30% (not to exceed \$180 annually). To qualify for the 30% discount, a homeowner must be 65 or older and must have been granted the Clause 41C elderly real estate exemption. For FY16, the income guidelines are as follows: single, income of \$25,197 with assets of \$50,392 or less; married, income of \$37,796 with assets of \$69,289 or less.

FUTURE OUTLOOK FOR RATES

Overall, the City has been extremely successful over the past five years in producing minimal water and sewer rate increases. The average annual increases for the FY12-16 period were as follows: water, 0.0%; sewer, 3.2%; and combined, 2.3%, which include both the water and sewer rates showing 0% increases in FY12 and FY13. The FY14, FY15 and FY16 water rate increase was also 0%.

Tables 4, 5, 6 and 7 contain five-year forecasts for water, sewer, and combined revenue estimates as well as water fund balances for the past five years and the projected FY16 fund balance. Although the City currently does not project the use of fund balance in the out years, it will continue to review appropriate use of fund balance for a specific project, or to lower the rate. As can be seen in Table 6, the annual combined water / sewer rate is projected to increase by an average of approximately 5.2% for FY17-21. The projected increase is the result of the City's commitment to bonding sewer infrastructure improvement projects and increases in the MWRA assessment (based on estimates received from the MWRA). MWRA increases are projected to be 1.4% - 7.1% in FY17-FY21. If increases in the MWRA assessment are more moderate, the rate increases that are shown will be lowered. If consumption increases and therefore revenues increase, rate increases will be affected positively. Conversely, if consumption decreases, there will be a negative effect on water and sewer revenues.

Our water and sewer program is structured to produce reasonable rate increases in the future. The goal of the City Administration and City Council is to minimize the effects of water and sewer rate increases on residents as much as possible, while continuing to invest in our infrastructure.

Very truly yours,

Richard C. Rossi
City Manager

Attachments