

TOWN OF PEGRAM
SEWER FUND
RATES AND CHARGES

SUMMARY

MTAS was requested to review the financial operation of the sewer fund and recommend any changes as to rates or the rate structure.

A review of the financial history of the sewer fund shows the town was operating with losses until the new rate structure was implemented in 2002. The rate change involved charging a \$34.15 per month “ready to serve” charge to all residential dwellings that have sewer service available to them but choose not to connect. The implementation of that additional charge resulted in sufficient revenues so that the sewer fund began operating with a positive net income in F/Y 2003.

This summary attempts to address two questions about the Pegram sewer fund.

1. Is the current rate structure sufficient for income and cash flow purposes?

The answer is yes and no. Projections for fiscal years 2006 through 2011 indicate that the current rate structure will generate positive net incomes and a positive cash flow. This is based on a modest 1% annual growth in revenues (from new customers), a 2% annual growth in operating and maintenance expenses, no additional new debt requirements, and essentially no additional capital improvements. Also projected is a substantial *decrease* in expense for Professional Services, which consists of legal and engineering fees. The income for each year is modest and does meet the tenets of the state law and the requirements of the Wastewater Financing Board. However, there is little room for any unforeseen increase in expenses or decline in revenues. Also, current funds don't appear sufficient to fund any additional capital improvements as either the sewer system ages or new expansion is considered. Certainly Pegram could not incur additional long term debt in the sewer fund without increasing revenues. While it may not be necessary to increase revenues now, an annual review of the sewer fund is essential. One suggestion MTAS would offer is to consider an annual cost of living increase to the rates in order to keep pace with inflation.

Obviously, substantial new growth in customers, either in number or usage amount, would change the picture dramatically.

2. Is the current sewer rate structure fair and equitable to all customers?

This is the more complex of the two questions, especially in light of the large number of customers paying the ready to serve charge. Per the audit for F/Y 2002 Pegram had 127 sewer customers who contributed \$43,139 in usage fees. This corresponds to an average monthly sewer bill of \$28.31:

$$\$43,139 / 127 = \$339.68 \text{ annually} / 12 = \$28.31$$

Beginning in F/Y 2003 the additional revenues accounted for as usage fees are being derived from the ready to serve charge. If the charge is based on average usage it would appear that the \$34.15 rate is substantially more than the average connected customer's bill.

The ready to serve charge raises other issues also. The TCA sections cited in the town ordinance do not specifically address charging this type of fee or rate. Cities are required "*to establish and maintain just and equitable rates and charges for the use of and the services rendered by the waterworks or sewerage system, to be paid by the beneficiary of the service.*" Cities have been granted additional leeway to charge for a service when it is available to the customer whether they utilize it or not. Does this charge include usage or volume charges? In theory water and sewer rates should be comprised of 2 parts, a minimum charge which is to cover fixed costs and a usage (volume) charge for variable costs. Fixed costs would include personnel (perhaps less overtime), insurance, depreciation, and debt service. It may also include some repairs and maintenance of the system. Variable costs are those that rise and fall with the level of sewer collected and treated. Obviously, the higher the volumes (and strength) the greater the electricity (pumping) costs, chemicals, and even personnel. What should a "ready to serve" charge entail? Logic would say that it would include the cost of making the facilities available, the fixed costs. There seems to be less argument for charging the variable costs as no waste is being treated. These are perhaps legal questions, but do speak to the matter of just and equitable rates. Whatever the methodology all rates and charges should have a firm basis in actual cost and expenses.

As to the rate structure itself, it is an increasing block rate which is appropriate as sewer cost of treatment generally rises with volume treated.