

## **CITY COUNCIL STUDY SESSION ITEM**

### **SUBJECT**

Water rate structure and water utility service rates

### **STAFF CONTACT**

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### **POLICY ISSUES**

In accordance with Council-adopted financial policies, a realignment of water rates was implemented in 2015 to ensure rate equity between customer classes and to enhance revenue stability.

In accordance with Council-adopted financial policies, water service rates are adopted at levels sufficient to maintain, operate, and invest in utility infrastructure to ensure reliable service delivery to water customers.

### **DIRECTION NEEDED FROM COUNCIL**

☐ Action

☒ Discussion

☒ Information

Staff will provide an informational briefing on the following:

- Water rate structure implemented in 2015
- Bellevue's current water utility service rates

### **BACKGROUND/ANALYSIS**

#### **WATER RATE STRUCTURE**

In accordance with City financial policies, a comprehensive water cost-of-service evaluation was conducted in 2014 to assure continued rate equity between customer classes. The objectives of the evaluation were to:

- Determine whether any adjustment to the water rate structure in place then was needed to ensure each customer class paid their equitable share of water system costs.
- Enhance revenue stability. The water utility was experiencing revenue volatility due to fluctuations in water consumption resulting from a combination of long-term water conservation, and fluctuations in weather and economic conditions.

The evaluation found the following regarding the previous water rate structure:

- The single-family customer class paid more than their share of water system costs, while the commercial and multifamily customer classes paid less than their equitable share based on the cost to provide water service to each customer class.
- To ensure equity, the evaluation recommended a shift of \$510,000 or 1.2% of total water service revenue from single-family to commercial and multifamily customers to reflect the full cost of providing water service to each customer class. The shift of revenue between customer classes is revenue neutral to the water utility.
- The water rate structure was out of alignment with current usage demographics and the pricing signals built into the old rate structure were no longer effective in promoting conservation as intended.

The evaluation findings were used to develop a new water rate design in 2014 that aligned with current customer consumption behavior, ensured ratepayer equity, and enhanced revenue stability. The Utilities Department conducted several outreach efforts, including presentations to the Building Owners Management Association, Bellevue Chamber of Commerce, and Bellevue Downtown Association, as part of the process to review and discuss the new cost-of-service rate changes.

The results of the cost-of-service evaluation and new rate design were reviewed in detail by the Environmental Services Commission over several meetings between May and November 2014. The Commission provided feedback which was incorporated into the final rate design Council adopted in December 2014 and implemented in January 1, 2015.

## **WATER SERVICE RATES**

The water utility operates as a business enterprise within the City structure and it faces a number of unique challenges, including services that are highly capital intensive and a significant portion of the water utility's expenditures represent nondiscretionary financial obligations that are contractually or legally required.

### **Water Supply Costs**

The cost of purchased water is the single largest cost center for the water utility, representing about 40% of annual expenditures. The City is a member of the Cascade Water Alliance, which serves to provide water supply to Bellevue and other neighboring jurisdictions. Payments to Cascade Water Alliance for water supply have increased 62% over the last 10 years. Consistent with Council-adopted financial policies, wholesale cost increases are passed through to customers so that local programs are not degraded.

### **Capital Intensive Water System**

Bellevue's water system comprises of over 600 miles of pressurized pipe, 25 reservoirs, 22 pump stations and 63 pressure zones. Most of the system is past its midlife. This requires greater investments to maintain, repair and replace system infrastructure now and into the future. The largest asset in the water system is water mains which are experiencing more frequent breaks. About 40% of Bellevue's mains are made of asbestos cement, which are wearing out faster than expected and the utility has accelerated replacement with a goal of replacing water pipe at a sustainable level of 5 miles annually by 2018.

Almost 20% of the water utility's expenditures represent investments to replace water system infrastructure now and in the future. The rate revenues required to support the water capital program has grown 68% over the last 10 years due to increasing system infrastructure renewal and replacement needs. 5 FTEs have been added in the last 10 years to support the Water CIP. As the system continues to age, long-term funding of infrastructure renewal needs will continue to increase.

### **Taxes and Payments to General Fund**

As an enterprise activity, the water utility pays taxes and franchise fees to the State, City and other local jurisdictions within its service areas. Additionally, the water utility pays the general fund for support services such as fleet management, information technology, human resources, and legal services. Tax obligations and payments to the general fund for support services represent about 20% of the utility's expenses. Taxes and payments for support services have grown 84% over the last 10 years. These payments are non-discretionary.

### **Local Operations**

About 20% of the utility's expenditures pays for local operations, where the utility has more direct control. The utility has made significant efforts to contain local program costs and leverage efficiencies to meet business needs. In the last 10 years, the water utility has only added 3 FTEs to meet its operational needs despite increasing maintenance needs of the aging water system, significant population growth and development, and increased regulatory requirements. Local operational costs have grown 53% over the last 10 years.

### **Rates as Primary Source of Revenue**

As a business enterprise, the water utility does not receive general fund revenues and relies primarily on rates to fund its operations and capital program. This includes investments to address aging infrastructure, provide utility services to accommodate growth and development, and meet complex regulatory requirement and mandates.

As any business, the utility needs sufficient revenues to meet business needs. Population and economic growth results in very little increase in water service revenues due to long-term conservation, stricter plumbing codes and more water efficient fixtures and appliances. Over the last ten years, water service revenues would have grown by 8% without rate increases, despite significant population growth and development. In contrast, water utility costs have grown by 65% during the same timeframe. Therefore, rate increases have been and will be needed in the future to provide sufficient revenues to meet the utility's operational and capital needs to ensure continued, reliable service delivery to customers.

### **Bellevue's Water Rates**

Bellevue's water rates are at levels appropriate to ensure continued delivery of reliable, safe, high-quality water to customers. Bellevue's water rates are on the higher end compared to neighboring water agencies and lower compared to Seattle, which provides Bellevue's water supply through the Cascade Water Alliance. One reason for this is due to the significant investments Bellevue has made to replace aging system infrastructure as discussed above. Also, unlike some neighboring water agencies, Bellevue does not have any independent water supply and must purchase all its water supply. Although Bellevue's water rates are higher compared to neighboring jurisdictions, Bellevue's combined rate for water, sewer, and storm and surface water services are very competitive compared to neighboring communities. See Attachments A and B for additional information.

In 2016, the typical single-family residential monthly water bill is \$58.42. Following is a breakdown of costs the bill pays for:

Cascade Water Alliance – Water Supply	\$ 22.36
Capital Investments	11.81
Taxes/Interfunds	12.02
Operations	12.23
<b>Total</b>	<b>\$ 58.42</b>

**ALTERNATIVES**

N/A

**RECOMMENDATION**

N/A

**ATTACHMENT(S)**

Attachment A – Water Utility - 2016 Monthly Bill Comparison

Attachment B – Water, Sewer and Storm and Surface Water Utilities - 2016 Combined Monthly Bill Comparison

**AVAILABLE IN COUNCIL DOCUMENT LIBRARY**

N/A