

**DISTRICT OF COLUMBIA**

**WATER AND SEWER AUTHORITY**

# Board of Directors

DC Retail Water and Sewer Rates Committee

## Tuesday, March 25, 2014

9:30 a.m.

MEETING MINUTES

**Committee Members in Attendance**

**DC Water Staff**  DC WATER STAFF PRESENTM

Alan Roth, Chairperson

Terry Bellamy

Ellen Boardman

Rachna Butani

Howard Gibbs

Robert Mallett

George Hawkins, General Manager

Mark Kim, Chief Financial Officer

Randy Hayman, General Counsel

Linda R. Manley, Board Secretary

**Call to Order**

Chairman Roth called the Committee meeting to order at 9:32 a.m.

**Integrated Planning Framework Affordability Presentation**

Mr. Kim outlined the meeting agenda and mentioned that an article from USA Today was passed out to committee members about DC Water and other utilities spending billions to keep sewage out of rivers. Mr. Kim introduced Mr. Alan Karnovitz (Director and Senior Economist) and Mr. Anwar Hassan (Senior Vice President) of Louis Berger Water Services, Inc. who had undertaken an Affordability Analysis of DC Water’s Capital Improvement Program. Mr. Kim stated that DC Water is projected to spend $1.5 billion over the next ten year period on the Long Term Control Plan, which is putting enormous financial pressure on DC Water and its retail rate payers.

Mr. Karnovitz explained that Louis Berger conducted the Affordability Analysis in partnership with Raftelis Financial Consultants, Inc. Mr. Karnovitz briefly described the Integrated Planning Framework (IPF). IPF is a decision making process that came from the Environmental Protection Agency (EPA). EPA recognized that compliance with consent decrees and regulations was putting severe financial burden on low income populations, communities and utilities. The IPF allows utilities and communities to take a look at consent decrees and regulatory requirements and to prioritize their projects in a way that defers large financial impacts while bringing forth as many benefits as possible. Ultimately it allows utilities greater flexibility in how they invest in their capital improvement programs while deferring costs to later years such that impact on the rate payers is minimized in the early years.

Mr. Karnovitz stated that Louis Berger Inc. in partnership with the City of Baltimore developed an IPF model that would modify their consent decree in a way that would ameliorate the impacts on low income communities while still achieving their regulatory requirements. IPF would allow a longer timeframe for their investments through extension on their consent decree, which would lower the burden on both the city and the rate payers.

DC Water performed an Affordability Analysis to assess annual sewer rate increases and financial impacts to low income households. Based on the analysis, Mr. Karnovitz concluded that the status quo CIP would result in sewer rate increases to the entire customer base over the next twenty years. From 2011-2013, sewer bills increased 35 percent and the average residential bill is projected to increase from $607 in 2015 to $952 in 2010, and to $1,623 by 2030. Financial impact to the poor and minority households would be significant over time. EPA guidance states that sewer bills exceeding 2 percent of median household income (MHI) would signal a large economic impact on residents.

Mr. Karnovitz explained that the traditional measures of affordability do not capture accurately the financial burden on poor and minority households. The household income distributions are particularly skewed in Washington DC:

* Mean income is approximately $96,100
* Median income is approximately $62,000
* Top 5 percent of DC households have a mean income of $500,031
* Lowest 20 percent of DC households have a mean income of $9,631

Mr. Karnovitz stated that mean and medium income in Washington DC are about 25 percent higher than the national average. The poverty rate in Washington DC is 18.2 percent compared to the national average of 15 percent.

He mentioned that the unadjusted income underestimates burdens due to a high level of expenditures for non-discretionary spending in high cost cities such as Washington DC. In 2012, DC was ranked the 8th most expensive city in the US with cost of living index of 144.7, which is 45 percent higher than other cities. The primary drivers of Washington DC’s high cost of living include housing, transportation, food and utilities. He noted that for these reasons and income disparities in Washington DC, the “2% of MHI” guidance used by EPA does not reflect true financial impact on lower income households.

Mr. Karnovitz discussed various scenarios of the Affordability Analysis:

* **Scenario 1: Status Quo CIP**
* Scenario 1a: Median household income (MHI)
* Scenario 1b: Unadjusted upper limit of the second quintile household income (top of bottom 40 percent)
* Scenario 1c: Adjusted upper limit of the second quintile household income (with cost of living adjustment)
* **Scenario 2: Modified CIP (via IPF)**
  + Scenario 2a: Upper limit of the first quintile household income
  + Scenario 2b: Upper limit of the second quintile household income
* **Scenario 3: Modified CIP and COLA**
  + Scenario 3a: Median household income
  + Scenario 3b: Adjusted upper limit of the first quintile of household income
  + Scenario 3c: Adjusted upper limit of the second quintile of the household income

Mr. Karnovitz provided Demographic Analyses (based on race/ethnicity and age) and Geographical Analysis (based on Wards) for the three scenarios, describing the impact on low-income households.

Mr. Karnovtz concluded that the traditional method of measuring affordability using citywide MHI does not fully capture the true impact on low income households. An alternative method using 2 percent of the cost of living adjusted income for the upper limit of the 2nd quintile more accurately predicts the “true effect” of residential sewer bills on low income populations. A modified CIP that defers certain capital costs related to DC Water’s Clean Rivers Project (and implements Green Infrastructure solutions) will delay and ameliorate affordability issues, but will not eliminate them entirely.

**FY 2015 Cost of Service Study Presentation**

Mr. Kim gave a brief overview on the FY 2015 Cost of Service Study. He stated that the study is done every three years to review the existing rates and charges for sufficient and equitable cost recovery, and to ensure that rates and fees are based on cost of providing services for each customer class.

Mr. Jon Davis of Raftelis described the Fixed and Variable Charges for utilities:

* Typically, water and sewer utilities’ costs are largely fixed while revenue is largely variable
* DC Water’s fixed revenue components have historically been below 30 percent of total revenue
* National and regional benchmarking shows that there is no consensus on the level of a customer bill that should be fixed
* By 2015, DC Water’s average customer bill will be 27 percent fixed, within the median range for large national utilities

To a question from Chairman Roth as to what percentages of DC Water’s charges are fixed, Mr. Davis responded that although 75 percent of the cost is fixed, DC Water will bill 27 percent fixed charges in 2015.

Mr. Davis explained the rate structure evolution. He pointed out that DC Water has a uniform rate structure as compared to other utilities on the west coast, which have a seasonal structure. The revenue uncertainty is low for flat or uniform rate structures, whereas for seasonal and inclining block rate structures, the revenue uncertainty is higher.

Mr. Davis presented the rate structure benchmarking chart showing the comparison of DC Water rates with other utilities. He mentioned that DC Water has a uniform rate as do New York City and Chicago, whereas Philadelphia and Baltimore have a declining block rate structure. Other cities/utilities such as Boston, Washington Suburban Sanitary Commission (WSSC), Charlotte-Mecklenburg and Fairfax County have inclining block rates to promote conservation among certain classes of customers. Some cities like Philadelphia, Baltimore and Boston have multi-block rates. To a question from Mr. Mallett as to how Mr. Davis chose these utilities in the rate structure benchmarking, and what are the commonalities, Mr. Davis responded that he tried to select a good cross section, for example, some peers of DC Water from a demographic perspective, an Urban system, Mid-Atlantic system, Northeastern system, and some peers in the metropolitan area. He also pointed out that customer impacts vary significantly based on:

* Number of blocks
* Differential between blocks
* Break points between blocks
* Application to customer classes

He further explained that the inclining block rate structure shifts costs away from low volume customers toward high volume customers and increases revenue volatility by assigning higher value to discretionary consumption.

Mr. Davis noted that the rate structure is designed to be revenue neutral.

In conclusion, Mr. Davis presented the objectives for the 2015 Cost of Service Study:

* Detailed analysis of customer usage
* Revenue sufficiency assurance
* Adherence to cost of service principals and DC Water policies
* Evaluation of alternative rare structures
* Evaluation of affordability alternatives
* Identification of alternative charges to relieve pressure on rates

**Retail Water and Sewer Rates Committee Workplan**

Mr. Kim updated the committee on the workplan, which is on track. Mr. Kim mentioned that the next committee meeting is scheduled for June 24th. However, if there is a need for discussion before the Public Hearing meeting, a teleconference would be scheduled in May.

**Other Business**

No other business was discussed.

**Executive Session**

Mr. Kim stated that the committee did not need to go into executive session.

**Adjournment**

The meeting was adjourned at 11:29 a.m.

**Follow-Up Items – DC Retail Water and Sewer Rates Committee Meeting (March 25, 2014)**

1. Provide information on whether the cost of living in DC is different than in the surrounding counties and cities including Fairfax, Arlington and Alexandria. (Robert Mallett)**:**
2. What is the income level for the upper limit of the second quintile for the next ten years? **(Chairman Roth) Status:** Complete.

1. How many utilities are operating under the consent decree and how many have a Capital Improvement Program? (**Mr. Mallett**) **Status:** Complete.

**Response:** All of the utilities on the Rate Structure Benchmarking slide are under some sort of consent decree except for Charlotte. Most of these entities have multi-billion dollar CIPs over the next several years. Baltimore, Boston, WSSC, PWD, Chicago and New York have large CIPs related to consent decrees for Combined Sewer Overflow (CSO)/Sanitary Sewer Overflow (SSO). They also have aging infrastructure concerns as well.