



THE PRINCE GEORGE'S COUNTY GOVERNMENT

(301) 952-3700

County Council

October 3, 2017

TO: Todd M. Turner, Chair
Transportation, Housing and the Environment Committee (THE)

FROM: Sandra Eubanks, *SE* Committee Director (Acting)
Transportation, Housing and the Environment Committee (THE)

Canjor D. Reed, Senior Auditor *CDR*
Office of Audits and Investigations (A&I)

THRU: Robert Williams, Council Administrator *Bill*
Prince George's County Council

William Hunt, Deputy Council Administrator *WH*
Prince George's County Council

SUBJECT: Washington Suburban Sanitary Commission (WSSC)
FY 2019 Spending Control Limits and Rate Case Update

I. Spending Affordability Process

The Washington Suburban Sanitary "Commission" (WSSC), Prince George's County and Montgomery County government working group participated in the Spending Affordability Process. The Prince George's County government is represented in the working group process by the following County agencies: County Council, Office of Audits and Investigations, the Office of Management and Budget (OMB), and the Department of Public Works and Transportation (DPWT). The Spending Affordability Process focuses debate, analysis, and evaluation, on balancing affordability considerations against the provision of resources needed to serve existing WSSC customers (including infrastructure replacement and rehabilitation), meeting environmental mandates, maintaining affordable rates,

sustaining WSSC operating and capital budgets, and maintaining debt service at prudent levels.

The goal of both the Prince George's and Montgomery County Councils is to set certain budgetary limits by November 1st of each year. These limits provide direction to WSSC as to what to request as a proposed budget. It is preferable (not required) that both County Councils are able to reach a consensus on the following four (4) limits:

- New Water and Sewer Debt
- Total Water and Sewer Debt Service
- Total Water and Sewer Operating Expenses
- Water/Sewer Rate

The WSSC base case scenario would provide the following:

- i. Funding for Year 1 of the Fiscal Years 2019 – 2024 Capital Improvement Program (CIP) budget (See **Attachment #1** for complete list of proposed capital projects);
- ii. Compliance with the Sanitary Sewer Overflow (SSO) Consent Decree;
- iii. Payment for WSSC's share of operating and capital costs for the District of Columbia Water and Sewer Authority's Blue Plains Wastewater Treatment Plant;
- iv. Inspection and monitoring of large diameter water main transmission systems;
- v. Meeting of all federal and state water and wastewater quality standards and permit requirements;
- vi. Retention of maintenance service at a level consistent with WSSC's performance metrics;
- vii. Funding for employee salary enhancements; and
- viii. Operating and maintaining a system of three (3) reservoirs impounding fourteen (14) billion gallons of water, two (2) water infiltration plants, six (6) wastewater treatment plants, an approximately 5,600 miles of both water and sewer mains.

II. Spending Control Limits

A. Spending Control Limit Base Case

The FY 2019 Spending Affordability Work Group met on September 7th and September 21st of 2017. WSSC prepared a preliminary Base Case spending control limits scenario for review and comment by both Prince George's and Montgomery County staff that was originally set at a 6.2% rate increase. See **Attachment #2** –

Meeting September 7th for details). Upon further analysis, WSSC provided a revised base case at a 5.2% rate increase as shown below on **Table 1: Revised Base Case Scenario**. Based on feedback from both Counties, alternate scenarios at a 3.5%, and a 4.0% rate increase were developed and are summarized in **Attachment #3 and #4** of this report.

The WSSC budget is not driven by the Consumer Price Index (CPI), but rather is capital intensive, and is driven by a combination of such factors as the construction market, commodity prices, compliance with the Sanitary Sewer Overflow (SSO) Consent Decree, the Potomac River Consent Decree, environmental regulations, security of water infrastructure, and Information Technology improvements. Many of these costs are legally mandated and are not easily deferred or reduced.

Table 1: Revised Base Case Scenario

WSSC FY 2019 – Revised Base Case Scenario @ 5.2%			
Spending Control Limits	FY 2019 Recommended	FY 2018 Approved Budget (\$, thousands)	Change from FY 2018 Budget (%)
Rate Increase	5.2%	3.5%	1.7%
New Debt	\$546,879	\$522,825	4.6%
Debt Service	\$281,174	\$257,071	9.4%
Total Water and Sewer Operating Expenses	\$764,711	\$725,348	5.1%

Revised Base Scenario Assumptions:

- Salary and Wages 4.5% increase
- All Other 1.0% increase in FY 19, and 2.0% projected in outer years
- Completion Factor 92% target to CIP
- Debt Service 36.8% of total expenditures
- Operating Reserves \$74 million (required at 10% level of revenues)
- Days Cash-on-Hand 81 days
- Ending Fund Balance 22% (minimum 10%)

The chart below (**Table 2: Changes to Major Budget Components**) shows the impact on the base case rate components which make the most significant contributions to the

WSSC FY 2019 operating budget as compared to FY 2018. See *Attachment #4* of this report for details on each component of the proposed FY 2019 rate increase.

Table 2: FY 2018 vs. FY 2019 Changes to Major Budget Components

Budget Components	Dollar Change between FY 2018 and FY 2019 (\$, millions)	Water and Sewer Rate Impact
Operating Expenses		
Salaries and Wages	\$5.4	0.9%
Heat Light and Power	\$0.6	0.1%
All Other	\$2.4	0.4%
Debt Service	\$24.1	4.0%
PAYGO	\$6.7	1.1%
Other Transfers and Credits	-\$7.9	-1.3%
Total Revised Base Case	\$31.1	5.2%

B. Spending Affordability Guideline Limitations

The WSSC staff presented a preliminary water and sewer rate increase of 6.2% as part of the FY 2019 Spending Affordability Guideline for both Prince George’s and Montgomery Counties. A revised Base Case of 5.2% increase was subsequently submitted for review by the Spending Affordability Bi-County Working Group. Additionally, Prince George’s County requested and received two (2) alternate scenarios at a 3.5% and a 4.0% rate increase. It is understood that in order to reconcile the Commission’s planned budget for FY 2019, it will be necessary for WSSC to make reductions to existing programs and defer implementation of other operating initiatives. To achieve a 3.5% or 4.0% rate increase, WSSC has identified approximately \$125 million in capital, bond-funded project reductions. See *Table 3: Summary of Project Deferrals* below as well as *Attachment #3*, pages 8 and 9 of this report for deferred capital improvement project details.

Table 3: Summary of Project Spending Deferments

Project Name	FY 19 Proposed Budget (in thousands, \$000)	Summary of Project Deferments	FY 19 Budget Amount of Reductions (in thousands, \$000)
Water Reconstruction Program	\$118,722	<ul style="list-style-type: none"> • Reduce the cost per mile from \$1,600 to \$949 • Reduce emergency contract for depots from \$1M to \$500K each • Reduce contract miles from 43 to 33 miles annually 	(\$ 21,991) (\$3,351) <u>(\$13,829)</u> (\$39,171)
Large Diameter Water Pipe Rehabilitation	\$53,622	<ul style="list-style-type: none"> • Reduce ferrous pipe mile replacement per year from 6 to 4 • Reduce PCCP repairs by 25% 	(\$7,711) <u>(\$5,000)</u> (\$12,711)
Water Storage Facility Rehabilitation Program	\$8,000	<ul style="list-style-type: none"> • Reduce the rate of rehab of tanks 	(\$2,000)
Engineering Support Program	\$16,000	<ul style="list-style-type: none"> • Defer the rate of rehabilitation 	(\$2,000)
Advanced Metering Infrastructure	\$27,494	<ul style="list-style-type: none"> • Defer project in planning stage 	(\$14,000)
Piscataway Waste Water Treatment Facility Upgrade	\$31,115	<ul style="list-style-type: none"> • Defer project schedule 	(\$5,000)
Patuxent Raw Water Pipeline	\$8,378	<ul style="list-style-type: none"> • Defer new supply pipeline 	(\$8,378)
Potomac WFP Submerge Channel Intake	\$1,470	<ul style="list-style-type: none"> • Defer due to lack of approval by National Park Service (on-hold) 	(\$1,400)
Blue Plains Projects	\$53,102	<ul style="list-style-type: none"> • Revise planned completion rate to 80% 	(\$6,372)
Trunk Sewer Reconstruction Program	\$84,457	<ul style="list-style-type: none"> • Reduce the annual replacement from 15 to 13 miles • Reduce the annual replacement from 13 to 10 miles 	(\$8,714) <u>(\$13,071)</u> (\$21,785)

Project Name	FY 19 Proposed Budget (in thousands, \$000)	Summary of Project Deferments	FY 19 Budget Amount of Reductions (in thousands, \$000)
Sewer Reconstruction Program	\$64,684	<ul style="list-style-type: none"> Reduce the annual replacement from 18 to 15 miles Reduce the annual replacement from 15 to 12 miles 	(\$4,243) (\$4,243) <hr/> (\$8,486)
Piscataway Waste Water Treatment Bio-Energy Project	\$42,310	<ul style="list-style-type: none"> Delay project by 2 months 	(\$4,000)
Total Project Cost Reductions			(\$125,303)

C. Staff Recommended Rate Case

The Spending Affordability process provides a framework within which the Councils can review and decide on the WSSC spending control limits. These limits do not cap what the Councils can approve within the regular budget process that concludes in May of each year.

Table 4: Staff Recommended - Spending Limit Scenario

FY 2019 – Staff Recommended Rate Case Scenario @ 4.0%			
Spending Control Limits	FY 2019 Recommended	FY 2018 Approved	Change from FY 2018 Budget (%)
Rate Increase	4.0%	3.5%	0.5%
New Debt	\$435,879	\$522,825	-16.6%
Debt Service	\$277,564	\$257,071	8.0%
Total Water and Sewer Operating Expenses	\$757,644	\$725,348	4.3%

Residential Customer Monthly Impact		
Usage Category	Dollar Increase	Percent Increase
100 gallons per day	\$1.26	3.1%
137 gallons per day	\$1.73	3.3%
160 gallons per day	\$2.30	3.4%

Recommended Alternate Rate Case Assumptions:

- Defer the implementation of Capital Improvement Project (CIP) Reductions as shown in *Table 3*, pages 5 and 6 of this report, with the exception of the Advanced Metering Infrastructure;
- A decrease in the amount of \$111 million in new debt due to deferment of CIP;
- No funding for additional or reinstated projects in FY 2019; and
- A reduction in debt service in the amount of \$20.5 million.

III. Council Staff Recommendation

- **Recommendation #1:** a rate increase not to exceed 4.0%, which adds no more than \$1.73 to a customer's average monthly bill who uses approximately 137 gallons per day. This can be achieved by:
 - \$3.4 million in unspecified adjustments reductions in operating expenses;
 - \$0 increase in operational improvements; and,
 - \$11.6 million in the use of fund balance. See *Attachments #5 and #6* of this report for explanation of WSSC use of fund balance.
- **Recommendation #2:** The Commission continue to seek opportunities and strategies, as well as programs that will yield long term benefits to the Commission and Consumers.

IV. Addendums

Addendum #1

Spending Affordability Background

In May 1993, the Montgomery and Prince George's County Councils created a Bi-County Working Group to focus on the financial concerns of increasing water and sewer rates, debt incurred, and debt service costs. The group's January 1994 report recommended "the creation of a Spending Affordability Process that would require both Counties to set annual ceilings on the Washington Suburban Sanitary Commission's (WSSC) rates and debt, thereby placing corresponding limits on the size of the capital and operating budgets of the Commission." The major objectives of this process are to establish the framework for:

- Controlling costs;
- Achieving low or moderate water/sewer bill increases; and,
- Slowing the rate at which the Commission incurs debt (not to exceed 40% of the Operating Budget).

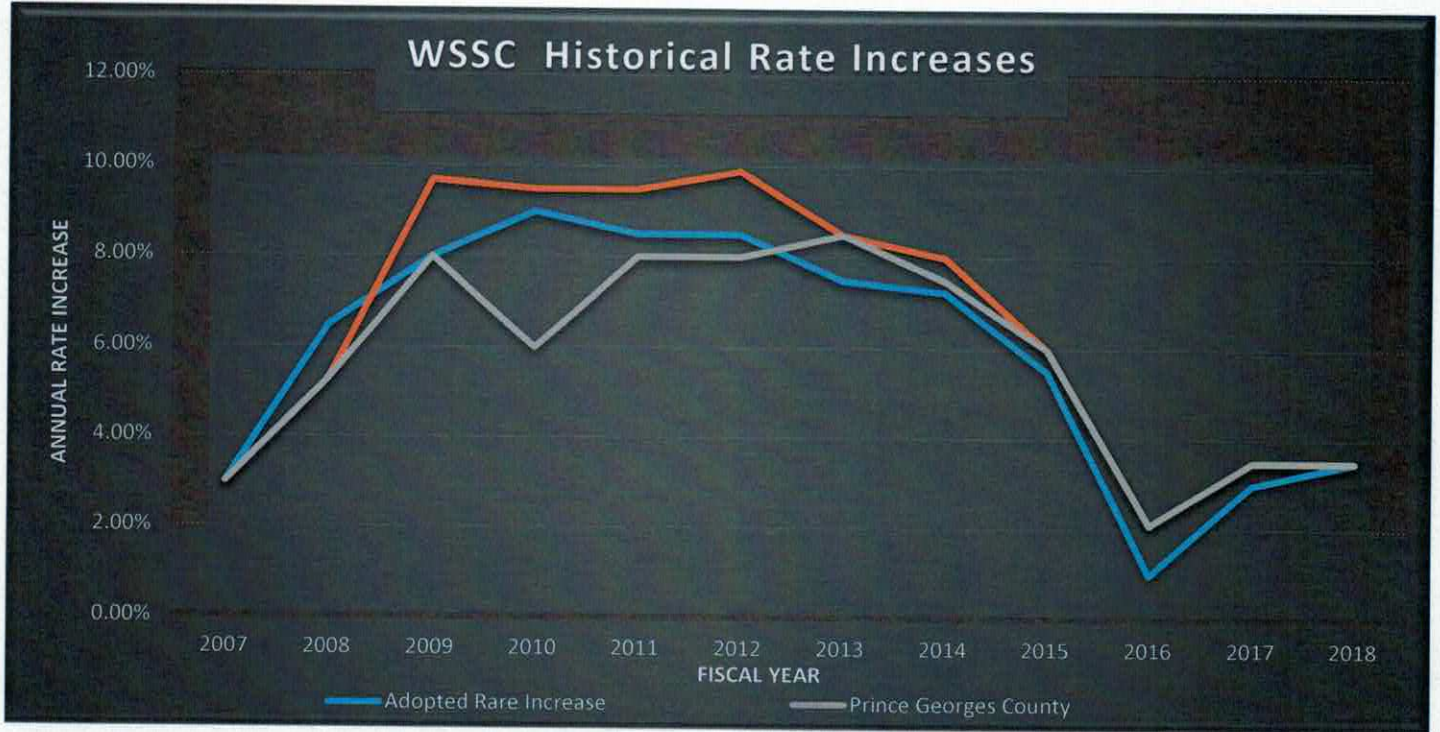
The Spending Affordability Process provides the framework within which each Council can review and decide on the spending control limits. The limits do not cap what the Councils can approve within the regular budget process that concludes in May of each year. The impact of this process has been integral in keeping customer bill increases at a stable and reasonable level.

Historically, the Spending Affordability Process has worked and the limits have been used as a basis to formulate the WSSC budget. Over the years, lower rate increases were achieved by use of fund balance. The staff continues to caution the use of this one-time revenue source, such as fund balance, to reduce rates, as this only reassigns expenses to outer years. Fund balance can be used for one-time expenditures or projects with finite periods. The Spending Affordability Process reviews four (4) limits:

- New Water and Sewer Debt;
- Total Water and Sewer Debt Service;
- Total Water and Sewer Operating Expenses; and,
- Water/Sewer Rate.

WSSC Historical Rate Increases

Fiscal Year	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016*	2017	2018
Adopted Rate Increase	3.00%	6.50%	8.00%	9.00%	8.50%	8.50%	7.50%	7.25%	5.50%	1.00%	3.00%	3.50%
Montgomery County	3.00%	5.30%	9.70%	9.50%	9.50%	9.90%	8.50%	8.00%	6.00%	2.10%	3.50%	3.50%
Prince Georges County	3.00%	5.30%	8.00%	6.00%	8.00%	8.00%	8.50%	7.50%	6.00%	2.10%	3.50%	3.50%



***Note: The actual bill impact in FY 2016 was 6.0% due to recalibration of the Account Maintenance Fee and the implementation of the Infrastructure Investment Fee.**

Addendum #2

Rate Case Study Update

The Commission's current 16-tier rate structure dates back to 1992 and is presently under a comprehensive review. The implementation of the Account Maintenance Infrastructure Fee (AMF) in FY 2016 was recommended by the Bi-County Infrastructure Working Group and was supported by the 2014 rate study. The Commission secured the services of a consulting firm to review the WSSC rates and fees, including the 16 tier water and sewer rate structure. The new study considered the input from both Counties, feedback from WSSC stakeholders, and conducted extensive customer outreach. The planned implementation date for the new rate structure is July 2018. WSSC projects that the AMF will remain constant at approximately \$32,000,000 per year for fiscal years FY 2019 – FY 2024.

Addendum #3

FY 2019 WSSC Proposed Preliminary Budget Highlights

In addition to the physical infrastructure, the WSSC preliminary budget may also provide for investment in the Commission's internal infrastructure through the use of strategic contributions from the Fund Balance. Funds are anticipated to be budgeted to support the Information Technology (IT) Strategic Plan. The IT Strategic Plan is an undertaking to improve the planning, design and implementation of WSSC IT systems that will replace the legacy systems. This will significantly improve business processes, and has proposed funding of \$11,180,000 in FY 2019. The preliminary proposed FY 2019 budget also includes \$200,000 in funds to continue the Climate Change Vulnerability Assessment, as well as to continue the implementation of the Strategic Energy Plan to further reduce WSSC energy consumption, in FY 2019. See *Attachment #5 and #6* of this report for the detailed Fund Analysis.

V. Attachments

- Attachment #1: FY 2019 – FY 2024 Proposed Capital Improvement Program
- Attachment #2: Spending Affordability FY 2019 September 7, 2017 Meeting #1
- Attachment #3: Spending Affordability FY 2019 September 21, 2017 Meeting #2
- Attachment #4: WSSC Multi-year Financial Forecast: Preliminary Budget (Revised Base Case at 5.2% and Alternate Scenario at 3.5% and Alternate Scenario at 4.0%)
- Attachment #5: WSSC Budgeted Uses of Fund Balance (FY 2019)
- Attachment #6: WSSC Fund Balance Analysis (FY 2017 – FY 2019)