

CITY OF UNALASKA
UNALASKA, ALASKA

RESOLUTION 2021-27

A RESOLUTION OF THE UNALASKA CITY COUNCIL AUTHORIZING THE CITY MANAGER TO IMPLEMENT A WASTEWATER PROPRIETARY FUND RATE INCREASE OF 40%, PHASED IN OVER A FOUR-YEAR PERIOD

WHEREAS, the City of Unalaska has determined, through a detailed Rate Study for each Utility, that specific Utility rate increases to achieve a Debt Service Coverage Ratio beyond 1.25 for each Utility Proprietary Fund are necessary to continue operations at the current level of service; and

WHEREAS, phased rate increases necessary to the maintain the required Debt Service Coverage Ratio in the Wastewater Proprietary Fund, distributed equally among all customer classes over the next four fiscal years (FY22-FY25), is 40%; and

NOW THEREFORE BE IT RESOLVED that the Unalaska City Council authorizes the City Manager to implement a Wastewater Proprietary Fund rate increase of 40%, phased in over a four-year period.

PASSED AND ADOPTED by a duly constituted quorum of the Unalaska City Council on May 10, 2021

Vincent M. Tutiakoff, Sr.
Mayor

ATTEST:

Marjie Veeder, CMC
City Clerk

MEMORANDUM TO COUNCIL

To: Mayor and City Council Members
From: Dan Winters, Director of Public Utilities
Through: Erin Reinders, City Manager
Date: May 10, 2021
Re: Resolution 2021-27: A resolution of the City of Unalaska City Council Authorizing the City Manager to implement a Wastewater Proprietary Fund rate increase of 40%, phased in over a four-year period.

SUMMARY: Through Resolution 2021-27, Staff is requesting rate increases for the Wastewater Proprietary Fund that would go into effect in July 2021. This rate increase will consist of a 40% rate increase to the Wastewater Proprietary Fund, equally distributed across all customer classes, phased in over four years.

Staff will incorporate these rate adjustments into the upcoming Schedule of Fees and Services Ordinance schedule, currently set for the May 25, 2021 Council meeting.

Staff will also work up materials for Council to consider an increase to the sale tax by 1%. Doing so would create a Utility Infrastructure Tax fund that will supplement the Utility Proprietary Funds. An increase in the sales tax will require a vote of the residents of Unalaska and will be addressed in future Council Meetings.

PREVIOUS COUNCIL ACTION: At the February 23, 2021 Council Work Session, James Keen and Amber Miller of Aldrich LLP presented the FY2021 Rate Study to Council.

At the March 9, 2021 Council Work Session, conversations focused on the cost of service and rates for Electric and Water. Council's consensus was for a one-time 6.1% increase in Electrical rates to all customer classes, and a one-time 3.6% increase in Water rates to all customer classifications. Council had general consensus to proceed with an increase to the sales tax by 1%, which will create a Utility Infrastructure Fund, supplementing the Utility Proprietary Funds.

At the April 12, 2021 Council Meeting, Staff presented the FY2022 Departmental Operating Budgets. During the budget presentation, Staff reported an overall budget reduction of \$2.8 million for the Department of Public Utilities (DPU). When only Personnel and Operating expenses are considered, the FY2022 DPU budget is \$2.6 million less than FY2021, a decrease of 14.1%.

At the April 13, 2021 Council Work Session, Council discussed the cost of services and rates for the Wastewater and Solid Waste Proprietary Funds. Council's general consensus for the Wastewater utility rate increase was a 40% across the board increase, phased in over four years. Although there was some discussion of options to phase in the

increase based on the cost of service instead. Council's general consensus for the Solid Waste utility was to increase the solid waste utility rates by 33%, phased in over four years. Again there was some discussion in support of focusing on cost of service rather than across the board increases. Just as with the Electric and Water discussion, Council had general consensus to proceed with an increase to the sales tax by 1%, which will create a Utility Infrastructure Fund, supplementing the Utility Proprietary Funds.

At the April 27, 2021 Council Meeting, Staff brought forward Resolution 2021-25. A resolution authorizing the City Manager to implement a one-time rate increase to the Electrical Proprietary Fund of 6.1%; a one-time rate increase to the Water Proprietary Fund of 3.6%; a Wastewater Proprietary Fund rate increase of 40%, phased in over a four-year period; and a Solid Waste Proprietary Fund rate increase of 33%, phased in over a four year period. Council voted to not adopt Resolution 2021-25.

BACKGROUND: Department of Public Utilities Staff performs a rate study on each of the Utility Proprietary Funds approximately every three years. This is a long-standing City Council goal for the budgeting process. The studies assist in the long-term fiscal sustainability of the utility as they help ensure that rates address the cost of providing the utility service and maintaining its infrastructure.

In 2012, Staff contracted Mike Hubbard of the Financial Engineering Company to perform a High-Level Rate Study, which depicted a rate increase of 29% for the Water Fund, 68% for the Wastewater Fund, and 75% for the Solid Waste Fund was needed by 2016. Rates increased consecutively for three years starting in FY2013. The sum of these rate increases was 21.3% for Water, 42.3% for Wastewater, and 32.1% for Solid Waste. These rate increases brought the difference between expenses and revenues closer to the budget before the new Water and Wastewater Plants became operational. However, the rate increases did little to make up for the budget shortfall after the new regulatory mandated; plants were online.

Staff performed the last rate study in 2016. A rate increase of 15% for the Wastewater Proprietary Fund over four years, and a rate increase of 13.5% for the Solid Waste Proprietary Fund, over three years, was initiated on July 1, 2017. During Staff's discussion with Council, there was a clear consensus that another monetary source was necessary to reduce impacts on needed rate increases. Council decided that using a portion of the 1% Sales Tax Special Revenue Fund was the most logical approach. Council approved using an amount not to exceed \$1,300,000 to supplement the Water, Wastewater, and Solid Waste Proprietary Funds. This supplement from the 1% Special Revenue Fund helped slow the timing of the inevitable rate increases. However, the lack of a rate increase to the full revenue requirements, increased costs of chemicals, personnel, and inflation, we are again looking at extreme rate increases for the Utility Proprietary Funds.

In July 2020, Staff contracted through Aldrich CPAs + Advisors LLP to conduct the FY2021 Utility Rate Study. This is the sixth meeting with City Council focused on this study and how utility rates might be impacted.

DISCUSSION: City of Unalaska Council and Staff have been discussing the utility rate increases since February of this year. During these rate discussions, Council members have had mixed opinions concerning the rise to the Wastewater Utility rates. Council discussion wavered between increasing the rates by 40%, equally distributed across all customer classes, or increasing the Wastewater industrial rates by 80% and the other customer classes 38.5%.

Wastewater Proprietary Fund: The completion of the federally mandated New Wastewater Plant construction was in October 2015. The Wastewater Proprietary Fund experienced a 15% rate increase in FY2016 and were phased in over four years. The rate increase accomplished bringing the revenue closer to the projected expenses. However, the rate increases did little to make up for the budget shortfall after the new plant was fully operational. According to Mike Hubbard’s September 2016 Rate Review presentation to Council, he stated *“future rate increases were necessary to balance the budgets”*.

Since FY2016, personnel expenses have increased by 60%. An increase in personnel wages increased over the five years by 3% per year, which equates to 15% of the 60% personnel increase. Planning for the added operational duties with the New Wastewater Plant, Council approved two new employees in 2019. The addition of the two employees and the lack of prior rate increases to meet the projected revenue shortfall contributed to the remaining 45% increase in personnel expenses.

Operation’s expenses have increased by 102.1% since 2016 due to the installation of the larger plant. Maintaining the repair and maintenance of the enhanced plant’s equipment increased by 1,200%. The new and more extensive process design takes more solids out of the wastewater through chemistry. Those chemical costs increased by 9,328%. After removing the solids from the wastewater, employees truck the sludge to the landfill for disposal. The disposal cost caused the solid waste line item to increase by 1,081%. Professional Services increased by 2,272% due to contracting a company with a Class 2 certification in wastewater to oversee our process. ADEC mandated us to do this until our supervisor has obtained his Class 3 certification and one operator has obtained their Class 2 certification.

The table below shows the comparison between the Wastewater FY2014 budget (before the completion of the New Wastewater Plant) and the FY2021 budget of those line items with significant increases.

Wastewater Major Operations Expense Increases			
	FY2014	FY2021	Total
Other Professional Service	\$ 9,000	\$ 213,500	\$ 204,500
Solid Waste	\$ 11,000	\$ 130,000	\$ 119,000
Repair and Maintenance	\$ 5,000	\$ 65,000	\$ 60,000
Chemicals	\$ 3,500	\$ 330,000	\$ 326,500
		Total	\$ 710,000

At the April 27, 2021 Council Meeting, Council’s decision concerning what method to increase the wastewater rate increases generally supported option 1B implementing a

40% rate increase equally distributed across all customer classes and phased in over four years. This is described below.

1B. Increase the Wastewater rates by 40%, evenly to all customer classes.

Class	Charge	Unit	Current	FY2022	FY2023	FY2024	FY2025
Unmetered Residential:	Customer	\$/month	\$ 114.04	\$ 125.44	\$ 136.85	\$ 148.25	\$ 159.66
	Volume	\$/000 Gal	\$ -	\$ -	\$ -	\$ -	\$ -
Annual Rate Increase:			0.0%	10.0%	9.1%	8.3%	7.7%
Rate Increase From FY2021			0.0%	10.0%	20.0%	30.0%	40.0%
Metered Commercial:	Customer	\$/month	\$ 20.87	\$ 22.96	\$ 25.04	\$ 27.13	\$ 29.22
	Volume	\$/000 Gal	\$ 17.79	\$ 19.57	\$ 21.35	\$ 23.13	\$ 24.91
Annual Rate Increase:			0.0%	10.0%	9.1%	8.3%	7.7%
Rate Increase From FY2021			0.0%	10.0%	20.0%	30.0%	40.0%
Metered Industrial:	Customer	\$/month	\$ 20.87	\$ 22.96	\$ 25.04	\$ 27.13	\$ 29.22
	Volume	\$/000 Gal	\$ 1.13	\$ 1.24	\$ 1.36	\$ 1.47	\$ 1.58
Annual Rate Increase:			0.0%	10.0%	9.1%	8.3%	7.7%
Rate Increase From FY2021			0.0%	10.0%	20.0%	30.0%	40.0%

There seemed to be some level of interest in an option that reflected more of a cost of service approach. Option 1C is a hybrid that works in this approach. This is described below.

1C. This option is only for the Wastewater proprietary Fund. Option 1C is a modified rate design that increases the Wastewater industrial rates more than the other classes. This option will reduce the increase needed from the other classes but short of the increase indicated by Option 1B. For example, the industrial class has an 80% increase phased in over four years. The other classes would have a minor increase, also phased in over four years. The table below shows each customer classes rate increase for each year, phased in over a four-year period.

Class	Charge	Unit	Current	FY2022	FY2023	FY2024	FY2025
Unmetered Residential:	Customer	\$/month	\$ 114.04	\$ 125.02	\$ 136.00	\$ 146.98	\$ 157.96
	Volume	\$/000 Gal	\$ -	\$ -	\$ -	\$ -	\$ -
Annual Rate Increase:			0.0%	9.6%	8.8%	8.1%	7.5%
Rate Increase From FY2021			0.0%	9.6%	19.3%	28.9%	38.5%
Metered Commercial:	Customer	\$/month	\$ 20.87	\$ 22.88	\$ 24.89	\$ 26.90	\$ 28.91
	Volume	\$/000 Gal	\$ 17.79	\$ 19.50	\$ 21.22	\$ 22.93	\$ 24.64
Annual Rate Increase:			0.0%	9.6%	8.8%	8.1%	7.5%
Rate Increase From FY2021			0.0%	9.6%	19.3%	28.9%	38.5%
Metered Industrial:	Customer	\$/month	\$ 20.87	\$ 25.04	\$ 29.22	\$ 33.39	\$ 37.57
	Volume	\$/000 Gal	\$ 1.13	\$ 1.36	\$ 1.58	\$ 1.81	\$ 2.03
Annual Rate Increase:			0.0%	20.0%	16.7%	14.3%	12.5%
Rate Increase From FY2021			0.0%	20.0%	40.0%	60.0%	80.0%

ALTERNATIVES: Staff and Aldrich LLP have researched alternatives concerning the needed rate increases and believe the options brought forward to Council are the most logical approach. However, the staff is always willing to research other options that Council may consider are viable. Council could decide to:

- Approve the Resolution as written.
- Amend the Resolution to only address certain funds at the point, and then continue discussion addressing the remaining funds at future meetings.
- Amend the Resolution to adjust the increase approach for one or more of the funds.

FINANCIAL IMPLICATIONS: The table below depicts the revenue gains and shortfall of the individual Utility Proprietary Funds, if Council adopts Resolution 2021-27. Even though there is a shortfall after the rate increases, a 1.25 DSC ratio will be realized for the Wastewater Proprietary Fund.

	Wastewater 40% Rate Inc.
Current Revenue Requirement	\$ 4,319,505
Current Revenue	\$ 2,468,212
Current Revenue Shortfall	\$ (1,851,293)
Revenue from Rate Inc.	\$ 987,284
Revenue Shortfall After Rate Inc.	\$ (864,009)

During the preparation of the FY2022 Budget, Staff reduced the utility division’s operating costs by \$2.6 million. Finding ways to save money and reduce the budget is an ongoing plight for the utility divisions. However, cutting the utilities operation’s budget is only one piece of the pie. Due to inflation, personnel cost increase, maintenance cost increases, and depreciation, and debt, rates need to be increased to cover the revenue shortfalls. There will be a shortfall of revenue after these rate increases. Staff will conduct another rate study in four years. A rate increase will be needed to cover the next four years of inflationary costs and the leftover revenue shortfall from this rate study.

If Council does not approve this rate increase, Payment for Operations, Equipment Maintenance, and Capital Projects will have to be supplemented through the General Fund Reserves. Wastewater services to the public may be limited or reduced, and the City's ability to sell bonds or receive low-interest loans will be limited.

LEGAL: None

STAFF RECOMMENDATION: Staff recommends Council approve Resolution 2021-27. This would approve a 40% rate increase to the Wastewater Proprietary Fund, equally distributed across all customer classes, phased in over four years.

PROPOSED MOTION: I move to adopt Resolution 2021-27

CITY MANAGER COMMENTS: City Council budgetary goals have historically called for a rate study every three years to help insure that rates are addressing the cost of providing the utility service and maintaining its infrastructure. However, when Council implements rate increases over the course of four years, a new study is not conducted until the final year of implementation of the prior study. This rate study this year supports what previous rate studies indicated, that the City would need to increase rates even further in the future especially when previous necessary rate increases were not approved. As it stands now,

what is being recommended still does not meet the full revenue requirement, but does get us closer and allows for us to have a minimum of 1.25 Debt Service Coverage Ratio for each utility. As outlined in the draft budget presentation last month, staff continues efforts to reduce operational expenditures.