



## Legislation Text

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File #: 21-1347B, Version: 1

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### **CITY COUNCIL AGENDA ITEM**

#### **ACTION REQUESTED:**

Pass the ordinance amending Title 8 (Public Utilities) Chapter 2 (Municipal Water and Sewer) Article C (Water and Sewer Rates, Connection Charges) of the Naperville Municipal Code

**DEPARTMENT:** Water Utilities

**SUBMITTED BY:** Darrell Blenniss, Director

#### **BACKGROUND:**

One of the primary factors in establishing rates was the ability to appropriately fund future capital needs that were highlighted during the utility's asset evaluation. At the Oct. 19 City Council meeting, the proposed split of fixed and volumetric costs was raised in the context of whether those who use more water should pay a larger proportion of the costs currently allocated as fixed.

#### **DISCUSSION:**

**Staff provides the following support for the proposed split of these cost categories.**

#### ***Naperville's fixed versus volumetric split is well within - and below - industry standards***

As a reminder, the fixed component of a customer's bill is static each month and represents the cost of being a customer of the utility. They address the assets and equipment used to provide the commodity and service as well as the backend and billing costs for the utility. Variable, or volumetric, costs, as the name implies, vary based on how much of the commodity or service is utilized during a billing period.

The City's current split between fixed and volumetric revenue averages 16% and 84% across all rate classes based on 2020 actuals. The proposed rates will adjust this split to 19% fixed and 81% variable by 2025 and 2026, with the residential split being closer to 25% fixed and 75% variable. The proposed split remains within - and is below - industry benchmarks. Surveys typically report an average split between 25% and 35% for fixed costs. According to Carollo, the most cited recommendation for fixed costs in the water and wastewater industry is 30%, which has been used successfully by many agencies seeking balance between affordability, conservation, and revenue reliability.

### **Sample Residential bill**

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<b>DWC volumetric</b>	<b>\$ 3.72</b>	<b>\$ 27.90</b>
<b>Naperville volumetric</b>	<b>\$ 2.08</b>	<b>\$ 15.60</b>
<b>Water fixed (3/4")</b>	<b>\$ 8.15</b>	<b>\$ 8.15</b>
<b>Water CIP</b>	<b>\$ 0.95</b>	<b>\$ 0.95</b>
<b>Wastewater Fixed (3/4")</b>	<b>\$ 10.25</b>	<b>\$ 10.25</b>
<b>Phosphorus</b>	<b>\$ 1.88</b>	<b>\$ 1.88</b>
<b>Wastewater volumetric</b>	<b>\$ 2.85</b>	<b>\$ 21.38</b>
<b>TOTAL:</b>	<b>\$ 86.11</b>	<b>25% fixed/75% volumetric</b>

**Variable revenue is less resilient**

Carollo developed the proposed model to provide more assurances for the City in planning for water and wastewater capital needs over the next three years. Increasing fixed revenues will allow the Water Utilities a stable baseline for funding major projects and ensures funds are available to cover the payments on additional debt included in the proposed rate structure. Shifting the rates toward greater variable revenues could result in funding shortfalls, as the City is already experiencing a long-term decline in water usage that is anticipated to continue. Greater fixed rates bolster revenue in the face of operating and capital costs, which are overwhelmingly fixed in nature, especially for a City like Naperville that directly passes on its water purchase costs.

If the City increased its reliance on variable rates, decreased water usage could negatively impact revenue available for capital projects. In that case, the city will either need to increase borrowing, which will necessitate future rate increases to cover annual debt service payments or defer further capital projects. Deferral of projects at this point is not recommended as the City will likely incur higher maintenance costs related to an increased need for repairs or could see a significant decline in the quality of water and wastewater services.

Ultimately, the fixed component of a customer’s rates represents the cost of access to clean, reliable water service and the proportionate cost to maintain the system regardless of the amount of water used. Therefore, increased fixed revenue is recommended to better equip the City to address capital funding challenges.

**Rate Impact of Using Capital Scenario 1**

At the October 19<sup>th</sup> City Council meeting, Councilman Hinterlong requested the rate increase information if the City pursued Capital Option #1, replacing one mile of watermain per year. The rate increases over the next three years would be 3.5%, 3.4% and 3.4% respectively. This calculation was completed early in the rate study process and also anticipates a higher level of borrowing. Staff does not recommend approval of this scenario because it maintains water main replacement at the current rate of one mile per year, well short of the 10 miles of water main replacement recommended by the asset evaluation study. The City will continue to fall behind in the replacement of these assets requiring larger rate increases in the future to accommodate a larger capital program.

The full memo from the first reading conducted on Oct. 19 is attached to this agenda item for additional information on the rate study’s goals and findings.

**FISCAL IMPACT**

Under the proposed rates and scenarios described, the average residential combined water/wastewater customer (750 cubic ft/month use) will see a 4.7% increase each year in 2022 through 2024. The average commercial combined water/wastewater customer (2,000 cubic ft/month use and 2" meter size) will see a 4.2% increase in 2022, 4.5% in 2023, and 4.6% in 2024.