

Understanding Costs Essential To Creating Fair and Adequate Water Rates

Adjusting water rates may be one of the most onerous things a city council or rural water district board deals with. Good board/council members should know the financial needs of the utility; they also should strive to be fair and reasonable about charges to the customers. No matter how hard anyone works to create rates that are fair, there are going to be customers who are likely to not agree with any revised structure.

When a public water supply addresses the need to adjust rates it is extremely important to keep the public informed as to why the adjustment is needed. Darron Leiker, former city

manager for the city of Sterling, Kansas, is now the city manager for Wichita Falls, Texas. When it was time for Wichita Falls to adjust water rates, Darron recently stated: *“The water fund is operated as a stand-alone business or enterprise, meaning that the only revenues we have to operate and maintain three reservoirs, two state-of-the-art water treatment plants, pumping stations and hundreds of miles of pipelines are from the charges on your water bills. The general fund (or property tax fund) does not support the water fund or vice versa. We do not use the water fund revenues to pay for streets, police, fire services, parks, MPEC, etc.”*

Darron's comment was well stated to the citizens of Wichita Falls. I called Darron to discuss his experience during the rate adjustment process; he commented that a main concern should be to provide information to customers as to why the rate adjustment is needed. There's no doubt that when customers are informed, there is likely going to be support for the rate increase – at least, less opposition. City council members and RWD boards and staff members should always provide good public relations and communications to customers.

Where do we begin?

When reviewing or considering a rate adjustment it is important to correctly categorize the expenses. KRWA provides no-cost, basic rate reviews. We begin by determining if the expenses are Fixed or if the expenses are Variable. Fixed expenses are those that must be paid regardless of the amount of water sold. Examples would be debt service, insurance, cost of an audit, some portion of salaries and perhaps the minimum bills on other utilities used in the operation of the water system. Typically, the Fixed Expenses are covered by the monthly minimum in the water rate. Variable Expenses include operations and maintenance costs, electrical charges, chemicals, etc. The cost of the Variable Expenses are typically recovered in the charge for the water that is purchased. When categorizing the expenses, it may be confusing but some costs fit both the "Fixed" and the "Variable" categories.

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Fixed vs. Variable Expenses

Assigning the percentages of costs to either Fixed or Variable can also be somewhat arbitrary. Each water system must decide how much of any Variable Expense should be assigned as a Fixed Expense. Systems that have no debt to service may want to maintain a higher minimum rate and therefore may decide to assign a portion of operating costs to the Fixed Expense category. The percentage assigned will have a direct impact on the monthly minimum and charge for water. Setting the percentage too low will reduce the amount needed for the monthly minimum, resulting in the necessity to increase the charge for water sold. Too high of a percentage increases the monthly minimum and increases the cost to sell one thousand gallons.

This table shows typical expenses of a small water system and how KRWA recently categorized the costs:

Most city councils and RWD boards in Kansas acknowledge the need to

Expenses	Amount	% Fixed Expense	Fixed Expense	Variable Expense
Water Purchases	\$52,616	0%	\$0	\$52,616
Water System Fees	\$6,656	0%	\$0	\$6,656
Office Expense	\$3,355	100%	\$3,355	\$0
Postage	\$2,167	100%	\$2,167	\$0
Telephone	\$2,618	65%	\$1,702	\$916
Vehicle Expense	\$10,285	50%	\$5,143	\$5,143
Mileage	\$13,005	50%	\$6,503	\$6,503
Utilities	\$59,366	0%	\$0	\$59,366
Water Testing	\$694	100%	\$694	\$0
Audit and Legal Expense	\$3,347	100%	\$3,347	\$0
Insurance	\$17,915	50%	\$8,958	\$8,958
Chemicals	\$14,222	0%	\$0	\$14,222
Maintenance	\$7,607	50%	\$3,804	\$3,804
Miscellaneous Fees	\$2,327	50%	\$1,164	\$1,164
Supplies	\$39,326	50%	\$19,663	\$19,663
Leases	\$6,000	100%	\$6,000	\$0
Wages; Field Staff	\$62,569	25%	\$15,642	\$46,927
Wages, Office Staff	\$28,080	100%	\$28,080	\$0
Contract Labor	\$17,582	0%	\$0	\$17,582
Professional Labor	\$5,042	50%	\$2,521	\$2,521
Capital Expenditures	\$9,711	50%	\$4,856	\$4,856
Annual Tank Maintenance	\$27,335	100%	\$27,335	\$0
Total Expenses	\$391,825		\$140,931	\$250,894

Q&A Concerning Water Rates

Here are some typical questions that city council and board members and water system staff frequently ask KRWA concerning water rate structuring and rate adjustments.

Question 1. Can our governing body legally give customers a one-time break and not charge the monthly minimum for one month? The idea is to return to the normal charge after that month. **Answer:** *KRWA would not recommend giving a one time break on the monthly minimum as it has the potential to create confusion on subsequent months; omitting the monthly minimum for one month will be very confusing for customers.*

Question 2. In the past, our system has been advised to not reduce the rates. If we do reduce rates, should we reduce the minimum or the rate per thousand? **Answer:** *That's one of the questions KRWA can provide a response in a very short timeframe; KRWA needs two or three years of prior financial reports (revenues and expenses, amount of water purchased and sold). KRWA will analyze the information and provide opinions on what rate adjustment may be appropriate.*

Question 3. What dollar amount is considered as enough cash to have in reserve? **Answer:** *This is a difficult question to answer; it's all relative. A major catastrophe could wipe out any excess revenue very quickly. However, if the water system is small and does not have any major components to operate, has no debt, has new meters and generally has done a very good job with maintenance, there's likely no reason to continue to impose a rate that only adds to the district's reserve funds. A basic rate review will provide the council or board with the costs attributed to the monthly minimum and the cost to sell each thousand gallons*

operate their water systems as businesses. The sale of water and connection fees is really the only revenue available to a rural water district. It is pure speculation to budget based on selling five or ten or fifty new benefit units. The theory of "Build it and they will come" has come back to bite more than one RWD in Kansas. RWDs should only rely on the sale of water for their revenue to operate and maintain the system.

A city can transfer funds into or out of the water fund. I know of many cities that transfer funds out of their Water Fund to cover shortages in other areas. But communities should try to have each utility be self-supporting.

Many water systems in Kansas will need to increase rates in the near future. However, there are also some cities and RWDs that have no debt on their water system and do not anticipate any improvements in the near future and also have funds set aside.



The Kansas RATES Program

There is help available for cities and RWDs to have rate reviews conducted. The Kansas RATES Program by KRWA is for water, sewer and other utilities. Kansas Rural Water Association (KRWA) will conduct simple rate reviews at no charge. When reviews become more complex, Carl Brown Consulting, LLC (CBC), under

Sunday	Monday	Tuesday	Wednesday	Thursday	Friday	Saturday
March 2015				Mark your calendar! March 24-26		
1	2	3	4	5	6	7
8	9	10	11	12	13	14
15	16	17	18	19	20	21
22	23	24	25	26	27	28
29	30	31	Plan Now to Attend! KRWA 48th Annual Conference and Exhibition			

the direction of KRWA, can perform comprehensive rate analyses for utilities. In so doing, CBC will satisfy or exceed performance standards. This program has achieved solid results for systems. To learn more, check the KRWA Web site at www.krwa.net/ratereviews/ratereviews.shtml.

Attend the 2015 Conference

Anniversaries at KRWA are measured in annual conferences. The conference & exhibition is a very BIG DEAL. The conference requires a lot of attention and work. And it's just one more thing that has to happen; the regular work doesn't stop because there's a conference coming up.

Check out the insert in this issue for the 48th Annual Conference & Exhibition that is being planned for March 24 – 26. There will again be an array of pre-conference sessions on Tuesday, March 24 and an additional 48 concurrent sessions on Wednesday and Thursday, March 25 and 26. EXPO Hall will have 331 exhibit spaces filled with products and services for the water and wastewater industries. Plan now to attend.

Greg Duryea has worked for KRWA since 1993 as Technical Assistant. He holds a Class I water certification and is the certified operator for Sycamore Springs Resort in Brown County.



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