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Low-Income Bill Affordability Related to Environmental Compliance Obligations of Water Utilities

NOTE TO READERS

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Local Water Utilities Must Ensure Bill Affordability in Order to Meet Environmental Compliance Obligations.

Local utilities providing water service frequently face the tension between meeting their environmental compliance obligations while maintaining bills at affordable levels to low-income customers. Increasingly, however, analysts are finding that achieving affordability is a necessary element of fulfilling environmental obligations.

The Affordability Concerns of Rhode Island's State Treasurer.

In a 2019 proceeding before the Rhode Island Public Utilities Commission ("RIPUC") involving the Narragansett Bay Commsision ("NBC"),[1] Rhode Island State Treasurer Seth Magaziner submitted Direct Testimony expressing concern about the impact that NBC borrowing to fulfill environmental compliance obligations would have on affordability. The State Treasurer's concern was not based exclusively on the impact which the resulting higher rates would have on low-income customers, but also on the extent to which unaffordable bills would threaten the ability of NBC to collect its billed revenue and, as a result, to repay the money it was borrowing to pay for its environmental clean-up costs.

[1] Before the Rhode Island PUC, In Re. Narragansett Bay Commission, Case No. 4890 (2019).

As State Treasurer, Magaziner said he is Chair of Rhode Island's Public Finance Management Board ("PFMB") as well as the executive responsible for Rhode Island's Office of Debt Management. "Under Rhode Island law," Magaziner explained to the RIPUC, "the PFMB is tasked with monitoring public borrowing practices at the state, quasi-public, public, and municipal levels, issuing legal opinions to these entities on matters of public debt. . ."

"In accordance with these responsibilities," he said, "my staff and I spend a lot of time studying issues of public debt affordability at all levels. I believe it is clear that the General Assembly intended the PFMB and our Office to not just be passive observers on these matters, but to weigh in when we have concerns about the affordability of existing or planned public debt."

The State Treasurer reported that "according to NBC's Fiscal Year 2019 budget, total outstanding debt as of June 30, 2018 was more than $594 million. Additionally, the NBC's capital improvement plan calls for nearly $300 million of additional borrowing between now and Fiscal Year 2024, primarily to support phase three of the Combined Sewer Overflow ("CSO") program."

He concluded that "in our view, the level of existing and planned borrowing has caused us to reach a point where a serious discussion must be had about the affordability of this debt to ratepayers."

The Metrics Used to Measure Affordability in Rhode Island.

The Rhode Island State Treasurer used two different metrics to measure the "level of public borrowing that is affordable." The first metric he used "compare[d] the cost of debt service payments to the availability of revenue to make those payments. Here, we look at the ability of the agency, in this case NBC, to raise revenues and whether those revenues will exceed the cost of the agency's operating expenses and debt service commitments, usually with an additional margin for safety." He reported, "by this set of metrics, we find that NBC is in good shape."

The second set of metrics, however, "has to do with the ability of the underlying population to afford the rates that are being charged. This is the area where our concern lies."

Using two percent (2%) of income as the measure of "affordability" for a sewer bill, the State Treasurer reported that "while the proposed rates for next year do not exceed 2% of median income across the whole service territory, it is important to note that the service area contains dramatic differences in income levels from neighborhood to neighborhood, and that proposed rates for the coming year are unaffordable for broad swaths of the community that NBC serves."

The State Treasurer warned that "as NBC embarks on the CSO III project and other capital improvements, rates are projected to become more unaffordable for many people in the coming years."

Ultimately, after emphasizing that he did not oppose the CSO III project, State Treasurer Magaziner recommended that "a resolution might be a system where low-income ratepayers could be eligible for discounts or rebates to help shield them from the cost of increasing rates.

The cost of such a program would be charged to the remainder of the rate base."

Environmental Compliance and Affordability in Baltimore.

The conclusions of the Rhode Island State Treasurer are closely aligned with the conclusions reached by FSC in its study of water and sewer bills in the City of Baltimore.[2] According to the FSC Baltimore study:

> Like most major cities in the United States today, the City of Baltimore is facing a major dilemma. On the one hand, Baltimore has major capital investments that it must make in the infrastructure used to deliver water and wastewater service to city residents. These investments are expected to cost billions of dollars. On the other hand, many of the residents of Baltimore simply cannot afford to pay the water and wastewater rates that will be required in order to fund these billion dollar investments.

FSC referred to this tension as "the conundrum facing city officials." Baltimore _must_ borrow money to invest in water and wastewater infrastructure improvements that can no longer be delayed in order to deliver an essential public service. Not making the improvements is not an option. In contrast, many Baltimore customers of the water / wastewater utility do not have the ability to pay the increase in bills that will be charged for those essential public services. Not using water and/or wastewater service is also not an option.

According to FSC, "Failing to acknowledge, let alone to address, this conundrum results in a multitude of problems for Baltimore. It results in environmental problems as City officials may seek to delay or avoid their responsibilities to deliver safe, clean and healthy service. It results in social problems as increasing numbers of Baltimore residents lose their water/wastewater service (and, frequently, correspondingly lose their homes). It results in financial problems to the City, as Baltimore, in its capacity as a municipal government, experiences increased expenses (such as addressing homelessness and municipal decay) while facing a decreasing property tax base (as water service is terminated and homes are abandoned)."[3]

Just as importantly as these impacts, however, FSC found that the failure to acknowledge and address the conundrum results in a business problem to the water / wastewater utility, as it unsuccessfully seeks to collect money that City residents don't have (and inefficiently spends money in those unsuccessful collection efforts).

Between 2010 and 2016, the City of Baltimore entered into agreements with the federal Environmental Protection Agency ("EPA") to undertake a significant expansion in its environmental compliance efforts. It borrowed heavily to meet those obligations. As FSC noted, "This increase in debt generates not merely a *noticeable* impact on annual expenses to be included in customer rates, but a *substantial* impact." From 2010 to 2016, the principal and interest paid by water customers *each year* increased by 86.3% (from

[2] Colton (December 2018). Baltimore's Conundrum: Charging for Water / Wastewater Services that Community Residents Cannot Afford to Pay, prepared for Food and Water Watch: Baltimore (MD).

[3] Throughout the Baltimore discussion, the term "water service" should be construed as referring to water, wastewater and stormwater services unless the context clearly indicates a contrary intent.

$26,466,000 in 2010 to $49,313,000 in 2016). During the same time period, the principal and interest paid by wastewater customers each year increased by 58.4% (from $44,740,000 in 2010 to $70,874,000 in 2016).

"The real question today," FSC said, "is whether Baltimore is both willing and able to take those steps necessary to face the following conundrum. The City of Baltimore does not have the discretion *not* to make these investments. However, and it is a huge 'however,' the need to make the investments does not make the ability-to-pay of Baltimore customers any greater."

The impact of Baltimore environmental borrowing has resulted in precisely the type of increases in bills identified as being of concern to the Rhode Island State Treasurer for NBC. Typical residential bills in Baltimore have increased by 127% from FY2010 to FY2018. Residential bills have increased by 37% simply from FY2014 to FY2018. The bill increases will become more and more dramatic. By Fiscal Year 2022, assuming the same three year annual increase as was adopted in the last three-year rate decision, the typical residential bill of $1,115 will be more than triple what the 2010 bill had been ($347).

FSC warned that one of the problems facing the City of Baltimore is that sending bills that exceed the capacity of the community to pay does not result in the revenue that is required to meet one's financial obligations.

> As a result, a downward spiral is created. Future rate increases have to be higher, in order to take into account the fact that much of the increase in billed revenue, in fact, will not be collected. In the meantime, arrearages grow, as do the expenditures that the utility devotes to its increasingly unsuccessful efforts to collect its revenue. What occurs, in other words, is that the City works harder and harder to collect less and less.

FSC examined the affordability of water bills in Baltimore on a geographically disaggregated basis. The Baltimore study considered bills for each Census tract in Baltimore. FSC examined bill affordability for households in the "First Quintile" of income[4] as well as the affordability with incomes at various Poverty Levels.

FSC found that beginning in 2015, the number of Census Tracts in which households in the First Quintile of income faced high bill burdens began to sharply increase. In 2015, 83 Census tracts experienced bill burdens exceeding eight percent (8%) of income for households with income in the First Quintile of their Census Tract (8% being four times higher than the 2% water / wastewater burden generally deemed to be affordable). By 2018, that number increased to 103 (more than half) of all Census Tracts. By 2022, that number had increased to 126 Census Tracts (or more than 70% of the City) that had water / wastewater burdens four times higher than the burden deemed to be affordable.

The importance of looking at customers with incomes at lower levels of Poverty, FSC said, cannot be over-stated for Baltimore. In 2016, nearly 35% of Baltimore's population lived with income at or below 150% of the Federal Poverty

[4] The Census Bureau rank orders households from those with the highest income to those with the lowest income. That ordering is then divided into five equal parts, each part of which is called a "quintile." The "Fist Quintile" is that quintile (i.e., that one-fifth of the population) with the lowest incomes.

Level. Nearly one-in-four (24%) of Baltimore's population lived with income at or below 100% of the Federal Poverty Level. Just as importantly, there are some areas of the City where poverty is concentrated. The percentage of population living at or below 100% of Poverty is greater than 25% more than the overall City average in 53 Census Tracts, while the percentage of population living at or below 150% of Poverty is 25% more than the overall City average in 61 Census Tracts.

FSC reported that by 2016, bills were affordable at 150% of Poverty Level in only five (5) of the 198 Census Tracts. By 2019, bills will not be affordable at 150% of Poverty anywhere in the City of Baltimore.

Baltimore Collection Impacts

As customers experienced these dramatic, and unaffordable, bill increases in Baltimore, collections for the Baltimore municipal water utility were serious eroded. Since 2010, FSC found, Baltimore's total water receivables have increased by nearly $15 million, while the City's total wastewater receivables have increased by nearly $125 million. Even more importantly, the City's wastewater non-current asset receivables have increased by $90 million (from $6.5 million in 2010 to $98.1 million in 2016).

In many ways, in other words, Baltimore is impeding its own progress in seeking to generate funding for current and future investments in its water and wastewater infrastructure in the manner in which it is now proceeding. As bills become more and more *un*affordable, the City realizes less and less cash from each rate increase. As the City collects less and less money, it is forced to raise rates even higher to replace the funds not collected. The City does not track information on the number or size of bills that remain unpaid, or on the efforts the City takes to collect those bills, let alone on the success (or lack of success) in converting billed revenue into collected revenue. The downward spiral is thus exacerbated.

The Baltimore Recommendation.

Ultimately, FSC recommended that Baltimore adopt a water affordability program that mirrors the Income-based Water Rate Affordability Program ("IWRAP") unanimously approved by the Philadelphia City Council in 2016.

FSC told the Baltimore City Council that:

> The City of Baltimore has an available option that it could implement to help it resolve the financial conundrum facing the City today. The City faces a choice today. It could choose to do nothing in response to the increasing unaffordability of water and wastewater bills (and the collection problems that accompany that unaffordability). Or it could choose to address the quandary in which the City finds itself.
>
> The recommendation of this report is that the City of Baltimore should choose to act. Baltimore should adopt an IWRAP program based on the Philadelphia model. A Baltimore IWRAP should include the following components: (1) a percentage-of-income-based bill affordability program; (2) an arrearage management component; (3) a crisis intervention component; and (4) a water conservation component.
>
> Given the problems facing Baltimore, and given the demonstrated success of percentage-

of-income based bill affordability programs in addressing precisely these types of problems, the time for the City of Baltimore to adopt a Baltimore IWRAP is today.

The EPA Guidance

The ability of a low-income affordable rate to improve the capacity of a water service provider to generate revenues is one reason the U.S. Environmental Protection Agency ("EPA") has historically not merely "approved" low-income rates, but has affirmatively ***encouraged*** local water providers to adopt such rates. The EPA has explicitly recognized the role that low-income rates play in improving the capacity of a community to make substantial environmental compliance investments.

In 2013, the EPA told its Regional Administrators that "EPA ***strongly encourages*** municipalities to consider establishing lower rates or subsidies for low income customers. This is consistent with one of the goals of integrated planning, which is to take advantage of synergies and savings that can be found through an integrated approach and thereby promote affordability." (emphasis added).[5] EPA said, "local officials have a great deal of latitude under these [Clean Water Act] regulations and the EPA continues to encourage communities to consider and adopt rate structures that ensure that lower income households continue to be able to afford vital wastewater services."

[5] Memo (January 13, 2013). Nancy Stoner, Acting Assistant Administrator, Office of Water, EPA, Cynthia Giles, Assistant Administrator, Office of Enforcement and Compliance Assurance, EPA, to Regional Administrators.

Summary

For more information regarding bill affordability programs for water utilities, or for a copy of either State Treasurer Magaziner's Rhode Island testimony, or FSC's Baltimore water affordability report, please write:

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Fisher, Sheehan and Colton, Public Finance and General Economics (FSC) provides economic, financial and regulatory consulting. The areas in which *FSC* has worked include energy law and economics, fair housing, affordable housing development, local planning and zoning, energy efficiency planning, community economic development, poverty and telecommunications policy, regulatory economics, and public welfare policy.