

Flint Water Interagency Coordinating Committee Water Rates Subcommittee Recommendations for Improving Water Ratemaking and Affordability in Michigan

The FWICC subcommittee on water rates offers the following recommendations as a blueprint for strengthening the commitment to providing access to safe, adequate, and reliable water service of high quality to residents of Michigan.

Revenues from rates support the cost of essential water services to communities and water rates send important economic signals. The water utility sector benefits from a community of expertise and generally accepted principles and practices related to ratemaking as well as to related practices in financing, accounting, and planning that support the development of rates.

The subcommittee's overarching recommendation is for a comprehensive and independent review of the state's approach to the regulating the water sector, including a focus on water rates and affordability. The review should identify and address specific legal authorities, agency responsibilities, and resources for implementing current and future policies to address these recommendations, as well as barriers to implementation. These ideas complement the findings of Michigan's 21st Century Infrastructure Commission.¹

A policy vehicle for addressing these issues exists in the 1996 Amendments to the federal Safe Drinking Water Act (SDWA), which required each state to develop a strategy to develop the technical, managerial, and financial capacity of all water systems.² Water systems that have these three essential capabilities are better prepared to meet their service obligations, especially public-health protection. Michigan's strategy was published by the State in 2000.³ A comprehensive update to the state's strategy, incorporating the ideas presented here, would constitute a significant step forward in advancing the state's water policy goals, including resilience in the face of various challenges.

The subcommittee's recommendations reflect a commitment at every level of government and by every stakeholder to the imperative of compliance with all applicable federal, state, and local drinking water and clean water standards, with enforcement as necessary. Water supplied to consumers must meet all parameters necessary to ensure public health, welfare, and safety. Service quality as referenced here encompasses not only standards related to public health and safety but also those related to the adequacy and reliability of service.

¹ See www.michigan.gov/snyder/0,4668,7-277-61409_78737---,00.html.

² SDWA Sec. 1420. www.epw.senate.gov/sdwa.pdf.

³ Michigan Department of Environmental Quality Drinking Water and Radiological Protection Division, *Capacity Development Strategy For Existing Public Water Systems* (August 1, 2000). www.michigan.gov/documents/deq/deq-wd-water-fos-tsu-CDExistingSystemsStrategy_247638_7.pdf.

1.0 Accounting, Finance, and Planning

- 1.1 Encourage enterprise organization of water utilities with political and financial separation from local governments and requirements for representative governance, accountability, and transparency.
 - 1.1.1 Prohibit transfers from ratepayer supported water funds to municipal general-revenue funds without full transparency and documented cost justification.
 - 1.1.2 Use state resources and tools to incentivize and support regional enterprise solutions, including the formation of water authorities and districts, to capture economies of scale.
- 1.2 Establish a statewide uniform system of accounts for use by water utilities in establishing revenue requirements (comprised of capital and operating costs), conducting cost-of-service studies, preparing financial reports, and benchmarking performance.⁴
 - 1.2.1 Require all water, wastewater, and stormwater utilities to publish annual financial reports and file them with a designated state agency to ensure transparency and accessibility.
- 1.3 Require all drinking water, wastewater, and stormwater utilities to prepare multiyear integrated asset management, human resource, and financial plans to ensure adequate capacity for meeting all applicable regulations and standards related to service quality, with review by a designated state agency.
- 1.4 Establish a formal review and approval process by a designated state agency for major capital projects requiring debt financing to ensure appropriate consideration of project merit, regional alternatives, and ratepayer impacts.

2.0 Cost Control and Cost Recovery

- 2.1 Establish a statewide policy regarding nonrevenue water (including leakage and loss) and requirements for system auditing, reporting, and remediation.⁵
 - 2.1.1 Encourage the use of district metering and remote sensors in conveyance and distribution systems to improve water accounting as well as leakage and loss control.
- 2.2 Promote and incentivize cost-effective demand management to reduce system peaks and avoid operating and capital costs over time (taking the terms of wholesale agreements into account).

⁴ The National Association of Regulatory Utility Commissioners and several states publish uniform systems of accounts for water utilities.

⁵ See American Water Works Association, *Water Audits and Loss Control Programs* (M36).

- 2.3 Encourage water utilities to optimize operations, including asset right-sizing, and coordinate with other infrastructure providers during asset replacement and renovation.
 - 2.3.1 Provide planning assistance and support to legacy systems with excess capacity and high fixed costs.
- 2.4 Encourage water utilities adopt generally accepted policies and practices for the equitable allocation of costs associated with water utility capacity requirements.⁶
 - 2.4.1 Ensure that growth pays for the cost of growth in the water service territory.
 - 2.4.2 Allow water utilities to require deposits or escrow funds as well as charge impact and exit fees to commercial and industrial ratepayers in order to shield residential ratepayers from the impact of stranded investment.
 - 2.4.3 Consider state policies regarding the connection of customers to existing water utilities and retention of customers within a franchised or certificated service area.
- 2.5 Encourage water utilities to build reserve or contingency funds consistent with generally accepted policies and practices related to capital asset management and emergency planning.
- 2.6 Accelerate the replacement of lead service lines with funding by various means to mitigate cost impacts on water ratepayers, particularly low-income households.
 - 2.6.1 Secure federal, state, and nonprofit funding for lead service line replacement.
 - 2.6.2 Authorize water utilities to fund lead service line replacement through on-bill financing and billing.
 - 2.6.3 Authorize water utilities to recover the replacement of lead service lines through base rates as part of the system cost of service.
 - 2.6.4 Authorize water utilities to assume ownership and control of water service lines on customer premises to the extent permissible by law.

3.0 Rates and Rate Structures

- 3.1 Advance adoption of just and reasonable rate structures that are legally defensible and promote universal and affordable access to essential water services, including lifeline rates, increasing-block rates, and minimum bills with a water usage allowance.⁷

⁶ See American Water Works Association, Principles of Water Rates, Fees, and Charges (M1).

⁷ See American Water Works Association, Principles of Water Rates, Fees, and Charges (M1).

- 3.1.1 Encourage incremental and phased approaches to changing rate levels and structures that consider both utility financial health and ratepayer equity.
- 3.2 Require all water, wastewater, and stormwater utilities to publish tariffs annually and file them with a designated state agency to ensure transparency and accessibility.
- 3.3 Encourage more transparent, inclusive, and participatory processes for establishing water rates and rate policies at the community level.
 - 3.3.1 Assist communities in developing capacity for communications and outreach about cost and rates, including plain-language approaches (e.g., gallons vs. cubic feet) and low-cost means of consumer education and engagement.
- 3.4 Encourage refinement of cost-of-service studies in order to improve the efficiency and equity of cost allocation and price signals across and within customer classes (residential, commercial, and industrial).
- 3.5 Promote ratepayer accountability and encourage water utilities to recognize prompt and complete payment behavior.
- 3.6 Remove legal barriers to rate design under the Headlee Amendment and Bolt and shield water utilities from frivolous legal challenges by redefining the cost of service in terms of public-health protection.

4.0 Affordability and Consumer Protection

- 4.1 Redefine water services and the cost of service in terms of the utility's obligation to provide affordable access for the protection of public health.
- 4.2 Establish statewide water disconnection (shutoff) rules and standards consistent with public-health protection and a business case for compassion.
 - 4.2.1 Encourage the adoption of alternatives to water disconnection, including prepaid meters and flow-restriction devices.
- 4.3 Promote the development of efficiency programs (such as leak detection and fixture replacement) as a means of targeted assistance to low-income households, with authorized recovery of costs through rates.
- 4.4 Enable water utilities to offer payment plans, including plans with arrearage forgiveness or bill discounts that facilitate payment compliance and reduce utility collection expenses.
 - 4.4.1 Establish a statewide bill-payment assistance program, possibly modeled after the Great Lakes Water Authority's Water Residential Assistance

Program (WRAP), or an expansion of the Low Income Home Energy Assistance Program (LIHEAP) to include water.⁸

- 4.5 Develop protective policies for water ratepayers who are renters, including regulation of submetering and penalties on landlords for nonpayment of water bills from rental income.
- 4.6 Establish an independent statewide appeals process for consumer complaints as well as processes for resolving disputes over service quality and rates, as an alternative to legal remedies.
 - 4.6.1 Establish a statewide process for tracking consumer complaints and appeals related to service quality and rates to identify patterns and inform policy development and enforcement.
- 4.7 Require a remediation action plan for utilities that fail to meet service quality standards and regulations.

5.0 General State Policies and Incentives

- 5.1 Align and link state incentives such as grants and loans to utility performance improvement goals, including cost control, asset management, operational efficiency, and cost-effective regional solutions.
 - 5.1.1 Provide model standards, codes, ordinances, and zoning policies that support state water policy goals.
 - 5.1.2 Support pilot programs, professional development, and mutual aid agreements that address state policy and water utility goals.
 - 5.1.3 Engage a wide range of stakeholders in the public, policy, and professional technical communities (such as engineering and construction) in the development of state water policies.
- 5.2 Support water utilities in developing technical, managerial, and technical capacity consistent with state water policy goals.
 - 5.2.1 Establish an information clearinghouse and provide educational materials and programs to support capacity development, including models for inclusive utility governance.
- 5.3 Require testing for and disclosure of lead risks in service lines and premise plumbing at time of property transfer.
- 5.4 Consider establishing state permit fees for large-volume withdrawals by entities other than public suppliers and devote these funds to water regulatory programs.

⁸ For WRAP, visit www.waynemetrol.org/wrap; for LIHEAP, visit www.benefits.gov/benefits/benefit-details/1545.

- 5.5 Develop policies that recognize the unique affordability challenges and public-health risks associated with community poverty, fiscal distress, emergency management and population loss.
- 5.6 Consider institutional mechanisms equivalent or comparable to economic regulation to promote transparency, accountability, and sound practices, with the level of oversight based on system conditions and capacities and opt-in or opt-out provisions as appropriate.