City of Birmingham
A Walkable Community

MEMORANDUM

Finance Department

DATE: **December 23, 2014**

TO: **Joseph A. Valentine, City Manager**

FROM: **Mark Gerber, Assistant Finance Director**
Paul O'Meara, City Engineer

SUBJECT: **Oakland County Water Resources Commissioner Operations**

Per your request, I have reviewed financial data of the Oakland County Water Resources Commissioner (WRC) related to the Evergreen-Farmington Sewage Disposal System (EFSDS), the George W. Kuhn Sewage Disposal System (GWKSDS), and the three combined sewage overflow basins for the past 5 years. I have attached the summarized data I reviewed to this report.

Evergreen-Farmington Sewage Disposal System

From the 2009-2010 to 2013-2014 rate years, the overall portion of the WRC sewage disposal rate increased from $2.04 to $3.08, an increase of $1.04, or 51% (see rate history page). Most of this increase (69%) is attributable to reserves. The reserves are used to fund capital improvement projects in the future. According to the WRC's rate notification letter dated April 22, 2009 (2009-2010 rate year), the reserve is required as follows, "Effective in 1992, as a part of the Evergreen-Farmington SDS grant program, the Michigan Department of Environmental Quality (MDEQ) required that the District establish a separate replacement reserve for the purpose of replacing equipment with a life expectancy of 20 years or less, such as pumps, motors, and control equipment. This amounts to $93,900 yearly or $.05 per MCF". As you can see this has now grown from $.05 to $.77.

The other major portion of the rate increase is for debt service on bonds issued by the County for the EFSDS. This increased the WRC rate by $.33, or 31%. While the maintenance and operations portion of the WRC rate increased $.10, this was offset by an increase in miscellaneous revenue of $.11.

According to the County's last audit report dated September 30, 2013, the EFSDS has a net position of $25,596,015 of which $1,782,024 is unrestricted and $7,175,188 is restricted for programs (see Evergreen-Farmington Sewage Disposal System Financial Summary). The remainder of the net position is invested in capital assets. The September 30, 2013, net position balance is down compared to the 2009 balance of $33,392,872 (which is made up of unrestricted balance $16,243,163 and investment in capital assets of $17,149,709). It appears that the system has sustained heavy losses in four of the last five years, which seems odd given that their largest expense (sewage disposal) is entirely charged back based on sewage flows. As a result of the low net position, the County has had to issue bonds to make capital improvements to the system. I would anticipate that the County will continue to raise the amount for reserves in their future rate letters to compensate for these low balances (for rate year 2014-2015 the reserve requirement increased $1,120,000 system-wide).

Potential questions to raise:

1. What projects are envisioned for the Evergreen-Farmington System and how will these be financed? Will any of these new projects be charged to Birmingham?
2. The Northeast Interceptor projects involve work at several locations mostly upstream of Birmingham. Will the funds needed for these projects be charged separate from the reserves?
3. What is the target construction date for the sewer replacement proposed in our municipal parking lot #6 (at 600 N. Old Woodward Ave.)?
4. How do you set your rates including the amount for reserves?
5. Does the WRC have a reserve policy (i.e. what are limits that the WRC tries to maintain reserves)? If so, what is it?
6. Are amounts for reserves in the rates for future projects or current projects?
7. If future projects, how can these reserves accumulate when the system has had significant operating losses over the past few years? How will this affect future rates?
8. What is the WRC's financial plan for this system?

<u>George W. Kuhn Sewage Disposal System</u>

From the 2009-2010 to 2013-2014 rate years, the overall portion of the WRC sewage disposal rate increased from $.76 to $.96, an increase of $.20 or 26%(see George W. Kuhn Sewage Disposal System Financial Summary). The amount of the rate contributed to reserves increased $.62. There was nothing contained in the rate letters explaining why a rate for reserves was added as there was nothing charged in 2009. Maintenance and operating expenses decreased during that same period by $.29, or 35%. It is not known whether part of this rate previously had a reserve built into it or whether it truly was a decrease in expenses for maintenance. Miscellaneous revenue increased during this period with the overall effect of reducing the rate by an additional $.13.

According to the September 30, 2013, audit report, the GWKSDS has a total net position of $36,891,933 which is consists of $3,728,047 investment in capital assets; $11,543,178 reserved for programs; and $21,620,708 unrestricted. This is an increase of $14,827,127, or 67%, in net position since 2009. The GWKSDS appears to be in sound financial condition, so the question arises about whether the reserve charges are appropriate as they remained the same for rate year 2014-2015.

In addition, there was an odd transaction in 2010, where an advance of $884,639 was made. This was a loan to the Drain Equipment Fund for a purchase of two vactor trucks and one jetter truck. It is being systematically paid back to the GWKSDS and appears it will be fully paid back in fiscal year 2014. The Drain Equipment Fund at the time was in a deficit and did not have the funds to purchase the trucks directly.

Potential questions to raise:

1. What projects are envisioned for the George W. Kuhn System and how will these be financed? Will any of these new projects be charged to Birmingham?
2. How do you set your rates including the amount for reserves?
3. Does the WRC have a reserve policy (i.e. what are limits that the WRC tries to maintain reserves)? If so, what is it?

4. It does not appear that much in terms of capital has been paid out of this fund. What are the plans for the reserves?
5. What is the WRC's financial plan for this system?
6. What effect will the solvency of the Drain Equipment Fund have on future rental costs to the various sewage disposal systems?

Combined Sewer Overflow Basins

In reviewing the budgets for the CSO's over the past 5 years (see Drain Budget Summaries), most of the budgetary line items are either holding steady or decreasing slightly. The two areas where we have seen increases are sewage disposal and replacement reserves. MDEQ does require that reserves be maintained for replacement of facility equipment. However, as you can see, the WRC also has reserves that are in addition to the MDEQ requirements. The purpose of these reserves was to provide a more stable budget from year to year instead of funding major repairs or maintenance items as they are needed. The Bloomfield Village CSO had a pipe collapse a couple of years ago which was repaired by using these reserves. The reserves then needed to be replaced in order to fund future planned projects. That is the reason why those reserves were increased so significantly in 2013 and 2014. In the 2015 budget, the Bloomfield Village CSO budget for reserves has decreased to $148,750.

Potential questions to raise:

1. Where in the County's financial statements are these RTB's recorded?
2. How are the amounts for reserves in the budget determined?
3. Does the WRC have a reserve policy for these RTB's? If so, what is it?
4. What is the reasoning for the various levels of reserves and what are their purposes?
5. Do you foresee any need for replacement of the RTB's which would require bonding?

WRC Charges in Birmingham's Sewer Rate

The WRC's portion of Birmingham's overall sewer rate in terms of sewage disposal is small (see History of Sewer Rate Components). Over the past 5 years, their portion of the City's sewer rate has increased from $.54 to $.67, largely due to the increase in reserve requirements. Also, the amount assessed to the City for the 3 RTB budgets has increased the City's sewer rate by $.30, or 25%, over the past 5 years as a result of higher sewage disposal costs and larger reserve requirements.

The City's portion for maintenance costs has risen $.23, or 14%, over the past 5 years, as a result of higher personnel benefit costs and depreciation as a result of capital improvements.

GEORGE W. KUHN SEWAGE DISPOSAL SYSTEM (GWKSDS) FINANCIAL SUMMARY

	2013	2012	2011	2010	2009
BALANCE SHEET					
ASSETS:					
CURRENT:					
POOLED CASH & INVESTMENTS	35,012,593	28,049,112	26,702,937	21,668,641	13,281,294
ACCOUNTS RECEIVABLE	7,572,360	9,172,804	6,832,302	6,386,505	5,138,320
PREPAYMENTS AND OTHER ASSETS	624,605	658,199	692,145	714,000	748,000
TOTAL CURRENT ASSETS	43,209,558	37,880,115	34,227,384	28,769,146	19,167,614
NONCURRENT:					
NON-DEPRECIABLE ASSETS	1,003,988	977,442	977,442	618,893	613,529
DEPRECIABLE ASSETS	2,724,059	4,009,604	5,331,189	6,666,841	8,020,112
OTHER	142,531	319,459	496,387	673,315	-
TOTAL NONCURRENT ASSETS	3,870,578	5,306,505	6,805,018	7,959,049	8,633,641
TOTAL ASSETS	47,080,136	43,186,620	41,032,402	36,728,195	27,801,255
LIABILITIES:					
CURRENT:					
ACCOUNTS PAYABLE	20,846	24,536	97,311	35,218	6,384
DUE TO OTHER GOVERNMENTS	9,987,654	8,670,686	9,536,534	7,247,937	5,628,603
OTHER ACCRUED	179,703	90,240	99,157	93,031	101,462
TOTAL LIABILITIES	10,188,203	8,785,462	9,733,002	7,376,186	5,736,449
NET POSITION					
INVESTMENT IN CAPITAL ASSETS	3,728,047	4,987,046	6,308,631	7,285,734	8,633,641
RESTRICTED FOR PROGRAMS	11,543,178	10,258,676	8,858,357	259,957	-
UNRESTRICTED	21,620,708	19,155,436	16,132,412	21,806,318	13,431,165
TOTAL NET POSITION	36,891,933	34,401,158	31,299,400	29,352,009	22,064,806
STATEMENT OF REVENUE, EXPENSE, AND CHANGES IN NET ASSETS					
REVENUES:					
CHARGES FOR SERVICES	46,586,236	47,206,980	44,742,494	40,773,899	33,971,834
OTHER	1,707,402	12,490	36,766	22,389	17,621
TOTAL OPERATING REVENUE	48,293,638	47,219,470	44,779,260	40,796,288	33,989,455
OPERATING EXPENSES					
SALARIES & FRINGE	12	159,209	932,348	885,172	836,219
CONTRACTUAL SERVICES	43,184,436	41,763,004	40,445,180	32,465,832	36,551,096
DEPRECIATION	1,326,045	1,321,585	1,335,652	1,361,190	1,360,745
INTERNAL SERVICES	1,195,334	880,959	205,192	186,523	197,425
OTHER	202,571	179,342	275,047	131,698	172,514
TOTAL OPERATING EXPENSES	45,908,398	44,304,099	43,193,419	35,030,415	39,117,999
NON-OPERATING REVENUE/(EXPENSES)					
INTEREST INCOME	105,535	186,387	303,650	1,521,330	400,735
CAPITAL CONTRIBUTION	-	-	57,900	-	-
CHANGE IN NET POSITION	2,490,775	3,101,758	1,947,391	7,287,203	(4,727,809)
BEGINNING NET POSITION	34,401,158	31,299,400	29,352,009	22,064,806	26,792,615
ENDING NET POSITION	36,891,933	34,401,158	31,299,400	29,352,009	22,064,806
INVESTMENT IN CAPITAL ASSETS PER CASH FLOW STATEMENT					
ASSET PURCHASES	67,046	-	358,549	13,283	34,725
CONTRIBUTED FROM OTHER SOURCES	-	-	(57,900)	-	-
NET INVESTED FROM FUND	67,046	-	300,649	13,283	34,725
OTHER USES OF FUND CASH					
ADVANCES				884,639	

EVERGREEN - FARMINGTON SEWAGE DISPOSAL SYSTEM FINANCIAL SUMMARY

	2013	2012	2011	2010	2009
BALANCE SHEET					
ASSETS:					
CURRENT:					
POOLED CASH & INVESTMENTS	10,442,984	14,767,052	15,751,784	17,912,380	14,090,409
ACCOUNTS RECEIVABLE	6,043,525	6,033,964	8,872,166	7,230,260	7,180,756
TOTAL CURRENT ASSETS	16,486,509	20,801,016	24,623,950	25,142,640	21,271,165
NONCURRENT:					
NON-DEPRECIABLE ASSETS	8,539,194	5,257,249	4,323,026	27,681	27,681
DEPRECIABLE ASSETS	13,710,524	14,563,400	15,416,276	16,269,152	17,122,028
TOTAL NONCURRENT ASSETS	22,249,718	19,820,649	19,739,302	16,296,833	17,149,709
TOTAL ASSETS	38,736,227	40,621,665	44,363,252	41,439,473	38,420,874
LIABILITIES:					
CURRENT:					
ACCOUNTS PAYABLE	269,162	690,466	91,997	142,899	41,193
DUE TO OTHER GOVERNMENTS	7,038,184	7,314,336	6,800,143	5,354,664	4,848,768
OTHER ACCRUED	221,951	135,929	499,137	752,608	138,041
CURRENT PORTION OF DEBT	235,000	235,000	135,000	-	-
NONCURRENT:					
LONG-TERM DEBT	5,375,915	3,916,226	3,925,000	-	-
TOTAL LIABILITIES	13,140,212	12,291,957	11,451,277	6,250,171	5,028,002
NET POSITION					
INVESTMENT IN CAPITAL ASSETS	16,638,803	15,669,423	15,679,302	16,296,833	17,149,709
RESTRICTED FOR PROGRAMS	7,175,188	11,231,478	12,399,486	-	-
UNRESTRICTED	1,782,024	1,428,807	4,833,187	18,892,469	16,243,163
TOTAL NET POSITION	25,596,015	28,329,708	32,911,975	35,189,302	33,392,872
STATEMENT OF REVENUE, EXPENSE, AND CHANGES IN NET ASSETS					
REVENUES:					
CHARGES FOR SERVICES	35,135,586	34,757,797	33,038,749	28,132,516	27,798,950
OTHER	86,143	346,424	18,894	5,737,792	113,134
TOTAL OPERATING REVENUE	35,221,729	35,104,221	33,057,643	33,870,308	27,912,084
OPERATING EXPENSES					
SALARIES & FRINGE	-	197,423	923,954	714,862	1,126,686
CONTRACTUAL SERVICES	36,471,998	37,150,136	32,958,710	27,591,661	31,014,621
DEPRECIATION	852,876	852,876	852,876	852,876	852,876
INTERNAL SERVICES	1,254,760	1,307,640	389,417	309,742	318,914
OTHER	90,259	136,374	182,634	79,839	138,631
TOTAL OPERATING EXPENSES	38,669,893	39,644,449	35,307,591	29,548,980	33,451,728
NON-OPERATING REVENUE/(EXPENSES)					
INTEREST INCOME	64,721	86,355	78,414	275,102	436,160
FEDERAL GRANTS	97,927	103,635	87,607	-	-
CAPITAL CONTRIBUTIONS	815,361	-	-	-	-
INTEREST EXPENSE	(263,538)	(232,029)	(193,400)	-	-
TRANSFER OUT	-	-	-	(2,800,000)	-
CHANGE IN NET POSITION	(2,733,693)	(4,582,267)	(2,277,327)	1,796,430	(5,103,484)
BEGINNING NET POSITION	28,329,708	32,911,975	35,189,302	33,392,872	38,496,356
ENDING NET POSITION	25,596,015	28,329,708	32,911,975	35,189,302	33,392,872
INVESTMENT IN CAPITAL ASSETS PER CASH FLOW STATEMENT					
ASSET PURCHASES	3,281,945	934,223	4,295,345	-	-
PROCEEDS FROM SALE OF BONDS	(1,694,689)	(226,226)	(4,060,000)	-	-
CONTRIBUTED FROM OTHER SOURCES	(815,361)	-	-	-	-
NET INVESTMENT FROM FUND	771,895	707,997	235,345	-	-

EVERGREEN-FARMINGTON RATE HISTORY

	2014	2013	2012	2011	2010
DETROIT RATES:					
FIXED	5.05	4.72	4.16	1.64	0.85
FLOW RATE	11.73	11.31	10.67	11.54	11.04
TOTAL DETROIT	16.78	16.03	14.83	13.18	11.89
WRC RATES:					
MAINT. & OPERATING	2.09	2.01	1.92	2.01	1.99
RESERVES					
EMERGENCY REPAIR & MAINT.			0.17	0.31	-
CAPITAL IMPROVEMENT PROGRAM	0.38	0.32	0.12	0.07	0.05
MAJOR REPAIR	0.39	0.38	0.31	-	-
SUBTOTAL RESERVES	0.77	0.70	0.60	0.38	0.05
DEBT SERVICE	0.33	0.32	0.22	-	-
MISC. REVENUE	(0.11)	(0.25)	(0.30)	(0.17)	-
TOTAL WRC	3.08	2.78	2.44	2.22	2.04
TOTAL RATE	19.86	18.81	17.27	15.40	13.93

GEORGE W. KUHN RATE HISTORY

	2014	2013	2012	2011	2010
DETROIT RATES:					
FIXED	5.84	5.40	4.72	3.06	2.22
FLOW RATE	9.00	8.68	8.77	8.98	8.85
TOTAL DETROIT	14.84	14.08	13.49	12.04	11.07
WRC RATES:					
MAINT. & OPERATING	0.53	0.56	0.55	0.85	0.82
RESERVES					
EMERGENCY REPAIR & MAINT.	0.07	0.07	0.26	0.25	-
CAPITAL IMPROVEMENT PROGRAM	0.16	0.16	0.07	-	-
MAJOR REPAIR	0.39	0.40	0.30	-	-
SUBTOTAL RESERVES	0.62	0.63	0.63	0.25	-
MISC. REVENUE	(0.19)	(0.21)	(0.20)	(0.07)	(0.06)
TOTAL WRC	0.96	0.98	0.98	1.03	0.76
TOTAL RATE	15.80	15.06	14.47	13.07	11.83

DRAIN BUDGET SUMMARIES

ACACIA PARK CSO DRAIN

	2014	2013	2012	2011	2010
SALARIES & FRINGES	132,140	133,483	139,481	175,000	175,000
UTILITIES	28,774	36,256	37,611	37,000	37,000
MATERIALS, SUPPLIES					
INSURANCE, & CONTRACTS	80,266	84,269	93,439	157,178	267,842
SEWAGE DISPOSAL	408,158	406,418	343,620	308,959	297,570
EQUIPMENT RENTAL	23,471	23,993	33,864	33,703	30,493
REPLACEMENT RESERVES	125,000	110,000	60,000	60,000	60,000
TOTAL BUDGET	797,809	794,419	708,015	771,840	867,905

RESERVE BALANCES @ 6/30/14	
CAPITAL IMPROVEMENT	152,767.10
MAJOR MAINTENANCE	111,154.23
CSO EQUIPMENT (MDEQ)	298,333.33
TOTAL	562,254.66

BIRMINGHAM CSO DRAIN

	2014	2013	2012	2011	2010
SALARIES & FRINGES	129,902	147,643	157,640	167,392	166,268
UTILITIES	44,762	46,503	42,768	51,274	44,000
MATERIALS, SUPPLIES					
INSURANCE, & CONTRACTS	94,390	81,265	90,798	192,219	241,746
SEWAGE DISPOSAL	474,808	481,401	537,270	359,367	340,080
EQUIPMENT RENTAL	23,861	24,828	27,607	39,410	37,097
REPLACEMENT RESERVES	99,000	100,000	72,000	72,000	72,000
TOTAL BUDGET	866,723	881,640	928,083	881,662	901,191

RESERVE BALANCES @ 6/30/14	
CAPITAL IMPROVEMENT	115,105.40
MAJOR MAINTENANCE	128,511.17
CSO EQUIPMENT (MDEQ)	396,000.00
TOTAL	639,616.57

BLOOMFIELD VILLAGE CSO DRAIN

	2014	2013	2012	2011	2010
SALARIES & FRINGES	198,768	178,743	179,974	208,748	195,607
UTILITIES	63,310	52,914	58,771	83,256	57,240
MATERIALS, SUPPLIES					
INSURANCE, & CONTRACTS	94,026	99,527	118,733	231,938	295,397
SEWAGE DISPOSAL	591,667	611,399	536,959	482,516	453,440
EQUIPMENT RENTAL	35,358	36,934	37,841	39,944	35,601
REPLACEMENT RESERVES	191,750	279,000	102,750	72,000	72,000
TOTAL BUDGET	1,174,879	1,258,517	1,035,028	1,118,402	1,109,285

RESERVE BALANCES @ 6/30/14	
CAPITAL IMPROVEMENT	167,571.71
MAJOR MAINTENANCE	21,764.52
CSO EQUIPMENT (MDEQ)	402,000.00
TOTAL	591,336.23

CITY OF BIRMINGHAM
HISTORY OF SEWER RATE COMPONENTS
FISCAL YEAR 2010-2014

COMPONENT SOURCE	2010	2011	2012	2013	2014
DETROIT CHARGE	$ 2.75	$ 3.43	$ 3.97	$ 4.29	$ 4.39
WRC CHARGE	0.54	0.55	0.53	0.64	0.67
CSO MAINTENANCE	1.22	1.50	1.30	1.37	1.52
CAPITAL IMPROVEMENT	0.53	0.58	0.58	0.59	0.58
CITY MAINTENANCE	1.62	1.76	1.80	1.88	1.85
TOTAL RATE	$ 6.66	$ 7.82	$ 8.18	$ 8.77	$ 9.01