

Setting Water Rates in Massachusetts: Important Lessons Learned from Suppliers

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Setting water rates is challenging, especially when balancing some or all of the following goals:

- Recovering all costs, including operations, long-term capital expenses, and debt service
- Distributing costs fairly among rate-payers
- Protecting affordability of water for essential needs
- Encouraging efficient water use and conservation

In August 2017, DER and DCR sent an online survey to MA water suppliers asking about their rate-setting experiences to better understand and support suppliers with this process. Based on the survey results we held follow-up interviews with seven suppliers to discern some of the key challenges of setting water rates and any lessons learned.

Interviewees included four town departments and three water districts that ranged in size, serving from 5,500 to 28,500 people, with annual budgets of \$0.8–5.2 million. All water suppliers had fixed charges with inclining block rates; two also used taxation to help finance water. Interviews included multiple personnel from each community, including politicians, water commissioners, department directors, superintendents, finance directors and treasurers, billing and IT staff, engineers, and environmental analysts.

Download the full report and find additional rate-setting resources:

<https://www.mass.gov/service-details/water-rates>

Key Lessons Learned

Communication. Routine, inclusive, and transparent communication, both internally among water utility staff and externally with customers and policy makers, was a crucial factor in rate-setting success. Good internal communication reduces surprises and silos across utility departments, and unifies and strengthens the utility's message around rates. Good external communication with elected officials and rate payers helps build trust in the utility, fosters understanding of the resources needed to maintain a water system, and creates support for sustainable rates.

Financial Planning. Suppliers who engaged in rigorous financial planning avoided surprises and were better able to address potential revenue deficiencies through informed rate increases. Those who developed multi-year plans were more confident in their financial projections and better able to communicate financial needs and justify rates to stakeholders.

Data Management. High-quality data (electronic, detailed, multi-year records) on customer water use, operational expenses, infrastructure maintenance, etc. can help suppliers better understand and anticipate changes in their system. Good data can also help suppliers assess how drought, seasonal variation, and pricing changes will affect consumption and revenues.

Governance. Water utilities operate under a variety of different organizational structures, which can influence their autonomy in financial planning and rate setting. Within any structure, there are steps suppliers can take to increase their ability to control financial planning and rate setting.

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Points of Guidance

Communication

- **Involve all utility departments in rate setting.** All-hands-on-deck meetings should be held throughout a rate-setting process to seek regular input from utility leadership, billing and environmental analysts (for insights on customer characteristics), finance personnel (to establish revenue requirements), and customer service staff (to discuss impacts of rate changes on customers). These meetings should help establish unified rate-setting goals within the utility well in advance of an external rate request.
- **Set clear internal priorities** of system improvement projects with specific costs and time horizons.
- **Communicate frequently with the governing body that decides rates**, including updates about current and projected operational and financial status. This strategy prevents surprises and builds momentum and buy-in for rate increases.
- **Use data and figures to communicate.** Utilities that used data and figures were better able to convince water commissioners of trends that necessitated rate increases.
- **Communicate frequently with customers** and solicit feedback from them on issues not only affecting their immediate water service, but also planned capital projects, conservation initiatives, public events, and rate increases. Using a variety of outreach methods (e.g., bill inserts and mailers, emails, social media, public events, schools) helps to reach diverse audiences. These efforts build goodwill towards the utility and understanding about rate increases.

Financial Planning

- **Create short- and long-term financial plans** that address operations and maintenance expenses, capital improvement costs, debt service payments, and reserve fund contributions. Plans should incorporate revenue predictions that reflect forecasted population changes and changing consumption patterns based on historical and current data. The most effective plans project a decade or more into the future with a detailed focus on the next several years.
- **Set prices that recover the full cost of water service** from each class of water user (e.g., residential, commercial, industrial). Not only does this ensure equity among ratepayers, it helps managers identify which parts of the system are most costly and ensure funds are available for their maintenance and replacement.
- **Maintain reserve funds** and regularly contribute to them. This reduces the need for abrupt rate increases.

Data Management

- **Analyze water consumption trends.** Evaluating how usage patterns are changing over time, using five to ten years of consumption data, can help suppliers identify trends and alert them to associated changes in revenues.
- **Use computer-based rate-setting models** that include all relevant data inputs, such as trends in population and consumption, capital funding plans, and current and future revenue requirements. Models can be developed in-house or by rate consultants.
- **Meter monthly or more frequently** to improve the precision of consumption and revenue projections for rate studies.

Governance

- **Create an enterprise fund** or equivalent. For utilities that are municipal departments, separating revenues and expenditures from other town departments facilitates financial planning efforts and allows managers to calculate the true cost of water.
- **Establish direct and frequent communication** with governing bodies. For utilities whose budgets and rates are determined by outside governing bodies, effective communication with these bodies can help utility managers earn trust and confidence in financial management decisions.
- **Incorporate as a water district.** While establishing independent water districts may not be politically feasible, where such districts are possible they afford a high level of financial independence and autonomy in rate setting.