

Communication 7h

TRANSMITTAL MEMORANDUM

TO: The Honorable Mayor & City Council

Initials:



FROM: Delilah A. Walsh, General Manager

File #: MGR25-118

DATE: February 20, 2025

Mtg. #: 02/20/25 NBh

RE: **Water Rate Analysis Reports**

Attached for your review are two documents:

1. The Water Rate Analysis report prepared by Michelle L. Johansen, Finance Director, in response to the City Council's request during the special budget meeting on December 16, 2024. As you recall, the Council directed staff to evaluate the feasibility of allocating the 2025 water rate increase towards usage, rather than a percentage increase across all rate classes, with a particular focus on addressing potential inequities within the fish processor and industrial customer class over residential users. The report provides an analysis of current water consumption data, revenue generation by customer class, and potential impacts of various rate adjustment scenarios. It also highlights the challenges associated with implementing a metered rate structure at this time, including data limitations and system capabilities. Three options are presented for your consideration, each with varying impacts on different customer classes.

2. A report from John Kleinegger, Water Division Manager/Project Engineer, dated January 15, 2025, providing a detailed analysis of the 2025 KPU Water Utility Operating Rates. This report examines water consumption by major users, including seafood processors, Vigor Alaska LLC, and cruise ships, and analyzes the financial implications of current rates. It also explores potential adjustments to residential rates and the reinstatement of fire hydrant billing. Mr. Kleinegger's report offers specific recommendations for rate adjustments and metering improvements.

Ms. Johansen and Mr. Kleinegger will be present at the February 20, 2025, City Council meeting to discuss the report and the proposed motion, and to answer any questions you may have. Staff is seeking Council direction on the preferred rate adjustment option in order to prepare the necessary rate ordinances for your consideration.

Recommended Motion:

I move the City Council direct staff to prepare the necessary water rate ordinances based on the Council's direction regarding the water rate adjustment options presented in the Water Rate Analysis report dated February 15, 2025, and discussed at this meeting.

MEMORANDUM
CITY OF KETCHIKAN, ALASKA
Finance Department
Office of the Finance Director

Michelle L. Johansen, Finance Director
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Phone: (907) 228-5621
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TO: Delilah A. Walsh, City Manager/KPU General Manager

FROM: Michelle L. Johansen, Finance Director

DATE: February 15, 2025

SUBJECT: Water Rate Analysis

During its special budget meeting of December 16, 2024, the City Council directed staff to evaluate allocating the 2025 water rate increase towards usage rather than a percentage increase across all rates. The City Council was particularly concerned about the inequities that exist within the fish processor and industrial customer class. The City Council directed staff to evaluate the current rate structure to determine if it can be adjusted to take the burden off residential customers.

The historical data available to date indicates the seafood processors and industrial customers account for approximately 30-50% of water processed through the water plant. Residential, Apartments and Commercial customer classes account for the other 50-70% water usage.

The total water production for 2024 was more than 1.5 billion gallons. We do not have consistent data for the 500 Business customers but based on the data we do have the consumption could be 165 million gallons or 1 billion gallons. We also know the Business customers account for 37% of the Water Division revenue while the Industrial/Cannery customers account for 16% of the revenue and Residential customers account for 46% of the revenue. The consumption data for the industrial and cannery customers amounts to approximately 313 million gallons or approximately 29% of total production. There are 8 customers that make up the industrial and cannery classes compared to 2,730 residential customers. While the residential customers base has the largest share of customers they are estimated to consume approximately 154 million gallons. This is less than estimated minimum consumption for business customers and half as much as industrial customers.

Seafood processors and industrial customers consume large amounts during their peak consumption months and the consumption fluctuates significantly depending on the customer. The fishing and fish processing industry has experienced significant decreases in the last few years, indicating there is no guarantee each of the seafood processors will continue operating in Ketchikan. Applying a rate increase to one class of customers, especially when that class of customers only has a handful of customers can have an adverse effect.

The significant variation of between business customers makes it difficult to start a metered rate structure and will likely need to be broken into more categories once the data is available. For example, grocery stores and hotels are likely to use more water than office buildings but how much is not known. Establishing a partially metered structure could unfairly penalize some customers while unfairly benefiting others. We need more data to establish minimum charges and additional charges once a customer exceeds the minimum.

The residential customer class is paying a higher share of the revenue when evaluating the consumption data available and assuming each residence is consuming an average of 4,000 gallons per month. The Water Division Manager has also made some good points regarding seafood

processors, the shipyard, cruise ships and hydrants. As a result, staff is providing three options for discussion purposes:

Option 1 – Increase Water Schedule B, C, D and G - 11.3% percent. This would increase the rates for services classified as Business, Industrial, Cannery and Miscellaneous only. The Residential customers will not see an increase under this option.

Option 2 – Increase Water Schedule B, C, D and G - 5.2% and bring back billing of fire hydrants over a three-year period. The Water Division Manager has identified hydrants that could be billed, offsetting the proposed increase Residential revenue.

Option 3 – Increase Water Schedule A - 2.5% and Water Schedule B, C, D, F and G - 8.0%. This option would increase the services classified as Residential 2.5% and Business, Industrial, Cannery, Hydrants and Miscellaneous 8.0%

The options listed above are expected to increase revenues approximately \$272,000 annually and \$181,000 in 2025 if implemented in April.

The following is a list of things to consider:

- Population – Ketchikan has a smaller population/customer base to share rate increases across and it is not expected to increase.
- Sustainability – Weighting increases to a certain class of customers can have a counterproductive effect. Consumption data is key to developing a strong rate structure that is fair to all classes. This data cannot be obtained until all the meters have been installed. Once the consumption data is available staff can evaluate how to set up customer classes that are sustainable across business categories.
- Capital needs – again the infrastructure replacement is a cost shared across the current customer base, Ketchikan's share compared to other locations is not equal to those locations.
- The City's utility billing system is currently not set up for a metered rate structure. My best estimate is a minimum of 4 months once we have the structure identified. Staff have contacted our software vendor but have not received an estimate of implementation time as of the date of this memo.
- In 2016, the City contracted with FCS Group to complete a rate study. The FCS staff that had the expertise to complete this are no longer available for consultation.
- If hydrant billing for the Ketchikan Fire Department is reinstated, there will be an increase in Fire Department costs in the General Fund. This can be mitigated by utilizing SEMT funds for EMS operations and relieving General Funds to pay the additional hydrant fees.
- Juneau announced it would be increasing its water and sewer rates 50% over the next five years and have already increased their water and wastewater rates 2.0% each of the last four years.

I will be attending the February 20, 2025 meeting to address any questions.



Memorandum

To: Delilah A. Walsh, KPU General Manager

From: John C. Kleinegger, Water Division Manager/Project Engineer

Date: January 15, 2025

Subject: **2025 KPU Water Utility Operating Rates**

Based upon the 2023 CAFR, KPU Water's total operating expenses were \$3,561,424. During 2023, KPU produced 1.518-billion gallons of potable water which is equivalent to an overall production cost of \$2.35/ 1000 gallons. During 2024, a similar amount of water was produced, 1.514-billion gallons, so very likely, the 2024 production cost will be a comparable amount.

Over the past 10 years, KPU Water has lost \$5,186,255, an average of over \$500,000 per year.

This is unsustainable and the question now becomes what other 2025 Water flat monthly rates in the KMC should be raised to reduce this continuing loss of revenue to the Water Division.

Seafood Processors

The major water consumers in 2024 include the three major Seafood Processors who together consumed 246,575,000 gallons of water, 16.3% of Water's annual production. At the probable production cost of around \$2.35/ 1000 gallons, this cost Water almost \$580,000 to produce and deliver to the Processors. The total 2024 revenue received for this amount of water from the three Seafood Processors totaled \$402,583 and represents net operating loss to Water of about \$177,000. To remain revenue neutral for Water, rather than the proposed increase of 3% in the 2025 KPU Budget, page D-3, for this rate classification, a 44% increase would be necessary.

In the Ketchikan Municipal Code, Seafood Processors – Schedule D provides for a minimum annual charge of \$67,628.48 for all water services sized three inches or greater. Each Processor has two large services meeting this criterion for an annual total amount of \$135,256.96. At the probable \$2.35/ 1000 gallons rate cost of production, this is sufficient funding that would supply each Seafood Processor annually with 57,556,000 gallons of water. However, neither Trident nor

Alaska General operated year-around in 2024 and only consumed 24,425,000 and 23,615,000 gallons respectively. By comparison, EC Phillips consumed 198,535,000 gallons. This continues to demonstrate the inequity of using flat water rates in Schedule D.

Vigor Alaska LLC Shipyard

Another major water customer is Vigor Alaska LLC's shipyard which consumed 47,319,000 gallons of water in 2024. At the probable 2024 production cost of \$2.35/ 1000 gallons, the cost to Water to produce and deliver this amount of water to Vigor Alaska cost \$112,000. At the monthly Industrial -Schedule C rate of \$3,956.26, Vigor Alaska was charged \$47,415 annually which represents a net annual loss to Water of \$64,500. However, rather than simply recommending an increase of the Industrial rate to all users, Schedule C also provides for a Special Contract monthly charge which is recommended below.

Residential Rates

As depicted on the attached page D-3 of the KPU's 2025 Operating and Capital Budget for Water, a 5.1% increase is proposed for General Domestic Water Service – Schedule A which is estimated to raise \$115,032. However, a proposal that has been discussed previously, is to instead reduce the present residential water rate now appearing in the KMC.

Based on a percentage reduction of the present Residential Rate, the following Table is presented:

Residential Water			Present	
			Annual	Net
	Present Flat	2024	Revenue	Reduction
	Rate/ month	Customers		
Ketchikan	\$68.75	2791	\$2,302,575	
5% Reduction	\$65.31	2791	\$2,187,446	\$115,129
10% Reduction	\$61.88	2791	\$2,072,318	\$230,258
15% Reduction	\$58.44	2791	\$1,957,189	\$345,386

If the proposed 5.1% increase is eliminated, and instead a reduction in residential rates is approved, the challenge becomes to identify a possible source of additional Water revenue that would offset the \$200,000 rate reduction and allow Water's Total Operating Revenue Amount to remain neutral.

Cruise Ship Rates

KMC 13.08.180 Water (a) establishes the fee for water servicing a vessel based upon its length. This fee is shared between the Port and Water; 25% to the Port and 75% of the revenue to Water. From the 2025 KPU Budget, page D-3, of the total 2024 revenue received from cruise ships of \$164,666, Water's share of vessel water deliveries was \$123,500.

The water volumes delivered to the cruise ships in 2024 were:

Berths 1 &2 (329 Spruce Mill Way)	6,992,000 gallons
Berth 3 (417 Water St.)	8,650,000 “
Berth 4 (90 Schoenbar Court)	<u>2,980,000 “</u>
Total	18,622,000 gallons

Based on the probable \$2.35/ 1000 gallons cost of production, the Water cost to produce and deliver water to the cruise ships in 2024 was \$43,760 resulting in a net income to Water of \$79,740.

Recommendations:

- 1. Seafood Processors.** All three Seafood Processors each have two separate water services already installed with mechanical water meters at their plants. Amend KMC 11.16.070 - Schedule D to include a rate per 1000 gallons with the proviso that in the event of mechanical meter failure, the minimum monthly charge of \$5,934.40 (includes the 5.3% proposed 2025 increase) returns until as such time as the mechanical meter is replaced or repaired. In addition, order new 6” & 4” Badger M-2000 Electromagnetic Meters and install these meters at each Seafood Processor.
- 2. Vigor Alaska LLC Shipyard** Create a special Schedule C rate for Vigor Alaska LLC of \$9,818.67 monthly which will recover both the probable 2024 cost of production and the already adopted 2025 budget increase of 5.2%. Information has been requested to determine if the existing 10-inch McCrometer meter installed at the Shipyard is compatible with KPU’s Cooper Power RFW-201 nodes and can be read remotely. If not, this meter will continue being read monthly.
- 3. Residential Rates** KMC 11.16.090 - Fire Hydrants-Schedule F-1, remains incorporated within the Ketchikan Municipal Code. It establishes a monthly rate for hydrants that are owned by the utility and whose sole purpose is to provide fire protection for the City. Although long established as a rate to be paid by the City to KPU, in the mid-1980’s, the monthly payment portion paid by the City to KPU was rescinded by motion of the City Council.

The present monthly rate in the KMC 11.16.090 for each hydrant is \$44.81. There are 412 hydrants located within KPU’s service area which are installed, owned, and maintained by the utility. If their earlier motion were to be now repealed by the City Council, on an annual basis, this payment for utility owned fire hydrants to KPU would be \$221,540. This would allow for a 10% decrease in the Schedule A - Residential Water Rate and have no impact on Water’s annual revenues.

Although Page D-3 of KPU’s 2025 Operating and Capital Budget does show Fire Hydrant revenue of \$36,700, this is the annual revenue from KMC 11.15.080 Fire Hydrants (privately owned)- Schedule F. These are hydrants that are also connected to the utility water mains and are maintained by the owner and/or user. Examples include the hydrants operated by the Borough located at the Ketchikan International Airport.

- 4. Cruise Ships.** While the sale of water to cruise ships 8- 10-years ago was in the 30 to 50-million gallons range, modern cruise ships have much improved their own individual water-making capability. In addition, the Norwegian Cruise Lines vessels and other ships that are now mooring in Ward Cove are no longer loading water in Ketchikan. The net result is, although the Port's delivery of water to the cruise ships is significantly reduced, the present rates established in KMC 13.08.180 are still producing a reasonable profit.