

## **Memorandum 11-094 Annual Budget for Water and Sewer Depreciation Reserves**

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**Memorandum Status:** Backup

MEMORANDUM 11-094

TO: Mayor Hornaday and Homer City Council

FROM: Walt Wrede

DATE: June 23, 2011

SUBJECT: Resolution 11-061 (A) (S)

Resolution 11-061 (A) (S) is sponsored by Council Member Roberts. Since the last meeting, a number of people have asked me to explain what the resolution means, what it actually does, and what impact it has, if any, on water and sewer rates. The amendments made at the last meeting may have added to the confusion for some. Resolution 11-061 (A) (S) addresses how transfers are made to the water and sewer fund depreciation reserve. This resolution can have an impact on water and sewer rates, but the impact is indirect. This will be explained below. The City's current practice is to establish the amount to be transferred into the reserves when the budget is prepared and approved. The amount of the transfer can be based upon a number of factors which include the amount transferred the year before, good business practices, the status of the reserve fund, fleet replacement schedules, auditor driven objectives, goals established by the Council, or other factors. Back in December, the Council approved a FY 2011 water and sewer budget which contained a \$500,000 transfer into the depreciation reserves. This is a larger transfer than some prior years and it reflects Council's desire to grow depreciation reserves across the board. It should be noted that the auditors would advise us to transfer significantly more. Since the water and sewer fund is operated as a special revenue fund, expenditures should not exceed revenues. The water and sewer fund is self sustaining which means that all revenues for maintenance and operations come from user fees (water and sewer rates). Transfers into the depreciation reserves are treated as an expense for the purpose of the budget and establishing water and sewer rates. This means that rates must be established that are high enough to cover all water and sewer operating expenses plus transfers into depreciation accounts. Therefore, the amount placed into depreciation is one of the big factors affecting water and sewer rates. During the workshops the past few months, Regina has illustrated that we will have an operating deficit or fiscal gap if we transfer \$500,000 and do not raise water and sewer rates or make additional large reductions in expenditures. The Council is under pressure to keep the rates the same or lower them if possible in order to let the economy recover and reduce the impact to utility customers. It is very difficult to keep rates the same for four years while all of the other fixed costs are rising every year; some dramatically. The Council is fortunate that the water and sewer reserve account is relatively healthy. This makes it possible to reduce the amount transferred to the depreciation reserve. If that occurs, it is possible to close the deficit and keep the rates at the same level they are today. Based upon prior discussions, Council appears to have two goals. First, it wants to do everything possible to avoid raising water and sewer rates. Second, it does not want to lose sight of the importance of depreciation reserves and wishes to guarantee that some reasonable transfer is made every year.

What Does the Resolution Do?

This resolution is a compromise which addresses both Council objectives. First, it states that at least \$200,000 must be transferred into depreciation reserves each year through the normal budget process. Second, it provides that any excess of revenues over expenditures at the end of the fiscal year will also be placed into the reserve account. If this resolution is adopted, it will make it possible for the Council to balance the budget and adopt water and sewer rates for the next two years that are the same as they are right now.

Related Resolutions **Memorandum - Related Resolutions:** [Resolution 11-061\(A\)\(S\) Setting Minimum \\$200,000 to Water/Sewer Depreciation Reserves Annually Through the Budget Process](#)

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