

# Town of Milton

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## **2013 WATER SYSTEM IMPROVEMENTS FINANCIAL CONSIDERATIONS**

The following provides an overview of the financial considerations related to the 2013 Water System Improvements referendum. The explanation begins with the broad view and ends with specific values that relate to possible outcomes of an approved referendum.

### Our Financial Partners

The federal Environmental Protection Agency (EPA) and State of Delaware Division of Public Health's Office of Drinking Water (ODW) work together to support the needs of public water utility systems. These systems are owned by both municipalities and private utilities. The type of support provided is both technical and financial. Both types of support require the allocation of a limited amount of funding.

The salaries and operations of the ODW are highly subsidized by the EPA. The annual funding from the EPA is based upon the performance of the ODW in the prior year. A significant aspect of this performance measure is good stewardship of the funding provided in the prior year. Grants from the ODW to recipients, such as the Town of Milton, are evaluated for their effectiveness in advancing public health and welfare. The most significant advances are those that involve capital improvements to the water systems. These capital improvements are most often financed through the State Revolving Fund (SRF) loan program.

Technical Assistance grants to recipient municipalities, therefore, are evaluated with respect to how the municipalities move forward on the professional recommendations that were funded by the grants. The ODW has the expectation that grantees will apply for a SRF loan. This expectation was part of the contract for our most recent grant – the Water Facilities Planning Update in 2012. The Town of Milton honored its contractual obligation by filing a pre-application for a SRF loan in 2012.

In 2007, the Town of Milton was the recipient of approximately \$20,000 for a Water Facilities Planning Grant. The grant resulted in a 2008 study that recommended certain system improvements. It did not proceed with a referendum until March 2012 – at which time the proposed borrowing was not approved by the voters. The referendum loss was indicative of the citizens' opinion that the town had not done its due diligence with regard to managing the water utility.

In 2012, the Town of Milton received \$7,415 for an engineer to update the 2008 study. And, it is anticipated that the town will receive approximately \$20,000 of technical assistance in 2013 for an update of the financial management of the water utility. EPA funding is the basis for these projects.

The ODW continues to monitor the progress of the Town of Milton's efforts to improve its water system. Their choice to partner with the Town of Milton has provided this town with significant financial assistance already. Because funding for ODW salaries and operations depends upon the effective use of EPA funds, the ODW is keenly interested in an outcome that includes a successful referendum and the use of SRF funds to finance water system improvements.

***2013 Water System Improvements  
Financial Considerations, continued***

Loan Applications and Estimated Costs

The Facilities Plan Update was presented to the Water Committee and, then, to the Town Council. The Town Council made the decision to file separate loan applications for the recommended system improvements. One application was made for the establishment of another well and treatment system, piping and control upgrades. A different application was made for another storage tank.

Both applications were rated favorably by the Office of Drinking Water. Subsequent to the release of the ODW Project List, the Council decided to move forward with the system improvements loan application, only.

The items detailed within the SRF loan application include estimated costs for the capital goods, construction services, engineering services and a reserve amount as a contingency for unanticipated events. The amounts listed in the July 2012 pre-application are the basis for the value in referendum ballot question. Changes in the scope of the project, since that time, have diminished the estimated total cost. The original and revised values are detailed below.

*July 2012 Pre-application estimates*

<b>Project Component</b>	<b>Estimated Cost</b>
Well #5 upgrade (supply south of Broadkill River and redundancy of treatment capabilities)	
Testing & Permitting	\$50,000
Well Pump Upgrades	\$250,000
Well Drilling	\$160,000
Well head, pumps & piping	\$120,000
Treatment Building Upgrades	\$250,000
Updated Control System	\$50,000
Interconnection with private utility	
Meter pit, control valve and connection piping	\$250,000
New Main to south side of town	
“Loop” from Wagamons to Federal St.	\$250,000
Engineering (at 15% of construction)	\$207,000
Contingency	\$138,000
Estimated Total Cost	\$1,725,000

The Town Council made the decision to remove an interconnection with a private utility from the project. This diminished the cost by \$250,000. The Town Manager instructed the engineer to incorporate recent control system upgrades into the project. This had the effect of further diminishing the cost. The repair of the foundation for the Shipbuilders’ tower was inserted into the January 2013 Budget Estimate that has been widely distributed.

*January 2013 Budget Estimate*

<b>Project Component</b>	<b>Estimated Cost</b>
Well #5 Upgrade	\$807,400
Water Main Loop	\$333,000
System Control Upgrades	\$50,000
Water Tower Foundation Repair	\$100,000
Estimated Total (incl. engineering & contingency)	\$1,703,328

***2013 Water System Improvements  
Financial Considerations, continued***

Loan Applications and Estimated Costs

It was determined that savings in the Water Utility account could finance repairs to the Shipbuilders' Tower foundation. Not only did this reduce the estimated cost of construction. It also reduced the engineering and contingency estimates – because these items are calculated as a percentage of the construction cost.

*March 2013 Budget Estimate*

<b>Project Component</b>	<b>Estimated Cost</b>
Well # 5 Upgrade	\$807,400
Water Main Loop	\$333,000
System Control Upgrades	\$50,000
Total Estimated Construction Costs	\$1,190,400
Engineering (@12% of construction)	\$142,848
Inspection (@5% of construction)	\$59,520
Construction Contingency (@ 15% of constr.)	\$178,560
Total estimated project costs	\$1,571,328

Loan Terms and Conditions

Drinking Water State Revolving Fund loans are financed through the sale of bonds. Both market conditions and the credit-worthiness of a borrower can affect the interest and terms of a bond. The State of Delaware provides a financial instrument to towns like Milton that those towns would not otherwise be able to get for themselves. Each year, the terms and conditions for SRF loans change, though.

Last year, the offering included a 35% “principle forgiveness” offer. This year, the principle forgiveness component was un-specified. Statements by the ODW that were repeated during public hearings related the fact that principle forgiveness might not be available and that there should be no expectation that loans would be reduced by any amount.

Two weeks ago, it was announced that a particular public water utility emergency would receive all funds that might have been allocated as principle forgiveness for SRF loans in 2013. While the possibility exists that future iterations of the SRF program may have a principle forgiveness component, there is no guarantee of that happening.

The approved ballot language specifies that the SRF loan would have an interest rate of 1.5% and be payable in installments over a twenty year period. There is no mention of principle forgiveness. Annual payments for the full estimated project cost (March 2013 Budget) would be \$91,523.16.

Project Timeline and Payback Options

At the February 26<sup>th</sup> Public Hearing, our engineer estimated that the project would take eighteen to twenty months to complete. The SRF construction loan is structured in a way that is very similar to a home construction loan.

First, a mortgage amount (maximum) is approved. As construction progresses, “draws” are taken against the loan to pay contractors and vendors. When construction is complete, a monthly repayment amount is determined. Considering the estimated project timeline, a start in May 2013 would result in a “known” monthly repayment amount in October 2014. Until then, there are just estimates.

**2013 Water System Improvements  
Financial Considerations, continued**

Project Timeline and Payback Options

The Town of Milton makes changes to the Fee Schedule during the Budget adoption process. These are made effective on October 1 of each year. The repayment of a loan for the purpose of making improvements to the water system must be done through the setting of rates and fees related to the use of that utility. If the referendum is approved, it is likely that there will be changes that will become effective in October 2014.

The discussion of what rates might change and how they would change has not occurred. The Town Council is empowered by the Charter to make changes in rates and fees. In order to further understanding of the subject, the following scenario has been developed. It is simply a “model”, though. The final outcome of rate discussions may change – just as the project cost estimate has.

And, similar to estimated costs, there are estimates that must be considered when developing a cost recovery model. In the third quarter of 2012 (when irrigation was still active), there were 1347 water accounts that used more than 500 gallons. The rate of new home additions is known to be 25 per year. So, at this rate, there will be approximately 1400\* customers on the system in October of 2014. (\*A previous estimate used the number 1280 customers. This was based upon trash billing – which does not include our commercial and irrigation water accounts.)

From October 1, 2011 through September 30, 2012 (our last fiscal year), approximately 88 million gallons of water was metered at the point of consumption (homes, businesses, etc.). The metering program is “capturing” more usage and the number of consumers grows. Customers are starting to take conservation measures, too. The figure used for 2014 estimated revenue from use will be the same as the 2012 fiscal year – just to be conservative. (Please note that 88 million is equal 88,000 thousand gallons. Charges are based upon thousand gallon units.)

<b>Type of Rate or Fee</b>	<b>Number of Units</b>	<b>Total Value</b>
Impact Fee for new homes to connect to the system - change from \$1,450 to \$1,950	Current rate of construction is no less than 25 units per year. An extra \$500 x 25 units is...	\$12,500
Availability Fee (a flat fee to cover fixed costs of utility operation) – change from \$35 to \$42 per quarter	Number of customers continues to increase. The current number is 1400. An extra \$6 x 4 quarters x 1400 is...	\$33,600
Usage Fee (the cost of consumption) changed from \$3 to \$3.52 per thousand gallons	The annual metered amount is 88,000 thousand gallons. An increase of .52 will yield...	\$45,760
<b>Total</b>		<b>\$91,860/year</b>

The average residential customer uses 46,500 gallons per year (some use less, some use much more). For the average customer, the combined effect of fixed and variable rates in a year is estimated at \$48.20, or \$12.05 per quarter (\$6 fixed cost/qtr. + 6.05 variable cost per quarter). Customers with larger households, pools and gardens may see a greater difference.

If the same type rate structure were used for a loan with ten or twenty percent principle forgiveness, the quarterly increase for an average residential customer would be from \$9.30 (20%) to \$10.58 (10%) – as opposed to the \$12.05 per quarter value listed above. All values are estimates and may change.