By Elizabeth Dietzmann, JD

Fiscal Conservativism Might Benefit Existing Customers, But Longer-Term, There's a More Chilling Effect

Many small towns and rural water systems seem to have fallen victim to a decrease in infrastructure development, which has been occurring in spite of stimulus funding. This is the subtle trend that will hamper economic recovery in rural areas. Rural water and wastewater system boards are conservative by nature and a tumbling economy and drastic decreases in new home starts have only solidified that tendency. This is especially true for systems with only one revenue stream, because these boards are reluctant to raise rates and expand when times are good – let alone when we struggle through the worst economic crisis since the 1930's. Unfortunately, this fiscally conservative approach, while it will benefit existing customers in the short term, will have a chilling effect on the long term economic recovery in rural areas and will also contribute to the continued shortfall in improvements in the national infrastructure that are so often cited. According to the American Society of Civil Engineers, which issues its annual report card on the nation's infrastructure, in 2009 America received a D- in both drinking water and wastewater. (I always notice that we get a higher grade in parks; in 2009 it was a C+ – because we all know that parks are fun and infrastructure is boring, right?)

According to the ASCE, as of 2009, America's drinking water systems face an annual shortfall of at least $11 billion to replace aging facilities that are near the end of their useful life and to comply with existing and future federal water regulations. This does not account for growth in the demand for drinking water over the next twenty years. Leaking pipes lose an estimated seven billion gallons of clean drinking water a day. Aging wastewater systems discharge billions of gallons of untreated wastewater into U.S. surface waters each year. The Environmental Protection Agency estimates that the nation must invest $390 billion over the next twenty years to update or replace existing systems and this does not account for growth either.

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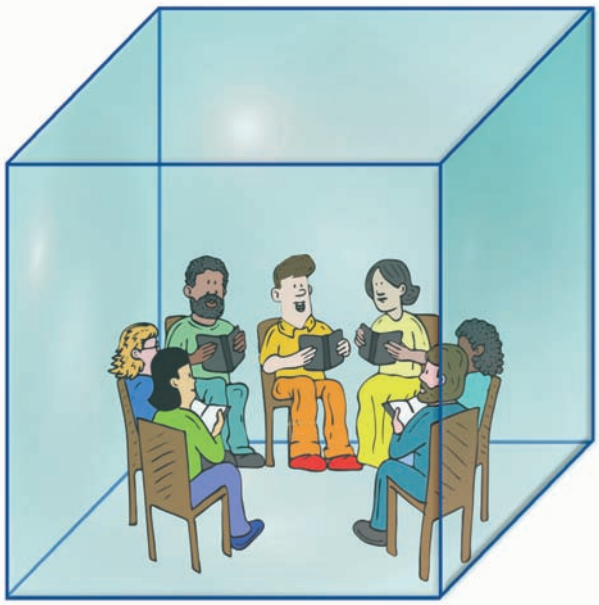
Two rural systems I know of are excellent examples of this rural reaction to the economic downturn. Per usual, the names are omitted. These systems are not to blame in any manner. Their boards are simply acting in a prudent manner in the short term, which appears to be logical and in the immediate best interests of existing customers. The problem is it will ultimately cost the systems more in the future to "catch up" and it will slow down local economic recovery.

System One

System One is really a classic type of rural water system. Even though it buys nearly half of its water from a neighboring city, it has struggled with territorial issues with this city for many years and it also needs infrastructure improvements. They have no full-time manager. They do have a dedicated board president who basically runs the district with the help of one field operations guy and one administrative assistant. The district is close to paying off its original USDA loan but faces subsequent loss of federal protection. The district is desperately in need of system repairs. The district has a vaguely worded agreement reached with the city twenty years prior that could cause the district to forfeit a lucrative nursing home client and subdivision once the USDA loan is paid off. There have been modest and

infrequent rate increases. Often there are not enough volunteers to fill the board vacancies. The system has about 1,500 customers, has one well as a water source and has been under constant pressure from state regulators to install another well or build an emergency interconnection. The system had lost some potentially lucrative blocks of new customers in recent years such as a prison and several subdivisions to the neighboring city because of an inability to provide expanded service. Several attempts at resolving territorial issues were stymied over the years by personality conflicts between the city and the district, a bizarre situation involving the conviction on drug charges and eventual disbarment of the city attorney, who had supported a territorial compromise, and the realization that the delineation of the district/city boundaries were jumbled and no one was really sure where city annexations had encroached into district territory.



Graphic by Vicky McCallum

Between 2005 and 2008 however, it looked like the district was making progress. The district had spent several thousand dollars on a much-needed map of its boundaries as well as the system itself. The map allowed everyone to sit down with municipal utility officials and realistically look at what areas each should/could serve and where past encroachments had taken place. The district had also spent several thousand dollars to promote passage of a revenue bond issue, which would allow it to pursue a new USDA loan. This certainly helped the negotiations with the city, which was much more willing to come to the table with the possibility of a new federal loan for the RWD on the horizon. The district had also begun preparation of a preliminary engineering report and started to develop a plan for system improvements, including a joint project with the city to drill a new well. The new well would have taken much of the regulatory pressure off of the district, allowed it to extend distribution lines to previously unserved areas and allowed it to share costs with the city as well as negotiate a favorable wholesale water contract as part of the overall deal. However, between 2008 and 2010, the mood shifted slowly but surely. While the city was willing to move forward with all of the plans (joint service agreement, wholesale water contract, shared well project) and the district was eligible for public funding, the water district board was increasingly unwilling to continue. Faced with the prospect of continued front-end expenditures in engineering and attorneys' fees and a reluctance to ask users to increase rates in order to service additional debt that would arguably benefit future customers, the board just decided not to proceed on any of the issues on the table.

The immediate impact on the district and its customers? Nothing really. However, the long-term effect will probably impact the district and growth in the area for many years to come. Realistically, the window for working out a compromise with the city is probably fairly narrow. A new utility director has subsequently taken over and it remains to be seen if the city's attitude towards territorial compromise will hold. The city will also move ahead with its plans for the new well and so the district could lose the benefit of a favorable wholesale water contract. One would hope that the city and the district could still work out an emergency interconnect agreement at a later time, but the other advantages of cooperative expansion are probably lost. In addition, some large new development such as a distribution center that might have occurred within district boundaries will go elsewhere, because the lag time in obtaining public funding and initiating a project from scratch is too long for developers to wait and other localities with available infrastructure will aggressively woo new commercial development away. So those construction dollars and long term jobs will not end up in the community. Short term it is a legitimate decision, but long term it will be a costly one.

System Two

System Two is a small municipal wastewater system located in a rural area on the edge of a large recreational lake. Interestingly enough, the city does not provide water service, which is handled by individual and shared wells dotted throughout the city. However, in order to protect those

wells and maintain the water quality in the lake, which draws the tourists upon which the city's economy depends, the city council decided to tackle its wastewater issues by constructing a wastewater treatment plant that would serve a key cluster of resorts and homes previously served by failing septic systems and small package plants. The process began in 2000 when the city first began exploring public funding. Eventually, it was determined that the city would handle construction in overlapping phases. The initial phase would be constructed with enough capacity to treat the core group of existing residential and resort users but would be designed so that it could be expanded and that additional capacity could be added as subsequent phases got underway. After a lengthy application process, in about 2005, the city received a combination of grant and loan funding for construction of the system.

The project was complicated. Although the cost of the first phase was relatively small (around $1 million), it involved, among other things, steep topography by disconnecting residents from septic systems and connecting them to a centralized collection system, and, coordination with the U.S. Army Corps of Engineers, that controlled wastewater discharges into the lake. In fact, the entire project went out to bid three times, because no bidders were able to comply with the bid specifications and stay inside the budget limits. However, by 2007, construction was started and the city had already begun preliminary work on the second and third phases, after numerous requests from residential users who were outside phase one but had failing septic systems. In addition, the city had entered into a public/private partnership with a local developer who wanted to connect a large new resort plus condos to the system. Under the terms of the agreement, the developer paid for additional capacity to be added to the treatment system and constructed the collection system for his project himself. The plan was for the collection system to be turned over to the city upon completion.

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The city was also moving ahead with funding for the next phases and was receiving numerous inquiries from individuals in those phases who had owned lots in the city but had been unable to build on them due to soil conditions. The city was also exploring creation of a water system which would incorporate and/or replace the patchwork system of existing wells. However, by the time the initial phase was completed in 2008, the economic climate had changed so dramatically that the city basically halted all further utility infrastructure plans. Even though existing residential users as well as new home builders were begging for construction of the second and third phases, and even though the city had spent the money to do the preliminary engineering work on those phases and received initial funding approval from the state, the city council was afraid to incur additional debt because of the poor economy. In fact, the city even reneged on its agreement with the developer and declined to take over ownership of the collection system from him upon its completion, because it did not want to spend money on maintenance.

It is true that the city council saved money in the short term by abandoning the additional phases. It did not have to spend money on engineering fees and attorney fees. And that will keep wastewater rates lower for the initial customers. However, the city has effectively halted all future growth and those people who can build new homes will be using septic systems instead of a centralized wastewater treatment system. This has a potentially negative impact on water quality in the wells and in the lake. This will also lead to future financial and political obstacles in order to require them to abandon a new septic system and connect to a city system. The city has also lost its place in the funding queue and will have to re-spend money in order to update engineering studies and reapply for public money in the future. Ironically, the developer who entered into the phase one agreement would like to expand his project into additional phases as well, but will be unable to do so because of the city's position.

No one who has ever served on a RWD board or town council can help but fail to appreciate the situations these systems are facing. A fiscally conservative approach now may be justified but unfortunately, these types of decisions will create delays and bottlenecks in future economic recovery and ultimately cost the systems more money later. Larger urban systems may have capacity to spare, but rural systems, which have traditionally expanded more cautiously, may be unable to meet demands for growth in a timely manner. And this could cause economic recovery to occur much more slowly in many rural areas. Weighing short-term savings vs. long-term savings is never easy, but I encourage rural systems to fully analyze the impact of these types of decisions and to look long term wherever possible.

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