University Neighborhood Housing Program

25th Anniversary Affordable Housing Forum

Water & Sewer Rate Reform Summit

Can New York City achieve affordable water rates, promote conservation, and control capital costs?

Thursday, April 10th, 2008

8:30—11:00 AM

Fordham University's Rose Hill Campus, The Bronx

Faculty Lounge, McGinley Center

Water & Sewer Rate Reform Summit

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Introduction

The link between affordable housing and the cost of water is not immediately clear to all New Yorkers. The connection between the cost of water and the affordability of housing became all too apparent to University Neighborhood Housing Program as we originated our first loan from our community development loan fund twenty years ago.

A review of the income and expense report of the building UNHP made its first loan to in 1988 showed that the expenses – specifically water and sewer costs – were prohibitively higher than expected. Bringing this cost down was critical as higher expenses would reduce the amount the building could borrow and in turn how much renovation work could be done. The building was billed on a frontage basis[1] for water (a flat-rate method), meaning higher than expected usage or a leak could not be the cause for the high water costs. The City's Department of Housing Preservation and Development (HPD), which was also involved in the deal, could not explain why the costs were so much higher than their own projected numbers. A call to the City's Department of Environmental Protection (DEP) eventually provided the answer; water and sewer charges had increased by 19% in 1988 and another increase was likely in 1989.

Twenty years later, water and sewer continues to be a topic of great interest to UNHP and many other providers and supporters of affordable housing. The urgency of addressing the cost of water and sewer service in New York is exacerbated by the rate increase projections of more than 11% for *each* of the next three years.[2] It is further amplified by the rising costs of fuel, taxes and renovation. While all areas of expense can be examined and management and construction practices should be improved to try to contain costs, water is one area where price can be directly affected by modifications in public policy.

UNHP understands that the issue is not merely controlling the price of the delivery of water in and sewage out. It is critical for New York to have a dependable source of clean water and that requires a substantial commitment of money for the City's water and sewer infrastructure. We also understand that the existing housing stock of New York is an equally important part of the City's infrastructure. Neither can be replaced and both require long-term capital commitments.

The goals of ample supplies of clean water and affordable housing must and can be balanced responsibly. As we mark our 25th year of affordable housing preservation and creation, University Neighborhood commits to working collaboratively with the private, nonprofit, and public sectors to achieve the goal of a safe, ample and affordable water supply for all New Yorkers.

1 Frontage was a water billing system where charges were determined by a series of set fees based on the size of the building (including the building's street frontage) and the number of water-using fixtures.

2 Rates are projected to increase 11.5% in FY2009, 11.4% in FY2010 and 11.3% in FY2011 according to DEP.

The New York City Water & Sewer System, 1985 – A Fundamental Shift

Until 1985, water rates were set by the New York City Board of Estimate and sewer fees were determined by the City Council.[3] As the City recovered from the fiscal crisis of the 1970s and the Koch administration sought the ability to finance major infrastructure improvements including housing, the City sought legislation to fundamentally change the way in which the water system in New York City was operated and funded.

In 1984, state legislation was passed, taking the direct responsibility for the provision of water and sewer services for the City of New York out of the hands of the City government and placing that control into the hands of the New York City Water and Sewer System ("the System"). By off-loading responsibility for the cost of supporting the System, the City was able to free general revenue money for other activities including increased borrowing for improvement of other infrastructure including affordable housing.[4] The newly freed-up city funds and borrowing capacity allowed the Koch Administration to announce a ten year, $4.2 billion housing program, an amount greater than the next largest 50 cities in the United States would spend combined over the same ten year period.[5] Ironically, a significant portion of the housing renovated under Koch's program is now threatened by rising water and sewer costs.

As described in its annual financial report, the NYC Water and Sewer System began operations on July 1, 1985 and is a joint operation consisting of two legally separate and independent entities, the New York City Municipal Water Finance Authority ("the Authority") and the New York City Water Board.[6]

The 1984 legislation empowered the Authority to issue bonds or notes to finance the cost of capital improvements to the System serving the City, and to refund any and all outstanding bonds and general obligation bonds of the City issued for water and sewer purposes. The Board of the Water Finance Authority is composed of seven members including the New York City Commissioners of DEP and Finance, the City Director of Management and Budget, the State Environmental Commissioner, and three public members, two appointed by the Mayor and one appointed by the Governor.

The same legislation empowered the Water Board to lease the System from the City, to set and collect rates, fees, rents and other charges for the use of the System. The Water Board is required to set rates at levels high enough to cover ***a)*** the operating costs of the system, ***b)*** the debt service for the bonds issued by the Water Finance Authority and ***c)*** a rental payment payable upon request to the City of New York. The Water Board is composed of seven members

3 Goldstein, Jared and Kolu Zigbi. "Saving Affordable Housing While Conserving Water: How poor people subsidize the rich in NYC's Water and Sewer System and what can be done about it." UHAB and ANHD, October 1993.

4 Von Hoffman, Alexander . House by House, Block by Block. New York: Oxford University Press, 2003.

5 Jonnes, Jill. South Bronx Rising. New York: Fordham University Press, 2002.

6 The Authority is a public benefit corporation created in accordance with the New York City Municipal Water Finance Act, duly enacted into law as Chapter 513 of the laws of 1984 of the State of New York, as amended by Chapter 514 of the laws of 1984 of the State of New York. The Water Board was created by Chapter 515 of the laws of 1984 of the State of New York.

appointed by the Mayor. The physical operation and capital improvements of the System are performed by DEP as part of contractual agreements with the Water Board. Similarly, the day-to-day staffing of the Water Board is provided by DEP. The Executive Director has historically been a Deputy Commissioner of DEP.

The impact of the transition to the new system was quickly felt by water rate payers ***(see Figure 1.1)***. Combined water and sewer costs went up 10.4% in FY1987, and was followed by increases of 17.9%, 2.9%, and 15.5% in the next three fiscal years. A mid-year hike in FY1990 resulted in an increase of 22.6%, and after remaining flat in FY1991 was followed up by an 18.4% increase in FY1992. Altogether, the cost of water & sewer went up 125% over just six years.[7]

Was Metering to Blame?

Many people thought the City's decision to implement a Universal Metering Program was the primary reason for the sharp rate increases. In 1985, the City Council passed legislation requiring meters in all newly constructed or substantially renovated buildings. Universal metering was subsequently included by the City in several consent decrees signed in response to state litigation. Due to concern about the impact of droughts on the City, the City Council passed legislation in 1985 requiring meters in all newly constructed or substantially renovated buildings. Universal metering was subsequently included by the City in several consent decrees that were signed in response to state litigation against the City for exceeding flows to several sewage treatment plants. Metering was presumed to result in conservation and less waste.[8]

Initial concerns with rising bills due to metering and problems with billing resulted in the creation of transitional programs that continue to allow many properties to remain on fixed-rate billing. The Transition Program, the Retroactive Transition Program, the Meter Billing Cap Program and the Multifamily Conservation Program were all established by the Water Board and DEP to ameliorate the impact of metering on affordable housing. DEP is preparing to launch a revamped version of the Multifamily Conservation Program (MCP) as part of another effort to bring owners of multifamily housing onto a metered bill or a capped rate through the MCP. While metering has resulted in higher costs in a number of buildings, the various temporary programs created to offer alternatives to metering have in most cases softened the impact of rising costs due to metering. UNHP has always held that the rising costs of water have less to do with metering and much more to do with the rate setting formula.

Data from the transition period indicated that metering led to lower-income areas with higher concentrations of people in residences paying more for water than higher-income and less

7 These numbers come from the Water Board website. DEP's Blue Books, published each year, offer a different history of increases. According to those numbers, an increase of 9.9% in FY1987 was followed by annual increases of 19%, 14% and 24.3%, 22.9%, 18.5% and 9.8%. According to these numbers, rates increased by 168% over six years.

8 Netzer, Dick, Michael Schill and Scott Susin. "The Impact of Water Metering on Affordable Rental Housing in New York City," Center for Real Estate and Urban Policy, March 2000, pg. 6.

dense areas.[9] Additionally, the ineptitude with which the metering program was implemented helped to support the notion that metering was the primary reason for higher bills. Former City Comptroller Elizabeth Holtzman in 1991 identified inefficient contract management as another part of the reason for the soaring costs at the Water Board. The Comptroller cited as an example one company with water meter installation contracts that was indicted for defrauding the City and for building code violations. The same report discussed under-estimating of costs and mismanagement of contracts negotiated by DEP for sludge management. The Comptroller showed costs to be 50% higher than DEP's projections.[10] Any additional expenditures due to mismanagement were (and continue to be) passed on to rate payers.

Increasing Expenses and Decreasing Funding

A number of other factors have played a more compelling role in the rising bills of rate payers in New York than metering. A Citizens Housing and Planning Council (CHPC) report issued in 1998 identified the rising capital costs and the resultant debt service that had to be borne entirely by the rate payers as the primary reason for the rising costs in the late 1980s and early 1990s.[11] CHPC contrasted the capital expenses of the system in 1983 which had been $608 million, with the capital commitments of the System in 1993 which amounted to $668 million. While the increase was less than 20%, there had been a drastic change in the source of funds for the System's capital work. In 1983, the System was directly responsible for 48% of the costs; ten years later, the System was responsible for 97% of the costs. The reason? Federal support for improvements in pollution control that had been mandated starting in 1972 with the Clean Water Act began to disappear in the 1980s. One such grant program had funded 75% of the costs of eligible projects under a federal water pollution control program during the '70s. The amount of the grant initially was reduced during the '80s and by 1988 the grant program had become a low interest loan program.[12]

In the early 1990s, new regulations and the mandates accompanying the 1993 Safe Drinking Water Act brought additional capital expenses to the Water System without any corresponding grant support. The 1997 Watershed Memorandum of Agreement among the City, State, EPA, upstate communities and environmental groups required the System to allocate funds to acquire land in the watershed area, issue and enforce watershed regulations and develop watershed protection programs in order to avoid filtration on the Catskill/Delaware watershed. Meanwhile on the Croton watershed, the City agreed to filtration. In 1999, the City authorized the construction of a filtration plant for the Croton system which, at the time, was estimated to

9 *Ibid.*
10 Holtzman, Elizabeth, "Who's Accountable for Soaring Water and Sewer fees?" December 1991, cited in "Saving Affordable Housing While Conserving Water." UHAB and ANHD, October 1993.
11 "Waterworld," The Urban Prospect. Citizens Housing and Planning Council, March/April 1998.
12 *Ibid.*

cost $900 million.[13]

The dramatic drops in federal support coincided with ballooning capital costs at DEP. For instance, DEP doubled its 10-year capital construction plan to approximately $16 billion in 2004.[14] In an April 2006 description of capital plan items, DEP included the Third Water Tunnel, upstate watershed programs, the filtration plant (now priced at $1.3 billion), and $579 million for an Ultraviolet Disinfection Facility for the Catskill and Delaware (Cat/Del) watershed.[15] By the next year, the updated 10-year capital construction plan totaled $23 billion, and included escalated costs at both the Filtration Plant ($1.6 billion) and the Ultraviolet Disinfection Facility ($828 million).[16] It is unclear why DEP's capital costs have risen so dramatically in such a short period of time.

Since virtually all of the money for these capital expenses will come from bonds issued by the Water Finance Authority, all of the costs will be borne by rate payers. Bond-financed expenditures result in debt service numbers that will continue to increase and take up a larger portion of System expenses. As recently as 2005, debt service accounted for just 54% of System expenditures ***(see Figure 1.2)***; in 2008 it will account for more than 80%.[17] The expense number itself is projected to more than double from 2007 ($722 million) to $1.56 billion in 2011.[18]

Paying Rent to the City

Unfortunately for the Water System and rate payers, the reduction in federal grant support and increases in mandated activities coincided with a severe City budget crisis in FY1990. One solution for the budget crisis was to take advantage of a provision in the 1984 legislation that created the Water Authority:

> *As per the agreement between the City of New York and the Water Board, the Board shall pay to the City, as a rental payment for the System, <u>but only to the extent requested by the City in each Fiscal year</u>, an amount not to exceed the greater of: a) the principal and interest payable on general obligation bonds issued by the City for water and answer purposes or b) 15% of the amount of the principal and interest payable on the bonds of the authority.*[19]

Until then, the City had never requested the full rental payment from the Water Board. With the budget crisis in 1990, the City for the first time requested and collected the entire rental payment of $180 million from the Water Board. This drastic action resulted in the only mid-year rate hike approved by the City Water Board in its 23 year existence, taking effect on January 1, 1990.

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13 "The Impact of Catskill/Delaware Filtration on Residential Water and Sewer Charges in New York City." New York City Independent Budget Office, November 2000, pg. 3.
14 DEP Blue Book, 2004.
15 DEP Blue Book, 2006.
16 DEP Blue Book, 2007.
17 *Ibid.*
18 Niblack, Preston. "Re: DEP." Email to Jim Buckley. March 25, 2008.
19 "Agreement of Lease By and Between the City of New York and New York City Water Board," July 1, 1985 and amended November 1, 1985, pg. 10.

The Water System has used the rental payment to show the financial strength of the Water Board. By keeping the rental payment at 15% of the amount of debt service paid on the bonds of the Water Finance Authority, the authority shows a healthy debt service coverage ratio. Sufficient debt service coverage enables the authority to protect its strong bond rating and maintain a lower interest rate.

When the rental payments started in full (as they continue to be requested each and every year since 1990), the entire amount was used to cover debt service payments for General Obligation Revenue bonds that were attributable to the Water System. In 2005, the City's old General Obligation Revenue bond debt had amortized to the point that the rental payment exceeded the debt obligation of the City by $23 million. That excess of $23 million went into the City's general operating budget. By FY2008, that excess number had increased to $76 million.[20]

In the past two years, Comptroller William Thompson and several City Council members have proposed that the rental payment be examined as a way to hold down rate increases. In 2007, that proposal was ignored by City Hall. As noted by Comptroller Thompson in his 2007 proposal to contain rates by re-allocating the excess rental payments, the debt service obligations of the Authority will grow and so will the rental payment to the City unless there is a change in City policy. Comptroller Thompson's proposal showed that if the status quo holds ***(see Figure 2.1)***, rate payers will be subsidizing the City's general operating budget between 2008 and 2036 by more than $8 billion.[21] The City Council extracted a commitment from the Mayor to discuss the rental payment as part of a Memorandum of Understanding. The Mayor agreed to the MOU as part of the negotiations with the City Council to pass the lien sale legislation. Lien sales were proposed by DEP and supported by the Mayor in order to enhance collections and are outlined in the next section.

Threat of Mid-Year Rate Hike Leads to Lien Sale Legislation

In 1996, the City enacted legislation that allowed the City to sell liens on properties that owed more than one year's worth of taxes. A companion piece of legislation was an act creating the Third Party Transfer Program, which allowed the City to pull distressed properties from the lien sale list, foreclose on the property and transfer it to a private third party.[22] In 2006, the lien sale legislation expired and City Hall launched an effort to amend the legislation and renew it. A major part of the negotiations related to unpaid water bills. The City wanted the ability to sell water liens on property that did not owe one year of taxes; these liens are referred to as "stand-alone" water liens.

DEP felt that some rate payers were staying current on their taxes and ignoring their water

20 Letter from NYC Comptroller William Thompson, Jr. to the Water Board, May 11, 2007. *Note:* While the data is now somewhat dated, it is the most recent available.

21 *Ibid.*

22 The Third Party Transfer Program enabled the Local Initiative support Corporation and the Enterprise Foundation to establish a non-profit entity to take title to properties known as Neighborhood Restore HDFC.

bill because they knew the City had no enforcement mechanism to collect the water bill alone. By early 2007, DEP showed $589.6 million in unpaid bills.[23] At a Water Board meeting in the Fall of 2007, DEP officials said the passage of amended lien sale legislation which allowed "stand alone" water lien sales would bring $200 million into the system.

DEP indicated that their collection rate was approximately 85% of water bills issued and that the non-payers, or "deadbeats" as they were referred to in the press, were responsible for the soaring rates. To gain City Council support for the lien sale legislation, DEP proposed a mid-year rate increase of 18% for January 1, 2008. In December, the City Council passed the lien sale legislation with the provision that stand-alone water liens on buildings with two or more units could be sold. The MOU between the Mayor and the City Council included a commitment that the Water Board would not proceed with the 18% increase.

Single family homes were exempted from lien sales but did not escape an enforcement mechanism. In the Fall of 2007, the Water Board approved resolutions to implement a water shut-off program for single family homes. In January 2008, over 8,000 such homes that owed DEP more than $1,000 for longer than a year received an ultimatum from the City: they could settle their bills at a discount with the newly created Payment Incentive Program (PIP) which eliminated late payment charges and capped the back water charge at $2 per day for the unpaid time period, or they could have their service shut-off. As this publication goes to print, approximately half of those homeowners had come forward and either paid their bill or made some kind of arrangement with the City. Meanwhile, DEP has issued the first two rounds of shut-off notices.

UNHP and non-profit homeownership programs have raised concerns about the shut-off program since the buildings were heavily concentrated in neighborhoods with high concentrations of sub-prime lending and foreclosures.[24] Our own analysis of the shut-off list from DEP showed that more than 15% of the 600 Bronx homeowners who remained in danger of shut-off in mid-February were actually already in foreclosure. The numbers were even more striking for the 2,200 2-4 family homeowners in the Bronx who were on the 90-day lien sale list in early March solely for water bills – nearly 20% of them were already in foreclosure.[25] DEP staff have stated that properties in foreclosure will be pulled from the shut-off list; homeowners in danger of foreclosure will have to come forward and document their situation to stop the turn-off procedure.

DEP staff has stated that these new collection weapons—the lien sale and the shut-off program – should improve their collection rates to 95% of the billed amounts. This improvement, along with reducing borrowing costs by controlling capital expenditures and reducing expenses by renegotiating the rental payment, represent the Water Board's only options for controlling rates under the current system.

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23 Booz, Allen, and Hamilton. "NYC DEP Bureau of Customer Services (BCS) Best Practices Customer Service Model Design Project Report." October 22, 2007, pg 50.

24 A map presented by DEP showed the concentrations of potential shut-offs in the same neighborhoods that have the highest concentrations of sub-prime lending and foreclosures, namely southeast Queens, central Brooklyn and the northeast Bronx.

25 Our analysis compared lists provided by DEP with *lis pendens* data from Profiles Publications.

The Impact on Affordable Housing Preservation:

Office of Management and Budget (OMB) Director Mark Page was very clear in City Council hearings in the Fall of 2007 prior to the passage of the lien sale legislation that OMB does not want to surrender the excess payment. Clearly, the declining financial projections of the City will not make the case for returning the rental payment to the Water System or passing some of the costs of the system over to the City general operating budget easier. The ideal time to make this change would have been in the past several years when finances were significantly stronger in the City. However, continuing to collect the rental payment will have a deleterious effect on the City's affordable housing preservation work.

For almost 20 years, affordable housing providers and several lenders have participated in efforts to highlight the impact of the cost of water on affordable housing. After initially ignoring the impact of water costs on housing, DEP and members of the Water Board began to understand that water pricing could have the unintended consequence of driving affordable housing into financial distress. The Retroactive Transition Program and other DEP programs have made allowances for multifamily buildings that resisted the switch to metered billing. According to a paper produced in March of 2000 by the Center for Real Estate and Urban Policy, a significant number of buildings would experience substantial increases in water and sewer bills due to metering. If transitional caps on water bills were lifted, approximately 9,000 buildings would have increases in annual bills of over $200 per unit per year in the short run and more than 3,700 buildings would experience similar increases in the long-run, even without rate increases.[26]

The paper went on to confirm another finding from the 1991 Holtzman report, stating that "while metering will bring about a reduction in water and sewer bills for buildings in census tracts with low poverty rates, it will lead to substantial increases in neighborhoods with high poverty rates." Moreover, the report stated that extremely large increases in bills could be anticipated in formerly City-owned housing that had been substantially renovated with public subsidies.[27] Properties in these neighborhoods house more people per unit due to larger family sizes, are of older housing stock, and often underwent only moderate renovation meaning plumbing systems were never completely updated.

The creation of the Retroactive Transition Program to allow buildings to be metered (but still pay on a per unit basis) was an acknowledgment of the Water Board's and DEP's awareness that a fully metered Water System would have a drastic impact on a significant percentage of housing in New York City. Ultimately, DEP created the Multifamily Conservation Program to encourage owners to agree to be metered and have the safety net of a capped bill. The program is currently being revamped since very few buildings initially qualified due to restrictive DEP guidelines. DEP would like to have all buildings either billed on a metered basis or in the MCP by

26 Netzer, Dick, Michael Schill and Scott Susin. "The Impact of Water Metering on Affordable Rental Housing in New York City," Center for Real Estate and Urban Policy, March 2000.
27 *Ibid.*

July 1, 2009. The program would be available to owners that would be hit with higher bills based on a metered program as long as they meet other water conservation requirements identified by DEP.

Paying More than Their Fair Share

Data from the Rent Guidelines Board Income and Expense Study ***(see Figure 2.2)*** support claims from the Center for Real Estate and Urban Policy's 2000 report as well. Lower income parts of the City (the Bronx and Upper Manhattan) pay more for water per apartment, while higher income parts of the City (Core Manhattan and Queens) pay less per apartment.[28] Through this lens, households in low-income parts of the City not only pay more to support the Water System, but pay a much higher percent of their income to do so. Thus water costs as a percent of median household income in Staten Island, Manhattan and Queens are comparable to such low-water-cost cities as San Jose, Indianapolis and Honolulu ***(see Figure 3.1)***. The Bronx, the borough with the lowest median income in the City, compares with higher-water-cost cities such as Newark and Boston, even without accounting for the fact that water bills are higher in the Bronx than they are in other boroughs. In the west Bronx neighborhoods that supply a huge chunk of the affordable rental units in the City, water costs account for about 3% of household income, above Cleveland and only below Atlanta and Philadelphia.[29] The double-digit increases that are predicted over the next three years will place an even heavier burden on the low-income parts of the City. This is true for both homeowners who pay the rates up-front and renters who will eventually pay for water through larger rent increases approved by the Rent Guidelines Board as a result of higher operating costs.

The NY Equity Fund which is involved with a portfolio of more than 25,000 units of housing primarily rented to households making less than 60% of the area median income and located in Brooklyn, the Bronx and Manhattan, recently analyzed a sample of their buildings' water expenses. In their portfolio, water and sewer costs were $633 per apartment per year in 2006.[30] Factoring in the 11.5% increase in July 2007 and the projected increase of 11.5% for FY2009, these apartments should be anticipating water and sewer charges in excess of $780 annually per apartment starting on July 1, 2008. This kind of increase will have a major impact on the efforts to maintain and preserve these affordable units.

A similar analysis of a set of community-controlled affordable buildings in the west Bronx showed that water rates for 2006 averaged $708 per unit ***(see Figure 3.2)***, compared to the $625 per unit for all New York City multifamily dwellings cited by DEP.[31] These buildings were billed on a

28 Housing NYC: Rents, Markets and Trends 2007. Rent Guidelines Board. Appendix C.1.

29 New York City income data is from the 2005 Housing and Vacancy Survey; All other data is from the 2007 DEP Blue Book.

30 NY Equity Fund Data

31 Data for all New York City multifamily dwellings is from the 2007 Blue Book. The west Bronx community-controlled housing sample includes 702 units in 27 buildings owned and/or managed by local nonprofit housing organizations.

metered basis since they were ineligible for the existing transition programs and the MCP under its existing guidelines. Based on this figure and the actual and projected rate hikes for the coming years, affordable housing owners and managers will be facing annual water bills approaching $1,100 per unit by FY2011.

Many existing projects will struggle to meet the bottom line with the rising cost of water. Operating expenses will claim a larger share of an already slim budget that includes other competing needs for maintaining quality housing and preserving affordability for low income tenants. As for new affordable housing projects, increased amounts of City subsidy will be necessary to defray these rising operating costs. Additionally, these increases will put even more pressure on owners of privately held rent stabilized stock to raise rents through whichever means they are employing. If the trend towards stagnating wages continues, rising water rates will adversely affect the affordability crisis in New York City.

Similarly, water cost increases will negatively impact the foreclosure crisis among 1-4 family homes in the City. The percent of homeowners in New York City who pay more than 60% of their income on housing costs jumped from 14.3% in 2002 to 16.6% in 2005. In conventional homes, the percentage also went up, from 15.9% in 2002 to a staggering 19.2% in 2005.[32] With the recent rise in sub-prime and adjustable rate mortgages, coupled with increased water and fuel costs, these numbers are likely significantly higher in 2008.

Immediate Action Needed

While the projections for the City's budget are not good, the time to reform the way we pay for the Water System is now. Ignoring the problem will compound City budget issues. Double-digit rate increases for the foreseeable future will have a negative effect on affordable housing in New York City and low- and moderate-income neighborhoods. Soaring rates will contribute to deterioration and foreclosure in both the single- and multi-family housing markets. If unaddressed, the demands for additional financial support for foreclosure prevention from the City will increase, and the underwriting on multi-family renovation will change dramatically either slowing or stopping renovation plans by increasing the amounts of subsidized dollars necessary to proceed with renovation and construction. In short, we can recognize and address the problem proactively or we can wait for the situation to reach crisis proportions and fix the problem over the devastated remnants of the dreams of homeownership and neighborhood development. Either way, the City general operating budget will have to pay the price.

We have developed a series of proposals that would address the water and sewer crisis that can be implemented immediately:

1) **Reject any rate increase proposal for FY2009**: While we do not believe the ultimate answer can be in place for the Spring ritual of rate setting that has already begun at DEP and the Water

32 2002 and 2005 Housing and Vacancy Surveys

Board, we do feel that immediate relief is necessary. The Water Board should reject DEP's projected rate increase for FY2009 based on the improved collections promised by DEP based on lien sales and improved collection practices. The improved collections combined with lien sale proceeds should allow the system to hold the cost of water at FY2008 numbers.

2) **Return the excess rental payment**: The rental payment that exceeds the debt service of the old General Operating Revenue bonds should be returned to the Water System in such a manner that the bond rating is maintained. In May of 2007, the Comptroller made such a proposal with a formula that would use some of the funds to reduce rate increases with the remainder covering construction costs to lower the amount borrowed by the system, resulting in lower long term debt service numbers.[33]

3) **Make water and sewer billing information accessible:** Real estate tax, violations, building registrations, ownership and mortgage information are all available on-line with either the building address or block and lot numbers.[34] Water and sewer bills continue to be publicly accessible online only with account numbers. Benefits of making water and sewer information as accessible as tax information would include providing tenants a chance to see if their landlord is staying current, owners an opportunity to check their billing status easily, lenders a chance to identify properties in their portfolio at-risk for lien sales, and homeownership preservation counselors an opportunity to identify homeowners in potential difficulty.

4) **Continue to implement improved collection practices:** DEP has begun to implement a number of recommendations to improve collections and to make the agency more rate-payer friendly. In conjunction with the Payment Incentive Program and the impending lien sales and shut-offs, DEP has taken a number of steps to get out into the community with information and answers to questions. These efforts should be maintained and expanded.

5) **Impose a moratorium on shut-offs:** The timing of the implementation of the shut-offs is extremely poor. While the affordability crisis worsens and we find ourselves in the midst of a foreclosure crisis, the City's broad-scale response is still not fully operational. While the Center for New York City Neighborhoods will coordinate and fund the expansion of foreclosure prevention work throughout the five boroughs, it is not yet staffed and is thus unavailable to assist in ensuring that homeowners in foreclosure or on the verge are not targeted for shut-offs. DEP should hold off on turning off water service until the Center is able to assist in the process,

33 Letter from NYC Comptroller William Thompson, Jr. to the Water Board, May 11, 2007. <http://www.comptroller.nyc.gov/press/pdfs/05-14-07_Water_letter.pdf.>

34 Real estate tax and other charges are available on the Department of Finance website; building registration and housing code violations are available on HPD's website; deed and mortgage information is available on the Automated City Register Information System (ACRIS) website.

and until the implications and costs of shut-offs are fully understood. In other cities, turning off water to a home costs between $35 and $100 and is as simple as turning a valve;[35] in New York City, turning off water service requires digging up the street, risks damage to other pipes, and results in health violations, all of which will likely cause the City to spend more on the shut-off than the amount of the outstanding bill.

6) **Proceed with plans to revise the Multifamily Conservation Program:** DEP has worked with real estate organizations to get constructive feedback on re-design of the MCP. Buildings such as those that make up the west Bronx Community Controlled Housing sample need to qualify for this program. The revised program with accessible criteria should be rolled out as soon as possible. DEP has already agreed to publicize the program and make information and applications as accessible as possible.

7) **Enact toilet rebate and other conservation incentive programs**: DEP has had plans for several years to re-institute a Toilet Rebate Program. UNHP supports the concept and suggests that dual flush toilets be included in the program and that the program should be enacted now. In the longer term, UNHP supports rebates, annual credits or other incentives to reward conservation efforts. Water saving toilets, shower heads and other fixture and system wide upgrades result in widespread water conservation benefits. Water conservation under the current rate setting structure leads to the need for higher rates to offset the loss of revenue to the system. A method for encouraging conservation through incentives should be created by DEP in the near future.

Longer Term Fundamental Change

The next set of recommendations reflect the need for carefully planned fundamental changes to the rate setting system that should be developed with the participation of the private, nonprofit and public sectors. Other changes reflect the need for the return of federal participation in water infrastructure and environmental projects as well as the need for system oversight, transparency and an essential shift away from the assumption that the total burden of cost must be borne by the rate payer. These changes will take longer to develop and implement, but planning and analysis should begin immediately.

1) **Examine proposals to invest more general operating revenue in the system:** There are certain construction items that are clearly distinct from the delivery of water to and removal of sewage from buildings. Specifically, the "Combined Sewer Overflow" (CSO) project is needed to address sewage overflow caused by run off from heavy rainstorms which currently results in untreated

35 Booz, Allen, and Hamilton. "NYC DEP Bureau of Customer Services (BCS) Best Practices Customer Service Model Design Project Report." October 22, 2007, pg 57.

sewage going into rivers and harbors.[36] The CSOs consist of building underground tanks to catch and hold storm overflow until it can be pumped at normal flow times for treatment in sewage plants. CSOs account for $1.5 billion of the current $23 billion capital plan.[37] Streets, parks, airports, etc., all contribute to making the CSO necessary. Debt service related to CSO projects of the Water Board should be moved to the City's general operating budget. Likewise, the City should increase its contribution to the Water System for water use to be comparable to the typical rate payer.

2) Oversight of the System and its capital needs: The Water Board operates with minimal public attention. The Board, composed entirely of Mayoral appointees, reviews budget and construction plans developed by a department headed by a Mayoral appointee. Since 1984, the main check and balance on the Water System has been the competence of the Water Board members and DEP staff. In 1991, then-City Comptroller Elizabeth Holtzman talked about the isolation of the Water Board from the public in a report entitled "Who's Accountable for Soaring Water and Sewer Rates?" The report states,

> *There is no incentive to hold down DEP's water and sewer spending because neither the administration nor the City Council has to propose tax increases to pay for those activities….The system works like a cost-plus contract—DEP has little incentive to control cost because rates charged to the public are automatically set to cover expenses.*[38]

In 2008, there is acknowledgment of the rising costs to the rate payer, but sympathetic approvals of rate increases do not lessen the impact of the rising rates. While the concern of the Board members and DEP staff is undoubtedly real, it does not provide enough incentive to give the public assurances that DEP and the Board are in fact doing everything that can be done to hold costs down. The City's Independent Budget Office (IBO) cites ballooning construction costs as part of the reason for the rising costs of projects like the Catskill/Delaware Ultraviolet Water Treatment, which is estimated at $1.5 billion in the Mayor's Preliminary capital budget for 2009, a 35% increase from the previous Mayoral Capital Commitment Plan.[39] But rising construction costs alone cannot be blamed for all the increases over initial estimates. For instance, a review of IBO reports shows the construction costs on the controversial filtration plant for the Croton system being constructed in Van Cortlandt Park in the Mosholu section of the Bronx had been originally estimated to be $900 million;[40] that estimate increased to $1.4 billion by 2004[41] and

36 Lenzer, Anna and Jarrett Murphy. "Water Pressure: Facing the challenge of New York's endless sewage spill." City Limits Investigates Summer 2007.
37 McCarthy, John. "Testimony to NYC Water Board." April 2007.
38 Holtzman, Elizabeth, "Who's Accountable for Soaring Water and Sewer fees?" December 1991, cited in "Saving Affordable Housing While Conserving Water." UHAB and ANHD, October 1993.
39 "Analysis of the Mayor's Preliminary Budget for 2009." NYC Independent Budget Office, March 2008, pg 55.
40 "The Impact of Catskill/Delaware Filtration on Residential Water and Sewer Charges in New York City." New York City Independent Budget Office, November 2000, pg. 3.
41 "Analysis of the Mayor's Preliminary Budget for 2005." NYC Independent Budget Office, March 2004, pg 88.

$2.4 billion by late 2007.[42] Opponents of the construction of the filtration plant felt that less capital intensive methods of filtration were not given serious consideration.[43] In a system without checks and balances, people cannot have confidence that an objective evaluation of alternatives has been conducted. Finally, the sudden drop in allocation of capital expenses for mandated projects from 70% to 50% raises questions about the justifications for some of the construction items in the capital plan.[44] UNHP recommends the creation of a third party method of evaluating the DEP budget, proposed rate increases and the construction needs of the Water System.

3) **Open the doors on the rate setting process and the Water Board:** Recent improvements in public access to information about the Water Board must be noted. The System recently set up a website for the Water Board which includes notices about public meetings, minutes and resolutions, the names and photos of the Water Board members. However, the board and the process are still shrouded in mystery, despite the fact that the System handles $2.2 billion dollars,[45] and has the second largest capital budget in the City.[46] On an annual basis, the Water Board issues their rate proposal in a document called the "Blue Book." The Blue Book provides an explanation of proposals including the justification for the proposed increase. Much of the information in the Blue Book is not useful without both a historical context and projections for the future. In order to note the rising costs of construction projects like the filtration plant, one needs to have established a collection of old Blue Books. To get useful feedback from the public, useful information needs to be made easily available. To start with, the Blue Book should include the past two years' information and the projections should be for three years.

4) **Expansion and simplification of water reuse programs**: Water reuse upgrades provide broad reaching benefits to NYC's water system as a whole by reducing the sewerage overflow and its associated costs, both financial and environmental. DEP has created the Comprehensive Water Reuse Program,[47] that if simplified and expanded could provide incentives to substantially reduce water and sewer charges on buildings that install rain water harvesting systems, street trees, porous pavements, gray-water systems, green roofs and/or other proven methods that reduce overflow. DEP should move to simplify and expand its program to include proven methods of water reuse and reward these improvements with credits, rebates or discounted rates. This type of program could be an important green addition to the Mayor's 2030 plan.

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42 "Croton Filtration Plant Budget Summary." NYC Independent Budget Office, December 2007, pg 1.

43 For a comprehensive look at the battle by neighborhood residents against filtration, including at the final site in Van Cortlandt Park, see the Norwood News archives at <www.norwoodnews.org>

44 DEP Blue Books, 2006 and 2007.

45 DEP Blue Book, 2007

46 "Analysis of the Mayor's Preliminary Budget for 2009." NYC Independent Budget Office, March 2008, pg 55. *Note:* School construction ranks first at $12 billion, Water and Sewer second at $11.5 billion, and transportation third at $7 billion. Of these, Water and Sewer is the only area where the City is paying more than 90% of the costs itself.

47 <http://www.nyc.gov/html/dep/pdf/waterreuse.pdf>

5) Rate Structure: The current rate structure should be revised with the goal of making the system more equitable to the people of the City of New York. In the 1990s there was discussion of a formula for water billing that combined both flat- and use-based billing. Disagreements over an acceptable formula and the absence of rate increases in the mid-1990s ended the debate. The return of double digit increases requires revisiting this discussion. While there has been dramatic reductions in the use of water, this has not led to reduced water charges; in fact, as the Blue Book has stated, the reduction in water use is part of the reason for rate increases. If those who are able continue to respond to rising rates by increasing conservation, total revenue for the System will decrease and the rates will need to go up again. Not only does this billing system result in a never-ending circle of rate increases, it will shift more and more of the burden on those who can least afford it. A process of examining alternative rate structures should be launched with the involvement of the various communities affected by water costs. A failure to have an inclusive process will result in a replay of past mistakes, such as the poorly planned attempt to move to universal metering 20 years ago. Included in this rate evaluation should be a discussion of programs to provide assistance to senior citizens, an investigation of programs that might assist lower income people, and an examination of alternate rates for certain types of housing. There are various "lifeline" programs in different cities around the country that could be explored.[48] A working group should be formed to begin looking at alternative rate structures and their potential impacts on the system and the rate payer.

6) Federal Support for Mandates: According to the American Water Works Association, the US Environmental Protection Agency estimates that water and wastewater infrastructure repair costs may range between $745 billion to $1 trillion over the next 20 years.[49] They affirm that the cost of water infrastructure replacement far exceeds the capacity of local utilities. The grant programs that existed until the late 1980s provided a critical financial support for the System. While various economic stimulus plans are explored, renewed support from the federal government should be sought.

Conclusion

The shift of responsibility for New York City's water from the general City budget to the NYC Water and Sewer System benefited New Yorkers. One of the results was the City's 10 Year Housing Plan which preserved and created thousands of apartments. We are sure that no one envisioned that this shift in control would become a threat to the preservation and creation of affordable housing twenty years later.

In 1984, there was still federal grant money available for water infrastructure. It is unlikely

48 NACWA 2005 Financial Survey. Washington, D.C., 2006.
49 "Straight Talk on Water Infrastructure." Drinktap.org. 3 March 2008. <http://drinktap.org/consumerdnn/Home/WaterInformation/WaterInfrastructure/StraightTalkonInfrastructure/tabid/198/Default.aspx>

that anyone envisioned ***a)*** rate payers fully shouldering the annual debt service for the billions of dollars that the Water Board has borrowed to preserve and improve the water infrastructure; ***b)*** low-income buildings paying larger water bills because they house larger families and therefore use more water; ***c)*** water shut-off notices being issued to hundreds of single family homeowners in the midst of a foreclosure crisis; or ***d)*** the water system becoming a major funder of the general operating budget through the Water Board's rental payment to the City.

It is clear that DEP and the Water Board have been trying to address some of these concerns. There has been evidence for many years that billing based solely on metering is a regressive charge that causes lower income communities to pay more for the water system than higher income communities. That evidence has produced many efforts on the part of DEP and the Water Board to devise alternatives like the Multifamily Conservation Program. It is also clear that DEP and the Water Board recognize the need to maximize collections, as evidenced by the recently enacted lien sale legislation.

The painful truth about water and sewer rate reform is it will require an infusion of funds other than payment of water bills. While we recommend getting the federal government to resurrect grant programs for water infrastructure, we know this is not a short term answer. We must acknowledge that some portion of funds for the Water System will have to come from the general operating budget of the City.

Failure to put general operating money into the Water System will not insulate the City budget from the secondary effects of the rising costs. Deteriorating housing conditions caused by foreclosures, lien sales and deferred maintenance will encumber the City budget. The need for deeper subsidies in rehabilitation and new construction projects will also impact the City budget. The stress on the lives of New Yorkers affected by soaring rates, foreclosures, deferred maintenance, and lack of access to affordable housing may not be as easily quantifiable in dollar amounts, but it will still have a budgetary impact.

We have made a number of proposals that would hold rates down in the short term, but a fundamental change in rate setting policy is necessary. Amending the lease agreement between the Water Board and New York City to reduce the rental payment would be a good first step, but it will not come close to solving the long term problem. Devising a new rate setting formula and allocating general operating funds from the City for water are essential elements of a long term solution.

On many issues, the current City administration has involved the public in the planning and decision making process, PlaNYC 2030 being a particularly noteworthy example. A similar process needs to be employed on water and sewer rate reform. The rush to metering and the subsequent creation of temporary programs to alleviate the resulting problems is an illustration of what can happen without careful planning and public input. A rate reform process that includes genuine input from neighborhood residents and representatives of the real estate, lending, nonprofit housing and environmental communities needs to begin now.

It is our hope that this summit and report will be a first step in the rate reform process. It is also our hope that in 2013 when UNHP celebrates its 30th anniversary that rate reform will be listed as another success accomplished through the kind of partnership of private, nonprofit and public sectors that has characterized all of our work.

Related Websites

NYC Department of Environmental Protection (DEP):
www.nyc.gov/html/dep/html/home/home.shtml

NYC Water Board:
www.nyc.gov/nycwaterboard

New York City Municipal Water Finance Authority:
www.ci.nyc.ny.us/html/nyw/home.html

NYC Independent Budget Office (IBO):
www.ibo.nyc.ny.us

NYC Office of the Comptroller:
www.comptroller.nyc.gov

Booz Allen Hamilton Report (including recommendations on DEP's collections):
www.nyc.gov/html/dep/pdf/bah_reports/BAH_report_full.pdf

Water Board and Water Finance Authority agreement on financing (includes covenant on 15% over debt service pledge):
www.ci.nyc.ny.us/html/nyw/pdf/nyc_water_board_financing_agreement.pdf

Lease between the Water Board and New York City:
www.ci.nyc.ny.us/html/nyw/pdf/nyc_water_board_lease_agreement.pdf

Multifamily Conservation Program information:
home2.nyc.gov/html/dep/pdf/mcpfaq.pdf

Payment Incentive Program information:
www.nyc.gov/html/dep/html/water_and_sewer_bills/pip.shtml

Comprehensive Water Reuse Program information:
www.nyc.gov/html/dep/pdf/waterreuse.pdf

The Bronx River Alliance:
www.bronxriver.org/theriver.cfm

Croton Water Clean Water Coalition:
www.newyorkwater.org

University Neighborhood Housing Program:
www.unhp.org

Figure 1.1

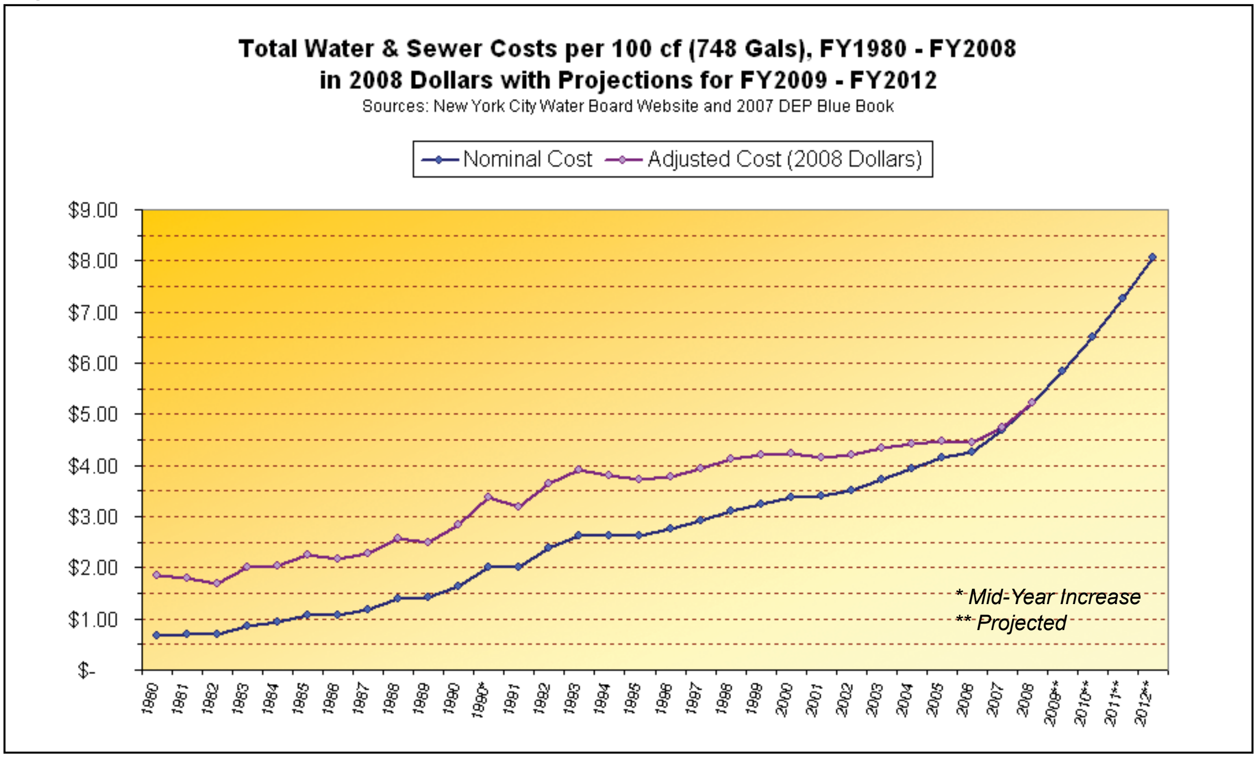


Figure 1.2

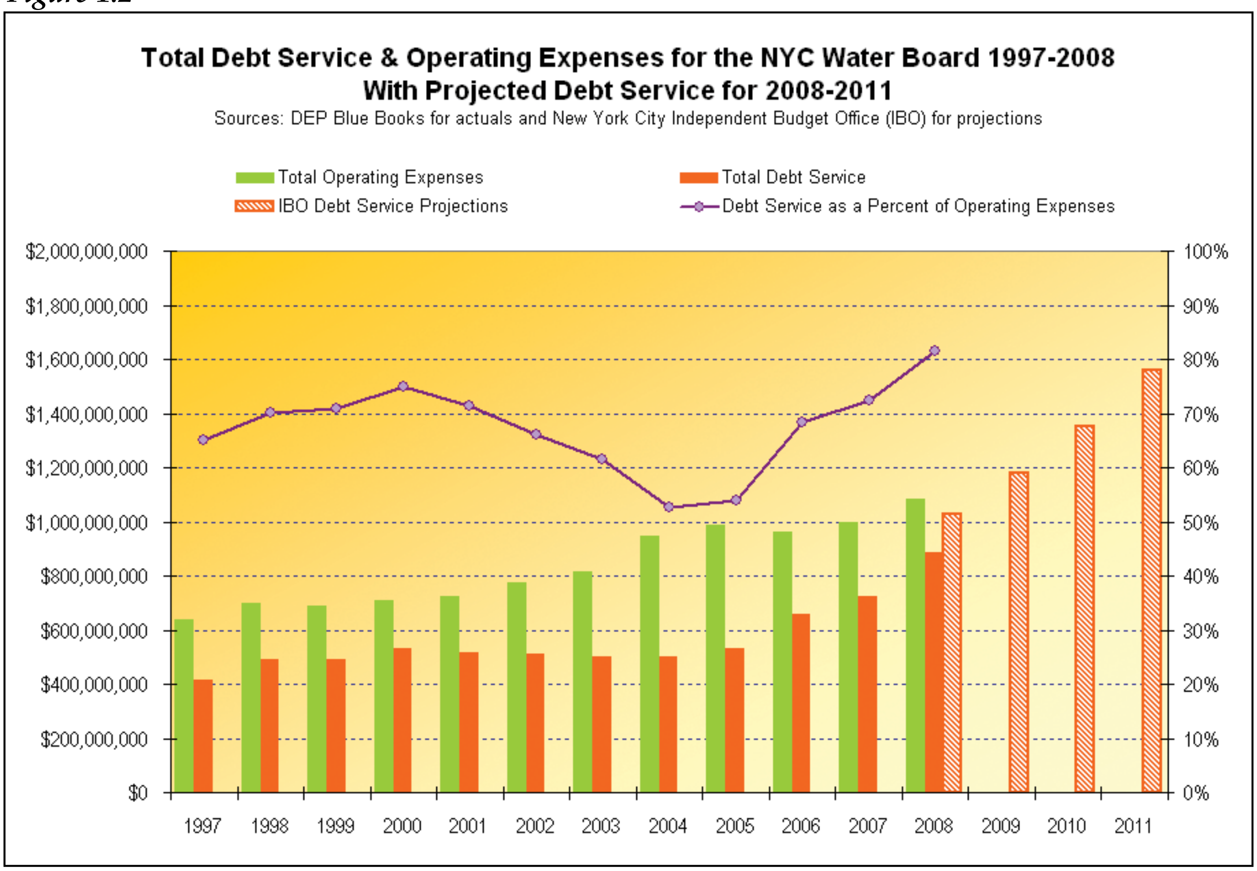


Figure 2.1

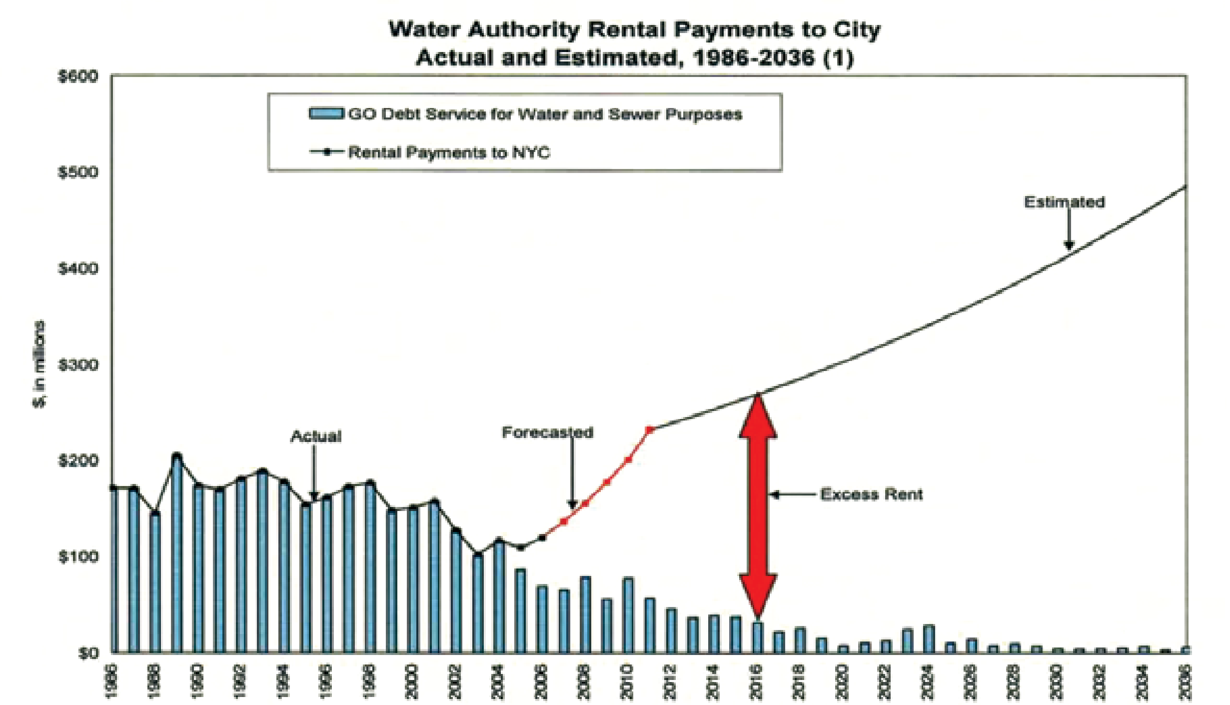
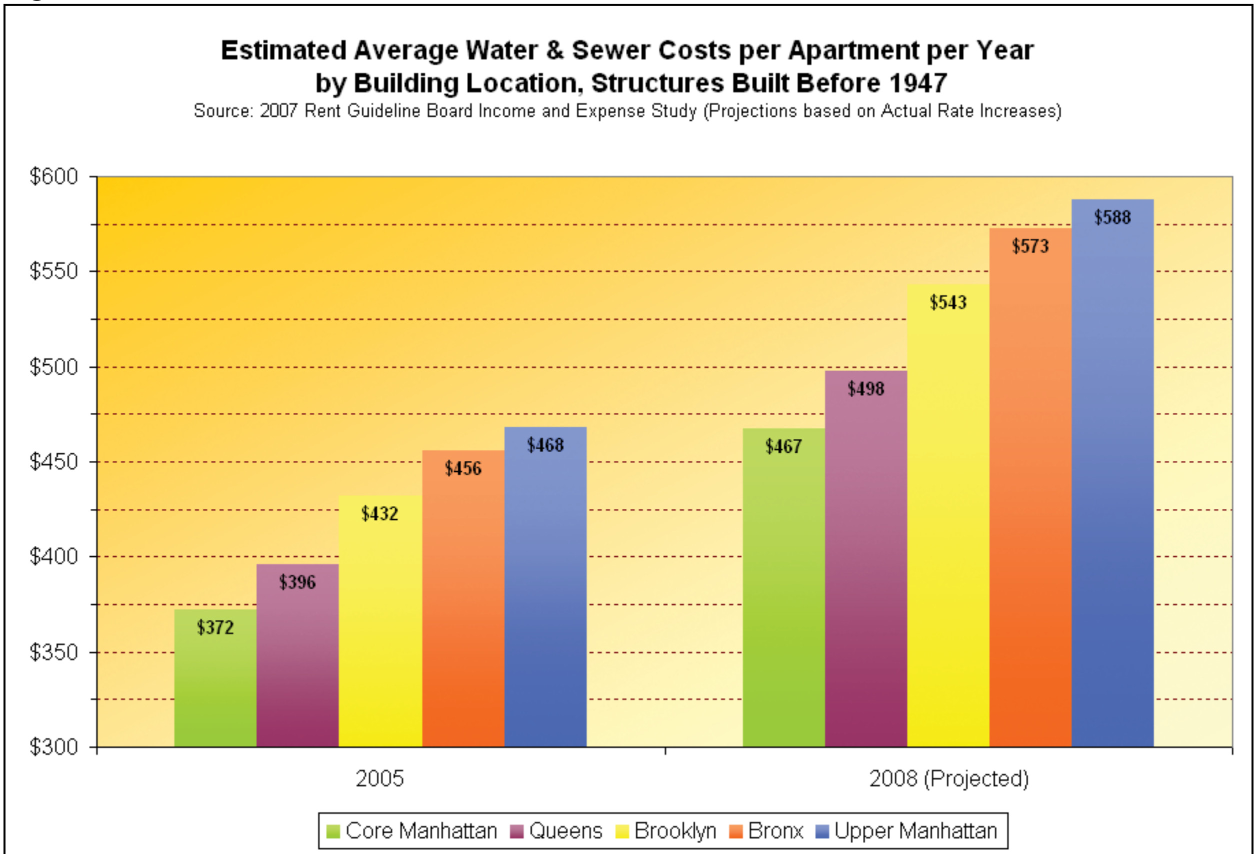


Chart from the NYC Comptroller's Office

Figure 2.2



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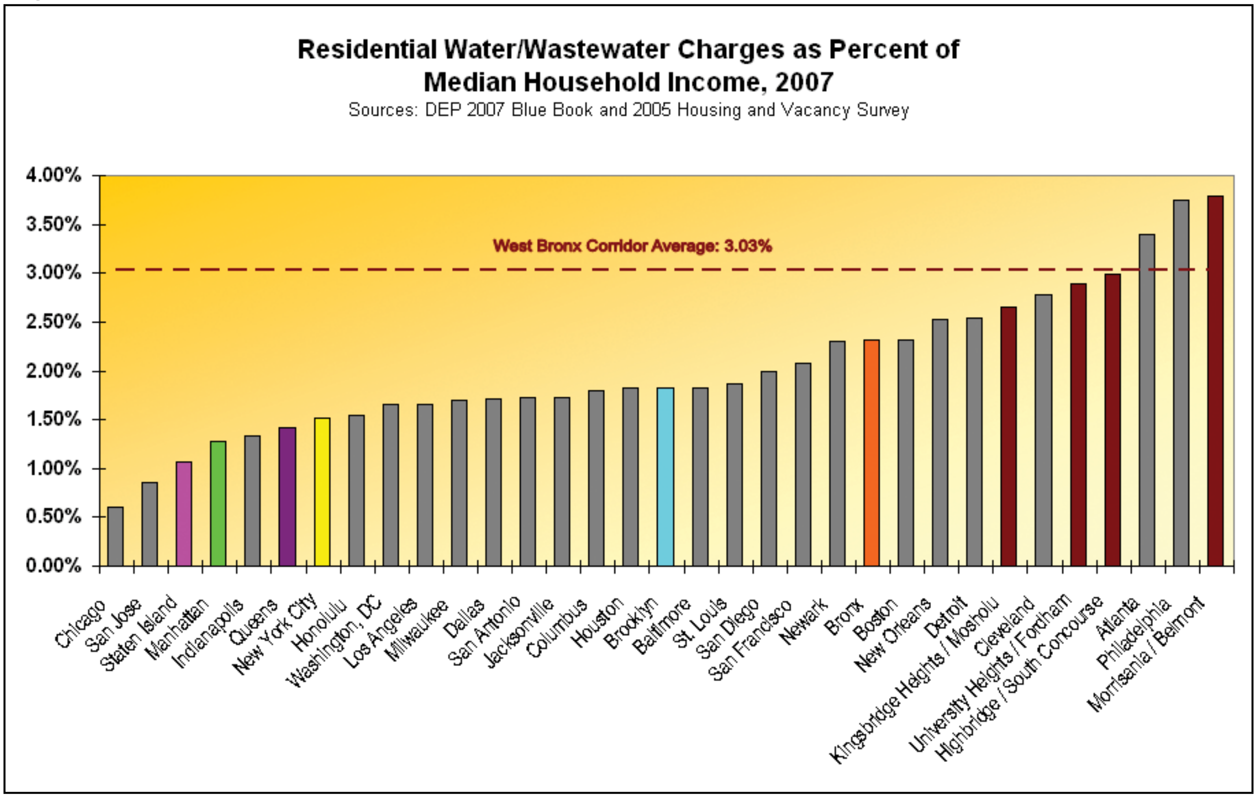
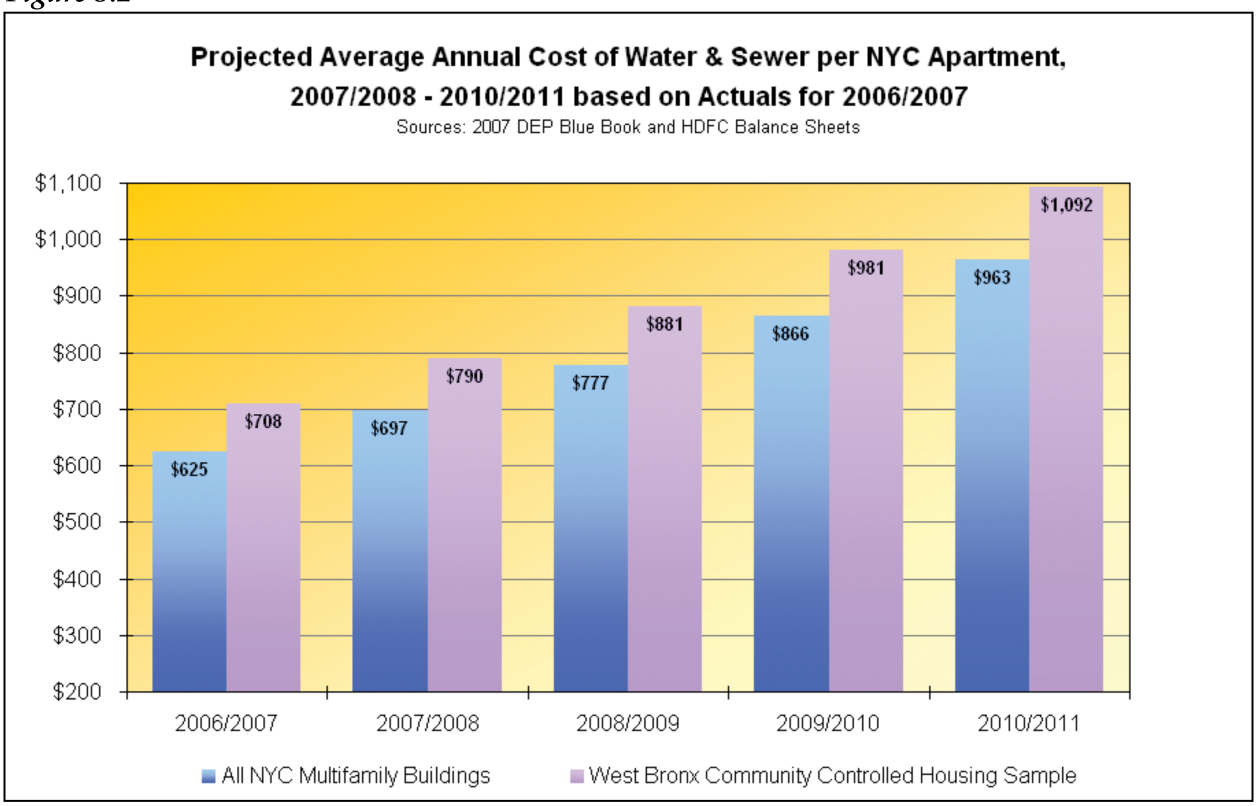


Figure 3.2



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