UTILITY BOARD STAFF REPORT

Item 2
September 8, 2026
Regular Business

AGENDA ITEM INFORMATION

TITLE:	2027 Water Rate Discussion/Recommendation	☒ Discussion Only ☐ Action Needed: ☐ Motion ☐ Ordinance ☐ Resolution
RECOMMENDED ACTION:	Review the proposed 8.0% utility rate increase for water services for fiscal year 2027.	

STAFF:	Matt Mornick, Finance Director Ben Schumacher, Financial Analyst II
COUNCIL LIAISON:	Wendy Weiker
EXHIBITS:	1. 2027-2032 Projected Water Utility Cash Flow

BACKGROUND

As part of the 2027-2028 biennial budget process, staff seeks a recommendation from the Utility Board regarding the Water Utility rate adjustment for the upcoming fiscal year. Staff recommends an 8.0% increase to the Water Utility rates for 2027 as proposed in the rate model.

The operating and capital budgets presented in this memo include adopted and amended figures through May 5, 2026, as well as preliminary 2027 and 2028 budget figures, contingent on City Council budget approval in December 2026.

2027-2028 PRELIMINARY OPERATING BUDGET

The operating budget for the Water Utility is presented in Table 1.

Table 1

Operating Expenditures	2025	2026	2027	2028	Percent Change	
($ in thousands)	Actual	Forecasted	Budget	Budget	26-27	27-28
Salary & Benefits	$1,949	$1,942	$2,212	$2,289	13.9%	3.5%
Water Purchased for Resale	1,912	1,997	2,123	2,315	6.3%	9.0%
Other Services and Charges	2,941	3,704	3,349	3,386	-9.6%	1.1%
Debt Service	2,224	2,430	3,834	3,829	57.8%	-0.1%
Total	**$9,026**	**$10,073**	**$11,517**	**$11,818**	**14.3%**	**2.6%**

Highlights from the Water Utility operating budget include:

- Combined personnel costs for 2027 are projected to increase 13.9% over the 2026 budget. This increase is driven by a 4.10% cost-of-living adjustment (COLA) tied to the first half of 2026 CPI-W for Seattle-Tacoma-Bellevue WA, rising benefit costs, and a fully staffed department in 2027 versus forecasted savings in 2026 that were a result of vacancies in the first half of the fiscal year.

- Water purchases from Seattle Public Utilities (SPU) are projected to increase 6.3% in 2027 when compared to the 2026 rates. Note that SPU sets a higher rate for the period of Peak usage (May 15-Sept 15) than for non-peak period usage (Sept 16-May 14).

- Other Services and Charges include all other costs of operations including supplies, insurance, and City administration costs. Administration costs include the Water Fund's share of administrative support provided by the City Attorney's Office, City Manager's Office, Finance, and Human Resources staff.

- Debt service payments include two schedules. First, debt service on a $3.3 million public works trust fund loan for the Booster Chlorination System project. Second, debt service tied to a $26.6 million sale of limited tax general obligation (LTGO) bonds for a selection of qualifying projects.

- In Q1 2027, staff anticipate a third LTGO bond sale for the water utility, raising outside capital to help pay for the list of qualifying projects outlined in the discussion section of this memo. This bond sale is likely to result in an additional annual ongoing principal and interest payment of $1.5 million. The rate model assumes a potential final bond sale in 2030 to support routine capital reinvestment. Staff will closely track capital program needs over the next biennium and evaluate the feasibility of this final sale.

DISCUSSION

CAPITAL REINVESTMENT PROJECTS

Proposed capital reinvestments for 2027 and 2028 are detailed in Table 2. Modernizing the water distribution system – particularly the water supply line and pressure reducing valve stations that are reaching the end of their useful lives – is the primary driver behind the proposed rate increase.

Table 2

Water Utility Capital Program Budget 2027-2028 *($ in thousands)*			
Project ID	**Description**	**2027**	**2028**
41904059	Capital Project Management	$720	$749
90.40.0001	Emergency Water System Repairs	220	227
90.40.0002	Water System Components Replacement	54	56
90.40.0003	Modeling & Fire Flow Analysis	40	41
90.40.0004	Street Related Water System Improvement	160	165
90.40.0006	WS Reliability Action Plan Improvement	300	309
90.40.0010	Water System Instrumentation	80	82
90.40.0011	First Hill BPS Upgrades	1,860	2,060
90.40.0014	Forest Avenue Water System Improvement	520	
90.40.0015	Phase 3 PRV Replacement	400	2,318
90.40.0016	Lucas Heights AC Main Replacement	700	3,090
90.40.0017	SE 59th & 61st Water Sys Improvement	550	2,318
90.40.0018	Phase 4 PRV Replacement		309
90.40.0019	SE 40th (East) AC Main Replacement	5,100	
90.40.0020	Avalon Park Water Sys Improvement	600	2,472
90.40.0023	Baxter AC Main Replacement		700
90.40.0032	City Water Supply Line Construction	8,320	
90.40.0043	Water System Plan Amendment	50	77
90.40.0044	EMW Water System Improvements Constructic	2,000	
Water Utility CIP Total		**$21,674**	**$14,972**

WATER RATE PROPOSAL

The proposed 8.0% water rate increase for 2027 is based on the City's updated rate model that reflects the 2027-2028 operating budget, the 2027-2032 Capital Improvement Program (CIP), debt financing requirements, and 2026 budget to actuals performance through July of this year. Prepared jointly by Finance, Public Works, and outside consultants, the rate model incorporates a third and potential final bond sale in 2027 and 2030, to finance the remaining City Water Transmission project costs as well as other major capital project work that exceeds $2.5 million with useful lives over 20 years.

This strategy spreads major infrastructure costs incurred in a relatively short period over the useful life of updated infrastructure, thereby avoiding spikes in annual rate adjustments year-over-year while generations of rate payers who benefit from these investments help pay down the associated costs.

The proposed 8.0% rate adjustment for 2027 ensures that the Water Fund has adequate resources to complete the critical capital project work detailed below and into the future, as well as meet long-established fiscal policy guidelines – specifically a 90-day operating reserve and a 1% capital reserve target established by the Utility Board in 2006 as a prudent measure to protect the City's multi-million-dollar investments in its utility assets. This 1% capital reserve target enables the City to support future replacement needs without extraordinary rate increases, while recognizing the responsibility of new development, existing customers, and future customers to fund both current and future reinvestment needs.

As detailed in Exhibit 1, the 8.0% rate increase in 2027 supports a planned LTGO bond sale in the estimated amount of $18.5 million in 2027. Table 3 compares the 2027-2028 rate proposal against historical projections from 2021-2025.

Table 3

Rate Recommendations	2025	2026	2027	2028	2029	2030	2031	2032
2027-2028 Rate Proposal			**8.00%**	8.00%	6.00%	6.00%	6.00%	6.00%
2025-2026 Rate Update	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%		
2023-2024 Rate Update	8.00%	8.00%	8.00%	8.00%				
2021-2022 Rate Update	5.25%	5.25%						

WATER UTILITY BOND ISSUANCE - Q1 2027

The current Water Utility rate proposal assumes a portion of the scheduled capital projects will rely on outside funding to offset the more than $65.9 million in escalated capital spending between 2027-2032. Exhibit 1 includes two debt issuances, one in 2027 estimated at $18.5 million and a second in 2030 for an estimated $2.5 million.

For modeling purposes, timing when to seek outside funding is based on when qualifying infrastructure improvements are scheduled in the six-year capital improvement program (CIP). In practice, staff closely manage cash-flow needs for capital projects as they unfold with the requirement to spend down bond proceeds within three years of receipt.

Staff forecast the Water Fund balance will require additional funding from an estimated $18.5 million debt issuance in 2027 to provide vital support for the water utility, including the following projects and programs:

- **City Water Supply Line Replacement** (90.40.0032) involves the realignment of approximately 5,000 feet of the City's 24-inch supply line. The existing SPU transmission line alignment traverses' steep slopes, which has raised concerns necessitating the transmission line realignment to more stable terrain. Total project costs are estimated at $18.8 million from 2025-2027. Staff anticipate additional outside financing is required in Q1 2027 to finance the remaining construction costs through completion, estimated at $8.3 million in 2027.

- **Pressure Reducing Valve (PRV) Station Replacements** (90.40.0015, 90.40.0018) is an ongoing program to systematically replace PRV stations throughout the island. Most stations are below the City's current operational standards. There is a total of 85 PRV stations in the City's water distribution system. In general, the life span of a new PRV station is around 50 to 60 years, with routine maintenance. Total project costs are estimated at $3.0 million in 2027-2028. PRV replacements are being grouped in smaller scopes to maximize soft costs and minimize additional mobilization and construction costs.

- **Water System Improvements** (90.40.0014, 90.40.0017, 90.40.0020, 90.40.0044) aims to install over 6,500 linear feet of new 8-Inch ductile iron water main at four different locations on the northern and eastern portions of Mercer Island. Water services and fire hydrants in these areas will also be replaced. Total project costs are estimated at $8.5 million through 2027-2028.

- **Asbestos Cement (AC) Water Main Replacements** (90.40.0016, 90.40.0019, 90.40.0023, 90.40.0026) is an ongoing program to systematically replace antiquated AC water mains with ductile iron water mains. The replacement program reduces the potential for catastrophic system failure, unexpected service disruptions, and large damage claims to the City.

  Staggered capital reinvestment for aging water mains is being accelerated as AC water main breaks have increased relative to prior years. Over the 2027-2032 CIP planning period, total project costs are estimated at $16.3 million.

NEXT STEPS

Staff seeks to answer the Utility Board's questions about the 2027 rate adjustment, follow up with additional information as required, and return at the October 2026 Utility Board meeting for final review and adoption of the proposed utility rate adjustment for water service for fiscal year 2027.

The 2027 Water Utility rate adjustment will be included in the City's fee schedule update at the December 1, 2026 City Council meeting. Staff will return during the 2027-2028 mid-biennial budget process with new information to inform potential annual rate adjustments for fiscal year 2028 and beyond.

RECOMMENDED ACTION

Review the proposed 8.0% utility rate increase for water services for fiscal year 2027.