



UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D.C. 20460

JAN 13 2013

MEMORANDUM

SUBJECT: Assessing Financial Capability for Municipal Clean Water Act Requirements

FROM: Nancy Stoner 
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Office of Water (OW)

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Office of Enforcement and Compliance Assurance (OECA)

TO: Regional Administrators
Regional Water Division Directors
Regional Enforcement Division Directors

We are working closely with local governments to clarify how the financial capability of a community will be considered when developing schedules for municipal projects necessary to meet Clean Water Act obligations. Our on-going conversations have been very encouraging and have helped identify several implementation issues, as well as more robust ways to present additional community-specific information within a financial capability analysis when considering a community's ability to achieve the shared goal of clean water. These issues are discussed in the attached financial capability framework document. We plan to develop an approach that addresses these issues in a way that achieves our shared goal of clean water. We expect to share a draft of the approach with you soon.

As we move forward, OW and OECA will continue to reach out to the Regions for your input and recommendations. If you have any questions, please contact one of us or have your staff contact Deborah Nagle, Director, Water Permits Division (nagle.deborah@epa.gov) or Mark Pollins, Director, Water Enforcement Division (pollins.mark@epa.gov).

cc: Randy Hill
Susan Shinkman
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Regional Permit and Enforcement Liaisons

Attachment

EPA's DIALOGUE WITH LOCAL GOVERNMENT FINANCIAL CAPABILITY FRAMEWORK

January 2013

Over the last several months, the U.S. Environmental Protection Agency (EPA) and local governments have engaged in a dialogue to clarify how the financial capability of a community will be considered when developing schedules for municipal projects necessary to meet Clean Water Act (CWA) obligations. This dialogue demonstrates EPA's strong support for ensuring that communities move forward in a sustainable manner and within their financial capability to meet CWA obligations. EPA is committed to ensuring that the policies reflected in this discussion are implemented consistently throughout EPA's Regional offices.

Local governments play a critical role in providing wastewater and stormwater infrastructure and services for their citizens, businesses and institutions. These municipal functions have been an important part of implementing the CWA to improve water quality and increased public health protection in streams, lakes, bays, and other waters nationwide. However, significant water pollution challenges remain. Elected officials remain strong supporters of the CWA goals and objectives by directing the public investment that is necessary to comply with the Act and to promote the quality of life for their citizens. Many local governments face complex water quality issues that are heightened by the need to address population growth, increases in impervious surfaces, source water supply needs, and aging infrastructure. In recent years, many local governments have increased their investment in their wastewater infrastructure by providing increased capital investments to rehabilitate existing systems, improve operation and maintenance and address additional regulatory requirements. As programs to improve water quality and attain CWA objectives are implemented, many state and local government partners find themselves facing difficult economic challenges. We recognize these challenging conditions and are working with states and local governments to develop and implement new approaches that will achieve water quality goals at lower costs and in a manner that addresses the most pressing problems first.

It is essential that long-term approaches to meeting CWA objectives are sustainable and within a community's financial capability. A community's financial capability and other relevant factors are important when developing appropriate compliance schedules that ensure human health and environmental protection. As EPA implements the recently released Integrated Municipal Stormwater and Wastewater Planning Approach Framework, EPA's "Combined Sewer Overflows: Guidance for Financial Capability Assessment and Schedule Development" (EPA 832-B-97-004) (Guidance for Financial Capability Assessment) will continue to be a valuable guide for evaluating the level of burden placed on a community by necessary clean water investments. Input from communities and others have pointed to a need to further clarify how financial capability is considered when developing schedules for municipal projects to meet their CWA obligations. In response, EPA is developing an approach to provide clarification of the financial capability analysis and that ensures consistent implementation among EPA Regions. The EPA's on-going conversations with communities and stakeholder groups have been very encouraging and are providing a deeper understanding of the fiscal impacts that regulatory

compliance has on consumers and households along the income distribution curve and on non-residential users. The flexibilities under the CWA, regulations, and EPA policies allow local government to continue to maintain existing wastewater and stormwater systems while making progress on clean water goals in a manner that is sustainable and within a community's financial capability. EPA and local government representatives will focus on the following topics associated with how a community's financial capability is assessed and considered when developing schedules to meet CWA objectives:

- How to expand the use of benchmark indicators of household, community and utility affordability, such as increasing arrearages, late payments, disconnection notices, service terminations, and uncollectable accounts;
- How to meet the obligations of the CWA by utilizing flexibilities in the statute and implementing regulations to prioritize necessary investments;
- How rate structures present both limitations and opportunities;
- How innovative financing tools, including public private partnerships, are related to affordability;
- How to facilitate consistent policy implementation at EPA Regional offices; and
- How other community specific factors, including obligations under the Safe Drinking Water Act, should be considered in developing appropriate compliance schedules

Prioritizing Investments

As articulated in the Integrated Planning Approach Framework, EPA encourages municipalities to balance CWA requirements in a manner that addresses the most pressing health and environmental protection issues first. For communities that have CWA responsibilities for stormwater and the collection and treatment of wastewater, it is entirely appropriate to consider the financial impacts of investments they need to make to manage both stormwater and wastewater discharges. EPA continues to explore ways in which the integrated planning approach can provide for meeting water quality standards and other CWA obligations by utilizing existing flexibilities in the CWA and its implementing regulations, policies and guidances.

Low Income Households

Uniform rate structures may place a disproportionately high financial burden on households with low incomes. EPA strongly encourages municipalities to consider establishing lower rates or subsidies for low income customers. This is consistent with one of the goals of integrated planning, which is to take advantage of synergies and savings that can be found through an integrated approach and thereby promote affordability.

Some communities have asked whether the CWA restricts a community's ability to set different rate structures to address such burdens or would limit their ability to receive grant funding from the Agency.¹ EPA plans to discuss both the limits and opportunities that different rate structures present for achieving clean water goals. Local officials have a great deal of latitude under these

¹ Section 204(b)(1) of the CWA recognizes the use of lower charges for low-income residential users as satisfying the stipulation that recipients of services must pay their proportionate share. The EPA's regulations at 40 C.F.R. Section 35.2140(i) reflect this and authorize low income residential user rates.

regulations and the EPA continued to encourage communities to consider and adopt rate structures that ensure that lower income households continue to be able to afford vital wastewater services. Several areas of discussion concerning rate structure involve state law, bond covenants, and implementation considerations.

In addition, EPA's Guidance for Financial Capability Assessment provides a flexible framework for considering the site-specific factors that impact a given community's rate base. The guidance encourages communities to consider and present any other documentation of their unique financial circumstances, so that it may be considered as part of the analysis. Where communities have adopted differential rates for low income customers, the income distribution that led to that approach may be valuable supplemental information that the community would choose to present as part of its financial analysis when determining the appropriate timeframe for reaching compliance. Examples of information that have been used in this context include poverty rates, income distribution by quintile, late payments, disconnection notices, service terminations, uncollectable accounts and average wastewater bill as a percentage of the median household income (MHI), although any information that the community believes is relevant may be presented.

The Role of Median Household Income in Developing Compliance Schedules

The EPA's Guidance for Financial Capability Assessment suggests using the percentage of MHI as one indicator for helping to determine the schedule for completing necessary work. The MHI indicator presents only one of many considerations that should be evaluated in determining the most appropriate schedule. EPA expects that the full range of financial indicators as well as municipal-specific information will be considered when developing schedules. A common misconception is that the EPA requires communities to spend to a level of 2% of MHI to meet CWA obligations. Rather, the percent MHI calculation is guidance, and is considered along with a suite of other financial indicators to assess the overall burden on a community. The guidance recommends that communities with higher burdens be given longer time periods to complete the needed work.

Community Specific Factors

The EPA's Guidance for Financial Capability Assessment provides a flexible framework for considering the site-specific factors that impact a given community's rate base. The guidance encourages communities to consider and present any other documentation of their unique financial circumstances, so that it may be considered as part of the analysis.