



Audit, Finance and Enterprise Committee Report

Date: August 28, 2025

To: Audit, Finance and Enterprise Committee

Through: Marc Heirshberg, Assistant City Manager
Michael Kennington, Deputy City Manager/Chief Financial Officer

From: Brian A. Ritschel, Management and Budget Director
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Subject: Fiscal Year 2025/2026 Utility Rate Recommendations

PURPOSE AND RECOMMENDATION

The purpose of this report is to provide staff recommendations for utility rate adjustments. The rate adjustments are recommended to be effective January 1, 2026.

For each utility, the forecasted expenses (uses) are compared to the forecasted revenues (sources). The table below shows the projected net sources and uses for FY 2025/26 and FY 2026/27 if the recommended utility rate adjustments are adopted. The FY 2025/26 and FY 2026/27 net sources and uses are projected to be negative, however the net sources and uses for the Utility Fund does improve throughout the forecast period (see Attachment 2 for more detail).

<u>Utility</u>	<u>FY 25/26</u>	<u>FY 26/27</u>
Water	(\$5,955,000)	(\$12,873,000)
Wastewater	(\$11,996,000)	(\$6,784,000)
Solid Waste	(\$5,859,000)	\$689,000
Electric	(\$1,067,000)	(\$742,000)
<u>Natural Gas</u>	<u>(\$3,793,000)</u>	<u>(\$2,082,000)</u>
Total	(\$28,852,000)	(\$21,964,000)

The method of implementation of rate adjustments can vary from year to year based on the needs and goals of the individual utilities. The impact on individual customers can vary based on the method of implementation and customer consumption.

For FY 2025/26, the following rate adjustments are recommended (see Attachment 1 for more detail):

Solid Waste:

- Residential barrel rates: 5.5% increase to monthly service charge
- Front-load rates: Overall 5.5% increase
- Commercial Roll-Off rates: Overall 5.5% increase

Electric:

- Residential: \$1.00 per month service charge increase
- Residential: 2.0% Summer Tier 1 usage charge increase
- Residential: 4.0% Summer Tier 2 usage charge increase
- Residential: 5.0% Winter Tier 1 usage charge increase
- Residential: 36.31% Winter Tier 2 usage charge increase
- Non-Residential: \$5.00 per month service charge increase
- Non-Residential: 3.0% Winter Tier 2 usage charge increase
- Non-Residential: 5.0% Summer Tier 2 usage charge increase
- Interdepartmental: 4.5% Tier 2 usage charge increase

Gas:

- Residential: 7.0% Summer and Winter Tier 1 usage charge increase
- Residential: 15.0% Summer Tier 2 usage charge increase
- Residential: 24.0% Winter Tier 2 usage charge increase
- Non-residential: \$3.00 per month service charge increase
- Non-residential: 3.0% Summer and Winter Tier 1 usage charge increase
- Non-residential: 5.0% Summer and Winter Tier 2 usage charge increase

Water:

- All customers: 5.5% service charge increase
- Residential: 5.5% Tier 1 usage charge increase
- Residential: 7.0% Tier 2 usage charge increase
- Residential: 8.0% Tier 3 usage charge increase
- Residential: 9.0% Tier 4 usage charge increase
- General Commercial and other non-residential: 12.0% usage charge increase
- Non-residential Landscape: 15.0% usage charge increase
- Large Commercial and Industrial: 19.0% usage charge increase
- Multi-Unit: 11.0% usage charge increase
- Non-residential General Excess Surcharge: 12.0% usage charge increase
- Non-residential Landscape Excess Surcharge: 15.0% usage charge increase
- Pumping Surcharge: 5.5% usage charge increase
- Phoenix-Mesa Gateway Airport Fire Protection: 30.0% demand charge increase
- Interdepartmental: 11.4% usage charge increase

Wastewater:

- Residential rate: 8.0% service and usage components increase
- Non-residential: 9.0% service and usage components increase

BACKGROUND AND DISCUSSION

Each utility is operated as a separate business center. As such, rate schedules are adjusted annually in a manner consistent with costs of capital, as well as the fixed and variable costs of operation and maintenance. In addition, rates are reviewed and updated with the requirements of Title 3, Chapter 3 of the Mesa City Code. To develop rate recommendations, staff consider the following five (5) Financial Principles to ensure the reliability, sustainability, and affordability of the utilities:

- Balance net sources and uses
- 20% or higher reserve fund balance
- Rate adjustments that are predictable and smoothed throughout the forecast
- Equity between residential and non-residential rates
- Affordable utility services

In alignment with the City Code and the Financial Principles, the reserve balances are combined in the Utility Fund and are managed to maintain a targeted ending reserve balance of 20% or higher of the following year's estimated expenditures. The reserve balance allows for the smoothing of rate adjustments. This smoothing avoids large rate increases and minimizes the impact to customers in any single year.

The Utility Fund Cash Flow Projections (Attachment 2) includes projections of growth. The Water, Wastewater, and Solid Waste utilities have a citywide service area and are expected to grow by an average of about 0.9% per year during the forecast. With the inclusion of the Magma service area, the Natural Gas utility is expected to grow by 1,400 accounts in FY 2025/26. The Electric utility, with a smaller and largely built out service area when compared to the other utilities, is expected to grow by 200 accounts in FY 2025/26.

The Utility Fund Cash Flow Projections also include expenditures that are increased by inflationary factors in future years. Some inflationary factors are unique to the individual utilities, such as those used for chemicals or purchased water. Other citywide expenditure pressures that are included in the forecast are listed below.

Capital Investment

The City continues to place a high priority on infrastructure investment to attract and service future development. The FY 2025/26 capital improvement program (CIP) includes the planning for increased customer demand, maintaining system reliability, and satisfying contractual commitments. The debt service on utility systems revenue bonds and obligations is funded through the utility rates paid by customers. The City issues obligations on an as-needed basis in order to minimize the interest cost. Anticipated future debt service has been included in the forecast and rate recommendations.

Review of the General Fund Contribution

The Utility Fund contribution to the General Fund is calculated based off 30% of each utility's gross operating revenues. The amount of the transfer throughout the forecast period is adjusted based on the gross operating revenue forecast. The adjustment for FY 2025/26 is projected to be an increase of \$9.2 million, increasing from \$137.8 million to \$147.0 million.

SOLID WASTE UTILITY

Solid Waste services are charged as fixed monthly rates for the various services provided.

The Solid Waste utility forecast includes increased costs related to fleet maintenance, material processing, and disposal charges. Material processing and disposal costs are increasing regionally. In total, material processing and disposal costs are projected to increase by \$4.4M from FY 24/25 to FY 25/26. Fleet maintenance costs have also increased by \$1.2M from FY 2024/25 to FY 2025/26 due to increased labor and parts costs.

Residential Rates

Staff are recommending a 5.5% increase to all residential rates. Additionally, staff is recommending a \$2.00 per load increased to scheduled bulk item pick-up requests. The standard black barrel refuse service includes a blue barrel recycling service.

90-gallon barrel service: Increase of \$1.82 per month, from \$33.17 to \$34.99
60-gallon barrel service: Increase of \$1.63 per month, from \$29.60 to \$31.23
35-gallon barrel service: Increase of \$1.53 per month, from \$27.89 to \$29.42
Additional trash barrel: Increase of \$0.86, from \$15.66 to \$16.52
Green barrel: Increase of \$0.43, from \$7.84 to \$8.27
Bulk Pick Up (no appliances): Increase of \$2.00 per load, from \$29.00 to \$31.00
Green and Clean Fee: no recommended increase

The projected annualized revenue increase is \$3,479,000.

Commercial Front-Load Trash

The Front-Load program serves customers in competition with private waste collection companies. There are various rate factors related to Front-Load service.

Staff are recommending increasing the base rate and out-of-zone fee, while eliminating the multi-day factor. The projected overall increase for Front-Load Trash is 5.5%.

Base rate for Trash:

Increase 2-yard from \$89.00 to \$93.00

Increase 3-yard from \$97.00 to \$101.00

Increase 4-yard from \$105.00 to \$109.00

Increase 6-yard from \$122.22 to \$127.48

Increase 8-yard from \$139.69 to \$145.70

Increase out-of-zone fee by \$5.00, from \$28.00 to \$33.00

Decrease multi-day discount by 5 percentage points, from 5.0% to 0.0%

Commercial Front-Load Cardboard/Commingled Recycling

Staff are recommending increasing the base rate.

Base rate for cardboard/commingled recycling:

Increase 2-yard from \$74.52 to \$78.62

Increase 3-yard from \$80.99 to \$85.44

Increase 4-yard from \$87.47 to \$92.28

Increase 6-yard from \$102.25 to \$107.87

Increase 8-yard from \$120.55 to \$127.18

Commercial Front-Load Compactor

Staff are recommending increasing the base rate.

Base rate for compactors:

Increase 2-yard from \$125.00 to \$131.88

Increase 3-yard from \$148.00 to \$156.14

Increase 4-yard from \$171.00 to \$180.41

Increase 5-yard from \$188.00 to \$198.34

Increase 6-yard from \$199.25 to \$214.99

The projected increase in annualized revenue is expected to be \$590,000 for Front-Load Trash, Recycle and Compactor services.

Commercial Roll-Off

The Roll-Off program serves residents and business customers in competition with private waste collection companies.

Staff are recommending the following Roll-Off rate adjustments:

Increase trash and green haul fees as follows:

Base rates for Roll-Off Trash:

Increase 15-yard/20-yard from \$135.00 to \$140.00

Increase 30-yard from \$145.00 to \$150.00

Increase 40-yard from \$160.00 to \$166.00

Increase Compactors from \$155.00 to \$161.00

Base rates for Green Waste:

Increase 15-yard/20-yard from \$135.00 to \$140.00

Increase 30-yard from \$145.00 to \$150.00

Increase 40-yard from \$160.00 to \$166.00

Increase trash per ton charge by \$3.75, from \$47.75 to \$51.50

Increase green waste per ton charge by \$4.32 from \$55.50 to \$59.82

The projected roll-off increase in annualized revenue is approximately \$126,000 for Roll-Off containers.

The projected annualized increase in revenue for all Solid Waste utility recommendations is approximately \$4,195,000.

ELECTRIC UTILITY

Rates for electric service are comprised of three major components: System Service Charge with a flat monthly rate, Energy Usage Charge based on units of consumption, and the Electric Energy Cost Adjustment Factor (EECAF) which passes the cost of the purchase of the electric commodity to the customer.

Adjustments to the system service charge component of the electric rate allow for a more stable revenue source for the program and insulates customers from higher energy costs during peak demand periods such as the summer. Currently, approximately 22% of the revenues (excluding EECAF) from electric customers are fixed revenues. The program is heavily reliant on consumption to cover fixed expenses. Rate adjustments applied to the system service charge allow for a movement toward a more balanced rate structure. Average customer bills for the City of Mesa are slightly above Salt River Project but are below Arizona Public Service.

Additionally, the electric program is experiencing inflationary pressures on operating costs, as well as increased debt service expenses related to system infrastructure improvements.

The EECAF component is adjusted monthly to “pass-through” increases and decreases in the costs of electric energy supplies acquired to meet customers’ needs. The electric energy market experiences price fluctuations due to availability of energy reserves, population growth in the Western Market, and weather conditions. The impact of these

factors resulted in increased costs for electricity until more favorable contract pricing was realized for FY 2025/26. Electricity costs were \$28.6M in FY 2023/24, \$30.2M in FY 2024/25, and are projected to be \$25.0M in FY 2025/26. Staff continue to actively monitor pricing for electricity and apply the increasing costs using a smoothing approach in order to manage spikes in customer bills.

Residential

Staff recommend the following rate adjustments:

System Service Charge: increase of \$1.00 per month, from \$19.50 to \$20.50
Usage Charges: 2.0% increase in Summer Tier 1 usage charge
4.0% increase in Summer Tier 2 usage charge
5.0% increase in Winter Tier 1 usage charge
36.31% increase in Winter Tier 2 usage charge

The increase in the Winter Tier 2 usage charge is the final portion of a 3-year plan to align Tier 1 and Tier 2 Winter charges. The adjustment to the Winter Tier 2 rate does not impact small and average customers.

Average residential bill with customer charge, energy usage charge, and EECAF: from \$135.71 to \$137.98, a 1.7% increase, or \$2.27 per month

Average residential customer bills for the City of Mesa are above estimated Salt River Project bills (\$124.96 multifamily & \$134.96 single-family) and comparable to estimated Arizona Public Service bills (\$159.58).

Non-Residential

Staff recommend the following rate adjustments:

Service Charge: increase of \$5.00 per month, from \$19.72 to \$24.72
Usage Charge: 3.0% increase for Winter Tier 2 and a 5.0% increase for Summer Tier 2

Average commercial bill with customer charge, energy usage charge, and EECAF: from \$529.60 to \$534.60, a 0.9% increase, or \$5.00 per month

Interdepartmental Electric

Staff recommend a 4.5% increase for the Interdepartmental Tier 2 usage charge. The Interdepartmental rates increased 4.5% in 2025, 3.5% in 2024, and prior to that had not been adjusted since 2016.

The projected annualized increase in revenue for the Electric utility recommendations is approximately \$780,000.

NATURAL GAS UTILITY

Rates for natural gas service are comprised of three components: System Service Charge with a flat monthly rate, Usage Charge based on units of consumption, and the Purchased Natural Gas Cost Adjustment Factor (PNGCAF) which passes the cost of the purchase of the natural gas commodity to the customer. Those customers that reside in the Magma service area also have a Magma adjustment factor rate component. The adjustment factor benchmarks the City's rates to the rates of Southwest Gas to provide market equity.

Additionally, the natural gas program is experiencing inflationary pressures on operating costs, as well as increased debt service expenses related to system infrastructure expansion and improvements.

The recommended residential system service charge adjustment is for no change, and the non-residential system service charge recommendation is for a \$3.00 per month increase. The customer bill increase will vary largely based on consumption. The higher the consumption, the higher the percentage impact would be. The residential Tier 2 Summer/Winter Usage increase would increase rates over 25 therms of usage and will continue the City's efforts to create a progressive rate structure for usage.

The PNGCAF component has been adjusted monthly to "pass-through" increases and decreases in the costs of natural gas supplies acquired to meet customers' needs.

Staff recommend the following rate adjustments:

Residential

- Service Charge – summer and winter: no change
- Usage Charge – Tier 1 – under 25 therms: 7.0% increase for summer and winter
- Usage Charge – Tier 2 – over 25 therms: 15.0% increase for summer
- Usage Charge – Tier 2 – over 25 therms: 24.0% increase for winter

Average monthly Mesa resident bill with customer charge, usage charge, and PNGCAF: from \$41.06 to \$42.49, a 3.5% increase, or \$1.43 per month

Non-Residential

- Service Charge - summer: increase of \$3.00, from \$44.66 to \$47.66
- Service Charge - winter: increase of \$3.00, from \$54.34 to \$57.34
- Non-Residential Usage Charge – Tier 1: 3.0% increase for summer and winter
- Non-Residential Usage Charge – Tier 2: 5.0% increase for summer and winter

Average monthly Mesa commercial bill with customer charge, usage charge, and PNGCAF: from \$510.19 to \$521.91, a 2.3% increase, or \$11.72 per month

The projected annualized increase in revenue for the Natural Gas utility recommendations is approximately \$2,430,000.

WATER UTILITY

Rates for water service are comprised of two components: Service Charge, with a flat monthly rate based on the water meter size and Usage Charge, based on units of water consumption.

The water utility forecast includes increased costs for debt service, joint venture costs for the operation of the Val Vista Water Treatment Facility, and power, commodity, and chemicals at the City's water treatment plants. Staff reviews and forecasts all costs each year to ensure rates are sufficient to keep up with expenses. This includes significant cost increases for operational (\$4.1M) and debt service (\$12.7M) costs from FY 2024/25 to FY 2025/26.

Over the last few years, the City has concentrated on aligning its fixed revenues with fixed costs. The goal is to achieve revenues from the Service (fixed) Charge at 35% to 40% of overall rate revenues. FY 2024/25 fell slightly below this goal at 33.3% of total rate revenues.

The variable rate component (Usage Charge) is based on water consumption rounded to 1,000-gallon increments. There are four residential tiers (or levels of usage). Each tier has a different rate. The tier structure allows for a demand-based rate as customers with higher usage patterns create a greater demand for infrastructure and service capacity.

Residential Water

Staff recommend a 5.5% increase to all service charges, and the following increases to Residential usage charges:

- Tier 1: 5.5% increase, from \$3.72 to \$3.92 per 1,000 gallons
- Tier 2: 7.0% increase, from \$5.67 to \$6.07 per 1,000 gallons
- Tier 3: 8.0% increase, from \$6.94 to \$7.50 per 1,000 gallons
- Tier 4: 9.0% increase, from \$7.83 to \$8.53 per 1,000 gallons

Typical Residential Water Consumer Impact:

Service Charge: \$1.77 increase per month, from \$32.17 to \$33.94
Usage Charges: \$0.61 per month, from \$11.40 to \$12.01

Typical monthly bill impact: \$2.38 per month, from \$43.57 to \$45.95

Arizona Water Company comparison:

Service Charge: \$47.04 per month
Usage Charges (6,000 gallons): \$16.51

Typical monthly bill: \$63.55

Non-Residential Water

Consistent with the direction promoting equity with residential rates and furthering conservation efforts, the City is focused on identifying necessary and discretionary water use. Additionally, FY 2024/25 continued the recent trend of higher usage for non-residential customers compared to residential customers. The impact of increased non-residential water usage impacts the amount of water and infrastructure needed to serve these customers.

Staff recommend the following non-residential usage rate adjustments:

General Commercial: 12.0% increase

General Multi-unit: 11.0% increase

General excess surcharge usage: 12.0% increase

Landscape usage and excess surcharge usage: 15.0% increase

Large Commercial and Industrial: 19.0% increase

Prior to FY 2020/21, the general commercial usage rate was aligned with the necessary usage tier (Residential Tier 1). The proposed rate increases continue to move the non-residential usage rates closer to the usage tiers representing discretionary usage (Residential Tiers 2, 3, and 4). Similar to residential customers, all non-residential customers would have a 5.5% increase in their Service Charge. As the recommended increase is higher for the Usage Charge, the monthly bill increase will be smaller for customers that consume less water.

Typical Non-residential Water Consumer Impact:

Commercial General typical monthly bill (consumption of 9,000 gallons):
increase of \$6.05, from \$78.59 to \$84.64, or a 7.7% increase.

Commercial Landscape typical monthly bill (consumption of 29,000 gallons):
increase of \$21.38, from \$177.01 to \$198.39, or a 12.1% increase

Mesa Gateway Airport Fire Protection Utility

Staff recommend a 30.0% increase to the Mesa Gateway Airport (MGA) Fire Protection demand charge. This is the second increase to the MGA Fire Protection rate in eleven years and applies to all facilities located in the North General Aviation Area (currently twelve customers). This increase will further align demand related revenues to the actual operation and maintenance costs of the MGA Fire Protection Utility, which are recovered through the demand charge.

Interdepartmental Water

For FY 2025/26, staff recommend a 11.4% increase to the interdepartmental water usage charges. FY 2025/26 represents the final year of a 4-year plan to increase interdepartmental water rates to align with the residential tier 1 usage charge.

The projected annualized increase in revenue for all Water utility recommendations is approximately \$17,831,000.

WASTEWATER UTILITY

Rates for residential wastewater service are comprised of two components: Service Charge with a flat monthly rate, and Usage Charge based on wastewater demand volume. Wastewater volume is calculated for each customer based on 90% of the average monthly water use for the three lowest water usage months from December through March (also known as the “winter water monthly average”). This approximates indoor household usage and the resulting demand on the wastewater system. A City-wide winter water monthly average is used for new customers until an individual customer average can be determined.

The wastewater utility forecast includes significant cost increases within the utility such as, the cost of chemicals, electricity, maintenance at the Greenfield Water Reclamation Plant, and the cost of ownership, operation, and maintenance of the 91st Avenue Wastewater Treatment Plant (a joint venture with the cities of Glendale, Phoenix, Scottsdale, and Tempe). Staff reviews and forecasts costs each year to ensure rates are sufficient to keep up with expenses. The debt service costs are projected to decrease by \$0.4M, however operational costs are projected to increase by \$2.5M from FY 2024/25 to FY 2025/26.

Staff recommends an 8.0% increase to the Service Charge and the Usage Charge for Residential customers, and a 9.0% increase to the Service Charge and the Usage Charge for Non-residential customers.

Typical Residential Wastewater Consumer Impact:

Service Charge: \$1.93 increase per month, from \$24.11 to \$26.04

Usage Charge (Winter water average): \$0.32 increase per month, from \$3.96 to \$4.28

Total average monthly bill impact: Approximately \$2.25 per month, from \$28.07 to \$30.32

Liberty Utilities comparison:

Total average monthly bill: \$47.51

EPCOR (formerly Johnson Utilities) comparison:

Total average monthly bill: \$46.30

Typical General Commercial Wastewater Consumer Impact:

Service Charge: \$2.40 increase per month, from \$26.63 to \$29.03

Usage Charge (based on water consumption): \$1.33 increase per month, from \$14.91 to \$16.24

Surcharge (based on water consumption): \$1.36 increase per month, from \$15.32 to \$16.68

Typical monthly bill impact: \$5.09 per month, from \$56.86 to \$61.95

Interdepartmental wastewater rates are recommended to be held constant.

The total projected annualized increase in wastewater revenue is approximately \$9,465,000.

ALTERNATIVES

Modify the FY 2025/26 utility rate adjustment proposal. Examples include but are not limited to: increase, reduce, or eliminate a recommended percentage.

The budgetary impact would need to be calculated by staff based on the modification requested.

FISCAL IMPACT

The projected annualized increase in revenues in the Utility Fund from the recommended rate adjustments is as follows:

<u>Utility</u>	<u>Annualized Increase</u>
Water	\$17,831,000
Wastewater	\$9,465,000
Solid Waste	\$4,195,000
Electric	\$780,000
Natural Gas	\$2,430,000

The projected ending reserve balance for the Utility Fund with similar adjustment to rates each year is:

<u>Fiscal Year</u>	<u>Ending Reserve Balance</u>
24/25	20.1%
25/26	13.4%
26/27	9.9%
27/28	8.0%
28/29	9.2%
29/30	13.4%
30/31	19.2%

The projected increase on the typical residential customer for by individual utility is:

<u>Utility</u>	<u>Monthly</u>	<u>Annual</u>
Solid Waste	\$1.86	\$22.32
Electric	\$2.27	\$27.24
Natural Gas	\$1.43	\$17.16
Water	\$2.38	\$28.56
Wastewater	\$2.25	\$27.00

Attachments:

1. FY 2025/26 Utility Rate Adjustment Recommendation Summary
2. City of Mesa Utility Fund Cash Flow Projections