

**State Water Infrastructure Authority
July 13-14, 2022 Meeting**

**Agenda Item F – Consideration of the Towns of McAdenville and Shallotte for Distressed
Designation Under Identification Criterion 4**

Division of Water Infrastructure Staff Report

Background

Session Law 2020-79, entitled in part “An Act to Improve the Viability of the Water and Wastewater Systems of Certain Units of Local Government...”, authorizes the State Water Infrastructure Authority (Authority) and Local Government Commission (LGC) to develop criteria to assess and review local government units (LGUs), and to utilize the assessment and review process to identify distressed units.

In the Fall of 2020, the Authority and LGC developed four Identification Criteria and the Assessment Criteria to evaluate local government units and identify distressed units. The Authority adopted the Assessment Criteria and the Identification Criteria at its meeting on November 18, 2020.

Identification Criteria

The Authority and LGC adopted the following Identification Criteria to be used to identify distressed units:

1. An LGU whose fiscal affairs are under the control of the Commission pursuant to its authority granted by G.S. 159-181 (“under Commission fiscal control”), or
2. An LGU that has not submitted its annual audits for the last two (2) fiscal years to the Commission as required by G.S. 159-34, or
3. An LGU with a total Assessment Criteria (see Attachment 1) score that:
 - a) Equals or exceeds 9 for LGUs providing both drinking water and wastewater services, or
 - b) Equals or exceeds 8 for LGUs providing only one service, either drinking water or wastewater, or
4. An LGU for which other information is available to or known by the Authority or LGC that reflects and is consistent with, but does not expressly appear in, the Assessment Criteria to account for situations in which the Assessment Criteria score does not wholly or accurately reflect a system’s level of risk due to the limitations of available data.

Previous Distressed Designations

In late 2020, early 2021 and early 2022, Division and LGC staff compiled LGU data in accordance with the approved criteria to identify distressed LGUs. Initially, 119 LGUs were identified as potentially distressed based on the approved criteria. Based on additional review and information received from LGUs, some of the 119 were determined to not be distressed or to no longer have active systems, 18 LGUs had their potential designations as distressed put on hold for further review, and the remainder were officially designated as distressed by the Authority and LGC. There are currently 115 LGUs with active water and/or wastewater systems that are designated as distressed, and 34 LGUs have been sent notification letters for scoring above the assessment criteria threshold for the first time in 2022. Once designated, LGUs must meet the requirements of the Viable Utility program before the designation is removed, even if future assessment scores drop below the threshold for designation.

Reassessment and Additional Designations

Session Law 2020-79 requires that the Authority and the LGC assess and review LGUs against the distressed criteria on a frequency of no less than every two years. At its July 14, 2021 meeting, the Authority agreed that the Division will conduct an annual review of the Assessment Criteria each spring, and use a two-year cycle for notifications and designations under Identification Criteria 2 and 3. Local Government Commission staff have determined the LGUs that have not submitted their annual audits for the past two fiscal years (Criterion 2). Division staff have recently completed the 2022 reassessment based on updated financial, rates, and compliance data (Criterion 3).

Identification Criterion 4 Distressed Designation Considerations

Given the availability of grant funding in the Viable Utility Reserve, non-distressed LGUs have recently expressed increased interest in becoming designated distressed. Two LGUs, the Towns of McAdenville and Shallotte, have recently presented information to Division staff in an effort to show that they are distressed units.

Criterion 4 in the approved distressed LGU Identification Criteria listed above allows for the Authority and LGC to consider additional information not explicitly reflected in the assessment process when considering units for designation. Division staff have developed a draft guidance document/standardized process by which non-distressed LGUs can request designation under Identification Criterion 4. This guidance document (previously discussed in brief at the April 13-14, 2022 SWIA meeting) includes both the generalized process as well as proposed documentation requirements and is intended to ensure that a level of equity is achieved by following a consistent process.

The Town of McAdenville (McAdenville) is requesting designation under Identification Criterion 4 on the basis of anticipated non-viability due to financial, managerial, and technical challenges faced in the next 5-10 years by the utility (Attachment F-1). Primarily, McAdenville has indicated that its rates will become untenable for its residents should the utility continue to

operate on its own and not seek consolidation. The current combined water and sewer rate for 5000 gallons is \$90.91. The combined water and sewer rates for 2026, based on the provided projections for necessary capital improvements as well as typical operation and maintenance, may be up to \$707.50 per 5000 gallons if McAdenville continues to operate independently and is not positioned to merge with Two Rivers Utilities.

McAdenville provided a resolution requesting designation, a summary document detailing their financial, managerial, and technical challenges, their current Asset Management Plan (AMP), a Rate Study complete by NC Rural Water in 2021, a Merger/Regionalization Feasibility (MRF) Study completed in 2022, and a letter of support for the distressed designation and consolidation with a neighboring, more viable utility, Two Rivers Utilities (TRU). The AMP and MRF both identify the necessary capital improvement projects necessary for physical viability of McAdenville's assets as well as the financial needs to complete those projects. TRU already operates and maintains McAdenville's systems via contract, is interconnected to McAdenville's water and sewer systems and is willing to complete the merger process by which McAdenville's water and wastewater systems would be fully consolidated with TRUs, and McAdenville's separate utility would cease to exist. These documents support the assertion that a complete consolidation with TRU is the only option to ensure McAdenville's viability in the future, and access to Viable Utility Reserve funding will provide financial support to complete the capital projects needed for consolidation.

The Town of Shallotte (Shallotte) is requesting designation under Identification Criterion 4 on the basis of anticipated non-viability due to financial challenges that affect the systems' technical and managerial abilities impacting the long-term sustainability of the water utility (Attachment F-2). Primarily, Shallotte has indicated that the cost of water purchased from Brunswick County (County) will increase in the future due to the addition of new treatment processes to address PFAS compounds. The County is the wholesale supplier of finished water to Shallotte. Shallotte indicated that it has healthy reserve funds and under consultation with the LGC, has been subsidizing rates out of the reserve fund to reduce costs to customers. The LGC only approved this to be done if Shallotte agreed to work with the County to consolidate the system. The current water rates for 5000 gallons are \$40.45 including the 80% increase from the County, no sewer billing data was provided. The water rates for 2026, based on the provided information, may be up to \$91.70 if Shallotte continues to operate their water system independently.

Shallotte provided a resolution requesting designation, a summary document detailing their financial challenges and briefly summarizing their potential managerial and technical challenges, an Asset Inventory and Assessment (AIA) completed in 2021, a Memorandum of Understanding (MOU) with the County indicating the desire to consider consolidation of the water utilities, and a copy of the Letter of Intent to Fund an MRF study evaluating the potential merger between Shallotte and the County from March 2022. The MRF study has not yet been completed to evaluate the financial, managerial, and operational aspects of merging the two systems. The MOU indicates that only consolidation of the water systems will be evaluated by

the MRF study, and that Shallotte will continue to own and operate their sewer collection system with the wastewater sent to a treatment plant owned and operated by the County. The current documentation provides an incomplete assessment of the impacts and potential benefits of merging Shallotte's water system with the County's while leaving the wastewater collection systems separate, as the MRF study has not yet been completed to evaluate those aspects.

Staff Recommendations

Staff recommend that the Authority take the following actions for LGUs listed above:

- Designate as distressed the Town of McAdenville under Criterion 4 on the basis of the provided information regarding their anticipated rates as well as the extensive previous study work completed to evaluate both McAdenville's system and the potential options for viability, which necessitate State grant support.
- Reconsider the Town of Shallotte's request for designation under Criterion 4 at such time when the currently in-progress MRF study has been completed to evaluate the financial, managerial, and operational impacts and benefits of a potential merger of Shallotte's water system with the County's water system.