

# **CONCEPT FOR PENNSYLVANIA URBAN SEWER REHABILITATION FUNDING**

An Environmental Law Institute Concept Paper

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## **Concept for Pennsylvania Urban Sewer Rehabilitation Funding**

Many older Pennsylvania communities own and operate aging connector sewers. Projects to restore or rehabilitate these disintegrating facilities are eligible for loans (or grants) from the funds administered by PENNVEST (the Pennsylvania Infrastructure Investment Authority), but they rarely score high on PENNVEST's priority ranking system. Typical failing sewer collection pipes in older urban areas often do not exhibit obvious impairments to drinking water or to surface water quality, and therefore score poorly in the two highest priority areas of public and aquatic health. Moreover, even if sewer projects do meet the scoring criteria, urban communities often find that financial offer terms are difficult to support because of high existing tax burdens on municipal residents. Unfortunately, Pennsylvania's grant and loan criteria have not been structured to take this fully into account.

Pennsylvania is facing a huge backlog of deferred capital expenditures for wastewater systems. The Sustainable Infrastructure Task Force reported in late 2008 that looming capital needs in Pennsylvania wastewater systems were \$25 billion, and that taking into account both capital expenditures and operating and maintenance expenses for the next twenty years, and projecting current user rates, the gap or shortfall is \$28.3 billion. While a variety of strategies will be needed to address these gaps, one of the major areas of need is rehabilitating and replacing connector sewers, many of which are 60, 80, or 100 years old in Pennsylvania's third class cities and older suburbs. The recently released 2010 Report Card for Pennsylvania's Infrastructure by the American Society of Civil Engineers gave the Commonwealth's wastewater infrastructure a grade of D+. (In contrast, Pennsylvania's well-documented legacy of crumbling bridges received a C.)

Pennsylvania needs to adopt a program to focus systematically on fixing sewers in order to prevent further loss and economic decay and to avoid future higher costs resulting from the deferral of capital expenditures in older communities; and PENNVEST should revamp its funding priorities to ensure that in the near future these reinvestments can be made.

### **PENNVEST Funding Priorities**

PENNVEST was established in 1988 to improve Pennsylvania's prioritization and funding for water and sewer infrastructure and to administer Pennsylvania's share of federal loan and grant funds distributed through the U.S. Environmental Protection Agency as the Clean Water State Revolving Fund and the Drinking Water Revolving Fund. It also administers some Growing Greener funding, some state bond funding, and other funds. PENNVEST makes loans or grants of \$250-300 million per year to

## *Urban Sewer Rehabilitation Funding*

Pennsylvania communities. Most of the PENNVEST money revolves as loan funds, with new loans being made as repayments allow. Over its lifetime, PENNVEST has made available more than \$6 billion to municipalities for water, wastewater and stormwater projects. After PennDOT, PENNVEST is the largest ongoing source of capital funding benefiting municipalities.

(Pennsylvania's General Assembly assigned several recent voter-approved bond funds relating to water to the Commonwealth Financing Authority, including the 2008 H2OPa \$800 million bond. The CFA uses its own procedures to determine awards, including requiring concurrence of legislative members from both political parties.)

Municipalities file applications with PENNVEST. These are reviewed and assigned scores under the "Project Priority Rating System Manual." These scores are used in determining whether to offer funds to projects. The scoring factors incorporate determinations by the Department of Environmental Protection (DEP), the Department of Community and Economic Development (DCED), and PENNVEST itself. The Manual is updated and the point totals available for various factors are adjusted by the PENNVEST Board from time to time. In each of three funding cycles per year, the PENNVEST Board awards the available funds, working downward from those projects with the highest point totals to those with lower totals; no offers are made to the lowest ranked projects.

In the wastewater/sanitary sewer arena, the PENNVEST rating system gives the highest priority to municipalities plagued with numerous failing on-lot systems, and to sewage systems with obvious and persistent dry weather discharges of raw sewage to waters of the Commonwealth. Several years ago PENNVEST and DEP reworked the scoring formulas to give somewhat more weight to urban wet weather (combined sewer overflow) problems than had previously been the case. The PENNVEST scoring system does not tend to favor replacement and rehabilitation of connector sewers absent some demonstrated impact on drinking water supplies or surface water quality. The scoring system is as follows:

- DEP can award up to 109 rating points, in five categories: Public Health (up to 32); Aquatic Health (up to 28); Infrastructure Health (up to 24); Compliance (up to 20); and Community Health (up to 5). Most of these potential totals are adjusted downward based not only the type of problem, but also based on the percentage of the population afflicted with the specific problem in the municipality.
- DCED factors account for 30 points at most. A project is ranked High, Medium, or Low for its projected economic development effects: 20 points for

direct job creation or preservation and private investment; 15 for indirect job creation or preservation and private investment; or 5 for project implementation. An additional 10 points are awarded if the project serves an Act 47 “distressed community.”

- PENNVEST factors offer a maximum of 40 points: 10 points if the project serves “infill” in a city, borough or first class township; 15 points if the project serves a DEP-designated “brownfield” site; 10 points if the project is designated by the governor’s Community Action Team for development support; and 5 points if the project is in a community with an adopted comprehensive plan whose local plan is consistent with a county comprehensive plan.

Because of these weights and assignments, the DEP factors alone usually determine whether a project will meet the funding threshold. As a result, replacement and rehabilitation of collector sewers not producing visible surface discharges of sewage to state waters, and not associated with specific economic development projects, tend to rank poorly in comparison with other project types.

Once a funding determination has been made, certain factors related to existing and resulting user rates and median household income for the municipality determine whether PENNVEST will offer a loan or grant, and what interest rates will apply. State law provides: “Grants shall be made only when the board, in its sole discretion, determines that the financial condition of the recipient is such that repayment of a loan is unlikely and that the recipient will not be able to proceed with the project without a grant;” when grants are made they are to be combined with loans if possible. 35 P.S. §750.10(e). PENNVEST loans are for 20 years and are capped at \$11 million (or \$20 million for a project that serves more than one municipality). These funding formulas do not take into account issues of municipal tax burden, school taxes, municipal pension liabilities, and projected population decline, that may affect ability to pay or repay.

A recent study by the Keystone Research Center found that over its entire history, Pennsylvania cities fared more poorly than other municipal types in the receipt of PENNVEST loans and grants.

### **Funding Opportunities**

Obviously there are many worthy uses for infrastructure funds. PENNVEST has fulfilled much of the promise of its first 20 years by addressing clean water issues and drinking water. But there is now a serious need for rehabilitation and replacement of

## *Urban Sewer Rehabilitation Funding*

older connector sewers – a hidden drag on the economic health of Pennsylvania’s urban places.

A mission shift is needed to enable Pennsylvania to address this problem effectively.

Fortunately, it appears that additional funding may be forthcoming to help address this backlog. Pennsylvania’s voters have in recent years shown themselves willing to incur bond debt for water and wastewater infrastructure; it is likely that after some period of economic recovery they may be willing to do so again. In the meantime, however, the federal contribution of funds to PENNVEST has increased, which provides an opportunity to re-prioritize funding to help restore these older sewer systems.

Nationally, the federal government was providing under \$700 million/year to all the states for wastewater improvements through the Clean Water State Revolving Fund; but in 2009 it provided \$4 billion through the American Recovery and Reinvestment Act, and in 2010 \$2.1 billion through the Clean Water State Revolving Fund. Proposed budgets for future years anticipate higher levels of expenditures for these purposes. Pennsylvania’s share went from \$27 million in prior years to \$81 million in the most recent year. Together with money already in the PENNVEST portfolio, increased expenditures on older urban sewer systems should be possible.

Such expenditures could be aligned with other federal, state and local expenditures, including plans for HUD, DOT, and EPA, and in among PENNVEST, PennDOT, DEP, DCED, and PHFA. Coordination of funding for the recovery of existing communities and rationalizing their management of rehabilitated systems will reduce abandonment of commercial and residential property, and support healthier municipal governments.

### **Proposal**

PENNVEST and DEP and the incoming administration in Harrisburg should:

- **Adopt a “fix it first” policy for sewers.** Given the lack of ready access by older municipalities to assured low-cost financing, Pennsylvania should adopt an ongoing program aimed at inventorying and systematically assisting local governments in timely replacement and rehabilitation of sewers.
- **Prioritize funding for sewer replacements.** PENNVEST should revamp its funding priorities by adopting additional scoring criteria to support sewer rehabilitation and replacement for older urban municipalities.

This additional focus on older urban communities is consistent with Pennsylvania's Keystone Principles as well as with new EPA priorities for the current and future years of funding. EPA issued a guidance document April 21, 2010 for new and future Clean Water State Revolving Fund grants to states. It says that "states should not encourage the expansion of centralized infrastructure to accommodate growth where there are available projects that repair, replace, and upgrade infrastructure in existing communities." The federal appropriation bill, moreover, specifies that a certain amount of each state's Clean Water State Revolving Fund grant must be designated an "additional subsidy" and used to support eligible projects in communities needing additional support. In Pennsylvania, this additional amount will be \$12-40 million (out of the \$81 million) for the current year.

Pennsylvania cities and urban areas tend to perform poorly on the existing PENNVEST priority scheme because their problems are beneath the surface and not as readily apparent as polluted streams or overburdened wastewater treatment plants. But continuing disinvestment in the underground infrastructure of the last century or more is not sustainable. In addition, some municipalities are less able to support available loan terms because of fiscal burdens not captured in the current funding formula (which relies on projected sewer rates and median income).

PENNVEST should change its priority system to favor system rehabilitation that does not encourage urban municipalities to continue to indefinitely defer these expenditures. This would be something of a mission shift.

In its 2010 guidance document, EPA emphasizes funding for projects that maintain "sustainable systems and that help build or maintain the technical, financial and managerial capacity of the recipient." Pennsylvania's own Sustainable Infrastructure Task Force called for improved asset management, planning for capital asset repair and replacement, and (in support of this) increases in federal and state assistance to these older systems.

In order to benefit from a revised PENNVEST priority system, including taking into account issues of fiscal burden that might allow a larger proportion of grants or offer of a lower interest rate, older urban systems could show not just that they now have failing sewer connectors needing replacement, but that they are adopting a management program and/or entered into management agreements with other municipalities and authorities to ensure a long term approach to the problem. In effect, the new PENNVEST priority or emphasis area on rehabilitating urban collector sewers would become an inducement for the planning and asset management called for by the Task Force.

## *Urban Sewer Rehabilitation Funding*

An element of a resulting local program could be creation of a repair and replacement fund like that recommended in the Task Force report. Although such a local fund could not itself be PENNVEST-supported under current law, the subsidy provided for the rehabilitation projects could make it feasible for municipalities to create such funds for the future using their own tax or ratepayer funds. This would ensure that the benefits of the capital reinvestment by PENNVEST could be sustained.

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*Also see the excellent resources available at 10,000 Friends of Pennsylvania's website at <http://10000friends.org/listing/Water-Infrastructure-and-Resources>*

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