

## ARTICLE



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# Multifamily Owners: Including Utilities May Be Killing Your Profits

## Learn how to protect your NOI

If your multifamily complex includes utilities in the rental fee, brace yourself. Utility cost increases are coming your way that may erode your hard-earned profits. Even more concerning is that you're responsible for a sizable expense that you have little or no control over. The "utilities included" model puts you squarely at the financial mercy of tenants, their usage tendencies, and utility companies. "Utilities included" also means that you have to be an accurate budget forecaster to ensure that your rental rates cover the annual utility expenses. Miss the mark and it's you who'll pay.

The exciting news is that you can quickly and easily change this situation by separating utilities from the rent fee and billing tenants directly--at no cost to you. By doing this, you'll make a positive and immediate impact on your net operating income (NOI) and the value of your property. From a price perspective, your complex will be more appealing to prospective tenants and you'll have effectively removed yourself from the utility equation altogether. Billing residents means no more worrying about the effects of runaway tenant usage and it leads to higher profits.

The sooner you get started the better, especially given the trajectory of utility rates. They seem only to move in one direction...up! Water rates for multifamily owners in Houston have increased by 30% this year alone. In New York City, water rates are up nearly 13% and in Milwaukee, they're projected to rise 27%. In Jacksonville, utility rates will increase 9%. Owners who can't adjust rents fast enough to cover the increased costs take a direct hit to their revenues.

*Billing residents means no more worrying about the effects of runaway tenant usage and it leads to higher profits.*

Tenant utility abuse is another reason why apartment owners and property managers should look closely at resident utility billing. You've probably leased to the tenant who kicks his thermostat up to "high" during the winter and then opens a window so that he can have fresh air. Or you've rented to the tenant who leaves the air conditioning up all day long so that she can come home to a cool house in the evening.

Clearly, these are examples of costly and wasteful ways to use heating and cooling. The tenant, however, does not bear the cost of this elevated consumption. What's also problematic is that tenants figure they can use utilities in any way they deem acceptable because "utilities are included." In their minds, they're already paying for these expenses.

Another intrinsic flaw of the "utilities included" model is that it offers no financial incentive for tenants to notify property management when maintenance problems occur. Water leaks are a perfect example. A broken toilet flapper can waste hundreds of gallons of water in a short amount of time. The owner relies on the tenant to inform the maintenance team when an issue like this arises. Tenants, however, aren't paying directly for the water bill so there's less incentive for them to respond quickly...if at all.

## ARE YOU AN EXPERT BUDGET-ER?

If you include utilities at your multifamily complex, you're already familiar with the never-ending budgeting game. To ensure that you cover utility costs, you'll have to accurately answer questions like:

- What percentage will utility rates increase this year?
- Where should I set my rents to make sure I don't lose money?
- How much water, gas, and electricity will residents use?
- How can I cover utility expenses and still keep my rents competitive?

Some owners choose to set their rents high enough so that, no matter what, utility costs get paid. This can have a negative effect on your occupancy rate, however, by putting your complex at the upper end of the price curve and making it less attractive to prospective renters. The flip side is that if you set your rents too low, you risk losing money.

## NERVOUS ABOUT CHANGING?

Some property managers and owners have initial concerns about separating utilities from the rent and billing tenants directly. They worry that renters will leave or that it will make their apartments less appealing than their competitors who do include utilities. It's worthwhile then to consider how a prospective tenant might evaluate two different apartments--one with utilities included and one with a resident utility billing program.

Assume you offer a two bedroom apartment for \$750 per month (resident-paid utilities) and another complex down the road offers a two bedroom unit for \$800 per month (utilities included). Your complex will naturally be more appealing from a rental price perspective, and everything else being equal, will see more traffic. But your property is also more advantageous from a total housing cost perspective too. Here's why.



When residents are billed for utilities directly, whether through a Ratio Utility Billing System (RUBS) or via utility submeters, they can influence their own monthly housing costs. If they conserve utilities, their bills will be lower. And if residents quickly report maintenance issues and minimize wasteful usage, everyone's utility bills will decrease.

## THE FINANCIAL IMPACT OF CONVERTING TO TENANT-PAID UTILITIES

An analysis of the financial benefits of billing tenants for utilities is worthwhile. Assume you have a 150 unit complex and the monthly water bill is \$6,300. If you can transition 80% of this bill back to tenants, you will realize:

Monthly savings:  $80\% \times \$6,300 = \mathbf{\$5,040}$

Yearly savings:  $12 \text{ mos.} \times \$5,040 = \mathbf{\$60,480}$

What do you have to invest to achieve these savings? Nothing more than your time. And if you use a third party utility billing provider, the time requirement is next to nothing.

## IT'S EASIER THAN YOU THINK

The exciting news for owners is that you can quickly and easily separate utilities from the rent and bill tenants directly for water, gas, and/or electricity. You can even include trash, cable, Internet, rent or other recurring fees on the bill to make paying simpler for tenants.



The two most widely used methods for multifamily utility billing are:

1. RUBS billings
2. Submetered billings

RUBS or "Ratio Utility Billing System" is a method of allocating utility costs to tenants based on number of occupants, size of the apartment, or some other factor. Submetered billings require that a utility metering system be installed to directly measure tenant usage. This usage data is used to calculate resident bills.

## RUBS IS A GREAT WAY TO START

The fastest, least expensive way to transition utility expenses back to residents is to implement a RUBS. Here are the steps:

### #1 - Research utility billing regulations in your state, county, and city

While most states approach resident utility billing in a similar way, a few states have unique rules. For example, in Colorado, as long as an owner has a signed lease in place stating that residents can be billed for utilities, the entire amount of the master-metered bill can be allocated back. The owner does not have to take a common area deduction of any kind.

In Texas, however, not only do you need a lease agreement signed by the tenant permitting utility billing, the Texas Commission on Environmental Quality (TCEQ) specifies the way bills are to be calculated and the deductions owners must take.

Either research the regulatory laws where your complex is located, or rely on your third party billing provider to perform this task. If you conduct your own research, your local or state apartment association is a helpful place to start.



### #2 - Have residents sign a new lease or lease addendum

Each resident must sign a lease agreeing that the owner/property manager can bill for utilities. At a minimum, the lease addendum should include: how bills will be calculated, when payments are due, any common area deductions (CADs). A sample lease addendum from the TCEQ is listed at the end of this article.

### #3 - Setup the billing process

To initiate resident billing for water, for example, you'll need mailing information, occupancy figures for each household, and copies of the master-meter water bills. Each month you will review updated move-in/move-out data to ensure that you are billing the proper tenants.

Use the information (above) to calculate tenant bills. Establish a billing schedule. For example:

- Billing period - 5th to the 5th. *You want these dates to coincide with the master-meter billing period.*
- Delivery date - Bills will be mailed on the 10th
- Due date - Bills are due on the 25th
- Past due notification date - Late letters will be sent on the 30th



#### **#4 - Notify tenants**

We recommend notifying tenants in advance of sending the first bill and clearly describing how the process will be administered. Be sure to include accurate contact information and describe how the bills will be calculated. Some property managers host community Q&A sessions to provide a forum for residents to ask questions and encourage a smooth transition.

#### **#5 - Send the first utility bills**

When you send the first bills, make sure resident support is available. We recommend offering different payment options so that tenants can pay by mail, telephone, or online via the Internet. Clearly define who payments should be made out to and where those payments should be delivered.

#### **#6 - Process payments and manage past due accounts**

Processing payments, keeping up with collections, and generating management reports is a labor and time intensive process. An accounting system or utility billing application will be useful to track your financial transactions. Be vigilant about notifying tenants when they are past due as this will improve collections.

### **CONCLUSION**

There's a real opportunity for multifamily owners and property managers, who currently include utilities in their rental fees, to improve their profits. By separating utility costs and billing tenants directly, owners can increase the value of their properties, insulate themselves from rising utility prices, and it's beneficial for tenants. Third party billing providers can help you get started quickly, competently manage the process on your behalf, and enable your staff members to focus on other important duties.

### **ABOUT AMERICAN CONSERVATION & BILLING SOLUTIONS, INC.**

AmCoBi offers the most affordable, highest quality utility billing services available in the multifamily industry. We also design, install, and service gas, electric, and water submetering systems. AmCoBi helps multifamily owners and managers improve profitability, reduce utility expenses, and save money.



# ATTACHMENT #1 - TCEQ SAMPLE LEASE ADDENDUM FOR ALLOCATING WATER/WASTEWATER COSTS

**1. Addendum.** This is an addendum to the TAA Lease Contract for Apt. No. \_\_\_\_\_ in the \_\_\_\_\_ Apartments in \_\_\_\_\_, Texas.

**2. Reason for allocation.** When water and wastewater bills are paid 100 percent by the property owner, residents have no incentive to conserve water. This results in a waste of our state's natural resources and adds to the overhead of the property—and that usually means higher rents. Allocation of water bills saves money for residents because it encourages them to conserve water and wastewater. We as owners also have incentive to conserve because we are required by law to pay a portion of the total water bill(s) for the entire apartment community.

**3. Your payment due date.** Payment of your allocated water/wastewater bill is due 16 days after the date it is postmarked or hand delivered to your apartment. You agree to mail or deliver payment to the place indicated on your bill so that payment is received no later than the due date. You will pay a late charge of 5 percent of your water/wastewater bill if we don't receive timely payment. If you are late in paying the water bill, we may not cut off your water; but we may immediately exercise all other lawful remedies, including eviction—just like late payment of rent.

**4. Allocation procedures.** Your monthly rent under the TAA Lease Contract does not include a charge for water and wastewater. We may include this item as a separate and distinct charge as part of a multi-item bill. Instead, you will be receiving a separate bill from us each month for such utilities. We will allocate the monthly mastermeter water/wastewater bill(s) for the apartment community, based on an allocation method approved by the Texas Commission on Environmental Quality (TCEQ) and described below. The allocation method that we will use in calculating your bill is noted below and described in the following subdivision of Section 291.124(e)(2)(A) of the TCEQ rules (check only one):

- subdivision (i) actual occupancy;
- subdivision (ii) ratio occupancy (TCEQ average for number of occupants in unit);
- subdivision (iii) average occupancy (TCEQ ave. for no. of bedrooms in unit);
- subdivision (iv) combination of occupancy and square feet of the apartment; or
- subdivision (v) submetered hot/cold water, ratio to total.

The normal date on which the utility company sends its monthly bill to us for the water/wastewater mastermeter is about the \_\_\_\_\_ day of the month. Within 10 days thereafter, we will try to allocate that mastermeter bill among our residents by allocated billings.

**5. Common area deduction.** We will calculate your allocated share of the mastermetered water/wastewater bill according to TCEQ rules. Before calculating your portion of the bill, we will deduct for irrigation of landscaping and all other common area uses, as required by TCEQ rules. We will also deduct for any utility company base charges and customer service charges so that you won't be paying any part of such charges for vacant units. No administrative or other fees will be added to the total mastermeter water/wastewater bill(s) to be allocated unless expressly allowed by TCEQ rules. No other amounts will be included in the bill except your unpaid balances and any late fees you incur. If we fail to pay our mastermeter bill to the utility company on time and incur penalties or interest, no portion of such amounts will be included in your bill.

**6. Change of allocation formula.** The above allocation formula for determining your share of the mastermetered water/wastewater bill cannot be changed except as follows:

- (1) the new formula is one approved by the TCEQ;
- (2) you receive notice of the new formula at least 35 days before it takes effect; and
- (3) you agree to the change in a signed lease renewal or signed mutual agreement.

**7. Previous average.** As required under TCEQ rules, you are notified that the average monthly bill for all dwelling units in the previous calendar year was \$\_\_\_\_\_ per unit, varying from \$\_\_\_\_\_ to \$\_\_\_\_\_ for the lowest to highest month's bills for any unit in the apartment community for this period, if such information is available. The above amounts do not reflect future changes in utility company water rates, weather variations, total water consumption, residents' water consumption habits, etc.

**8. Right to examine records.** During regular weekday office hours, you may examine:

- (1) our water/wastewater bills from the utility company;
- (2) our calculations of your monthly allocations; and
- (3) any other information available to you under TCEQ rules. Please give us reasonable advance notice to gather the data. Any disputes relating to the computation of your bill will be between you and us.

**9. TCEQ.** Water allocation billing is regulated by the TCEQ, which has published a summary of the rules (called a tenant guide). A copy of this summary or a copy of the rules is attached. This addendum complies with those rules.

**10. Conservation efforts.** We agree to use our best efforts to repair any water leaks inside or outside your apartment no later than 7 days after learning of them. You agree to use your best efforts to conserve water and notify us of leaks.