

Water and Sewer Rate Study

Questions & Answers

March 2022

- 1) *What are the main assumptions built into the rate model to arrive at the proposed Water and Sewer rate increases?*

Assumptions for the Rate Study in each utility are as follows:

- Labor, professional/special services increased by 6.5%
- Materials and supplies, equipment, utilities increased by 10%
- Water and sewer increased by 17.5%
- Annual customer growth of 0.1% annually
- Operating budget contingency in year 1 in the amount of \$200,000 for both utilities
- Salaries for additional positions in the amount of \$230,000 for both utilities
- Combined beginning reserve balance was approximately \$16.5 million at the beginning of FY 2022
- Analysis assumes annual debt service terms of 4.5% for 20 years
- Future year projections based upon inflationary assumption of 3.5%

- 2) *How much of the recommended rate increase(s) are due to the deferral of rate increases for 2020/21 and 2021/22?*

Rate increases in for FY 2021 were recommended to be 4.2% for water and 6.4% for sewer with future years estimated at 4.2%. The deferral of rate increases for the last 2 years account for approximately 8.4% of the proposed water utility rate increase and 10.6% of the proposed sewer utility rate increase.

- 3) *What cost increases have been built into the rate model(s) (i.e. Staffing, O&M, Capital adjustments)?*

See assumptions as provided in question #1 above. No other increases over and above the budget and assumptions for projecting O&M have been included. The rate model also takes into consideration the identified capital needs for each of the utilities. In this way, the proposed rates are sufficient to meet ongoing capital replacement and improvements over the long-term. Capital improvement projects provided by the District were also increased annually by a 2.7% inflationary factor to reflect the future costs of the project.

- 4) *Do the recommended Sewer Rates eliminate the \$ 2million per year Capital Charge currently being collected to support the Effluent Pipeline Project?*

Yes and no. The analysis eliminates the \$2 million in annual funding for the effluent pipeline funding (e.g., prefunding of the project). However, roughly \$2 million is required in the future years to fund the annual debt service need pay for the remaining effluent pipeline project costs. The manner in which the District establishes the capital charge will result in increases, and decreases, over time as the capital plan is updated

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and refined. As a result, the Board should expect that as the capital plan is updated, or project costs change (like we've seen recently) the capital charge will need to be revised to reflect the projected costs from year to year.

- 5) *How much of the Sewer Rate increase(s) is attributable to the cost the Effluent Pipeline Project?*

Pipeline cost in the rate model is estimated to be \$44.8 million. Prior rate studies included \$2.0 million per year in annual funding contributions for the Effluent Pipeline Project, with an underlying assumed project cost of \$23.0 million.

The impact on required rates is not an exact calculation, and varies over the projected time period, given the debt service impact to rate levels for this project. In addition, the debt service is funded through the annual capital charge. Given this, the capital charge has increased by approximately 21% from FY2022/23-FY 2025/26 when annual debt service is being fully funded.

- 6) *What is the baseline funding plan for the Effluent Pipeline Project used in the Sewer rate model?*

As outlined in the capital funding analysis, the effluent pipeline project costs are being funded entirely through existing reserves in FY2022/23. Project costs in FY 2023/24-FY 2025/26 are funded entirely through long-term borrowing.

- 7) *How might alternative financing options impact future sewer rates?*

Alternative financing (e.g., low interest loans) or grant funding would reduce the overall capital charge revenue necessary to support the effluent pipeline project. Three alternatives were developed to provide the Board an understanding of how future rate levels may be impacted.

As noted in question #5, the effluent pipeline project costs in FY2022/23 are funded entirely from current reserves. Given this, alternative funding approaches for the effluent pipeline project has no impact on the FY2022/23 rate revenue adjustment need.

When reviewing the loan alternative, the assumption was for a low interest loan for 20 years at 2.5% interest. This results in the ability to decrease the rate adjustments in FY2023/24-FY2026/27 by 7% cumulatively over that time period.

Assuming a grant of \$5 million in FY2023/24, the overall revenue adjustment could also be lowered by 7% cumulatively over the FY2023/24-FY2026/27 time period.

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When assuming a total of \$10 million in grant revenues (\$5 million in both FY2023/24 and FY2024/25), the overall revenue adjustment could be decreased by 12% cumulatively over the FY2023/24-FY2026/27 time period.

Again, it is important to note, that as the Board is considering rate revenue adjustments for FY2022/23, these alternatives do not change the FY2022/2023 revenue adjustment needs. The study should also not develop proposed rates based on an assumed grant or lower-interest borrowing given that they are not certain. Should the District be successful in receiving additional grant funding, or receive a low interest loan, the Board can revise the rate plan to reflect this in the future.

- 8) *Why have water and sewer rate revenues increased over the past two years, given that rates have not been adjusted since FY2019/20?*

Rate revenues will vary from year to year based on the actual consumption patterns of the District's customers. In dry years, outdoor use generally increases and higher levels of revenue may be received. The opposite is also true, in wet years, revenues will be less than projected given the lower than average water consumption.

As the District continues to evaluate rates on an annual basis, these considerations can be taken into account. However, from a planning perspective (i.e., rate study) we cannot plan on a dry year, or wet year, to project revenues. This will continue to occur regardless of the level of the rates. However, the additional revenue from consumption is not sufficient to fund the identified operating and capital needs as outlined in the rate study.

- 9) *How sensitive is the rate model (recommended rates) to assumptions related to water consumption?*

Consumption plays a role in the overall revenue profile. However, the majority, approximately 63%, of the District's revenue is received through the fixed charges (meter charge, capital charge, admin fee, defensible space). As a result, changes in consumption should have a minimal impact on the overall revenues. For example, if residential consumption was reduced by 10%, the revenue only decreases by 4%.

However, for the irrigation customer class, the majority of the revenue is collected through the consumption charge. For these customers, a reduction in consumption would have a larger impact on irrigation revenues. However, irrigation revenues are a smaller proportion of the overall District revenues, and therefore, it does not have a significant impact on total revenue levels.

- 10) *What growth factor is built into the rate model? What is the basis for this factor?*

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For both water and sewer, a 0.10% annual growth factor was used. This was based on a review of the historical change in the number of accounts for the District. This average reflects the typical increase in the number of customers annually. While additional customer growth on the system can have an impact, it is generally minimal, and a one-time increase to revenues through fees.

However, the majority of the fees charged to customers reflect the cost of providing the service to the customer (e.g., plan check, inspections, meter) and therefore only offset costs being incurred. For the connection charges, these revenues would be placed into reserves and used as appropriate. As noted in the rate study, District reserve minimums are not being met until the outer years of the five-year plan. Given this, additional revenues would simply allow the District to meet minimum target levels sooner.

- 11) *Are utility connection charges and PW inspection fees being adjusted? How much revenue does these adjustments account for?*

The fees are recommended to be adjusted by 12% which reflects the Construction Cost Index increase from January 2019 to January 2022. The proposed increase in water and sewer connection fees is estimated to yield an additional revenue of \$2,400 and \$3,780, respectively.

- 12) *How does the rate model factor in the funding reserved by the Board for the Effluent Pipeline Project?*

The available effluent reserve funds are used in their entirety to fund the costs of the effluent pipeline project in FY2022/23. If these reserves were not available, the District would need outside funding (e.g., loans, grants), or absent these funds annual rate revenues, to fund the costs in FY2022/23. This would result in a larger increase in rate revenues being necessary to fund these costs, or fund the annual debt service payments, increasing the overall revenue adjustments necessary for the sewer utility.

- 13) *What is the impact of the recently-approved Reserve Policy on the proposed water and sewer rates?*

Since the reserves identified under the policy are not met, the policy does have an effect on the rates as revenue needs to be generated to meet the reserve levels. However, as developed, the rate model achieves the reserve levels over time rather than in year 1 which is a best practice and minimizes the rate impacts in the short-term.

- 14) *Do the proposed rates result in achieving reserve levels established by the new policy?*

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Yes, the reserve levels will meet the policy requirements within 3 to 5 years.

15) *What options does the Board have to reduce the required Year 1 rate increases?*

The Board can reduce rates by reducing capital or operating expenses. Any reduction of the recommended year 1 rate increase will likely lead to higher than proposed increases in future years to fund the identified O&M and capital needs.

16) *Why are CIP costs in rate model significantly greater than last Board-approved Multi-Year CIP Plan?*

The CIP project list and costs were updated as the Rate Study got underway in the fall of 2021. The CIP is a living document and PW staff updated the Board approved FY2021/22 CIP to reflect new projects and costs that had been recently identified. This was done to reflect the anticipated future costs so that the rate analysis could support the identified needs. Since CIP costs in the Utility Rate Study are largely consistent with the costs reflected in the updated Multi-year CIP plan presented to the Board of Trustees at the Budget Workshop held on March 1st. In addition, funding for the Pipeline project is reflected at approximately \$10M over each of the first four years for construction of the project, which is \$8M over the \$2M that was annually being collected as funding for the project.

17) *Can the anticipated connection and CIP fees from the proposed 40-unit condominium development be used to offset the proposed rate increases?*

PW staff has estimated the connection fees from the proposed development to be approximately \$230,000 for water and \$340,000 for sewer. Receipt of these fees is not guaranteed until the development receives their permit at which time the fees are paid to the District. The collected fees would also be considered “one-time money” as they are not recurring on an annual basis.

It is important that the revenue collected to support the ongoing maintenance and capital costs of the water and sewer utilities be received annually. Should the project move forward and the District collect the fees, the funds would be placed in the associated utility fund balance. This would help achieve required policy reserves and potentially reduced revenue requirements in future years.