



ADDENDUM TO THE WATERWORKS FACILITIES ASSESSMENT AND COST OF SERVICE EVALUATION REPORT

November 2015

BACKGROUND

In April 2015, Carollo Engineers (Carollo) completed the Waterworks Facilities Assessment and Cost of Service Evaluation Report (Report), on behalf of the Ventura County Waterworks District No. 8 (District). The Report assessed the condition of the facilities that comprise the District's water distribution system, and developed a risk-based capital improvements program to ensure its sustainability. The Report included a detailed cost-of-service evaluation that analyzed the District's revenues and expenditures for operations and maintenance of its water facilities used to deliver water service to its customers. Carollo determined that the District's revenues are insufficient, failing to cover its planned expenditures and maintain adequate reserve funds for capital expenditures and unplanned fiscal emergencies. Based on this analysis, Carollo provided a recommendation for a five-year revenue increase with an associated water rate increase.

The revenue and rate increases were summarized in the Report and presented to the District's Board of Directors (Board) on June 15, 2015 in support of the District's Proposed Water Rate Increase. District staff recommended that the District initiate the Proposition 218 process for the water rate increases, including notifying rate payers and scheduling a Public Hearing, to implement the proposed rate increase on October 1, 2015. At the Council/Board meeting, the District's Board of Directors authorized staff to proceed with the Proposition 218 process based on the water rates calculated by Carollo and included in the Report.

However, due to administrative issues with the Proposition 218 noticing process, implementation of the proposed rates identified in the Report was postponed and not implemented as originally planned. Subsequently, the District requested that Carollo revise the financial plan and rates analysis, taking into account various changes in several key Report assumptions as well as certain situational changes described below that developed in the interim. The Board reviewed the revised financial plan and the recommended revised rate increase at a Council/Board meeting on September 21, 2015 and recommended that District staff proceed with the Proposition 218 notification process and to set a Public Hearing based on the proposed rates included in this Report Addendum.

REVISIONS TO REPORT ASSUMPTIONS

Several assumptions in the Report will need to be revised due to situational changes that occurred following the June 15, 2015 Council/Board Meeting. While these revised assumptions will impact the resulting financial plan and proposed rates, the basis of the revenue requirements analysis, cost-of-service evaluation, and functional allocations developed in the Report have not changed and remain reasonable and consistent with industry standards. The following assumptions were the only factors updated in the financial model in order to develop the revised financial plan and proposed rates.

Water Demand Reductions Due to Water Conservation

In April 2015, the California State Water Resources Control Board (SWRCB) dictated that all urban water providers throughout the State reduce demand by 25 percent, with individual agency targets provided based on existing demands and customer usage rates. The District is required to reduce demand by 28 percent compared with its 2013 baseline. Through the end of August, the District's customers have reduced usage by approximately 30 percent, exceeding the State's mandated target.

Water demand projections are an important factor in the financial model as they directly impact the District's estimated expenses for purchased water, which are the largest portion of the District's budget, and the projected revenues from water sales. The initial proposed rates in the Report were developed prior to the State's drought-mandated actions, and built upon baseline usage in Fiscal Year (FY) 2013/14. For the revised analysis, the initial decrease in demands for FY 2015/16 have been estimated at 25 percent, based on initial water sales figures through the summer months of 2015. The District believes these dramatic cutbacks are not sustainable and therefore, in the following four years, forecasts demands to increase by 5 percent annually. This anticipated bounce-back in demands is based on the District's observations following previous droughts.

Calleguas Water Rate Increase for January 2015

Calleguas Municipal Water District (Calleguas), a member agency of the Metropolitan Water District of Southern California, provides about 98 percent of the District's water supply. In January 2015, Calleguas initiated a rate increase for its retail agency customers. For the District, this increase amounted to approximately 4 percent in per acre-foot water purchasing costs for calendar year 2015.

As the bulk of Carollo's initial analysis took place prior to 2015, the Report and initial proposed rates were based on Calleguas 2014 rates, and it was assumed that all future increases would be recovered as a "pass-through" added directly to the District's rates as a per billing unit surcharge. Based on discussions with the District staff, it was decided that the updated financial analysis should be built upon Calleguas' 2015 rates, with the District's resulting water purchase costs as the baseline, instead of the 2014

rates. When calculating the pass-through, the District will use the 2015 Calleguas rates (fixed and variable) as a baseline, and increase the retail rates that the District charges by the difference between the new Calleguas rate and the prior year Calleguas rate. For 2016, the Calleguas pass-through has been calculated at \$0.16 per billing unit and added to the rate tables included in this Addendum.

Implementation Delay in Water Rate Increases

As the June 2015 water rate increases were not implemented as originally scheduled in the Report, there has been a delay in the anticipated additional water revenues, thus extending the period during which District expenses are exceeding revenues. As a result, the financial projections were revised to reflect a delay in the implementation of the water rate increases to a projected start date of January 1, 2016.

In addition, the District has decided to implement future water rate increases on January 1st of each year, so that the Calleguas pass-through increases and the District's water rate increases will occur simultaneously, one time per year. Because the District's fiscal year begins on July 1st of each year, and budgeting for operations and capital improvements are based on the fiscal year, this will effectively delay the District's rate increases and anticipated additional water revenues by 6 months each year. Carollo's original analysis in the Report was based on the assumption of District rate increases on July 1st of each year (with the exception of the 2015 rate increases to be implemented on January 1, 2016) and Calleguas pass-through increases on January 1st of each year. This Addendum provides the revised financial projections based on the change in the assumption for future District and Calleguas pass-through rate increases to occur simultaneously on January 1st of each year.

Phased Shift in Variable to Fixed Charges

Carollo's initial analysis recommended increasing the portion of revenues collected from fixed service charges, which are set charges billed to every customer, regardless of usage, with the goal of better recovering the District's fixed costs. This recommended shift would place the District better in line with current industry best practices that recommend a 70/30 percent split of revenues between variable and fixed, respectively. The initial rate analysis in the Report recommended that this shift take place within the first year of new rates.

Based on direction from the District staff, Carollo's revised analysis phases the shift of District revenues from variable commodity to fixed service charges over five years, mitigating the immediate impact to the service charges for the District's customers in the short-term. Additionally, the District staff identified \$61.00 as a limit for the single-family residential bimonthly service charge. Carollo modeled the needed volumetric rate increase to cover this cap in years 2019 and 2020. The lost revenues from capping the

single family service charge were then re-allocated to the commodity portion of the single family rate to provide appropriate cost recovery.

REVISED WATER RATE ANALYSIS

Carollo provided the District with various alternative water rate scenarios based on the revised Report assumptions and the updated financial model. At the September 21, 2015 Council/Board Meeting, the District's Board of Directors recommended proceeding with the Proposition 218 notification process and setting a public hearing for the scenario with the following water revenue projections and rate components:

- Five-year revenue increases of 8-8-4-1-1 percent starting with fiscal year 2015/16.
- Implementation of District fiscal year 2015/16 water rate increases and Calleguas 2016 pass-through effective January 1, 2016, and on January 1st of future years for 2017 through 2020 rate increases.
- Five-year phased shift in variable commodity to fixed service charges.
- Change to a uniform single-family residential (SFR) rate from the current three-tier increasing block rate structure.
- Cap the fixed Service Charge for SFR customers at \$61.00 per two-month billing cycle.

The results of the proposed financial scenario in terms of effective revenue adjustments for the next five years are shown in Table 1, which is an update to Report Table 3.5.

Table 1 Proposed Revenue Adjustments Schedule

Fiscal Year	Proposed Revenue Adjustments* (%)	Effective Revenue Adjustments (\$)	Proposed Implementation Date
FY 2015/16	8.00%	\$764,000	January 1, 2016
FY 2016/17	8.00	1,282,101	January 1, 2017
FY 2017/18	4.00	717,521	January 1, 2018
FY 2018/19	1.00	193,431	January 1, 2019
FY 2019/20	1.00	202,657	January 1, 2020
*Outside of FY 2015/16, proposed revenue adjustments do not include forecasted increases to Calleguas purchased water rates. Any future increases to the cost of purchased water would be automatically passed-through to rate payers as detailed later in this addendum.			

Table 2 provides an updated cash flow with the impacts of the proposed revenue adjustments. This table is a revision to Table 3.6 in the Report and incorporates actual fund balances for July 1, 2015 which are higher than FY 2014/15 budget projections

used in the original model. The results of the revenue requirements analysis show that the proposed rate increases do not generate annual revenues that are adequate to cover expenditures or provide an operating reserve contribution until FY 2018/19. In order to address the projected drawdown of reserve funds and extended negative cash flows for the next 3 years, the District may need to consider delaying capital projects to future years, or reducing annual operations and maintenance expenses.

Table 2 Revenue Requirements Analysis (Post-Increases, thousand dollars)

	FY 2015/16	FY 2016/17	FY 2017/18	FY 2018/19	FY 2019/20
<u>Water Revenues</u>					
User Charges	\$28,650	\$32,050	\$35,880	\$38,690	\$40,530
Other Revenues	2,550	2,590	2,620	2,660	2,700
Additional Revenues	-	-	-	-	-
Revenue from Annual Rate Increase	760	1,280	720	190	200
SFR Service Charge Cap Adjustment ⁽²⁾	-	-	-	-60	-850
Total Revenues ⁽¹⁾	\$31,970	\$35,920	\$39,210	\$41,470	\$42,580
<u>Expenditures</u>					
Personnel	\$5,010	\$5,160	\$5,320	\$5,480	\$5,640
Supplies/materials	24,730	26,020	27,190	28,470	29,760
Services	1,490	1,550	1,610	1,670	1,740
Reimbursements/transfers	1,860	1,930	2,010	2,090	2,170
Capital outlay	30	30	30	30	30
Debt service	-	-	-	-	-
Rate funded capital	3,730	4,890	3,980	2,690	2,240
Additional O&M	-	-	-	-	-
Total Expenditures ⁽¹⁾	\$36,850	\$39,590	\$40,140	\$40,430	\$41,590
Cash Flows	-\$4,880	-\$3,660	-\$920	\$1,040	\$990
Total Reserves	\$5,350	\$1,680	\$760	\$1,800	\$2,800
Days of Operating Reserves (Target: 90)	48 days	7 days	-2 days³	8 days	17 days
Note:					
(1) Totals may not sum due to rounding.					
(2) Adjustment for decrease in water rate revenues due to District proposed SFR Service Charge cap of \$61.00 in FY 2018/19 and FY 2019/20.					
(3) Days of operating reserves do not account for a minimum reserve fund level of \$1M that could be used in case of emergencies to cover a negative operating fund balance.					

The calculated bimonthly service charges and commodity rates for the proposed revenue adjustments with revised assumptions are shown in Table 3 and Table 4. These tables are updates to Table 3.10 and Table 3.11 in the Report.

Table 3 Proposed Service Charges (Bimonthly)						
Meter Size	Current	2016⁽¹⁾	2017	2018	2019	2020
Single-Family	\$33.38	\$38.85	\$47.20	\$54.85	\$61.00 ⁽²⁾	\$61.00 ⁽²⁾
Multi-Family	\$21.96	\$24.45	\$30.85	\$37.00	\$42.70	\$48.85
3/4"	\$44.00	\$56.90	\$67.60	\$77.10	\$85.20	\$93.95
1"	\$87.99	\$92.90	\$108.40	\$121.65	\$132.40	\$144.00
1.5"	\$175.98	\$182.90	\$210.40	\$232.95	\$250.45	\$269.20
2"	\$307.97	\$290.90	\$332.75	\$366.55	\$392.10	\$419.40
3"	\$659.93	\$633.00	\$720.35	\$789.55	\$840.60	\$895.15
4"	\$1,319.86	\$1,137.10	\$1,291.55	\$1,413.00	\$1,501.60	\$1,596.20
6"	\$2,639.72	\$2,523.35	\$2,862.30	\$3,127.35	\$3,319.35	\$3,524.10
Notes:						
(1) Rates have been modeled assuming the implementation dates shown in Table 1.						
(2) Actual calculated fixed charges for SFR in 2019 and 2020 are \$61.60 and \$68.90, respectively. This analysis accounts for the difference between these rates and the District proposed \$61.00 Service Charge cap as a water revenue adjustment shown in Table 2.						

Table 4 Proposed Commodity Charges per Billing Unit (Bimonthly)						
Customer Class	Current	2016⁽¹⁾⁽²⁾	2017⁽³⁾	2018⁽³⁾	2019⁽³⁾	2020⁽³⁾
Single-Family	<i>Tiered⁽⁴⁾</i>	\$3.40	\$3.36	\$3.36	\$3.25	\$3.15
Commercial / Multi-Family	\$3.06	\$3.41	\$3.37	\$3.36	\$3.25 ⁽⁵⁾	\$3.06 ⁽⁵⁾
Landscape / Schools / etc.	\$3.06	\$3.59	\$3.56	\$3.56	\$3.45 ⁽⁵⁾	\$3.26 ⁽⁵⁾
Lift Charge ⁽⁶⁾	\$0.09	\$0.09	\$0.10	\$0.11	\$0.12	\$0.13
Notes:						
(1) Rates have been modeled assuming the implementation dates shown in Table 1.						
(2) Calleguas has adopted a rate increase effective January 1, 2016 that causes a \$0.16 per Billing Unit (BU) increase. This increase is only shown in the 2016 Commodity Charges.						
(3) Commodity Charges for 2017 through 2020 do not include Calleguas future rate increases. Calleguas rate increases will be added to the future years reflecting their yet to be determined increases.						
(4) Current SFR tiered rates are \$2.58, \$3.09, and \$4.02 for tiers 1, 2, and 3, respectively.						
(5) Commodity Charges for Commercial/Multi-Family and Landscape/Schools have been adjusted for 2019 and 2020 by -\$0.01 and -\$0.10, respectively, to maintain equity across customer classes due to the SFR Service Charge cap in these years. The resulting water revenue adjustments are included in the SFR Service Charge Cap Adjustment shown in Table 2.						
(6) Charged per unit of lift per HCF.						

For comparison purposes, the typical bills for Single Family Residential (SFR) customers were calculated for the current and proposed rates at various bimonthly water usages as shown in Figure 1. This figure is an update to Figure 3-4 in the Report.

Figure 1 – Typical SFR Bill Comparison

