

TO: BOARD OF DIRECTORS

FROM: MARIO IGLESIAS  
GENERAL MANAGER 

DATE: APRIL 6, 2017

**AGENDA ITEM  
E-1  
APRIL 12, 2017**

**REVIEW DRAFT COST OF SERVICE PROPOSED FINANCIAL PLAN  
AND CONSIDER WATER RATE COST RECOVERY STRUCTURES**

**ITEM**

Receive Financial Plan and Water Rate Study Presentation and consider cost recovery options to fund the Water Enterprise. [RECOMMEND REVIEW AND DISCUSS FINANCIAL PLAN AND WATER RATE OPTIONS AND DIRECT STAFF].

**BACKGROUND**

The Nipomo Community Services District ("District") provides customers in its service area with a safe drinking water supply through its water enterprise. To accomplish this critical mission the District must collect fees from its customers to meet operational and maintenance expenditures. District revenue requirements for the water enterprise are supported primarily through water rates and charges. The District conducts water rate studies every three to five years to evaluate the current and future projected financial position of the water enterprise.

On October 26, 2016, your Board awarded a contract to Tuckfield and Associates ("Tuckfield") to conduct a water rate study ("2016 Rate Study"). There have been two water rate studies in the last six years, one in 2011 and one in 2014. The 2014 rate study was necessary when a second source of supply was introduced into the District's water supply portfolio. In July 2015 the Nipomo Supplemental Water Project ("NSWP") began importing water onto the Nipomo Mesa. The District now has two sources of water supply, groundwater produced from groundwater wells owned and operated by the District referred herein as Basin Water, and an imported water supply from the City of Santa Maria, referred herein as Supplemental Water.

The last Basin Water rate study was completed in July 2011. Your Board adopted a five-year rate schedule with the first rate adjustment beginning in November 2011 and adjusting annually through November 2015. This rate study was applied to the Basin Water rates exclusively as Supplemental Water was not yet being imported. The Basin Water rates have stayed constant for nearly 2 years.

In November 2014, your Board passed Resolution 2014-1360 establishing Supplemental Water rates and charges. In July 2015, Supplemental Water first flowed onto the Nipomo Mesa through the NSWP and the rates and charges for Supplemental Water were implemented. The rate study for Supplemental Water addressed the revenue needs for the first three years of operations and maintenance of the NSWP. These rates and charges also recovered the cost of purchased water from the City of Santa Maria. The last adjustment for Supplemental Water is set to take effect in July 2017, with an increase of four cents per billed unit. One billing unit is equivalent to one-hundred cubic feet (HCF) or 748 gallons.

The 2016 Rate Study proposes to combine rates and charges of the two sources of supply into one rate structure. The District's Basin Water and Supplemental Water rate adjustments take effect at different times of the year. The City of Santa Maria adjusts its water rates in July and the District applies that adjustment to its customer's bills at that time as a pass-through cost. The District's Basin water rate adjustments are on a calendar year cycle, January through December. Staff is recommending these costs be combined and a single adjustment be made based on a calendar year cycle starting January 2018.

The recent drought and the subsequent water conservation mandates by the State directed towards water purveyors required an overall 25% conservation objective. Nipomo was one of many water purveyors required to reduce consumption by 28%. As a result, water sales revenue is down approximately \$1.2 million annually. Reduced water sales have negatively impacted the water enterprise budget.

As previously mentioned, water rates are constructed to support the water enterprise budget. Budget forecasts are based on revenue and expenditure assumptions. On the revenue side, rates and charges only recover monies needed to meet the cost of providing water service. Cash reserves are used to manage water sales variability. Where gaps develop between revenues and expenditures, cash reserves from the water enterprise make up the difference. The impact on cash reserves in the water enterprise are well below District reserve policy goals. The 2016 Rate Study demonstrates how, over a 10 year period, the District will stabilize its financial position and meet its reserve policy goals.

The 2016 Rate Study also shifts the District's revenue recovery model away from inclining tiered block rate structure where the cost of a unit of water increases as consumption increases. The 2016 Rate Study proposes a revenue recovery model that sets a uniformed cost for each unit of water consumed. The decision to shift away from a tiered rate model was driven by the recent San Juan Capistrano court ruling. The courts found that, while not prohibited, tiered rates must be constructed based on the incremental cost increase to produce water for each inclining tier. Water purveyors can no longer utilize tiered water rates to encourage water conservation unless they can provide evidence there is an incremental cost increase between each rate of their tiered rate structure.

Tuckfield's Water Rate Study presentation will provide the Financial Plan assumptions as well as several options for your Board's consideration as you evaluate potential water rate structures and their impact on the community. Included in the presentation will be an explanation of the methodology used to construct a fair, equitable, and defensible rate structure.

### **FISCAL IMPACT**

Budgeted staff time was used to prepare this staff report.

**STRATEGIC PLAN**

Goal 4. FINANCE. Maintain conservative, long-term financial management to minimize rate impacts on customers while meeting program financial needs.

4.4 Maintain adequate rates to fund future capital replacements.

Goal 6. GOVERNANCE AND ADMINISTRATION. Conduct District activities in an efficient, equitable and cost-effective manner.

Goal 7. COMMUNICATION. Use public outreach to communicate effectively with the public to obtain their input and build understanding and support for the District.

**RECOMMENDATION**

Staff recommends that your Board:

- receive and discuss the rate consultant's presentation,
- select public outreach approach - 2 alternatives provided,
- select a preferred rate option and direct rate consultant to Draft Report,
- direct staff to make the Draft Report available for comment through public workshops and to create a Public Hearing and Water Rate Implementation Schedule and provide this information to the Board at the next Board Meeting.

**ATTACHMENTS**

No Attachments