

TO: James L. App, City Manager
FROM: Doug Monn, Public Works Director
SUBJECT: Selection of Proposed Water Rate Structure and Water Capacity Charge
DATE: July 1, 2008

NEEDS: For the City Council to consider selection of a revised water rate structure, water capacity charges (connection fees), and authorize staff to proceed with customer notification.

- FACTS:**
1. Current water rates and water capacity charges generate revenues to provide drinking water to residents and businesses from groundwater with an allowance for a portion of initial Nacimientto Water Project expenditures.
 2. Improvements to the City water system are needed, primarily to improve quality and supplement the limited ground water supply especially during peak summertime demand periods, and also to provide adequate distribution, treatment, and water storage capacity.
 3. The planned and needed improvements amount to approximately \$210 million over the coming decade, including Nacimientto supply and treatment capital costs. Operations costs, debt service, etc. is in addition to this estimated capital cost.
 4. Areas of water system need include quality improvements and supply:
 - The hardness of well water is increasing over time, a sign that the groundwater basin is stressed. Customers react by softening water in their homes and businesses, adding to a problematic salt build-up in the City's waste stream. Softer supply would break this cycle of ever increasing salt loading into the watershed.
 - Each summer as weather heats up and irrigation needs increase, the City's existing well system cannot keep pace with demand. Storage tanks do not recover overnight, dropping ever closer to firefighting reserves. Supply is needed now to remedy that shortcoming.
 - Groundwater sources are stressed as evidenced by ever deeper well pumping depths and local ground water depressions. An alternative supply is required to assure continued water supply reliability.
 - More water supply is needed to reliably support General Plan build-out.
 5. In March 1992, the City Council committed to participation in the Nacimientto Water Project. Then, in August 2004, the Council entered into a delivery entitlement contract, formally securing 4,000 acre-feet per year of Nacimientto supplies. Also in 2004, Council adopted water user fees to begin phasing in payments for a portion of the Nacimientto project (Ordinance No. 882). The fees adopted were in the form of a \$6/month flat rate set to increase by \$6 each year until they reached \$36/month in July 2010. Council set out to modify that rate structure in 2007 (Ordinance No. 935) to cover the pipeline project actual annual debt service costs, adjusting the flat rate to increase to \$60 per month over time.

6. A petition signed by approximately 1,750 people was submitted opposing the modification. The Council chose to rescind the rate proposal.
7. On January 15, 2008, following initiation of a second rate modification effort and subsequent citizen request, Council directed that an independent third party expert study of water rates and water capacity charges be prepared in light of both the Nacimiento project and other planned water system improvements. Tonight's discussion is the result of that authorization.
8. A major aspect of the proposed water system improvements will be bringing Nacimiento Water into the City supply system. Both the supply and the debt obligations for the revenue bonds associated with Nacimiento Water begin in 2010.
9. The benefits to the community resulting from the planned improvements include a noticeable improvement in water quality (i.e. softer water) and the City's ability to keep up with summertime water demand. In the long term, the City will enjoy a properly-maintained distribution system along with more reliable supply, and reduced salt loading into the basin.
10. The revenues generated by the existing water rate structure are inadequate to sustain water system operations and supply in compliance with State Dept of Public Health, local fire code, and other requirements.
11. Similarly, the existing water capacity charges need updating to reflect new development's impact on the water system and the need for future water resources.

**ANALYSIS &
CONCLUSION:**

The revenue needs associated with operation of the water infrastructure system over the coming decade were analyzed in the report entitled "City of Paso Robles Water Rate Revenue Analysis Public Review Draft Report" dated June 2008, prepared by Kennedy Jenks Consultants.

Concurrently, the allocation of water system costs to new development was analyzed in the report entitled "Water Capacity Charge Study – Public Review Draft" dated June 2008, prepared by HF&H Consultants.

The foundation of both studies was that all pay their fair share for the City's water system. To that end, new development's share in each component of the water system was taken into account in establishing a revenue program from both the water rates and water capacity charges.

In keeping with prior Council direction and public input, a variety of water rate structures was analyzed. These included 1) an all-fixed rate approach by which each user would pay a flat rate each month regardless of the amount of water used; 2) a combination of fixed and variable rate similar to the current rate structure; and 3) and all-variable rate structure in which users pay according to the amount of water use.

For the water capacity charges, the recommended charges would pay for one-half of the City's current entitlement in the Nacimiento Water Project and one-half of the proposed water treatment plant costs. Further, revenue from new development would be used to secure additional water (such as additional Nacimiento entitlement) over time. In other words, securing additional water supplies would be fully paid by new development.

Details about the proposed water rate structure and the water capacity charge analysis are included in the attached reports. In summary, the recommended water rate structure would have both a fixed monthly rate and a variable component, and would provide a tiered structure. For single family residences, the proposed water rate structure is such that usage rates would double as compared to the existing structure upon implementation, then increase +65% in year 2, +15% in year 3, and then pace at more modest annual increases of approximately +3% each year. The fixed monthly service charge for residential users would start at \$18 per month, increasing to \$19.98 in year 2, to \$22.48 in year 3, and to \$24.95 in year 4.

For example, a single family residence consuming an average of 30 hundred cubic feet (HCF) now pays \$56.40 per month. (30 HCF = 22,400 gallons; a supply of 245 gallons per person per day for a family of 3 for 30 days) Under the proposed rate structure, this same household would pay \$92.88 per month in year 1, \$143.42 in year 2, and \$164.64 in year 3. The rate structure depicted in the table below is recommended for adoption:

Recommended Water Rate Structure

Meter Size (inches)	Current Rate	Proposed Monthly Service Charge				
		2009	2010	2011	2012	2013
5/8" & 3/4"	\$18	\$18.00	\$19.98	\$22.48	\$24.95	\$24.95
1"	\$18	\$25.20	\$27.97	\$31.47	\$34.93	\$34.93
1-1/2"	\$18	\$32.40	\$35.96	\$40.46	\$44.91	\$44.91
2"	\$18	\$52.20	\$57.94	\$65.18	\$72.36	\$72.36
3"	\$18	\$198.00	\$219.78	\$247.25	\$274.45	\$274.45
4"	\$18	\$252.00	\$279.72	\$314.69	\$349.30	\$349.30
6"	\$18	\$378.00	\$419.58	\$472.03	\$523.95	\$523.95
8"	\$18	\$522.00	\$579.42	\$651.85	\$723.55	\$723.55
Proposed Consumption Charge (\$/HCF)						
All Customers Except Single Family						
All usage	\$1.28	\$2.56	\$4.22	\$4.86	\$5.00	\$5.15
Single Family Customers						
0-5 HCF	\$1.28	\$2.18	\$3.59	\$4.13	\$4.25	\$4.39
> 5 HCF	\$1.28	\$2.56	\$4.22	\$4.86	\$5.00	\$5.15

Note: HCF = 100 cubic feet, or 748 gallons.

Alternative rate structures were evaluated, including options for all fixed rates and all variable. The resulting rates are described in the following table. The all-fixed rate approach is simple, but is not consistent with the principle that each user pays a fair share, nor is such rate structure conducive to water conservation. The all-variable approach better aligns with payment for actual water usage, but does not create a dependable, predictable revenue stream – an important financial feature given that an estimated 70% of the City’s water system costs are fixed. For these reasons, the alternatives depicted in the table below are not recommended for adoption.

**Alternative Rate Restructuring Approaches
Considered for Paso Robles**

Rate Restructuring Alternatives						
Rate Alternative Description	FY 2007-08	2009	2010	2011	2012	2013
All Fixed Rate per Account/Month	n/a	\$74.29	\$111.59	\$127.93	\$134.09	\$137.65
All Fixed Rate/Equiv Meter/Month	n/a	\$65.13	\$97.82	\$112.15	\$117.54	\$120.67
All Variable Rate (per HCF)	n/a	\$3.54	\$5.31	\$6.08	\$6.35	\$6.50
Typical Bills (based on ¾” meter and 30 HCF)	Current Bill	Typical Bills				
100% Fixed Rate per Account	\$56.40	\$74.29	\$111.59	\$127.93	\$134.09	\$137.65
100% Fixed Rate per Equiv Meter	\$56.40	\$65.13	\$97.82	\$112.15	\$117.54	\$120.67
100% Variable Rate (at 30 HCF)	\$56.40	\$106.13	\$159.25	\$182.26	\$190.54	\$194.90

Water Capacity Charges for New Development

Water capacity charges for a single family residence are proposed to increase from \$9,119 to \$17,386 in year 1, to \$21,719 in year 2, then to \$28,687 in year 3 and increase annually thereafter according to the consumer price index. The following table lists the proposed capacity charges by connection (meter) size:

Proposed Water Capacity Charges

Connection Size	Current Charge as of July 1, 2008	Proposed Charge as of		
		January 1, 2009 ^a	January 1, 2010 ^b	January 1, 2011 ^c
5/8" and 3/4"	\$9,119	\$17,386	\$21,719	\$28,687
1"	\$15,226	\$29,035	\$36,271	\$47,812
1-1/2"	\$30,364	\$57,895	\$72,324	\$95,625
2"	\$48,601	\$92,667	\$115,762	\$152,999
3"	\$97,292	\$173,860	\$217,190	\$286,874
4"	\$152,002	\$289,825	\$362,056	\$478,123
6"	\$303,914	\$579,475	\$723,894	\$956,246
8'	\$486,280	\$927,195	\$1,158,274	\$1,529,994
10"	\$699,100	\$1,332,985	\$1,665,196	\$2,199,366

^a Proposed water capacity charges in year 1 would omit the water treatment plant and additional future water supply components.

^b In year 2, the water treatment plant component would be included.

^c In year 3, the full proposed capacity charges would be in effect; annual increases thereafter would be escalated according to published construction cost indices.

Rates and Charges in Nearby Communities

Many people have asked how the proposed rates and charges compare to other area communities. The findings are tabulated below:

Comparison of Monthly Water Bills and New User Connection Fees Single Family Residential Based on 30 HCF Usage (22,400 gallons)

Community	Monthly Meter Fixed Rate	Water Usage / Quantity Rate	Calculated Monthly Bill	Water Connection Fee^e
Cambria CSD ^a	\$12.15	\$6.17 to \$8.02	\$194.38	n/a - under moratorium since 2001
City of Morro Bay ^a	\$16.43	1.39 to \$12.62	\$179.93	\$2,063
City of San Luis Obispo ^b	\$0.00	\$3.71 to \$5.81	\$140.40	\$15,292
Oceano CSD	\$11.97	\$1.14 to \$4.09	\$119.52	5,030
City of Paso Robles - Proposed	\$18.00	\$2.18 to 2.56	\$92.88	\$17,386
Nipomo CSD ^c	\$16.98	\$1.81 to \$3.14	\$84.53	\$15,242
City of Pismo Beach	\$13.97	\$1.78 to \$2.31	\$80.09	\$1,500
City of Grover Beach	\$6.75	\$1.82 to \$2.20	\$64.45	\$4,791
City of Paso Robles - Current	\$18.00	\$1.28	\$56.40	\$9,119
Atascadero Mutual Water Co. ^d	\$14.5	\$1.122 to \$2.543	\$55.63	\$12,500
City of Arroyo Grande	\$5.25	\$1.16 to \$1.77	\$42.39	\$2,910
Templeton CSD	\$12.19	\$1.17 to \$2.62	\$35.29	\$13,453 (proposed at \$25,000)
Community Average (Excluding City of Paso Robles) =			\$95.49	\$8,087

Source Documentation:

Basis is for 5/8 and/or 3/4 inch meter; HCF = hundred cubic foot.

^a Monthly fixed charge includes 3 HCF.

^b Current single family rate is a 3-tiered rate structure with no fixed service charge; a 5% utility user tax is also applied to the water portion of the bill (excluded from this comparison).

^c Average of Town and Blacklake Subdivision rates

^d Monthly fixed charge includes 2,000 gallons (2.67 HCF); quantity rates shown are per HCF

^e Agencies define this in a wide variety of ways; common cost elements of such fees are tabulated here.

Many factors were taken into account in proposing Paso Robles' water rates and charges. Some noteworthy considerations are:

- Currently, the fixed rate component of the water rate structure is the same regardless of whether a customer has a 5/8-inch meter (as is typical for a single family residence) or, say, a 2-inch meter needed for a higher water using business. In keeping with the foundation of all pay a fair share, the recommended fixed rate component would be higher for larger meters.
- Current City practice is to allow customers to apply for a "life line" water rate, allowing low income customers to benefit from lower water rates. The proposed rate structure would extend the "life line" lower rate to all residential customers such that the first tier of water use (up to 5 hundred cubic feet per month¹) would be delivered at a reduced unit cost. This tiering has the added benefit of rewarding low water use customers for their water conservation success.
- Current City practice is to provide a credit back to City park/facility and school irrigation in proportion to public usage. Any school that opens its recreational fields for public recreation is eligible for this credit, as is any municipal park or facility. The proposed rate structure would cease this practice and approach City park/facility billings as payable from the General Fund. Sports and event fees will require adjustment to provide a revenue stream for that water billing.

Both the proposed water rates and new user water capacity charges are proposed to go into effect on January 1, 2009. This implementation date is recommended for the proposed water rates to go into effect to allow time for required customer notification and to put the new rates into effect during a time of year when usage is traditionally low, thus allowing customers time for a seasonal adjustment.

New user water capacity charges would follow a similar phase-in. Projects for which complete applications are in place as of July 1, 2008, would be allowed through December 31, 2008, to have building permits issued at the current water capacity charge. All applications deemed complete after July 1, 2008, would pay the proposed, higher water capacity charges in accordance with the fee schedule.

Paso Robles is on the road to a well-planned, reliable water system and water resource portfolio. The Nacimiento Water Project plays a key role in that portfolio. The proposed supply and distribution systems are tailored around the City's obligation to provide for the public health including a safe and reliable water supply, qualitative challenges and peak demand shortages, and adopted General Plan. The aim of both the proposed water rate study and the water capacity charge analysis is to fairly generate revenues to meet those community needs.

POLICY

REFERENCE: General Plan, Economic Strategy; Urban Water Management Plan; Integrated Water Resource Plan; Nacimiento Water Project Entitlement Contract.

¹ It is common for water usage to be metered in units of hundred cubic feet (HCF). One HCF = 748 gallons.

FISCAL IMPACT: Failure to put new water capacity charges and water rates in effect would come hand-in-hand with the requirement to make the Nacimiento bond debt payments. In other words, the debt service would still have to be paid and if water rates were insufficient to do so, the City's General Fund would be used. The General Fund typically funds such things as police and fire, library services, children and senior programs, parks, and other City amenities. Serious budget cuts and notable reductions in such programs would result if water rates failed to go into effect.

- OPTIONS:**
- a.** Adopt one of the attached Resolutions No. 08-xx thereby selecting a water rate structure; and
 - 1.** Authorize initiation of the Proposition 218 procedures and instruct staff to send out public notices regarding the proposed water rate structure.
 - 2.** Introduce the proposed water capacity charges (connection fees) and instruct staff to send out advance notices regarding consideration for adoption at the July 15, 2008, Council meeting.
 - 3.** Instruct staff to draft a resolution for possible adoption of the water capacity charges on July 15, 2008; or
 - b.** Amend, modify, or reject the above option.

Prepared by:Christine Halley, Water & Utility Consultant,
TJ Cross Engineers, Inc.

Attachments

- 1) "Water Rate and Revenue Analysis Public Review Draft Report" dated June 2008, prepared by Kennedy Jenks Consultants
- 2) "Water Capacity Charge Study" dated June 20, 2008, prepared by HF&H
- 3) Alternative Resolutions No. 08-xx (fixed and variable rate structure), 08-yy (all fixed rate structure), and 08-zz (all variable rate structure)

Kennedy/Jenks Consultants

2355 Main Street Suite 140
Irvine, CA 92614
949-261-1577
949-261-2134 (Fax)

City of Paso Robles
Water Rate and Revenue
Analysis
Public Review Draft Report

June 23, 2008

Prepared for
City of Paso Robles
Department of Public Works
1000 Spring Street
Paso Robles, CA

K/J Project No. 0883005

Kennedy/Jenks Consultants

Engineers & Scientists

2355 Main Street, Suite 140

Irvine, California 92614

949-261-1577

949-261-2134 (Fax)

23 June 2008

Mr. Doug Monn
Director of Public Works
City of Paso Robles
1000 Spring Street.
Paso Robles, California 93446

Subject: Draft Report - Water Rate and Revenue Analysis
K/J 0883005

Dear Mr. Monn:

Kennedy/Jenks Consultants is pleased to submit the Water Rate and Revenue Analysis Draft Report to the City of Paso Robles (City). By way of process, we have submitted this report as a digital ".pdf" file for your distribution as appropriate within the City.

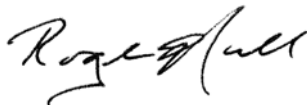
This Rate Study Report is a compilation of the analysis and findings of the City's water fund and incorporates the City's comments and direction obtained from previous draft work products. The results of the study are intended to serve as a plan for future revenue and rate adjustments based on the projected costs and utility water demands.

There are several important factors associated with the performance of the City's water fund that impact the study findings. First and foremost is the need to plan for the funding of the new Nacimiento water supply. The capital, debt, and operational costs associated with the City's transition to this source of supply will continue to place pressure on the City's water rates for several years. Fortunately, it appears that within the five-year planning period, the City's water system cost obligations and associated rate adjustments will have stabilized, positioning the City's water system for long-term financial stability.

We look forward to meeting with you to discuss the findings and recommendations of the study. Please contact us if you have any questions or need additional information.

Very truly yours,

KENNEDY/JENKS CONSULTANTS



Roger Null, V.P.
Project Manager



Ken Shuey, P.E.
Senior Technical Financial Consultant

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Section 1: Introduction

1.1 Background and Objectives

The City of Paso Robles (City) is a central coast community located in San Luis Obispo County. The City provides commonly sought services, including water and sewer services, to approximately 28,000 residents through 10,000 service connections. To provide a reliable and quality water supply to its customers, the City is now in the implementation phase of a comprehensive long range water system improvement program. Implementation of this program as well as other factors may affect the financial condition of the City's water utility. These factors are:

- The need to assess the future water utility revenue requirements.
- The need to fully implement the financial and operational requirements of the new Nacimiento water supply. These financial obligations include generation of an appropriate level of revenues to pay the annual debt service on the new regional supply pipeline, financing the construction of a proposed water treatment plant to treat the new supply, and funding the increased operating expenses associated with the Nacimiento water supply.
- The need to evaluate the future operating and non-operating revenues and expenses and their effect on the utility's operation.
- The need to fund other capital improvements associated with the City's recent Potable Water Distribution Master Plan and other water system planning projects.
- The need to develop updated rates to fund the projected enterprise financial requirements.
- A need to review and develop an appropriate rate structure to support the water fund's obligations and meet various rate equity and cost recovery requirements.

1.2 Project Scope and Authorization

The City identified the need for a financial evaluation to support the implementation of its long range water system improvement program. As such, the City entered into an agreement with Kennedy/Jenks Consultants on January 15, 2008, to conduct this study to assess the impact of its diversified water supply costs, changing operating expenses, forthcoming debt obligations, and the proposed capital improvement program expenditures. The scope of work for the water rate and revenue study is summarized as follows:

- Perform a financial projection of the City's water enterprise revenue and funding requirements, including the financial impact of future water supply costs.
- Review and develop recommendations regarding appropriate fixed and variable water rates to recover the identified costs.
- Develop a schedule of updated water rates required to meet the financial obligations of the City's water utility.
- Prepare a report of findings that presents the analysis information, conclusions, and recommendations of the water revenue and rate analysis study.

Section 2: Historical and Current Conditions

2.1 Evaluation of Historical & Current Financial Condition

The financial condition of the City's water utility was reviewed and a summary of financial performance is presented in Table 1. The information presented in this table was derived from the City's Comprehensive Annual Financial Reports (CAFRs). The CAFR for Fiscal Year (FY) 06-07 represents the most recent audited financial document of the water utility's financial performance.

The financial condition of a water utility is assessed by contrasting several financial parameters with the financial performance as reported in the City's CAFRs. Foremost among these parameters are criteria for net operating revenues and an assessment of the utility's fund balance. The findings related to each of these elements are provided as follows.

Net operating revenues are an important financial parameter of a utility's performance. This financial parameter is generally desired to be at least 20% of total operating revenues to generate adequate capital improvement funding for new and replacement (depreciation-based) assets. As shown in Table 1, the water utility has historically fallen short of this parameter, in the last three years and there has been a steady decline in operating financial performance. During the three year period, this parameter has ranged from a positive 7% in FY 04-05 to a negative 7% in FY 06-07. In this last fiscal year, the utility fell short of the 20% benchmark parameter by approximately 27%. *As such, the utility currently is not generating sufficient funds to provide for future capital expenditures and increased water utility operating expenses.*

In addition to this operational performance, the impact of various non-operating revenues and capital expenditures is included so that an assessment of the annual ending cash fund balance can be derived. As indicated at the bottom of Table 1, the water fund has experienced a drawdown in cash reserves in the last two years. In FY 06-07, this drawdown was approximately \$2.3 million, or 15% of the available water fund balance.

In consideration of these factors, additional revenues from water rates appear to be needed to improve the financial position of the water fund. The following sections of this study provide the supporting information for the level and timing of proposed rate adjustments to meet the water funds current and future financial requirements.

2.2 Current Accounts and Water Demands

The City's Calendar Year (CY) 2007 customer information related to customer billing classes, number of accounts, and water demands per class/meter size are detailed in Table 2. As shown, the City provided water service for approximately 10,000 accounts. The majority of these water accounts are represented by base-level residential customers with 5/8" and 3/4" meters.

**TABLE 1
HISTORICAL OPERATING REVENUES AND EXPENSES**

Sources and Uses of Funds	Actuals		
	FY 04-05	FY 05-06	FY 06-07
Operating Revenues			
Charges for Service	3,378,686	3,590,654	\$4,312,130
Water service charge			
Other	(11,898)	(4,507)	(\$31,781)
Total Operating Revenues	3,366,788	3,586,147	\$4,280,349
Operating Expenses			
Maintenance, Operations, & Administration	2,690,697	3,045,284	\$3,721,874
Depreciation and Amortization	452,106	688,798	\$841,196
Total Operating Expenses	3,142,803	3,734,082	\$4,563,070
Net Operating Income (Loss)	223,985	(147,935)	(\$282,721)
Net Op Rev as % of Total Op Rev	7%	-4%	-7%
Non-Operating Revenue (Expense)			
Interest Revenue	389,548	489,045	\$800,945
Water Connection Fees	na	1,745,683	\$669,578
Nacimiento Water Fees	0	701,862	\$573,706
Total Non-Op Revenues (Exp.)	389,548	2,936,590	\$2,044,229
Net Income (Loss) Befor Capital/Other Costs	613,533	2,788,655	\$1,761,508
Net Increase (Decrease) in Cash (a)	\$1,221,622	(\$1,111,385)	(\$2,275,728)
Beginning Cash and Equivalent	\$15,108,839	\$16,330,461	\$15,219,076
Ending Cash and Equivalent	\$16,330,461	\$15,219,076	\$12,943,348

Source: City of Paso Robles, CAFRs

(a) Includes the integration of capital expenditures and other non-operating costs.

**TABLE 2
CURRENT USER CLASS ACCOUNTS AND WATER CONSUMPTION**

Code/Customer Classes	(5/8 & 3/4")	1"	1-1/2"	2"	3"	4"	6"	8"	Totals
SF Single Family Residences									
Number of Meters	7,926	132	8	20	4	2	0	0	8,092
Consumption (HCF)	1,661,525	56,846	3,320	48,019	598	218	0	0	1,770,526
CR Commercial Retail									
Number of Meters	335	100	44	54	4	2	0	0	539
Consumption (HCF)	51,782	39,472	35,077	88,359	17,984	9,041	0	0	241,715
DF Discount SFR									
Number of Meters	256	2	0	0	0	0	0	0	258
Consumption (HCF)	34,448	150	0	0	0	0	0	0	34,598
LS Landscape									
Number of Meters	89	65	29	34	2	2	0	0	221
Consumption (HCF)	20,212	51,247	50,624	86,724	5,538	13,755	0	0	228,100
W2 Water Duplex									
Number of Meters	127	21	0	1	0	0	0	0	149
Consumption (HCF)	31,375	3,807	0	277	0	0	0	0	35,459
W4 Water 4 or More									
Number of Meters	26	65	17	11	2	1	1	2	125
Consumption (HCF)	12,383	31,112	25,229	27,935	7,707	2,453	16,038	55,305	178,162
CW Construction Water									
Number of Meters	103	11	2	5	0	0	0	0	121
Consumption (HCF)	12,580	14	47	5,695	0	0	0	0	18,336
W3 Water Triplex									
Number of Meters	36	63	3	1	0	0	0	0	103
Consumption (HCF)	10,925	20,999	1,669	106	0	0	0	0	33,699
CL City Landscape/Light									
Number of Meters	28	23	20	30	1	0	0	0	102
Consumption (HCF)	13,932	10,341	18,977	30,813	1,387	0	0	0	75,450
CF City Facility									
Number of Meters	35	24	7	18	1	3	0	1	89
Consumption (HCF)	22,272	15,112	7,117	22,018	3,453	9,775	0	47,239	126,986
IM Industrial/Manufacturing									
Number of Meters	16	18	9	24	0	0	0	0	67
Consumption (HCF)	2,063	7,462	8,423	48,787	0	0	0	0	66,735
S Schools									
Number of Meters	8	1	3	8	5	5	0	0	30
Consumption (HCF)	6,345	67	442	5,342	4,577	6,081	0	0	22,854
M Motels									
Number of Meters	5	0	5	15	3	1	0	0	29
Consumption (HCF)	3,557	0	4,185	39,008	9,416	3,687	0	0	59,853
SL School Landscape									
Number of Meters	1	0	0	8	3	5	0	0	17
Consumption (HCF)	9	0	0	13,270	8,548	32,579	0	0	54,406
PA Public Agencies									
Number of Meters	5	1	4	2	0	0	0	0	12
Consumption (HCF)	230	131	746	250	0	0	0	0	1,357
MR Multi Residential									
Number of Meters	0	1	0	2	0	0	0	0	3
Consumption (HCF)	0	949	0	2,670	0	0	0	0	3,619
Total Billable Meters	8,996	527	151	233	25	21	1	3	9,957
Total Billable Usage (HCF)	1,883,638	237,709	155,856	419,273	59,208	77,589	16,038	102,544	2,951,855

Source: City of Paso Robles; CY 2007 water usage by class data; does not include unbillable accounts/usage.

Also shown in Table 2 is the utility's water consumption data. The water consumption data is segregated by customer type and meter sizes. In CY 2007, the total annual water consumption was approximately 2,951,855 Hundred cubic foot (HCF) and the average consumption per account was approximately 300 HCF per year, or 25 HCF per month (613 gallons per day).

The City's water fund has two primary sources of revenue. These are the sale of water to its customers and the Nacimiento water charge that is assessed monthly to each account. At a current water rate of \$1.287 per HCF, the sale of water is estimated to generate approximately \$3.8 million per year based on CY 2007 usage. Similarly, applying the \$18 monthly fixed charge per account to the City's 9,957 accounts generates approximately \$2.1 million per year. Combined, these sources generate approximately \$5.9 million per year.

Section 3: Future Revenue Requirements

An evaluation of future revenue requirements can be focused in the projection of four specific areas. These areas are customer growth, water supply costs, capital-related expenditures, and operating costs. The following sections discuss the impact of these factors on the City's water utility revenue requirements over the next five years.

3.1 Projected Customer Growth and Water Sales

Customer growth affects the revenue requirements of the City's water utility in two ways. First, it increases the customer base that is paying for more water usage through the water usage rate, is subject to the monthly service charge, and pays a connection fee to buy into to system capacity. Second, it increases the level of those costs that vary with the quantity of water used such as water supply, treatment, and pumping expenses. In financial planning, applying low to moderate growth factors provides a conservative assessment of future utility revenue requirements.

Based on discussions with City staff, current economic factors suggest a minimal level of additional growth in the next several years. Current growth estimates for the next five years are:

- FY 2008-09 No New Accounts
- FY 2009-10 60 Accounts
- FY 2010-11 100 Accounts
- FY 2011-12 150 Accounts
- FY 2012-13 225 Accounts

In addition to the projection of new account growth, it is also important to project changes in water sales that may affect the utility's financial performance. For the City, foremost among the factors that needs to be considered is the impact of reduced water usage associated with increased water costs and rates. Based on discussions with City staff, a 15% reduction in water usage is projected in the first year after the proposed rate increase goes into effect, with a gradual return to current levels through the addition of new water system customers.

It should be noted that predicting annual growth and water usage can not be derived as precise values. As such, the future growth and water demand values used herein are to be considered as estimates only and are intended to provide a realistic yet conservative forecast of new customers so that connection fee revenues are not overestimated. Similarly, while it can be assumed that water usage should decline with the forthcoming increase in water costs and rates, behavioral changes can not be quantified. Accordingly, the magnitude of future water conservation is included in the Water Rate Study to estimate future water sales.

3.2 Budgeted/Projected Operating Expenses

Costs associated with the management, administration, and operations of the City's water utility are contained primarily in two Departments/Divisions. Utility Billing and Cashiering is responsible for the billing, accounting, and administration of the water fund, while Water Production and Distribution is responsible for the operation, maintenance, and management of the water system. The budgeted and projected water utility costs for these Departments are shown in Table 3. These projections are primarily inflation driven, with the integration of some additional costs associated with anticipated future personnel and cost allocation adjustments. The line item detail of these programs as reflected in the City's budget is provided in Appendix A.

In addition to these base-level costs, an additional operational cost assessment is derived to forecast new water fund operation and maintenance expenses associated with the new Nacimiento water supply and with other planned system improvements. As shown in Table 3, water fund operating costs are projected to increase significantly to integrate the new water supply. This cost increase is expected, as the City has proactively determined the need to diversify its water portfolio, and switch from its local groundwater supply to a new high quality/reliable surface water supply. This new supply will be the primary water supply beginning in 2010 and will be supplemented with groundwater as needed to meet then current demand. A summary documentation of the City's water supply plan is provided as supporting information and is also included in Appendix A.

It is important to note that the largest line item in Table 3 is depreciation. While depreciation is a non-cash expense, it does represent the estimated costs associated with the annual wear and tear of the City's assets. Although the City currently does not specifically fund depreciation, it does fund an ongoing local capital improvement program (CIP) that includes specific repair and replacement project costs. As such, a portion of this cost is implicitly recovered in the City's CIP. To proactively plan for this activity, the City should consider integrating the full recovery of depreciation on an annual basis through rates so that adequate funds are available for future capital reinvestment in significant water fund assets. This activity can be accounted for through a new capital repair and replacement program reserve fund. Fund reserves are discussed in a subsequent section of this study.

3.3 Projected Capital Improvement & Debt Service Financing Program

Utility systems are by nature capital intensive operations. To evaluate system capacity and long range water supply reliability, the City has completed several water system studies in the last few years. These documents provided much of the basis for the development and subsequent adoption of the City's 10-year capital improvement program (CIP) for water, wastewater, and other City services.

The City's water system CIP is separated into four basic categories. These are: Nacimiento Water Project Improvements, Well Improvements, Tank/Booster Station/Metering Project Improvements, and Pipeline Improvements. A summary of the five year plan for these project categories is provided in Table 4. A comprehensive listing of the specific projects included in the City's 10-year water system CIP is provided in Appendix A.

**TABLE 3
BUDGETED AND PROJECTED OPERATION AND MAINTENANCE EXPENSES**

Description	<u>Budgeted</u>	<u>Budgeted</u>	<u>Projected</u>			
	FY 2007-08	FY 2008-09	FY 2009-10	FY 2010-11	FY 2011-12	FY 2012-13
<u>Utility Billing and Cashiering</u>						
<u>Dept. No. 140 - Division No. 127</u>						
Department Salaries and Benefits	\$283,400	\$309,300	\$318,600	\$328,200	\$338,000	\$348,100
Maintenance - Utilities	\$1,300	\$1,300	\$1,400	\$1,500	\$1,600	\$1,700
Charges from Other Departments	\$23,400	\$23,100	\$23,800	\$24,500	\$25,200	\$26,000
Other Expenses	\$282,800	\$221,400	\$228,000	\$234,800	\$241,800	\$249,100
Subtotal - Utility Billing and Cashiering	\$590,900	\$555,100	\$571,800	\$589,000	\$606,600	\$624,900
<u>Water Production and Distribution</u>						
<u>Dept. No. 310 - Division No. 165</u>						
Department Salaries and Benefits (a)	\$929,800	\$1,060,185	\$1,092,000	\$1,124,800	\$1,158,500	\$1,193,300
Maintenance - Utilities	\$940,000	\$940,000	\$1,021,400	\$1,082,700	\$1,147,700	\$1,216,600
Depreciation (b)	\$845,000	\$848,000	\$1,572,557	\$1,962,557	\$2,243,025	\$2,273,272
Charges from Other Departments	\$184,800	\$249,500	\$347,000	\$407,400	\$419,600	\$432,200
Other Expenses	\$928,200	\$675,200	\$705,500	\$726,700	\$748,500	\$771,000
Subtotal - Water Production and Distribution	\$3,827,800	\$3,772,885	\$4,738,457	\$5,304,157	\$5,717,325	\$5,886,372
<u>Charges to Other Departments</u>	(329,200)	(310,200)	(\$319,500)	(\$329,100)	(\$339,000)	(\$349,200)
Total Existing O&M Expenses	\$4,089,500	\$4,017,785	\$4,990,757	\$5,564,057	\$5,984,925	\$6,162,072
<u>Forecasted Changes in O&M Expenses for Nacimiento Supply (c)</u>						
New Nacimiento WTP O&M - Estimate			\$1,041,000	\$2,094,920	\$2,220,600	\$2,353,800
New Nacimiento Pipeline O&M Costs			\$770,866	\$1,341,731	\$1,341,731	\$1,341,731
Changes in Existing O&M Costs (Reductions)			(655,975)	(448,889)	(475,800)	(504,300)
Subtotal New Water Supply O&M Costs			\$1,155,891	\$2,987,762	\$3,086,531	\$3,191,231
Allowances for New Water Division Positions		\$251,415	\$942,671	\$970,952	\$1,341,918	\$1,382,175
Net New Nacimiento Water Supply Costs		\$251,415	\$2,098,562	\$3,958,714	\$4,428,449	\$4,573,406
<u>Total New and Existing Forecasted Water Fund Costs</u>		\$4,269,200	\$7,089,319	\$9,522,771	\$10,413,374	\$10,735,478

Source: City of Paso Robles Finance Department budget for Department/Division Data

(a) Source: City FY 08-09 Labor Budget adjusted to coincide with forecasted Nacimiento O&M cost estimates.

(b) Source: Table 4 CIP Table, Depreciation Estimate.

(c) Source: TJCross Ops Budget. Values provided have been inflated herein.

**TABLE 4
PROPOSED CAPITAL IMPROVEMENT & DEBT FINANCING PROGRAM**

Description	PROJECTED					
	FY 2007-08	FY 2008-09	FY 2009-10	FY 2010-11	FY 2011-12	FY 2012-13
Water Projects - Total Project Costs (a)						
Proposed Water Treatment Plant	\$3,789,830	\$19,000,000	\$11,400,000	\$7,600,000	\$0	\$0
Well Improvements	\$2,796,241	\$4,958,500	\$1,335,630	\$234,848	\$247,765	\$1,568,352
Tank, Booster Station and Metering Projects	\$2,430,940	\$2,817,862	\$6,206,739	\$5,583,025	\$934,792	\$986,206
Pipeline Improvements	\$343,784	\$90,673	\$557,627	\$605,527	\$329,803	\$823,281
Total Water Fund CIP	\$9,360,795	\$26,867,035	\$19,499,996	\$14,023,401	\$1,512,360	\$3,377,839
<u>Water System Debt Financing Program</u>						
New Debt Issuances (b)		\$43,660,000	\$0	\$0	\$0	\$0
Existing Debt						
Nacimientto Water Pipeline Project		\$0	\$0	\$1,587,995	\$4,224,589	\$4,225,889
Subtotal Existing Annual Debt Service		\$0	\$0	\$1,587,995	\$4,224,589	\$4,225,889
New Annual Debt Service						
Initial New Debt Service Costs (c)		\$0	\$0	\$0	\$2,900,000	\$2,900,000
Subsequent New Debt Service Costs			\$0	\$0	\$0	\$0
Subtotal New Debt			\$0	\$0	\$2,900,000	\$2,900,000
Total Annual Debt Service		\$0	\$0	\$1,587,995	\$7,124,589	\$7,125,889
New Total CIP	\$9,360,795	\$26,867,035	\$19,499,996	\$14,023,401	\$1,512,360	\$3,377,839
New Depreciation per Year		\$187,216	\$537,341	\$390,000	\$280,468	\$30,247
Cumulative New Depreciation Per Year		\$187,216	\$724,557	\$1,114,557	\$1,395,025	\$1,425,272

- (a) CIP Source: TJ Cross June 2008; Does not include the cost of additional Nacimientto entitlements as its timing is unknown & beyond 5 years. Capitial Facility Charge revenues are included in the financial projection tables as total Water Fund costs are included herein. Comprehensive 10-Year CIP and water supply summary is included in Appendix A.
- (b) New Debt Issuances are based on 30 years @ 5% per City staff.
- (c) New debt includes the capitalization of interest until FY11-12.

In addition to the CIP, Table 4 also reflects the projected water system debt financing program. Although debt funding of capital expenditures is common among utilities, the City has historically funded most of its water fund obligations from cash. However, in 2007 the City, as well as other regional water purveyors, entered into a contractual obligation with the San Luis Obispo County Flood Control & Water Conservation District to fund a regional water system pipeline project that will convey water from Lake Nacimiento to the City and nearby agencies. The City's proportional share of the debt obligation for this issuance is approximately \$4.2 million per year. This debt is scheduled to begin in FY 11-12, with a smaller payment due the preceding year. A copy of the comprehensive bond payment schedule is also provided in Appendix A.

To treat this new water supply to drinking water standards, the City must construct a new water treatment plant. The total estimated project costs are projected at approximately \$43 million. Similar to the Nacimiento pipeline project, the financing program estimates that approximately \$43.7 million in new debt will be needed to fund the construction of this critical facility. Annual debt service payments of approximately \$2.9 million are programmed to begin in FY 11-12.

It should be noted that funding the construction of the new water treatment plant is vital to the City as it is a cornerstone component of the City's water resources program. Since contractual commitments have been made to procure this new water supply and construct the pipeline, without a water treatment plant, the City will be paying over \$5.5 million per year (\$4.2 million in debt and \$1.3 million in water supply O&M) for water it can not use. Without additional funding and rate-related revenue increases, the new Nacimiento water supply can not be used as drinking water by the City and would have to be discharged into the river. Construction of the water treatment plant needs to begin in 2009 to utilize this valuable water resource.

Lastly, at the bottom of Table 4 is an estimate of the additional annual depreciation associated with the implementation of the capital improvement program. As shown, by the end of the five year planning period, the City's assets will accrue an additional \$1.4 million per of annual depreciation expense. As previously discussed, to account for depreciation funding and expenditures, this funding level should be programmed into an ongoing capital repair and replacement reserve fund.

3.4 Summary of Projected Revenue Requirements

As expected, the City's water fund is projected to experience significant increases in costs to implement the new water supply program. The magnitude of the new debt obligations and increased operating cost associated with the Nacimiento water supply are expected to increase significantly in the next five years to fully implement the City's comprehensive water system improvement program.

A projected revenue plan is developed to compare the water utility's revenues and revenue requirements for the five-year study period. The financial projection is based on the City's projected customer account characteristics, the projected O&M expenses and the inclusion of the City's comprehensive capital improvement program. Additionally, several ratemaking criteria were also integrated in the revenue plan. These key criteria include:

- Growth is conservatively estimated to be flat for the next couple of years, with a modest increase during the balance of the five year planning period. (Refer to Section 3.1.)
- Water sales are projected to reduce by approximately 15% in the first year after implementation of the proposed rates; demands from future new accounts are projected at current levels,
- A new \$43.7 million debt issuance is projected in FY 08-09 to fund the construction of the Nacimiento water treatment plant; debt has been capitalized until FY 11-12 to better coincide with additional cash-flow from new water utility customer connections,
- Debt coverage covenants are to be met through utility rates, with additional Connection Fee (Capacity Charge) revenues used to pay down long term debt and fund identified capital improvements,
- Water Connection Fees (Capacity Charges) are based on a 2008 study by HF&H. The fee proposed for a 5/8" and 3/4" meter is \$28,687. This fee increases by the size of the water meter in accordance with the meter capacity ratio and is schedule to increase annually at a rate of 5.5%, the projected annual increase in the construction cost index. The proposed fees derived in this study is provided in Appendix A.
- Target water fund reserves have been established based on the sum of the following financial criteria: Operating Reserve – 30% of operating expenses, Economic Uncertainty/ Rate Stabilization Reserve – 20% of Operating Expenses, and Capital Emergency Reserve – one year's average cash-based CIP (\$2 million). Additionally, two new funds are recommended to manage and account for ongoing water supply and capital rehabilitation program activity. These funds are: a Water Supply Fund – to be used to account for the acquisition of new water supply rights and a Capital Repair/Replacement Fund – to be used to account for depreciation that is funded and ongoing/projected system renewal expenditures.

A five year revenue plan of the City's water utility is developed by integrating the ratemaking criteria with the projected water system costs and capital expenditures.

3.5 Projected Revenue Requirements Using Proposed Rates

As expected, the results of the revenue plan indicate that additional revenues are needed to meet the current and future obligations of the water fund. Accordingly, a projected revenue plan using proposed rates is prepared to balance the water utility financial obligations and revenues and position the utility for a sustainable positive financial performance. Several cash flow evaluations and alternatives were prepared with City staff to balance financial performance with ratepayer impact. These alternatives varied the debt financing strategies, projected growth scenarios, water consumption levels, rate increase levels/phases, and rate structure elements such as fixed meter and water usage charges so that short term cash flow obligations were met and debt service coverage ratios were sustained above the level required by bond covenants. The resulting revenue plan using proposed rates is shown in Table 5.

**TABLE 5
PROJECTED REVENUE PLAN USING PROPOSED RATES**

Description	Adjusted Budget			Projected		
	FY 2007-08	FY 2008-09	FY 2009-10	FY 2010-11	FY 2011-12	FY 2012-13
Revenues						
Fixed Monthly Service Charges (As Modeled)	\$2,150,712	\$2,889,430	\$2,603,926	\$2,939,966	\$3,332,807	\$3,583,400
Consumption Charges (As Modeled)	\$3,778,375	\$4,014,523	\$8,571,124	\$11,608,603	\$12,824,036	\$13,547,503
Total Operating Revenues	\$5,929,100	\$6,904,000	\$11,175,100	\$14,548,600	\$16,156,800	\$17,130,900
Operating Expenses						
Department Salaries and Benefits	\$1,213,200	\$1,369,485	\$1,410,600	\$1,453,000	\$1,496,500	\$1,541,400
Maintenance - Utilities	\$941,300	\$941,300	\$1,022,800	\$1,084,200	\$1,149,300	\$1,218,300
Charges from Other Departments	\$208,200	\$272,600	\$370,800	\$431,900	\$444,800	\$458,200
Depreciation	\$845,000	\$848,000	\$1,572,557	\$1,962,557	\$2,243,025	\$2,273,272
Other Material, Services, and Maint. Expenses	\$1,211,000	\$896,600	\$933,500	\$961,500	\$990,300	\$1,020,100
Charges to Other Departments	(\$329,200)	(\$310,200)	(\$319,500)	(\$329,100)	(\$339,000)	(\$349,200)
Net New Nacimiento Water Supply Costs	\$0	\$251,415	\$2,098,562	\$3,958,714	\$4,428,449	\$4,573,406
Total Operating Expenses	\$4,089,500	\$4,269,200	\$7,089,300	\$9,522,800	\$10,413,400	\$10,735,500
Net Operating Revenue	\$1,839,600	\$2,634,800	\$4,085,800	\$5,025,800	\$5,743,400	\$6,395,400
Non-Operating Revenue (Expense)						
Interest Revenue	\$85,100	\$190,600	\$574,800	\$231,200	\$75,300	\$209,600
Water Connection Fee Revenues	\$0	\$0	\$1,815,887	\$3,192,935	\$5,052,819	\$7,996,087
Depreciation Adjustment (Non-Cash Expense)	\$845,000	\$848,000	\$1,572,557	\$1,962,557	\$2,243,025	\$1,704,954
Existing Debt Service				(\$1,587,995)	(\$4,224,589)	(\$4,225,889)
New Debt Service (a)					(\$2,900,000)	(\$2,900,000)
Total Non-Op Revenues/Expenses	\$930,100	\$1,038,600	\$3,963,244	\$3,798,697	\$246,555	\$2,784,751
Net Income Before Capital Activity	\$2,769,700	\$3,673,400	\$8,049,044	\$8,824,497	\$5,989,955	\$9,180,151
Capital Expenditures	\$9,360,795	\$26,867,035	\$19,499,996	\$14,023,401	\$1,512,360	\$3,377,839
Capital Financing						
Proposed Debt Issuance		\$43,660,000	\$0	\$0	\$0	\$0
Subtotal - Capital Financing Issuance Expenses		\$7,660,000	\$0	\$0	\$0	\$0
Net Change in Funds Avail. After Capital Activity	(\$6,591,095)	\$12,806,365	(\$11,450,952)	(\$5,198,904)	\$4,477,595	\$5,802,312
Transfer to New Water Supply Fund					\$0	\$5,420,669
Ending Cash Balance - After Water Supply Fund Xfers	\$6,352,253	\$19,158,618	\$7,707,666	\$2,508,762	\$6,986,357	\$7,368,000
Target Reserve Fund Balance (b)	\$4,045,000	\$4,135,000	\$5,545,000	\$6,761,000	\$7,207,000	\$7,368,000
Development of New Capital Repair/Replacement Fund						
Annual Level of Depreciation Funding						\$568,318
Cummulative Fund Balance for Capital R/R Fund						\$568,318
Development of New Water Supply Fund						
Annual Level of Funding						\$5,420,669
Cummulative Water Supply Acquisition Fund Balance						\$5,420,669
Estimated Debt Service Coverage Ratio (Does Not Include Connection Fee Revenues)				4.55	1.13	1.17

(a) Per City staff, Debt is based on 30 years and 5% interest; interest is capitalized until FY 11-12

(b) Target Reserve based on 50% of annual operating expenses (30% ops reserve & 20% economic uncertainty), plus 1-Year's average cash CIP (\$2.0 M)

Proposed Annual Rate Increases & Growth/Usage V _ε	Proposed Rates and Projected Changes in Accounts and Water Usage					
	50%	51%	16%	6%	5%	
Projected Increase in Revs (includes new demand)	0.00%	11.00%	12.50%	11.00%	0.00%	
Proposed Fixed Rate Increase	100.00%	65.00%	15.00%	3.00%	3.00%	
Proposed Usage Rate Increase						
Proposed Fixed Rate per Equivalent Meter/Month	\$18.00	\$18.00	\$19.98	\$22.48	\$24.95	\$24.95
Proposed Average Usage Unit Rate/HCF	\$1.28	\$2.56	\$4.22	\$4.86	\$5.00	\$5.15
Proposed Connection Fee: Inflate @ 5.5%	\$8,426	\$28,687	\$30,265	\$31,929	\$33,685	\$35,538
Water Conservation Factor	100.0%	85.0%	100.0%	100.0%	100.0%	100.0%
Increase in Number of Equivalent Meters (#)	0	60	100	150	225	

As shown in Table 5, double digit rate-based revenue increases are proposed for the next three years so that water utility will generate adequate revenues to meet its increased operating cost and debt obligation in FY 11-12. However, inflationary increases appear to be adequate in years four and five of the planning periods as the new water supply costs and debt obligations have stabilized. Additional water sales and connection fee revenues are projected to begin to support the water utility's financial obligations in a few years so that the water fund balance is projected to meet target reserve levels beginning in FY 11-12. If growth continues as projected, funds should be available for the acquisition of additional water supply in FY 12-13. These funds will have been generated from connection fee revenues and are to be accounted for in the new water supply fund.

It is recommended that projected rate increases be adopted for implementation in January of each year. While the magnitude of these increases may vary based on unforeseen change in costs, demand conditions, or reserve requirements, these values are projected to provide a reasonable estimate of the projected revenue requirements of the City's water fund for the next five years. As discussed with staff, additional review of the cost components and revenue requirements should be made during the annual budget development and review process. Accordingly the level of the required annual rate increases may differ from the rate and revenue projections derived herein based on those annual findings. A discussion of the City's current and proposed rates and rate structure is provided in the following sections.

Section 4: Current Water Rates

Historically, the City's water rates have been among the lowest in the State, as it benefited from a low cost water supply and purposefully minimized non-essential capital and operational expenditures. As previously discussed, upon completing various comprehensive studies of the City's water supplies and overall water system, the City has embarked on a proactive program to assure the long-term reliability and sustained quality of the City's water system.

Given this need, the City began to increase its water rates to fund the City's capital improvement program including the new Nacimiento water supply program. Additional increases are needed to meet the City's current and projected debt obligations.

The City's present water rates and rate structure went into effect on February 1, 2008. It consists of a fixed monthly service charge that is charged per account regardless of meter size, and a water volume charge that is charged uniformly for all water used by the City's customers. The characteristics of the present rate structure are provided in Table 6 and include:

Current Fixed Monthly Account Service Charge. Pursuant to a 2004 ordinance, the City adopted a fixed charge per account to begin to recover additional revenues for the new Nacimiento water supply. The current fixed monthly charge per account is \$18.00, regardless of the customer class.

Current Usage Based Rates. The City's current usage based rates (or variable rates) are applied uniformly to all water usage. Uniform rates are commonly used to recover those costs in a water system that vary with volume of water produced. As such, this rate component correlates a customer's costs of service with the quantity of water consumed and therefore a customer's water bill will fluctuate in direct proportion to the variance in water usage. This usage based rate element supports a fundamental pay for use ratemaking philosophy. The City's current water quantity rate is \$1.28 per one hundred cubic feet (HCF), as shown in Table 6.

Low and Fixed Income Lifeline Program. The City currently has a low and fixed income lifeline program in place to provide financial assistance for qualifying single family residential accounts. The current lifeline rate provides a 15% discount on the current volume-based commodity or water usage charge. Eligibility in the program is based on a single-family dwelling unit's participation in Pacific Gas & Electric's (PG&E) or Southern California Edison's (SoCalGas) lifeline programs. Currently, there are approximately 250 lifeline accounts served by the City's water system.

**TABLE 6
CURRENT WATER RATES**

Meter Size (Inches)	Monthly Service Charges (\$)
Monthly Charges (Fixed Nacimiento Charges)	
5/8" and 3/4"	\$18.00
1"	\$18.00
1 1/2"	\$18.00
2"	\$18.00
3"	\$18.00
4"	\$18.00
6"	\$18.00
8"	\$18.00
12	\$18.00
Usage Charges (\$/Hundred Cubic Feet - HCF)	
\$1.28 per Hcf for all water usage	

Source: City of Paso Robles
Effective: February 1, 2008

Section 5: Proposed Water Rates

Proposed rates are developed to meet the revenue and rate restructuring requirements of the City's water utility. The proposed rate increases are developed as staged adjustments to both the fixed and variable water rates. To minimize ratepayer impact, annual increases are suggested to be implemented in January of each year, as this is a seasonal period when water usage is at its lowest. A discussion of the City's fixed and variable rates, development of the proposed service and usage charges, development of monthly bills, and a comparison of charges with other communities is provided in the following.

5.1 Fixed and Variable Rate Assessment

An important element of the City's rate structure evaluation is a financial assessment of its vulnerability to short-term revenue shortfalls. Depending on the utility's rate structure and water supply situation, short-term revenue shortfalls can occur during periods of drought, economic downturn, or wet or atypical weather conditions that reduce water sales.

Similar to most water utilities, the City's current rate structure includes a fixed and variable rate component. These rates are designed to provide a fixed revenue source based on the City's active accounts and a variable revenue source based on the amount of water used or consumed by the City's customers.

Fixed costs are defined as any costs that generally do not vary within a year if there is a variation in the level of water demand required. For example, City personnel costs should not vary during a one-year period, although it may vary over longer periods to reflect the level of personnel required to support changes in operating conditions. In contrast, variable costs are those costs that vary with the quantity of water used. Because water systems are capital and labor intensive, total system costs for most water systems are generally recognized as approximately 60 to 75% fixed. It is for this reason that most water agencies throughout the United States utilize a fixed and variable component in its rate structure.

One method to evaluate the financial health or stability of a particular rate structure is to contrast the nature of the utility's costs with the source of its revenues. This assessment, while not intended to be precise, is developed to provide a framework for utility management decisions related to the balance of fixed versus variable revenues and rate stabilization related reserves. These elements are important because if the fixed and variable revenues are improperly balanced, the utility is financially vulnerable and revenue shortfalls may occur. A summary of the fixed and variable rate assessment for FY 11-12 is provided in Table 7. For this cost assessment, FY 11-12 is used as this fiscal year represents the first year of full debt service water system burden. Current revenues are used to demonstrate the current rate structure's effectiveness at recovering fixed costs and generating usage-based revenues.

**TABLE 7
FIXED AND VARIABLE COST/REVENUE ASSESSMENT**

Description	Cost Allocation		Allocation Results		
	Fixed %	Variable %	Total	Fixed	Variable
<u>System Expenses/Expenditures</u>			Costs (FY 2011-12)		
Capital Expenditure	50%	50%	\$1,512,360	\$756,180	\$756,180
Debt Service	100%	0%	\$7,124,589	\$7,124,589	\$0
<u>Operation and Maintenance Expenses</u>					
Department Salaries and Benefits	80%	20%	\$1,453,000	\$1,162,400	\$290,600
Maintenance - Utilities	20%	80%	\$1,084,200	\$216,840	\$867,360
Charges from Other Departments	50%	50%	\$431,900	\$215,950	\$215,950
Depreciation	50%	50%	\$1,962,557	\$981,278	\$981,278
Other Material, Services, and Maint. Expenses	50%	50%	\$961,500	\$480,750	\$480,750
Charges to Other Departments	80%	20%	(\$329,100)	(\$263,280)	(\$65,820)
Net New Nacimiento Water Supply Costs	50%	50%	\$3,958,714	\$1,979,357	\$1,979,357
Total Expenses/Expenditures			\$18,159,719	\$12,654,064	\$5,505,655
Allocation of System Costs			100%	70%	30%
			Revenues (FY 2007-08)		
<u>System Revenues</u>			Total	Fixed	Variable
Nacimiento Fixed Revenues (a)			\$2,150,712	\$2,150,712	
Consumption Based Revenues (a)			\$3,778,375	\$0	\$3,778,375
Total System Rate Based Revenues			\$5,929,087		
Percentage of Fixed and Variable Revenues			100%	36%	64%

Notes: FY 11-12 is used for cost assessment as this represents the first year of full debt service burden; current revenues are used to demonstrate the current rate structure's effectiveness at recovering the percentage of fixed costs.

(a) Based on estimate for FY 07-08, Table 5.

Based on the allocation derived in Table 7, approximately 70% of the City's projected water utility costs are shown to be fixed and 30% are derived as variable costs. In contrast, approximately 36% of the current revenues are derived from the fixed Nacimiento account charge and 64% is collected from water usage consumption charges.

The implications of this assessment are twofold. First, the imbalance in the fixed/variable percentages of costs and revenues suggests a strong need to increase (and at a minimum continue) the fixed charge established in 2004. Second, this assessment demonstrates the need for a methodical rate stabilization/economic uncertainty fund reserve policy. This fund reserve is an integral element in managing the City's risk associated with financial shortfalls resulting from a short term reduction in water sales and inadequate fixed revenues. Accordingly, the City should perform a periodic review of the fund reserve and cost recovery effectiveness as an ongoing financial risk management activity of the water fund.

5.2 Development of Proposed Rates

Proposed water rates have been developed to support the financial health of the City's water system over the five year planning period. The charges proposed are based upon an analysis of future system costs and financial obligations. A discussion of the development of proposed monthly service charges and water usage rates is provided in this section of the study.

5.2.1 Development of Proposed Fixed Monthly Service Charge

As discussed extensively in the fixed and variable rate assessment section, fixed rates are an important component of a utility's water rates and are commonly used throughout the United States. Since the City's current \$18 per account charge is its only substantial source of fixed revenue, it is recommended this charge be maintained in the City's schedule of rates and charges.

One important enhancement to the City's current fixed rate is the recommendation to convert this fixed monthly service charge from an account basis to a meter size basis. Since much of the water system's costs such as meter replacement/repair, fire protection, and the investment in system services and capacity are related to the size of the meter, it is recommended that the City's fixed monthly charge utilize meter size in its rate structure. Applying this approach will increase the monthly fixed charge for the larger meters in a manner commensurate with their potential use of the system, recover a designated portion of the utility's fixed costs and provide additional overall revenue stability.

The indexing that is recommended for this rate element are the equivalent meter service ratios developed by the American Water Works Association, Manual M1. Adoption of the monthly service charge based on these AWWA meter ratios will improve the equity in the City's rate structure and align the new fixed rates with the general purpose of this rate component; to support the recovery of the utility's fixed monthly (readiness-to-serve) costs. The documentation of these ratios and an estimate of the implications on annual revenues are provided as a supporting table in Appendix A.

5.2.2 Development of Proposed Usage Charge

Consistent with the revenue requirements derived in Table 6, usage charges are developed to bill customers for their metered water usage. The City currently charges \$1.28 per HCF for all water used regardless of the type of customer or the amount of water used in any particular billing cycle. Charging for water on this consistent basis is referred to as a uniform block rate structure. Approximately 40 percent of all agencies in California utilize this billing method because it provides basic support for water conservation as a pay for what you use structure, is simple to understand, generally fosters public acceptance, and provides relatively predictable revenues. Continuation of a uniform rate structure to bill for a customer's water usage is the basic method proposed for the City at this time.

To meet the financial obligations of the utility, a series of several rate increases are needed. The proposed rates for the five year planning period are shown in Table 8. Implementation of these rates as reflected in the financial plan (Table 6) should fund the construction of the critically important water treatment plant, meet the anticipated debt covenants for the water fund debt, provide the necessary funds for ongoing system management and operation and return the water fund to a desired level of financial performance.

As previously noted, the City currently offers a low and fixed income lifeline program to qualifying single family customers in the City. While this program is consistent with the goals and objectives of many communities and public agencies, recent California legislation has made these types of community programs difficult to continue. Accordingly, it is recommended the City discontinue its current lifeline program and consider an alternative approach to providing financial support to its single family ratepayers.

An alternative to a focused lifeline program which requires no administrative effort is to implement a new inclining block rate structure that will provide water for the entire single family customer class at a reduced rate to meet basic health and sanitation needs. Base level sanitation needs are defined as the minimum amount of water required to provide for basic health requirements. This value is estimated on a per capita basis and typically ranges from 40 to 50 gallons per day (gpd) per person.

Given the City's population, household, and usage information, these values translate to approximately 4 to 5 HCF per dwelling unit per month. Based on this finding and discussions with City staff, it is recommended a base use block be implemented. Since this block is designed to reflect minimum/base level usage, the revenue derived from this block will be very consistent and for all practical purposes, can be considered as additional fixed revenues. Increasing the fixed revenues in this manner is consistent with other City pay-for-use goals and provides additional financial security for the water fund.

The proposed rate structure is based on providing the first 5 HCF per month at a unit rate equal to 85% of the price of the uniform rate. Utilizing this approach appears to enable the City to continue and broaden its community support goals and establish a mechanism to account for a portion of the City's water sales as a fixed revenue source. The proposed single family block rate structure is also shown in Table 8.

**TABLE 8
PROPOSED WATER RATES**

	Current Rates	Projected				
		FY 2008-09	FY 2009-10	FY 2010-11	FY 2011-12	FY 2012-13
Meter Size (inches)	Current	<u>Proposed Monthly Service Charges</u>				
5/8" and 3/4"	\$18.00	\$18.00	\$19.98	\$22.48	\$24.95	\$24.95
1"	\$18.00	\$25.20	\$27.97	\$31.47	\$34.93	\$34.93
1 1/2"	\$18.00	\$32.40	\$35.96	\$40.46	\$44.91	\$44.91
2"	\$18.00	\$52.20	\$57.94	\$65.18	\$72.36	\$72.36
3"	\$18.00	\$198.00	\$219.78	\$247.25	\$274.45	\$274.45
4"	\$18.00	\$252.00	\$279.72	\$314.69	\$349.30	\$349.30
6"	\$18.00	\$378.00	\$419.58	\$472.03	\$523.95	\$523.95
8"	\$18.00	\$522.00	\$579.42	\$651.85	\$723.55	\$723.55
		<u>Proposed Usage Charges</u>				
Volume Rate	<u>\$/HCF</u>	<u>\$/HCF</u>	<u>\$/HCF</u>	<u>\$/HCF</u>	<u>\$/HCF</u>	<u>\$/HCF</u>
<u>All Customers Except Single Family</u>						
All Usage	\$1.28	\$2.56	\$4.22	\$4.86	\$5.00	\$5.15
<u>Single Family</u>						
0-5 HCF	\$1.28	\$2.18	\$3.59	\$4.13	\$4.25	\$4.38
Over 5 HCF	\$1.28	\$2.56	\$4.22	\$4.86	\$5.00	\$5.15

5.3 Comparison of Monthly Bills

Typical customer bills are often developed to evaluate the impact of a water rate schedule on a utility's customers. Current typical bills are derived by correlating the current schedule of charges shown in Table 7 with the average or typical consumption values for various customer types. Similarly, typical bills are calculated by applying the proposed increase to both the monthly service charge and the usage charge components of the water rate schedule. Table 9 reflects the resulting impacts of the proposed rate increases over the five year planning period.

As shown, the calculated typical bills reflect a steady climb in ratepayer impact as the proposed rate increases are implemented to recover the City's water system costs of service. With the conversion to a fixed monthly charge based on meter size, the customers with the large water meters will experience a higher percentage increase in their water bills in the first year after the proposed rate plan is adopted. Since the percentage increase in the monthly service charge and usage charge are not proposed to be the same, some fluctuation in account level impact will continue among the City's large and small water users over the next few years.

Given the projected level of ratepayer impact, the City should expect additional water usage awareness, experience a reduction in overall water demand, and incur an increase in customer requests for a water audit and/or capacity review in an effort to downsize reduce water usage or downsize to a smaller water meter. The City has budgeted for additional customer service programs and support to assist customers in their water conservation efforts over the next several years. These program costs and reduced water usage estimates have been integrated in the City's Water Rate Study.

5.4 Comparison of Monthly Bills with Other Communities

In addition to the development of typical bills for City customers, Table 10 provides a comparison of the City's current and proposed FY 08-09 monthly single-family bill with other local communities in San Luis Obispo County. The comparison is based on a monthly water usage of 30 HCF.

As shown, there is a wide range of charges among the surveyed communities, with the City's current bill in the lower range of costs and the estimated bill under the proposed rates at the mid-range of the agency comparison. It is interesting to note that even with the increase proposed for FY 08-09, a Single Family Resident customer using 30 HCF per month in the City will still pay \$45 to \$100 per month less than the upper range water purveyors in the County.

In addition to this finding, it should be noted that rate surveys often do not provide the full picture of the utility's position. For example, some of the agencies may have additional increases that are in process or being proposed, may have varying water supply program cost, quality, and reliability issues or objectives, and certainly there is often a wide range of variance in local level of service, capital reinvestment, and preventive maintenance considerations. Given the current condition and direction of the City's water utility and water resource requirements in the County, it appears the City's water rates are in line with other local communities.

**TABLE 9
PROPOSED WATER RATES AND TYPICAL BILLS**

	Current Rates	Projected				
		FY 2008-09	FY 2009-10	FY 2010-11	FY 2011-12	FY 2012-13
Meter Size (inches)	Current	Proposed Monthly Service Charges				
5/8" and 3/4"	\$18.00	\$18.00	\$19.98	\$22.48	\$24.95	\$24.95
		Proposed Usage Charges				
Volume Rate	\$/HCF	\$/HCF	\$/HCF	\$/HCF	\$/HCF	\$/HCF
<u>All Customers Except Single Family</u>						
All Usage (a)	\$1.28	\$2.56	\$4.22	\$4.86	\$5.00	\$5.15
<u>Single Family (a)</u>						
0-5 HCF	\$1.28	\$2.18	\$3.59	\$4.13	\$4.25	\$4.38
Over 5 HCF	\$1.28	\$2.56	\$4.22	\$4.86	\$5.00	\$5.15
Meter Size (inches)	Current	Typical Monthly Bills				
<u>Single Family</u>						
Low User - 5/mo	\$24.40	\$28.88	\$37.93	\$43.12	\$46.21	\$46.85
Medium User - 18/mo	\$41.04	\$62.16	\$92.84	\$106.27	\$111.26	\$113.85
High User - 45/mo	\$75.60	\$131.28	\$206.89	\$237.43	\$246.35	\$252.99
<u>Commercial</u>						
Low User - 15/mo	\$37.20	\$56.40	\$83.34	\$95.34	\$100.00	\$102.25
Medium User - 30/mo	\$56.40	\$94.80	\$146.70	\$168.21	\$175.05	\$179.55
High User - 60/mo	\$94.80	\$171.60	\$273.42	\$313.93	\$325.15	\$334.16

Note: All typical bills are based on one 3 /4 inch meter and the low, medium, and high usage/month indicated (in HCF).
(a) The "All Usage" rate is for all customer usage except for Single Family. Single Family block rate is as shown.

**TABLE 10
COMPARISON OF MONTHLY WATER BILLS
SINGLE FAMILY RESIDENTIAL**

Community	Monthly Meter Fixed Rate	Water Usage/ Quantity Rate	Water Usage (HCF)	Calculated Monthly Bill
Cambria CSD (a)	\$12.15	\$6.17 to \$8.02	30	\$194.38
City of Morro Bay (a)	\$16.43	\$1.39 to \$12.62	30	\$179.93
City of San Luis Obispo (b)	\$0.00	\$3.71 to \$5.81	30	\$140.40
Oceano CSD	\$11.97	\$1.14 to \$4.09	30	\$119.52
City of Paso Robles - Proposed	\$18.00	\$2.56	30	\$92.88
Nipoma CSD (c)	\$16.98	\$1.81 to \$3.14	30	\$84.53
City of Pismo Beach	\$13.97	\$1.78 to \$2.31	30	\$80.09
City of Grover Beach	\$6.75	\$1.82 to \$2.20	30	\$64.45
City of Paso Robles - Current	\$18.00	\$1.28	30	\$56.40
Atascadero Mutual Water Co. (d)	\$14.50	\$1.122 to \$2.543	30	\$55.63
City of Arroyo Grande	\$5.25	\$1.16 to \$1.77	30	\$42.39
Templeton CSD	\$12.19	\$1.17 to \$2.62	30	\$35.29
Agency Average (Excluding City of Paso Robles)				\$95.49

Source Documentation:

Basis: 5/8 &/or 3/4-inch meter

(a) Monthly fixed charge includes 3 HCF.

(b) Current SFR rate is a three tiered rate structure, with no fixed service charge; a 5% utility user tax is also applied to the water portion of the bill (not included in this comparison).

(c) Average of Town and Blacklake Division rates

(d) Monthly fixed charge includes 2,000 gallons (2.67 HCF); Quantity rates shown are per HCF

5.5 Future Rate Review and Restructuring Considerations

In addition to the rate-related adjustments provided herein, the City should plan for the methodical review of system costs, water demands, and utility rates. Much of this work can be incorporated as an element of the annual budget process as additional information is being developed and evaluated.

One area that the City may want to consider as part of a focused rate and rate structure review is the development of a more comprehensive inclining block rate structure for all City customer classes. As previously mentioned, due to the magnitude of the rate increases necessary to meet the near-term water fund financial obligations, a conservation focused block rate structure for the City's customers is not recommended at this time. However, a new block rate structure may be appropriate as the new water supply program becomes integrated into the City's daily operation. A broader inclining block rate structure would enhance the City's support for resource management and sustainability through additional water conservation participation by all City water customers.

Proceeding in this direction, rates could be restructured through the development of pricing strategies that will increase usage awareness and influence customer behavior. This expanded conservation-based rate structure could support the City's water conservation goals while conforming to the City's water system revenue requirements and better align the City's rates and rate structure with California's Best Management Practices for Water Conservation.

Should the City pursue this rate restructuring direction, a partial listing of cornerstone elements that should be in place prior to undertaking this program include: predictable water supply costs/water sales, dedicated City water conservation support staff, documented water conservation, landscape, and drought contingency guidelines, and applicable municipal code provisions. The City may also want to consider an interruptible water rate for dedicated exterior water uses and potential customer class modification/consolidation as other elements of the rate restructuring and cost of service evaluation.

Appendix A

Miscellaneous Supporting Information

APPENDIX A - WATER FUND EXPENSE BUDGET DETAILS

PUBLIC WORKS Department No. 310 Funding Source:		Water Production & Distribution Division No. 165 Fund 600 - Water Operations Fund		
		Current Budget FY 2006-07	Adopted Budget FY 2007-08	Adopted Budget FY 2008-09
EMPLOYEE SERVICES				
Total Employee Services		807,900	929,800	1,311,600
MAINTENANCE & OPERATIONS				
5212	Materials & Services	234,600	234,600	234,600
5216	Utilities	940,000	940,000	940,000
5221	Facility Maintenance	71,500	165,500	105,500
5222	Equipment Maintenance	4,000	4,000	4,000
5223	Vehicle Maintenance	40,400	42,600	44,700
5224	Professional Services	65,400	115,000	55,000
5225	Legal Services	38,000	43,700	43,700
5226	Education, Travel & Meetings	8,700	8,700	8,700
5229	Depreciation	833,600	845,000	848,000
5236	Franchise Fees	-	-	-
5235	Special Projects	15,000	109,600	117,100
5238	Charges from Other Departments	297,200	184,800	249,500
	Other M&O Expenses	477,600	723,700	613,300
Total Maintenance & Operations		2,548,400	2,693,500	2,650,800
CAPITAL OUTLAY				
5451	Buildings		100,000	
5454/5	Equipment	19,000	104,500	61,900
Total Capital Outlay		19,000	204,500	61,900
DIVISION SUBTOTAL		3,375,300	3,827,800	4,024,300
PUBLIC WORKS Department No. 140 Funding Source:		Utility Billing/Cashiering Division NO. 127 Fund 600 - Water Operations		
EMPLOYEE SERVICES				
Total Employee Services		288,000	283,400	309,300
MAINTENANCE & OPERATIONS				
5212	Materials & Services	51,700	105,700	103,600
5216	Utilities	1,300	1,300	1,300
5221	Facility Maintenance			
5222	Equipment Maintenance	300	300	300
5223	Vehicle Maintenance			
5224	Professional Services	136,300	114,800	108,300
5225	Legal Services			
5226	Education, Travel & Meetings	12,700	7,500	7,500
5229	Equipment Replacement	9,600	1,700	1,700
5230	Insurance Prop./Liability			
5235	Special Projects		30,000	
5238	Charges from Other Departments	32,800	23,400	23,100
	Other M&O Expenses	210,600	260,000	221,400
Total Maintenance & Operations		244,700	284,700	245,800
CAPITAL OUTLAY				
5454/5	Equipment	14,000	22,800	-
Total Capital Outlay		14,000	22,800	-
DIVISION SUBTOTAL		546,700	590,900	555,100
5239	Charges to Other Departments	(174,400)	(329,200)	(310,200)
DIVISION TOTAL		3,747,600	4,089,500	4,269,200

Source: City of Paso Robles Finance Department

DATE: June 24, 2008

TO: Roger Null, Kennedy Jenks Consultants

FROM: Christine Halley, TJCross Engineers

cc: Doug Monn

**SUBJECT: 2008 Water Rate Study
Revised Draft Projected Water Supply Plan and 10-Year CIP**

A fundamental component of the City of Paso Robles' water rate study is a forecast of capital expenditures accompanied by a water supply plan outlining the manner in which the City plans to meet increasing community water needs. I am writing to summarize City plans along both veins.

10-Year Capital Improvement Plan

The City provided financial reports for water operations in recent years such that you have a good idea of actual expenditures – both operational and capital. The City also adopted a 10-year Capital Improvement Program (CIP) for water, wastewater, and other City services as part of the Integrated Water Resources Plan dated February 2007. Attached is the updated water utility CIP dated June 2008.

Under the Nacimiento Water Project category, it is noted that both Paso Robles' share in the regional project and the proposed water treatment plant are to be debt-financed. I understand that you captured the bond payments elsewhere and I have not repeated those figures here. Operations and maintenance costs were approached in a similar manner.

After dialogue with the San Luis Obispo County Flood Control & Water Conservation District staff, additional buy-in of Nacimiento water in addition to the City's current 4,000 AFY entitlement is estimated at \$15,000/acre-foot. The City's Urban Water Management Plan and Potable Water System Master Plan point to the need for an additional 4,000 AFY supply to meet General Plan build-out needs. Thus, a \$60 million placeholder is listed under the Nacimiento Water Project category representing that forecasted water supply cost.

Next listed are Well Improvements. The \$4.7 million Ronconi filtration system cost is an estimate at this time and makes up a portion of the \$14.2 million capital needs forecasted over the coming decade.

I verified projected costs for tanks and booster stations with both the City capital projects engineer and Boyle Engineering Corp. You will see a line item scheduled for FY 10/11 to convert to remote-read water meters. I spoke to Doug Monn briefly about this and understood that a \$4 million '08 estimate applies.

The City Engineer guided me on the waterline list, particularly in assigning priorities. He also provided the "Percent Allocated to New Development" figures for all entries. For example, water

rates must generate 50% of the revenues needed to fund the well improvements with the balance coming from new connection fees.

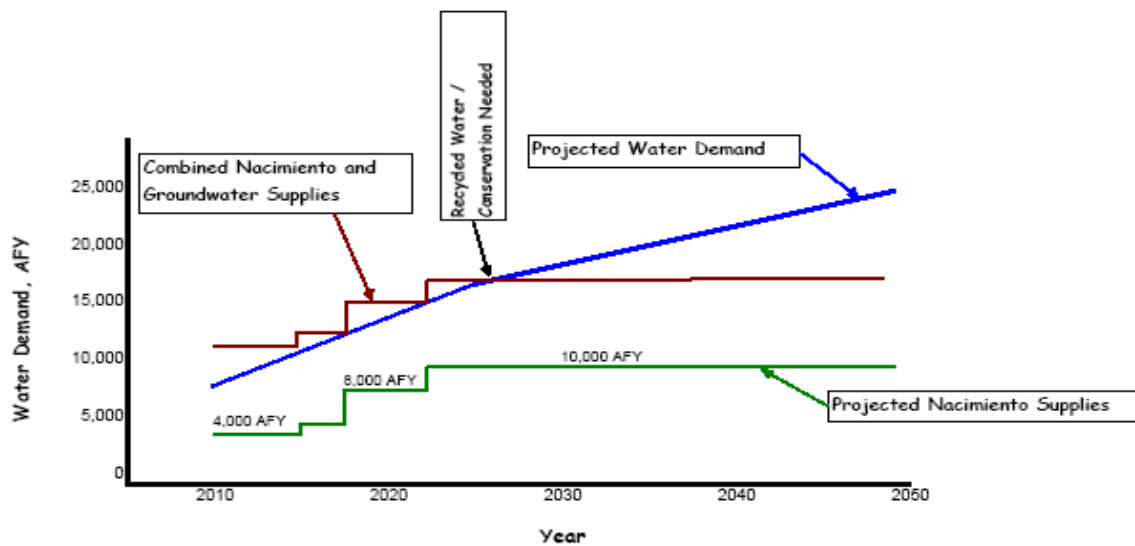
Staffing Plan

The staffing plan was submitted on March 31, 2008, and later reconciled to City budget projections.

Water Supply Plan

City water supplies are 100% well water now, pumping from both the Salinas River underflow and the Paso Robles Groundwater Basin. When Nacimiento deliveries begin in 2010, the City will operate such that the full 4,000 AFY of Nacimiento entitlement will be utilized. River wells will supplement Nacimiento deliveries such that the City pumps its full allocation and groundwater wells will make up any remaining difference.

A simplified graphic of anticipated demand vs. supply is:



Paso Robles - Conceptual Water Supply Needs

Notes:
Based on Paso Robles successful in securing +6,000 AFY of Reserve Water from Nacimiento Water Project.
Estimated 7,500 AFY yield available from groundwater.
Projected water demand illustrated without offset from successful conservation or recycled water program.

You will see that over the next 10 years that the initial 4,000 AFY of Nacimiento deliveries, increasing to as much as 8,000 AFY for new development, in addition to groundwater will be needed to meet demand.

Costs to Secure Additional Nacimiento Entitlement

As mentioned above, the City is expected to need an additional 4,000 AFY of Nacimiento entitlement by 2018 depending on the pace of development and other factors. Serious concerns regarding the availability of Nacimiento entitlement exists such that the City wishes to plan for the purchase of availability entitlement as soon as financially feasible.

Updated estimates of buy-in costs from the Flood Control District are such that to double the City's entitlement to a total of 8,000 AFY, costs may be on the order of an additional \$60 million in capital. This is shown on the attached CIP table. The approach used in HF&H's Water Capacity Charge analysis is to calculate a portion of the charge to purchase of additional water supply, and to build reserves designated for such purchase.

Regarding the cost to provide additional capacity at the water treatment plant, if the plant were operated to take additional entitlement during the peak Summer months, the treatment plant process would require a capacity increase as well as construction of the second planned treated water storage tank and increased pumping capacity at the treated water pump station. As previously discussed, the plant expansion may not be needed concurrent with the purchase of additional entitlement, thus the expansion costs are not included in the 10-year rate study planning window.

Closing

There are voluminous documents that provide backup for estimated yield from wells, forecasted demand, and other water supply aspects. Please let me know the level of detail that you seek from Paso Robles and I would be happy to embellish this summary.

PROPOSED CAPITAL IMPROVEMENT PROGRAM (C.I.P.) BUDGET

Revised to show capital projects only

Water Utility

FY 2007-08 to 2017-18

Inflationary adjustment =

5.50% per year
 1 2 3 4 5 6 7 8 9 10

Project ¹	Group ¹	Goal Advancement ²	Percent Allocated to New Development ²	FY 2007-08	FY 2008-09	FY 2009-10	FY 2010-11	FY 2011-12	FY 2012-13	FY 2013-14	FY 2014-15	FY 2015-16	FY 2016-17	FY 2017-18	TOTAL PROJECT COST ³	COMMENT
Water Projects:																
Nacimiento Water Project																
1	WS	ALL	50%	\$0	\$0	\$0	0.00	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	Paso's share in Nacimiento regional project is debt financed and not reflected here as a capital project
2		ALL	0%			\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	Similarly, O&M charges are omitted from this table as these are not capital costs
3	WS	ALL	50%	\$0	\$0	\$0	\$0								\$0	Paso's planned water treatment plant is to be debt financed and not reflected here as a capital project
4	WS	ALL	100%			\$60,000,000									\$60,000,000	Est. \$15 million per 1,000 AFY buy-in; timing of purchase to pace with development
5	WS	ALL	100%										\$0		\$0	
Subtotal Nacimiento Water Project =				\$0	\$0	\$60,000,000	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$60,000,000	
Allocation to new development = (Supply Component)				\$0	\$0	\$60,000,000	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$60,000,000	
Well Improvements																
6	WS	RELIAB	50%	\$500,000											\$500,000	Confirm source of estimate
7	WS	WQ, RELIAB	50%	\$2,096,241											\$2,096,241	Get actual cost data
8	WS		50%		\$4,747,500										\$4,747,500	Estimate based on initial vendor quote:
9	WS	RELIAB	50%												\$0	Included in annual budget stated below
10	WS	RELIAB	50%												\$0	Included in annual budget stated below
11	WS	RELIAB	50%	\$200,000	\$211,000	\$222,605	\$234,848	\$247,765	\$261,392	\$275,769	\$290,936	\$306,937	\$323,819	\$341,629	\$2,916,700	Annual budget - compare to historic
12	WS		50%			\$1,113,025			\$1,306,960			\$1,534,687			\$3,954,672	Revised 3/12/08 per D Monn edits
Subtotal Well Improvements =				\$2,796,241	\$4,958,500	\$1,335,630	\$234,848	\$247,765	\$1,568,352	\$275,769	\$290,936	\$1,841,624	\$323,819	\$341,629	\$14,215,113	
Allocation to new development = (Supply component)				\$1,398,121	\$2,479,250	\$667,815	\$117,424	\$123,882	\$784,176	\$137,884	\$145,468	\$920,812	\$161,909	\$170,814	\$7,107,556	
Tank, Booster Station and Metering Projects																
13	W	INF	50%	\$2,410,940	\$2,543,541	\$5,366,872									\$10,321,353	Nov 05 Prelim Eng Design Report by Boyle. Latest opinion available as of 2/08
14	W	INF	50%	\$20,000	\$21,100	\$22,261	\$23,485	\$24,776	\$26,139	\$27,577	\$29,094	\$30,694	\$32,382	\$34,163	\$291,670	Annual budget - compare to historic
15	W	INF	0%		\$253,221										\$253,221	CA concurs with estimate 2/08
16	W		0%				\$4,696,966								\$4,696,966	Activity in planning through Finance Dept.
17	W	RELIAB	50%			\$817,606	\$862,574	\$910,016	\$960,067	\$1,012,870	\$1,068,578	\$1,127,350	\$1,189,354	\$1,254,769	\$9,203,184	Start FY 09/10 per DM; Source is UWMP Admin Draft dated 2-29-08. Seems like a big investment in meters.
Subtotal Tank and Booster Station Projects =				\$2,430,940	\$2,817,862	\$6,206,739	\$5,583,025	\$934,792	\$986,206	\$1,040,447	\$1,097,672	\$1,158,044	\$1,221,736	\$1,288,932	\$24,766,394	
Allocation to new development = (Conveyance Component)				\$1,215,470	\$1,282,321	\$3,103,369	\$443,030	\$467,396	\$493,103	\$520,224	\$548,836	\$579,022	\$610,868	\$644,466	\$9,908,104	

Project ¹	Group ¹	Goal Advancement ²	Percent Allocated to New Development ⁵	FY 2007-08	FY 2008-09	FY 2009-10	FY 2010-11	FY 2011-12	FY 2012-13	FY 2013-14	FY 2014-15	FY 2015-16	FY 2016-17	FY 2017-18	TOTAL PROJECT COST ³	COMMENT
Pipeline Improvements																
18	W	INF	0%	\$343,784											\$0	
19	W	INF	0%									\$202,676			\$202,676	x
20	W	INF	0%		\$90,673										\$90,673	x
21	W	INF	0%			\$480,633									\$480,633	x
22	W	INF	50%				\$444,300								\$444,300	x
23	W	INF	50%			\$76,995									\$76,995	x
24	W	INF	0%				\$161,228								\$161,228	x
25	W	INF	0%					\$329,803							\$329,803	x
26	W	INF	50%						\$412,325						\$412,325	x
27	W	INF	50%							\$410,956					\$410,956	x
28	W	INF	50%							\$307,826					\$307,826	x
29	W	INF	50%								\$1,846,387				\$1,846,387	x
30	W	INF	50%									\$398,917			\$398,917	x
31	W	INF	50%										\$1,216,753		\$1,216,753	x
32	W	INF	50%											\$1,342,756	\$1,342,756	x
Subtotal Pipeline Improvements =				\$343,784	\$90,673	\$557,627	\$605,527	\$329,803	\$823,281	\$307,826	\$1,846,387	\$601,593	\$1,216,753	\$1,342,756	\$8,066,011	
<i>Allocation to new development = (Conveyance component)</i>				<i>\$0</i>	<i>\$0</i>	<i>\$38,497</i>	<i>\$222,150</i>	<i>\$0</i>	<i>\$411,640</i>	<i>\$153,913</i>	<i>\$923,193</i>	<i>\$199,459</i>	<i>\$608,377</i>	<i>\$671,378</i>	<i>\$3,228,607</i>	
Totals =				\$5,570,965	\$7,867,035	\$68,099,996	\$6,423,400	\$1,512,360	\$3,377,839	\$1,624,042	\$3,234,994	\$3,601,260	\$2,762,309	\$2,973,317	\$107,047,517	
Capital Project Allocation by FY to Rate Payers =				\$2,957,374	\$4,105,464	\$4,290,314	\$5,640,797	\$921,082	\$1,688,919	\$812,021	\$1,617,497	\$1,901,968	\$1,381,154	\$1,486,658	\$26,803,250	
Subtotal allocation by FY to Supply Component =				\$1,398,121	\$2,479,250	\$60,667,815	\$117,424	\$123,882	\$784,176	\$137,884	\$145,468	\$920,812	\$161,909	\$170,814	\$67,107,556	
Subtotal allocation by FY to Conveyance Component =				\$1,215,470	\$1,282,321	\$3,141,867	\$665,179	\$467,396	\$904,743	\$674,137	\$1,472,029	\$778,480	\$1,219,245	\$1,315,844	\$13,136,711	
Total Capital Project Allocation by FY to New Development =				\$2,613,591	\$3,761,571	\$63,809,682	\$782,603	\$591,279	\$1,688,919	\$812,021	\$1,617,497	\$1,699,292	\$1,381,154	\$1,486,658	\$80,244,268	

¹ W = Water; WS = Water Supply Component; WW = Wastewater; SD = Storm Drain;

² WQ = improve water quality; SALT RED = reduce basin salt loading; W RTS = maintain strong water rights; RELIAB = increase water supply reliability; GW DEP = reduce groundwater dependence; ALL = advances all major goals. INF = other infrastructure projects to meet existing customer needs and projected development.

³ Total Project Costs have both been adjusted to current dollars using ENR 20 Cities Construction Cost Indexes and adjusted for inflation at the rate shown.

⁴ Cost estimates in Boyle Potable Water M Plan include +25% engineering, admin, and CM allowance plus +25% project contingency.

⁵ Source: City Engineer John Falkenstien Feb 13, 2008

APPENDIX A - EXISTING DEBT SERVICE SCHEDULE

NET DEBT SERVICE
 SLO County Financing Authority
 City of El Paso de Robles
 Series 2007 A Revenue Bonds
 (Nacimiento Water Project)
 Insured Market Conditions as of 9/10/2007
 TAX-EXEMPT
 FINAL PRICING

Date	Total Debt Service	General Fund	Capitalized Interest Through 9/1/2010	Debt Service Reserve Fund	Net Debt Service
3/1/2008	1,451,521.18		1,451,521.18		0.00
9/1/2008	1,685,637.50		1,685,637.50		0.00
3/1/2009	1,685,637.50		1,685,637.50		0.00
9/1/2009	1,685,637.50		1,685,637.50		0.00
3/1/2010	1,685,637.50		1,685,637.50		0.00
9/1/2010	1,685,637.50		1,685,637.50		0.00
3/1/2011	1,685,637.50			97,642.94	1,587,994.56
9/1/2011	2,755,637.50			97,642.94	2,657,994.56
3/1/2012	1,664,237.50			97,642.94	1,566,594.56
9/1/2012	2,779,237.50			97,642.94	2,681,594.56
3/1/2013	1,641,937.50			97,642.94	1,544,294.56
9/1/2013	2,801,937.50			97,642.94	2,704,294.56
3/1/2014	1,620,187.50			97,642.94	1,522,544.56
9/1/2014	2,825,187.50			97,642.94	2,727,544.56
3/1/2015	1,596,087.50			97,642.94	1,498,444.56
9/1/2015	2,851,087.50			97,642.94	2,753,444.56
3/1/2016	1,570,987.50			97,642.94	1,473,344.56
9/1/2016	2,885,987.50			97,642.94	2,788,344.56
3/1/2017	1,538,112.50			97,642.94	1,440,469.56
9/1/2017	2,918,112.50			97,642.94	2,820,469.56
3/1/2018	1,503,612.50			97,642.94	1,405,969.56
9/1/2018	2,953,612.50			97,642.94	2,855,969.56
3/1/2019	1,467,362.50			97,642.94	1,369,719.56
9/1/2019	2,992,362.50			97,642.94	2,894,719.56
3/1/2020	1,429,237.50			97,642.94	1,331,594.56
9/1/2020	3,034,237.50			97,642.94	2,936,594.56
3/1/2021	1,389,112.50			97,642.94	1,291,469.56
9/1/2021	3,074,112.50			97,642.94	2,976,469.56
3/1/2022	1,346,987.50			97,642.94	1,249,344.56
9/1/2022	3,121,987.50			97,642.94	3,024,344.56
3/1/2023	1,302,612.50			97,642.94	1,204,969.56
9/1/2023	3,162,612.50			97,642.94	3,064,969.56
3/1/2024	1,256,112.50			97,642.94	1,158,469.56
9/1/2024	3,216,112.50			97,642.94	3,118,469.56
3/1/2025	1,207,112.50			97,642.94	1,109,469.56
9/1/2025	3,262,112.50			97,642.94	3,164,469.56

APPENDIX A - EXISTING DEBT SERVICE SCHEDULE

NET DEBT SERVICE
 SLO County Financing Authority
 City of El Paso de Robles
 Series 2007 A Revenue Bonds
 (Nacimiento Water Project)
 Insured Market Conditions as of 9/10/2007
 TAX-EXEMPT
 FINAL PRICING

Date	Total Debt Service	General Fund	Capitalized Interest Through 9/1/2010	Debt Service Reserve Fund	Net Debt Service
3/1/2026	1,155,737.50			97,642.94	1,058,094.56
9/1/2026	3,315,737.50			97,642.94	3,218,094.56
3/1/2027	1,101,737.50			97,642.94	1,004,094.56
9/1/2027	3,376,737.50			97,642.94	3,279,094.56
3/1/2028	1,044,862.50			97,642.94	947,219.56
9/1/2028	3,434,862.50			97,642.94	3,337,219.56
3/1/2029	985,112.50			97,642.94	887,469.56
9/1/2029	3,495,112.50			97,642.94	3,397,469.56
3/1/2030	922,362.50			97,642.94	824,719.56
9/1/2030	3,562,362.50			97,642.94	3,464,719.56
3/1/2031	856,362.50			97,642.94	758,719.56
9/1/2031	3,631,362.50			97,642.94	3,533,719.56
3/1/2032	786,987.50			97,642.94	689,344.56
9/1/2032	3,706,987.50			97,642.94	3,609,344.56
3/1/2033	713,987.50			97,642.94	616,344.56
9/1/2033	3,783,987.50			97,642.94	3,686,344.56
3/1/2034	637,237.50			97,642.94	539,594.56
9/1/2034	3,867,237.50			97,642.94	3,769,594.56
3/1/2035	556,487.50			97,642.94	458,844.56
9/1/2035	3,951,487.50			97,642.94	3,853,844.56
3/1/2036	471,612.50			97,642.94	373,969.56
9/1/2036	4,036,612.50			97,642.94	3,938,969.56
3/1/2037	382,487.50			97,642.94	284,844.56
9/1/2037	4,127,487.50			97,642.94	4,029,844.56
3/1/2038	288,862.50			97,642.94	191,219.56
9/1/2038	4,233,862.50			97,642.94	4,136,219.56
3/1/2039	190,237.50			97,642.94	92,594.56
9/1/2039	4,325,237.50			97,642.94	4,227,594.56
3/1/2040	97,200.00	-442.94		97,642.94	0.00
9/1/2040	4,417,200.00	442.94		4,521,722.94	-104,965.88
144,190,933.68	0.00	9,879,708.68	10,282,656.40	124,028,568.60	

PROPOSED WATER CAPACITY CHARGES

Connection Size	Current Fee	Proposed Fee
5/8" and 3/4"	\$9,119	\$28,687
1"	\$15,226	\$47,812
1-1/2"	\$30,364	\$95,625
2"	\$48,601	\$152,999
3"	\$97,292	\$286,874
4"	\$152,002	\$478,123
6"	\$303,914	\$956,246
8"	\$486,280	\$1,529,994
10"	\$699,100	\$2,199,366

Source: HFH Water Capacity Charge Study dated June 2008.

APPENDIX A - MONTHLY FIXED METER CHARGE RATIO ASSESSMENT

Meter Size (Inches)	Current Number of Meters	Meter Service Ratios (a)	Number of Equivalent Meters	Resulting Service Charges	Annual Svs. Charge Revenue
5/8 & 3/4	8,996	1.0	8,996	\$18	\$1,943,136
1	527	1.4	738	\$25	\$159,365
1.5	151	1.8	272	\$32	\$58,709
2	233	2.9	676	\$52	\$145,951
3	25	11.0	275	\$198	\$59,400
4	21	14.0	294	\$252	\$63,504
6	1	21.0	21	\$378	\$4,536
8	3	29.0	87	\$522	\$18,792
Totals	9,957		11,358		\$2,453,393
Revenues Derived From Current \$18/Account Charge					\$2,150,712
Additional Revenues from Equivalent Meter Charge Approach					\$302,681

(a) Source: American Water Works Association (AWWA) Manual M1



2175 North California Boulevard, Suite 990
Walnut Creek, California 94596
Tel: (925) 977-6950
Fax: (925) 977-6955
hfh-consultants.com

Robert D. Hilton, CMC
John W. Farnkopf, PE
Laith B. Ezzet, CMC
Richard J. Simonson

June 25, 2008

Mr. Jim App
City Manager
City of Paso Robles
1000 Spring Street
Paso Robles, CA 93446

Subject: **Water Capacity Charge Study
Public Review Draft**

Dear Mr. App:

With this letter I would like to report the results of our analysis of the City of Paso Robles' water capacity charge. This report describes the study background, approach and analysis, and summarizes our findings.

1.0. INTRODUCTION

The scope of this study is to update the city's water capacity charge based on the best available data and in conjunction with an update of the city's water rates. In this way, the same set of assumptions concerning capital costs and growth rates can be used in both studies.

2.0. BACKGROUND

The City charges new development one-time capacity charges at the time that the connection is made to the City's water facilities. The purpose of the capacity charges is to ensure that development pays its fair share of the costs associated with providing capacity. Capacity charges are a type of development impact fee that public agencies may impose as a condition of development under the authority of California Government Code Section 66000 *et seq.*, the Mitigation Fee Act. The Act requires that "those fees or charges shall not exceed the estimated reasonable cost of providing the service"¹. Because the Act does not prescribe a formula or procedure for determining "the estimated reasonable cost," it is the responsibility of the analyst to employ a method that yields a reasonable result.

¹ Mitigation Fee Act Section 66013(a).

The courts generally regard fees as being reasonable if they are not capricious, arbitrary, or discriminatory. Fees are capricious if there is no factual basis for the underlying data used to make the calculations. Fees are arbitrary if there is no logical rationale for choosing among alternatives. Fees are discriminatory if they disproportionately allocate costs to one class of service at the expense of another class. The purpose of this report is to document that the conditions have been met to establish that the City's water charge is reasonable.

Figure 1 summarizes the City's current capacity charges, which became effective July 1, 2007. Residential connections pay the fees shown in Table A. For non-residential connections the applicable fee is the higher of Table A or Table B. It is the City's practice to conduct studies to periodically update its capacity charge calculations with the latest capital costs. The capacity charges are escalated annually between studies to reflect inflationary cost increases. The current fees reflect a study conducted in 2004², and have been increased subsequently by the increase in the Engineering News Record's (ENR) Construction Cost Inflation index.

Figure 1. Current Capacity charges (Effective July 1, 2008)

Table A

Type of Development	Fee
Single-Family Residence	\$9,119
Multi-Family Residence	\$7,230 per unit
Mobile Home Park	\$9,119 per space
Mobile Home Subdivision Lot	\$9,119 per lot
Commercial/Industrial	\$9,119 + \$626 per unit
Hospital/Convalescent	\$9,119 + \$626 per room
Motel/Hotel	\$9,119 + \$626 per room
School	\$9,119 + \$626 per classroom

Table B

Meter Size	Fee
3/4"	\$9,119
1"	\$15,226
1 1/2"	\$30,364
2"	\$48,601
3"	\$97,292
4"	\$152,002
6"	\$303,914
8"	\$486,280
10"	\$699,100

3.0. APPROACH AND ANALYSIS

The approach used to calculate the water capacity charges derives the capacity charges in terms of the unit cost of facilities required to provide service for growth. The value of existing and future facilities was expressed in current dollars. It is our understanding that none of the existing facilities were funded from debt. Existing facilities are included in the

² Foresight Consulting Services. This study also derived water capacity charges based on equivalent dwelling units; water capacity charges are now charged based on the size of the water service connection.

capacity charge calculation because they provide capacity for growth. The existing facilities constitute a network with capacity for both existing rate payers as well as capacity for growth. Growth does not use only the increment of future capacity in the future facilities. These future facilities will be integral with the existing facilities.

Most, if not all, of the existing facilities have been paid for. They are included in the capacity charge calculation so that growth reimburses existing rate payers for the investment made on behalf of growth. The investment is valued at replacement cost to give effect to the appreciation in value since the original cost was occurred as well as the value of subsequent maintenance. The value of maintenance is reflected in replacement cost, which is appropriate because, since their construction, all facilities have been maintained and provide service indistinguishable from recently constructed facilities.

The unit cost of capacity was calculated by dividing the cost of existing and future facilities by the corresponding capacity associated with the facilities. In effect, the approach follows the "buy-in" or "average cost" methodology (with one exception discussed below). By using the buy-in methodology, it was not necessary to determine the portion of facilities attributable to growth, as was done in previous capacity charge studies. The buy-in method is based on the average cost of capacity, which is the same for existing and new connections. For the most part, the combination of existing and future facilities was divided by the total number of equivalent meter units at build out.

To make the calculation, existing and future facilities were identified, their values determined, the capacity associated with the facilities determined, and, by dividing the values by the respective capacity, the unit cost of capacity charge was calculated. A spreadsheet model was prepared to make the calculations. Each of these steps is described below.

3.1. Facilities Included in Calculation

An inventory of the existing and future facilities was compiled based on fixed asset records, facilities master plans, and related engineering data. It is likely that the inventory of existing facilities is not comprehensive and that there are facilities which are undocumented and have been excluded. Most of the existing facilities constitute the transmission pipelines, which are well documented. All of these facilities are known to exist and constitute a city-wide network of pipelines that provide capacity for growth. Existing wells and distribution system reservoirs are also included, but it is likely that the list is far from complete. Again, these facilities are an integral part of the water supply network that provides capacity for growth.

The future facilities are derived from the water master plan and related documents. These facilities will provide capacity for growth as well as benefit existing rate payers by improving reliability and upgrading facilities between now and build-out as documented in the city's general plan.

The combination of the existing and future facilities represents all of the infrastructure known at this time that will be required to meet demands at build-out. There will no doubt be additional facilities that should be included in future updates. There will also be other facilities that are currently projected for future construction that are modified or and replaced by other facilities. Again, changes like this can be reflected in future updates. We note that City staff has reviewed the list of existing and future facilities to ensure that there are no existing facilities that are also included in the future facilities.

3.2.1. Value of Existing Facilities

It is our understanding that none of the existing facilities was funded from debt. Hence, there are no financing costs to include in valuing the facilities. The historical cost of existing wells and reservoirs was escalated to 2008 using the Engineering News Record construction cost index.

The value of transmission mains was derived from an inventory of the amount of pipe of each diameter. The cost was determined by multiplying the number of linear feet of each pipeline size by the unit cost per linear foot. The resulting cost of the transmission mains represents the estimated construction cost at face value. Again, it is assumed that these facilities were not debt financed. By using historic book values, it is possible that other indirect overhead costs have been omitted. For example, land acquisition, legal, management, and similar project overhead may not be reflected in the historical costs or in the unit costs used in this report for estimating current construction cost.

The value of existing facilities is full replacement cost; depreciation was not deducted. Deducting depreciation from the replacement cost is a valuation technique used in determining the fair market value of utilities for purposes of selling the systems. In selling a system, however, a buyer will be unwilling to purchase a used asset at today's cost of a new asset. A buyer would expect to pay fair market value. By paying capacity charges, development does not acquire any ownership interest in the facilities. In calculating capacity charges, using depreciated replacement cost undervalues the assets, which are not being purchased.

Paying a capacity charge is intended to reimburse rate payers for any costs they incurred in providing surplus capacity for growth at such time as growth occurs. The cost of providing

such surplus capacity for the convenience of growth commands a premium compared with the value of a system that is being sold and must therefore attract buyers. Rate payers do not have to provide surplus capacity and should receive a return on their investment to provide an incentive for doing so. Full replacement cost reflects the fact that rate payers not only incurred the initial capital cost of construction (and the subsequent opportunity cost for having invested in infrastructure rather than in interest earning investments), but also incurred the cost of maintaining the facilities so that the facilities provide the equivalent level of service as new facilities.

3.2.2. Value of Future Facilities

The cost of future facilities was based on current engineering cost estimates and escalated to the projected date of construction. It is our understanding that these cost estimates include all associated engineering and construction costs but may not include the cost of City overhead. As such, the costs slightly underestimate the total cost.

The Nacimiento regional pipeline is debt-financed and the City's obligation for bond payments commences in 2010. It was assumed that the cost of the Nacimiento water treatment plant would be debt-financed as well and that all other project costs would be funded on a pay-as-you-go basis. Financing costs were included in the value of these two debt-financed future facilities. The financing costs that were provided with the cost estimates include interest payments and issuance costs. The effect of including financing costs in the value of these two assets roughly doubles their value.

It was assumed that all future facilities would be of common benefit to existing and future rate payers with the exception of the cost of future water supply in addition to the City's current 4,000 acre-feet of Nacimiento water. By common benefit, we mean that their capacity provides for both existing and future rate payers. The future water supply in addition to the City's current 4,000 acre-feet of Nacimiento water is assumed to benefit only growth and is the only existing or future facility that is allocated to growth only. Treating the future water supply in addition to the City's current 4,000 acre-feet of Nacimiento water as an increment of purely growth-related capacity is the only exception to what is otherwise a standard buy-in capacity charge calculation.

3.3. Projected Equivalent Meter Units

Figure 2 shows the derivation of the total and growth-related equivalent meter units (EMUs³) at build-out. The projection is based on an extrapolation of population figures from the City's General Plan. The data indicate the distribution of EMUs for each meter size in 2008, the estimated EMUs in 2025, and the incremental EMUs for each meter size. The projection shows an increase in EMUs from 12,106 to 20,716, an increment of growth of 8,610 EMUs.

Figure 2. Equivalent Meter Units

(1) Meter Size	(2) EMU Multiplier ¹	(3) 2008		(5) 2025		(7) Growth Increment	
		(3) Accounts ²	(4) EMUs (2)*(3)	(5) Accounts (3)*% Incr.	(6) EMUs (2)*(5)	(7) Accounts (5)-(3)	(8) EMUs (6)*(4)
5/8" & 3/4"	1.00	8,961	8,961	15,342	15,342	6,381	6,381
1"	1.67	503	838	861	1,435	358	597
1 1/2"	3.33	144	480	247	823	103	343
2"	5.33	215	1,147	368	1,963	153	816
3"	10.00	24	240	41	410	17	170
4"	16.67	18	300	31	517	13	217
6"	33.33	1	33	2	67	1	33
8"	53.33	2	107	3	160	1	53
10"	76.67	0	0	0	0	0	0
12"	116.67	0	0	0	0	0	0
		9,868	12,106	16,895	20,716	7,027	8,610
Population:	1/1/2008	29,934	³				
	2025	51,251	⁴				
	Increase	21,317					
	Increase	71%	Used to escalate accounts in column 5 above				
1. AWWA <i>Water Meters - Selection, Installation, Testing, and Maintenance</i> 2. City of Paso Robles; CY 2007 water usage by class data; does not include unbillable accounts. 3. Source: California Department of Finance, E-4 Population Estimates, May 2008. 4. Buildout to 2025 is from City Council resolution adopting new general plan buildout population of 44,000 plus potential for 7,251 residents beyond General Plan associated with potential annexations and/or General Plan amendments.							

³ The capacity of a 3/4" meter is considered one meter unit. The capacity of larger meters, divided by the capacity of a 3/4" meter, equals a ratio referred to as the "EMU multiplier." As shown in Figure 2, a 1" meter equals 1.67 EMUs. The EMU multipliers are taken from American Water Works Association standards.

3.4.1. Capacity Charges

The capacity charge is calculated by dividing the value of the existing and future facilities by the associated units of capacity. **Figure 3** summarizes this calculation for each future and existing facility.

Figure 3. Facility Costs and Capacity Charge

	Project Costs			Capacity Charge Components		
	Cash Funded	Debt Funded ¹	Cost in 2008 Dollars	Common Benefit (20,716 EMUs)	Growth-Only Increment (8,610 EMUs)	Total Capacity Charge Per EMU
Existing Facilities						
Supply	\$3,033,386	\$0	\$3,033,386	\$146	\$0	\$146
Treatment	\$0	\$0	\$0	\$0	\$0	\$0
Conveyance	\$174,168,967	\$0	\$174,168,967	\$8,407	\$0	\$8,407
Existing Facilities Total	\$177,202,353	\$0	\$177,202,353	\$8,554	\$0	\$8,554
Future Facilities						
Supply						
Nacimientto Regional Pipeline	\$0	\$144,190,000	\$144,190,000	\$6,960	\$0	\$6,960
Other	\$5,700,000	\$0	\$5,700,000	\$275	\$0	\$275
	\$5,700,000	\$144,190,000	\$149,890,000	\$7,235	\$0	\$7,235
Treatment						
Nacimientto Treatment Plant	\$0	\$89,770,000	\$89,770,000	\$4,333	\$0	\$4,333
Other	\$6,596,241	\$0	\$6,596,241	\$318	\$0	\$318
	\$6,596,241	\$89,770,000	\$96,366,241	\$4,652	\$0	\$4,652
Conveyance	\$26,479,662	\$0	\$26,479,662	\$1,278	\$0	\$1,278
Additional Future Water Supply ²	\$60,000,000	\$0	\$60,000,000	\$0	\$6,968	\$6,968
Treatment Plant Expansion (6 to 7.5 MGD)	\$0	\$0	\$0	\$0	\$0	\$0
Future Facilities Total	\$98,775,904	\$233,960,000	\$332,735,904	\$13,165	\$6,968	\$20,134
All Facilities Total	\$275,978,257	\$233,960,000	\$509,938,257	\$21,719	\$6,968	\$28,687

1. Costs include principal and interest. For example, the City's \$61 million bond financing of the Nacimientto regional pipeline translates into \$144,190,000 in total principal and interest payments over the 30 year life of the bond. A similar calculation was performed for the proposed water treatment plant debt financing.

2. Value shown is the estimated buy-in cost for an additional 4,000 acre-feet per year Nacimientto entitlement; Flood Control District estimate as of June 2008 is \$15,000 per acre-foot.

The project costs are itemized into cash-funded and debt-funded components (the cost for the debt-funded component comprises cumulative principal and interest payments). The capacity charge is itemized into the components that are of common benefit and of benefit to growth alone. The result shows a capacity charge of \$28,687 per EMU. **Figure 4** itemizes the capacity charges for the larger meter sizes.

Figure 4. Proposed Capacity Charges by Meter Size

Meter Size	Maximum Capacity ¹	Equivalent Meter Units	Capacity Charge
5/8" & 3/4"	30	1.00	\$28,687
1"	50	1.67	\$47,812
1 1/2"	100	3.33	\$95,625
2"	160	5.33	\$152,999
3"	300	10.00	\$286,874
4"	500	16.67	\$478,123
6"	1,000	33.33	\$956,246
8"	1,600	53.33	\$1,529,994
10"	2,300	76.67	\$2,199,366
12"	3,500	116.67	\$3,346,861

1. Rated maximum capacity in gallons per minute
 Source: AWWA *Water Meters - Selection, Installation, Testing, and Maintenance*

Note that the proposed capacity charges are shown for meter sizes only. The City currently has two schedules of charges, one based on development type and the other based on service connection size. The industry standard for water capacity charges is to charge on the basis of meter size, not development type. Development type matters with sewer capacity charges because there is a difference in wastewater loadings among classes of development. With water capacity charges, however, capacity does not vary by development type. The capacity in a two-inch connection, for example, is the same regardless of what type of development uses the capacity.

SUMMARY

Figure 5 summarizes and compares the current and proposed capacity charges.⁴ The increased costs shown in **Figure 3** result in significant increases in the capacity charges.

⁴ Omitting the charges for different development types.

Figure 5. Current and Proposed Capacity charges

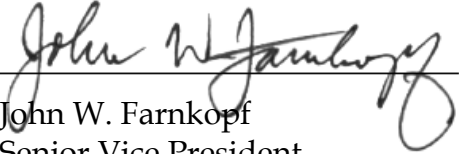
Connection Size	Current Fee	Proposed Fee
5/8" and 3/4"	\$9,119	\$28,687
1"	\$15,226	\$47,812
1-1/2"	\$30,364	\$95,625
2"	\$48,601	\$152,999
3"	\$97,292	\$286,874
4"	\$152,002	\$478,123
6"	\$303,914	\$956,246
8"	\$486,280	\$1,529,994
10"	\$699,100	\$2,199,366

In order to maintain the capacity charge in current dollars going forward, we recommend escalating the capacity charges shown in this report on an annual basis using an appropriate construction cost index. We also recommend maintaining an accounting of the capital expenditures so that, as future facilities are constructed and become existing facilities, any variance in cost can be reflected in the updated capacity charge.

Please do not hesitate to call if you have any questions. Thank you for asking HF&H to assist with this matter.

Very truly yours,

HILTON FARNKOPF & HOBSON, LLC



John W. Farnkopf
Senior Vice President

RESOLUTION NO. 08-XX

A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF PASO ROBLES
PROPOSING WATER USER RATES AND AUTHORIZING INITIATION OF THE
PROPOSITION 218 PROCEDURES

WHEREAS, improvements to the City water system are needed, primarily to improve the quality, increase the reliability, and supplement the limited ground water supply, and also to provide adequate distribution, staffing, and water storage capacity; and

WHEREAS, the planned improvements as outlined in the 2007 Integrated Water Resources Plan and Capital Improvement Program amount to approximately \$210 million over the coming decade, including Nacimiento Project supply and treatment capital costs as well as other distribution system capital costs plus financing and operations costs; and

WHEREAS, in August 2004, the Council entered into a delivery entitlement contract, securing 4,000 acre-feet per year of Nacimiento supplies; and

WHEREAS, on January 15, 2008, Council directed that a study of water rates and water connection fees be prepared in light of both the Nacimiento project and other planned water system improvements; and

WHEREAS, the revenues generated by the existing water rate structure are inadequate to sustain safe, reliable and high quality water system operations and water production in compliance with State Department of Public Health, local fire code, and other requirements; and

WHEREAS, the City wishes to ensure the ability to produce water to meet peak demands, extend water reliably and improve water quality; and

WHEREAS, an all-variable rate structure in which users pay strictly according to the water used will provide the necessary funding to provide a reliable, well-maintained, infrastructure system and reliable water resource to serve the needs of its existing and future customers.

THEREFORE, BE IT RESOLVED AS FOLLOWS:

SECTION 1. The City Council of the City of El Paso de Robles does hereby propose a combination of a **fixed and variable rate structure** for the purpose of providing a reliable, well-maintained, infrastructure system and reliable water resource.

SECTION 2. That the City Council hereby authorizes City Staff to initiate the necessary Proposition 218 ballot process associated with the potential adoption of a combined **fixed and variable** rate structure.

PASSED AND ADOPTED by the City Council of the City of Paso Robles this 1st day of July 2008 by the following votes:

AYES:
NOES:
ABSTAIN:
ABSENT:

Frank R. Mecham, Mayor

ATTEST:

Deborah D. Robinson, Deputy City Clerk

RESOLUTION NO. 08-YY

A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF PASO ROBLES
PROPOSING WATER USER RATES AND AUTHORIZING THE INITIATION OF THE
PROPOSITION 218 PROCEDURES

WHEREAS, improvements to the City water system are needed, primarily to improve the quality, increase the reliability, and supplement the limited ground water supply, and also to provide adequate distribution, staffing, and water storage capacity; and

WHEREAS, the planned improvements as outlined in the 2007 Integrated Water Resources Plan and Capital Improvement Program amount to approximately \$210 million over the coming decade, including Nacimiento Project supply and treatment capital costs as well as other distribution system capital costs plus financing and operations costs; and

WHEREAS, in August 2004, the Council entered into a delivery entitlement contract, securing 4,000 acre-feet per year of Nacimiento supplies; and

WHEREAS, on January 15, 2008, Council directed that a study of water rates and water connection fees be prepared in light of both the Nacimiento project and other planned water system improvements; and

WHEREAS, the revenues generated by the existing water rate structure are inadequate to sustain safe, reliable and high quality water system operations and water production in compliance with State Dept of Public Health, local fire code, and other requirements; and

WHEREAS, the City wishes to ensure the ability to produce water to meet peak demands, extend water reliably and improve water quality; and

WHEREAS, the proposed fixed-rate structure will provide the necessary funding to provide a reliable, well-maintained, infrastructure system and reliable water resource to serve the needs of its existing and future customers.

THEREFORE, BE IT RESOLVED AS FOLLOWS:

SECTION 1. The City Council of the City of El Paso de Robles does hereby propose a **fixed-rate approach** by which each user would pay a flat rate each month regardless of the amount of water used for the purpose of providing a reliable, well-maintained, infrastructure system and reliable water resource.

SECTION 2. That the City Council hereby authorizes City Staff to initiate the necessary Proposition 218 ballot process associated with the potential adoption of a **fixed-rate structure**.

PASSED AND ADOPTED by the City Council of the City of Paso Robles this 1st day of July 2008 by the following votes:

AYES:
NOES:
ABSTAIN:
ABSENT:

ATTEST:

Frank R. Mecham, Mayor

Deborah D. Robinson, Deputy City Clerk

RESOLUTION NO. 08-ZZ

A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF PASO ROBLES
ESTABLISHING WATER USER RATES AND AUTORIZING THE INITIATION OF THE
PROPOSITION 218 PROCESS

WHEREAS, improvements to the City water system are needed, primarily to improve the quality, increase the reliability, and supplement the limited ground water supply, and also to provide adequate distribution, staffing, and water storage capacity; and

WHEREAS, the planned improvements as outlined in the 2007 Integrated Water Resources Plan and Capital Improvement Program amount to approximately \$210 million over the coming decade, including Nacimiento supply and treatment capital costs as well as other distribution system capital costs plus financing and operations costs; and

WHEREAS, in August 2004, the Council entered into a delivery entitlement contract, securing 4,000 acre-feet per year of Nacimiento supplies; and

WHEREAS, on January 15, 2008, Council directed that a study of water rates and water connection fees be prepared in light of both the Nacimiento project and other planned water system improvements; and

WHEREAS, the revenues generated by the existing water rate structure are inadequate to sustain safe, reliable and high quality water system operations and water production in compliance with State Dept of Public Health, local fire code, and other requirements; and

WHEREAS, the City wishes to ensure the ability to produce water to meet peak demands, extend water reliably and improve water quality; and

WHEREAS, an all variable rate in which users pay strictly according to the water used will provide the necessary funding to provide a reliable, well-maintained, infrastructure system and reliable water resource to serve the needs of its exiting and future customers.

THEREFORE, BE IT RESOLVED AS FOLLOWS:

SECTION 1. The City Council of the City of El Paso de Robles does hereby endorse an all variable water rate structure in which customers would pay strictly according to the actual amount of water used for the purpose of providing a reliable, well-maintained, infrastructure system and reliable water resource.

SECTION 2. That the City Council hereby authorizes City Staff to initiate the necessary Proposition 218 ballot process associated with the potential adoption of an all variable rate structure.

PASSED AND ADOPTED by the City Council of the City of Paso Robles this 1st day of July 2008 by the following votes:

AYES:
NOES:
ABSTAIN:
ABSENT:

ATTEST:

Frank R. Mecham, Mayor

Deborah D. Robinson, Deputy City Clerk