



Legislation Details (With Text)

File #: ID-458-17 **Version:** 1 **Name:**
Type: Informational Report **Status:** Agenda Ready
File created: 11/21/2017 **In control:** City Council
On agenda: 11/28/2017 **Final action:**
Title: Clarifications to Utilities 2018 Proposed Rates and Fees Presentation
Sponsors:
Indexes:
Code sections:
Attachments:

Date	Ver.	Action By	Action	Result
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Department of Utilities

Reference: **Clarifications to Utilities 2018 Proposed Rates and Fees Presentation**

To: Mayor Richard N. McLean and Members of City Council
Through: Philip Rodriguez, City Manager
Prepared By: Curtis Bauers, Director of Utilities
Date Prepared: November 20, 2017

PURPOSE:

To present additional information requested following the November 14th Study Session to support the results and rationale to modify the current Utilities rates and fees based on Willdan Financial Services rate study analysis, in conjunction with the Utilities Cash Flow Model, to meet 2018 Utilities revenue requirements.

BACKGROUND/HISTORY:

Rates

Willdan Financial Services and the Utilities Department staff have completed a rate study analysis on the City's utility rates and fees. The analysis included a thorough review of current and future operational and capital expenditures required to operate City utilities in a conscientious and sustainable manner over the next 30 years.

Willdan reviewed the Department's updated information and analyzed the model for consistency and validity. The result of this study showed the need for a 2018 revenue increase of 2% in the water fund, 4% in the wastewater fund, and 15% in the stormwater fund, over the average revenues that were generated from 2016-2017. Not merely meeting future expenditure needs, rates are also required by Colorado statute to be based

on “cost of service”. This means that each customer class (such as residential, commercial, or irrigation users) should be charged fairly and equitably based on how much it costs to provide those services to those particular customer classes. While a full cost of service rate analysis has not been performed this year, it is anticipated that this more detailed analysis will occur late in 2018. However, it is a fair position that there are no significant changes to our most recent analysis that the proposed rates would not still represent the cost of service.

The results are also generally consistent with the advanced projection of 2018 rate increases which have been presented to Council in past years; 15% for storm water and 4% for wastewater. The notable exception being the water usage and water fixed fee rates, which had been projected at 7% for 2018 previously. Due to the new municipal rate taking effect in 2017, and the receipt of unanticipated revenue from hydraulic fracturing activities, water customers were projected to see only a moderate 2% increase in their bills, with the cost-of-living inflationary indices showing at slightly over 3%.

However, based on Council feedback, staff and the financial consultant are suggesting that support for no changes to the water usage rates or flat fees can be justified with one caveat. Projected revenues for 2018 could not reasonably include revenue that is not yet contracted or otherwise anticipated. Yet, we have significant reason for some optimism that several things may result in favorable revenue conditions, or reduced expenses. First, we have several grant applications under consideration by the State’s Water Fund, and if one is approved, it will exceed the anticipated revenue from the proposed 2% increase. Second, there are a number of oil and gas leases operating in our general vicinity and if any of these operators choose to purchase water for their fracking operations from the Water Activity Enterprise, this would also likely exceed the anticipated revenue from the proposed 2% increase. If we include these potential revenues, as ‘anticipated revenues’, then the recommendation for 2018 is that there be no rate increase for water.

Differing from prior years, and in an effort to minimize the perceived effect of longer billing periods on our customers, staff is proposing the adoption of a modified water usage tier structure. In effect, the second tier has been extended out to 20,000 gallons from 15,000 gallons and the third and fourth tiers have each in turn been extended by 5,000 gallons apiece. The extension of the tiers will eliminate any effect of the higher rates for all billing periods up to 38 days. Billing periods will all be 38 days or less, with most falling between 26-32 days.

Changes are still suggested to the wastewater rate schedules, which will be highlighted in the presentation. In general, wastewater revenues need to increase by 4%, and it is proposed that wastewater rates will each increase by approximately 4%. The minimum wastewater usage fee will remain at 3,000 gallons in 2018.

We have also taken a closer look at residential storm drainage fees which had been proposed to increase by 15% or \$.75. We are now recommending only a 10% increase, to \$5.50 per month for Single Family Residential customers. This results in an annual impact of \$6 rather than \$9 as originally proposed. This is moderated by a slightly larger increase in stormwater PIF, costs of which are born entirely on new development.

Connection Fees (PIFs)

Water, wastewater, and stormwater impact fees are charged to new developments to cover the cost of establishing new services to a development. These fees are sometimes referred to as connection fees, impact fees, or plant investment fees. These fees cover costs of the general buy-in from the developer to the existing infrastructure that was paid for by customers already served by the system. These costs include things like purchasing water for the development’s use, upgrades to existing or installation of new adequate infrastructure necessary to add service of the property to the existing system, investments in additional water and wastewater treatment capacity, and other costs associated with bringing a new development online.

Because of increasing costs to provide service to new developments, staff is generally recommending a 3.5% increase to all impact fees in the water and wastewater funds. The 3.5% increase is a conservative estimate,

derived from all available developmental information, and takes into account, changes in the current Construction Cost and Building Cost Indices for the Denver Metro area. With the completion of each of the Water, Wastewater, and Storm Drainage Master Plans over the past year, staff has budgeted for a full connection fee financial analysis to be performed in 2018.

We are recommending a slightly higher increase to the Storm Drainage PIF (impact fee) of 6% because this existing fee is most noticeably falling short of creating the necessary revenue for future storm drainage infrastructure and will likely have a bigger gap to fill when a full study is undertaken in late 2018.

The 2018 PIF increases will not affect existing customers and are not associated with monthly water bills.

FINANCIAL IMPACT

Approval of this rate and fee structure will provide the necessary revenue increases to meet the increased cost of providing the service needs of the water, wastewater, and stormwater systems. It will have similar effects on all residential and commercial users. The structure maintains compliance with general cost-of-service rate making principles and does not significantly alter the overall rate structure approved last year.

STAFF RECOMMENDATION

Willdan Financial Services and City staff have performed rigorous analysis on necessary expenditures, revenue requirements, and equitable rate structure design. Based on this analysis and review, staff recommends the approval of the proposed 2018 utility rate structures.