CITY OF MORRO BAY

City Council
NOTICE OF SPECIAL MEETING

The City of Morro Bay provides essential public services and infrastructure to maintain a safe, clean and healthy place for residents and visitors to live, work and play.

AMENDED
SPECIAL MEETING AGENDA
Thursday, June 28, 2018 at 6:00 P.M.
Morro Bay Community Center (Auditorium)
1001 Kennedy Way, Morro Bay, CA

ESTABLISH QUORUM AND CALL TO ORDER

PUBLIC COMMENT FOR ITEMS ON THE AGENDA

SPECIAL MEETING AGENDA ITEM:

I: **Review of Proposed Water and Sewer Rate Increases and Authorization to Submit the Water Infrastructure Financing Innovation Act (WIFIA) Loan Application**

Staff Recommendation: Council:

1. Receive draft financial plan and rate analysis for the Water Reclamation Facility (WRF) from City staff and representatives and provide direction as appropriate, and
2. Authorize the City Manager to serve as the authorizing agent and submit the Water Infrastructure Financing Innovation Act (WIFIA) Loan Application accompanied by an application fee of $25,000 paid for from previously budgeted amounts within the Water Reclamation Facility Capital Project.

ADJOURN

DATED: June 27, 2018

Jamie L. Irons, Mayor

THIS AGENDA IS SUBJECT TO AMENDMENT UP TO 24 HOURS PRIOR TO THE DATE AND TIME SET FOR THE MEETING. PLEASE REFER TO THE AGENDA POSTED AT THE PUBLIC WORKS DEPARTMENT/COMMUNITY DEVELOPMENT DEPARTMENT, 955 SHASTA AVENUE, FOR ANY REVISIONS, OR CALL THE DEPARTMENT AT 772-6261 FOR FURTHER INFORMATION.

IN COMPLIANCE WITH THE AMERICANS WITH DISABILITIES ACT, IF YOU NEED SPECIAL ASSISTANCE TO PARTICIPATE IN A CITY MEETING, PLEASE CONTACT THE PUBLIC WORKS DEPARTMENT/COMMUNITY DEVELOPMENT DEPARTMENT AT LEAST 24 HOURS PRIOR TO THE MEETING TO INSURE REASONABLE ARRANGEMENTS CAN BE MADE TO PROVIDE ACCESSIBILITY TO THE MEETING.

AGENDA NO: I

MEETING DATE: June 28, 2018

Amended Staff Report

TO: **Honorable Mayor and City Council** **DATE: June 22, 2018**

FROM: **Scott Collins, City Manager**
Rob Livick, Public Works Director
Eric Casares, WRF Program Manager
Jennifer Callaway, Finance Director

SUBJECT: **Review of Proposed Water and Sewer Rate Increases and Authorization to submit the Water Infrastructure Financing Innovation Act (WIFIA) Loan Application**

RECOMMENDATION

Council:

1. Receive draft financial plan and rate analysis for the Water Reclamation Facility (WRF) from City staff and representatives and provide direction as appropriate, and
2. Authorize the City Manager to serve as the authorizing agent and submit the Water Infrastructure Financing Innovation Act (WIFIA) Loan Application accompanied by an application fee of $25,000 paid for from previously budgeted amounts within the Water Reclamation Facility Capital Project.

ALTERNATIVES

None proposed.

FISCAL IMPACTS

There are no fiscal impacts related to this recommendation. However, water and sewer rate increases would be necessary to fund the WRF program as currently proposed. Fiscal impacts would be addressed in a future staff report to City Council.

EXECUTIVE SUMMARY

City Council selected the South Bay Blvd. location as the preferred site for the Water Reclamation Facility (WRF) in September 2017, and directed staff shortly thereafter to pursue an accelerated timeline to qualify for the Environmental Protection Agency (EPA) Water Innovation Financing Infrastructure Act (WIFIA) low-interest loan program to help subsidize the cost of the project. Since that time, the City has hired a new City Manager, Finance Director and WRF Program Manager, completed the draft Environmental Impact Report, lobbied state agencies, Congress and federal agencies for additional outside funding, and selected a preferred proposer to negotiate with to design and construct the onsite improvements at the South Bay Blvd. site. Over that same period of time, the project estimates have been reduced from the original estimate of $167M in 2017 to today's estimate of $126M (costs of the major components will be discussed later in the report) as elements of the project have become better defined. In addition, the City Council is nearing adoption of an

Prepared By: ___SC_____ **Dept Review: _____**

City Manager Review: _SC_____ **City Attorney Review: _____**

infrastructure master plan that addresses the long-term needs of the water distribution and collection systems. (i.e., OneWater Plan).

As the City has made significant progress on the project, staff recently began work on the rate study with Bartle Wells Associates, which will help establish a potential rate increase to sufficiently fund the WRF project, sewer and water systems operations and maintenance and sewer and water infrastructure improvements. The City Manager also formed a Blue Ribbon Commission in April, consisting of four Morro Bay residents with extensive finance and business experience and expertise to review and offer an independent evaluation and recommendation regarding water and sewer rates.

Through the work of the rate consultant, City staff and Blue Ribbon Commission, the City developed a draft proposed maximum combined water and sewer rate of $191/month (for the typical water and sewer customer), which would go into effect in July 1, 2019 if rates are approved through the Proposition 218 process. That proposed rate represents a 27.3% increase over the maximum rate approved by voters in 2015 ($150/month for typical customer, to go into effect in July 1, 2019). This rate would fund the WRF project, provide approximately $1M investments in both water and sewer improvements each year, and fund operations and maintenance at current staffing levels.

The Advisory bodies (WRFCAC, CFAC, PWAB) will have an opportunity to provide input into the rates, and in particular a few options regarding methodology, at the joint meeting on Monday, June 25th. City Council will have the same opportunity at their June 28th Special meeting. Those options are discussed toward the end of this report.

BACKGROUND/DISCUSSION

The City engaged Bartle Wells to conduct the rate study. They are a respected firm that provides these services to hundreds of water and sewer agencies. Their representative on the Morro Bay rate study, Alex Handlers, conducted the City's previous rate study in 2015. In addition to Mr. Handlers, City staff, including City Manager, Finance Director, Public Works Director, Utility Division Manager, and the WRF Program Manager, Eric Casares (Carollo Engineers) assisted in developing the rate study. The other major contributor to the rate study is the Blue Ribbon Commission. The City Manager appointed a Blue Ribbon Commission in April 2018 to, according to their mission statement, independently evaluate “the costs of the major components of the WRF program and water and sewer capital project needs and provide a recommendation to the City Manager for equitable and reasonable rates to pay for those needs.”

The Blue Ribbon Commission met with the City team eight times over the past several months. The objective of those meetings was to gather and analyze information about all the costs and various scenarios for financing to determine the impact on user water and sewer rates. Commissioners consistently challenged staff on all major components of the cost structure used to develop new rates. Their analysis and recommendations regarding the proposed rates are attached.

Special thanks are due to the Commission in driving some of the costs of the project down. Through that process, and other efforts including those by the WRFCAC in recommending a preferred proposer for the WRF onsite improvements, staff developed the following assumptions for costs and financing scenarios that inform the proposed new rates (discussed in the next section).

Key Rate Assumptions

1) WRF Program Costs and Annual Operating and Maintenance Expenses

The WRF program costs are now estimated to be approximately $126M. That estimate was

reduced from the $128.5M figure provided to Council on June 13, 2018 by examining what has been spent to date toward the program in terms of program management, planning, design engineering, and contingencies, and refined those based on actual contracts the City has negotiated and refined estimates. In addition, on the advisement of the Blue Ribbon Commission, the City removed the current wastewater treatment plant demolition from the program costs, as that component is years away from being realized, and the City will need to negotiate cost sharing with the Cayucos Sanitation District. As there are no immediate plans for that area, there isn't a need to include this component in the cost, and as a result, in the proposed rate increases.

The following table identifies the major costs of the WRF program:

	Cost Distribution			
Project Component	**Construction**	**Soft Costs**	**Project Reserves**	**Total**
General Program Implementation	$-	$5,159,500	$-	$5,159,500
Onsite WRF Facilities	$62,616,335	$8,488,729	$3,130,817	$74,235,880
Conveyance Facilities	$21,086,013	$2,820,403	$2,342,890	$26,249,305
Offsite Recycled Water Facilities	$8,592,314	$2,647,654	$859,231	$12,099,199
Total	**$92,294,661**	**$19,116,285**	**$6,332,938**	**$117,743,885**
			Total Financed Amount	**$117,743,885**
			Previous Program Expenditures (March 2013 to Present)	$5,063,150
			Project Total	**$122,807,035**
			Additional Project Reserves held with Cash on Hand	$3,130,817
			Total Program Costs	**$125,937,851**

As noted in the table above, a 5% project reserve is built into the proposed financing of the project as a matter of best practice. In addition, staff recommends that a 5% additional project reserve be retained with existing available cash on hand. While this is a conservative approach, the City would be required to retain a debt coverage ratio by maintaining minimum cash balances in addition to the City's recently adopted fund reserve policy to maintain minimum cash balances in both the water and sewer funds. The additional 5% project reserve is a creative use of these minimum required balances that staff believes is prudent given the changes in both city staff and program management of this project. Furthermore, as the project progresses, should this project reserve not be needed for the WRF project, the annual rate review and accounting process would offer an opportunity for the Council to reallocate these funds for the demolition of the current facility, completion of deferred capital projects and or leverage them to reduce rates.

The following table demonstrates the assumptions for the overall sewer and water operations and maintenance expenses, including the new WRF program going online in 2022.

Project Component	**2018 Estimate**	**Escalation**	**2022 Projection**
WRF and Collection System Operations	$2,383,000	$299,000	$2,682,000
Conveyance Facilities	$246,000	$31,000	$277,000
Recycled Water Operations	$193,000	$24,000	$217,000
Total	**$2,822,000**	**$354,000**	**$3,176,000**

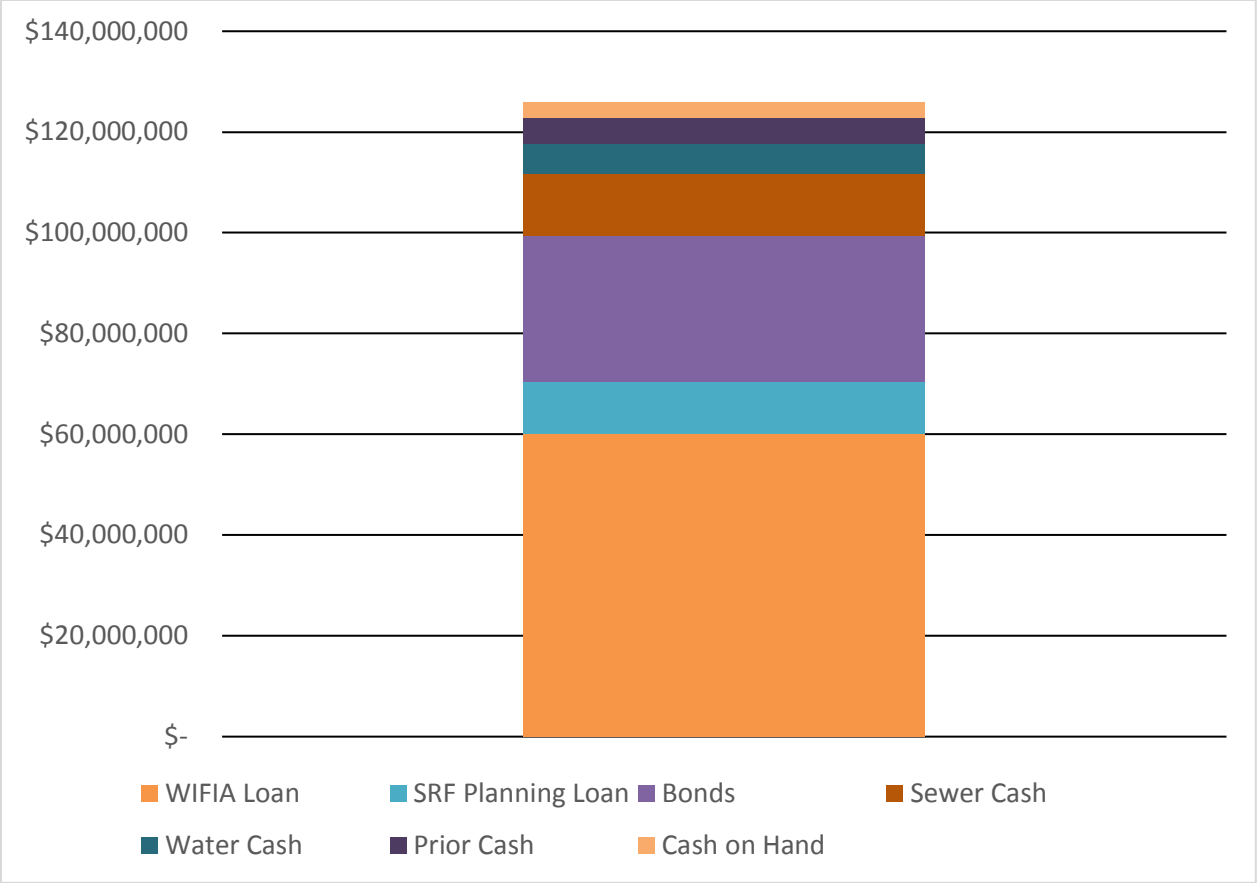
2) Capital Improvements for Water and Sewer System (Non-WRF)

The new rate assumes an annual capital projects program of $1M each for Water and Sewer. Through that investment, the major projects to be accomplished over the next five years for sewer focus efforts on reducing inflow and infiltration (i.e., N. Main Street sewer main and sewer lines in Beachcomber Drive). For water infrastructure over the next five years, the City's major capital project is the replacement of the Nutmeg Tank. The Nutmeg Tank is at risk of failure due to corrosion additionally it is undersized. Replacement of the tank will improve the distribution system's reliability and ability to achieve adequate fire flows. The water capital improvements include the addition of pipelines and valves necessary to eliminate the Vashon pump station, which is in poor condition and poses operational challenges for City staff.

3) WRF Program Financing

In developing the new rate, the City assumes the WRF program will be funded by a low-interest EPA Water Infrastructure Finance and Innovation Act (WIFIA) loan for up to 49% of the program, the recently awarded State Revolving Fund Planning Loan for 8%, cash contributions for approximately 14%, conventional bond financing for 25%, and 4% of prior expenditures made toward the program. The City is not assuming inclusion of the SRF low-interest construction loan as we do not possess an invitation to apply at this time. SRF does not provide an invitation to apply, and the City will not know if SRF will be awarded until the financial (i.e., rate to support the loan have been approved), technical, and environmental (i.e., certification of the Final EIR) packages have been reviewed and the SRF loan application is complete and submitted. However, Staff are confident that the City will secure an SRF loan should the WIFIA loan be awarded, which again is contingent on the reclamation component of the project. Staff will also continue to pursue grant opportunities. If an SRF loan is secured, or grant awarded to the City, Council will have the opportunity at that time to review water and sewer revenues and expenses and determine to either reduce water and sewer rates or investment additional dollars into other water and sewer capital needs.

Below is a table of the sources of financing for the project (on next page).



Proposed Rates

The assumptions discussed above were used to develop the draft proposed rate. It is important before discussing the new rate, however, to look back at the water and sewer rate increases approved in 2015. The City adopted increased water and sewer rates to fund a $75M waste water project with no reclamation and in partnership with Cayucos, and to address capital needs. Since that time, Cayucos has pursued its own wastewater project, while the City has added potable reuse to the program and selected a different preferred location with far fewer neighborhood impacts compared to the previous site identified in 2015. The City meanwhile has accumulated $10M in cash reserves through June 30, 2016 to apply to the project and developed a master plan for water and sewer infrastructure that defines the specific projects the City needs to undertake over the next 20 years (OneWater Plan).

The 2015 approved rate is set to end in FY 2019/20 and is outlined in the table below. The average residential user is defined as using 500 cubic feet of water per month (the row that is bolded).

Water Usage per Month (100 cubic feet)	Sewer Rate	Water Rate	Usage Charge (Water)	Total
1	$83.00	$32.00	$6.00	$121.00
2	$83.00	$32.00	$12.00	$127.00

Water Usage per Month (100 cubic feet)	Sewer Rate	Water Rate	Usage Charge (Water)	Total
3	$83.00	$32.00	$18.00	$133.00
4	$83.00	$32.00	$26.50	$141.50
5[1]	**$83.00**	**$32.00**	**$35.00**	**$150.00**
6	$83.00	$32.00	$43.50	$158.50
7	$83.00	$32.00	$52.00	$167.00
8	$83.00	$32.00	$60.50	$175.50
9	$83.00	$32.00	$69.00	$184.00
10	$83.00	$32.00	$77.50	$192.50
Notes: 1. Average residential user is defined as using 500 cubic feet per month.				

Based upon the rate study conducted by Bartle Wells Associates, informed by Blue Ribbon Commission analysis and recommendations, the following 2019 proposed rate increase is proposed:

Water Usage per Month (100 cubic feet)	Sewer Rate	WRF Surcharge (Sewer)[1]	Water Rate	WRF Surcharge (Water)[1]	Usage Charge (Water)	Total
1	$83.00	$25.00	$32.00	$16.00	$6.00	$162.00
2	$83.00	$25.00	$32.00	$16.00	$12.00	$168.00
3	$83.00	$25.00	$32.00	$16.00	$18.00	$174.00
4	$83.00	$25.00	$32.00	$16.00	$26.50	$182.50
5[2]	**$83.00**	**$25.00**	**$32.00**	**$16.00**	**$35.00**	**$191.00**
6	$83.00	$25.00	$32.00	$16.00	$43.50	$199.50
7	$83.00	$25.00	$32.00	$16.00	$52.00	$208.00
8	$83.00	$25.00	$32.00	$16.00	$60.50	$216.50
9	$83.00	$27.00	$32.00	$16.00	$69.00	$225.00
10	$83.00	$27.00	$32.00	$16.00	$77.50	$233.50
Notes: 1. Total WRF surcharge is $41.00 (i.e., $25.00 + $16.00) 2. Average residential user is defined as using 500 cubic feet per month.						

Analysis of proposed rates:

The proposed rate for the typical water and sewer customer will be $191/month beginning in FY 2019/20 (July 1, 2019). That rate represents a 27.3% rate increase over the maximum rate approved in 2015 ($150/month). Thus, the City has determined there is approximately a $41/month surcharge to finance the WRF program in its entirety. The Blue Ribbon Commission determined that this rate

is reasonable. They did however state that further savings could be identified through negotiations with the preferred proposer who will construct the onsite WRF facilities and recommended waiting until August 2018 to initiate the Proposition 218 process as opposed to July. In addition, they noted further savings may be identified through additional study of the injection wells, which could inform modifications of that component of the project and rightsizing the WRF facility's advanced water treatment process. Staff agrees that further savings can be identified through these processes. Staff however does not believe a delay in the overall project timeline will prevent the City from saving money on the project, because rates can be adjusted down at anytime by City Council if savings of notable amount are realized.

Options for Advisory Committees and Council

City staff will bring input to City Council gathered from the PWAB, CFAC, WRFCAC Monday, June 25, 2018 joint advisory Board meeting regarding the proposed rates in general, and the following options in particular:

1) Billing options for the WRF surcharge

As allowed by the California Health and Safety Code, the City could choose to put the WRF surcharge of $41 on individual property owners' County property tax roll as an alternative to including the capital costs associated with the WRF program on the monthly water and sewer bill. This process is used by other water and sewer agencies, and this method of payment could potentially shift the burden from the rate payer to the parcel property owner.

As noted in the Blue Ribbon Commission, there are a number of pros and cons to either method of billing. Billing the WRF surcharge on the monthly water and sewer bill provides timely receipt of revenues to the City and provides more funds to the Utility Discount Program. The downside of the monthly billing approach is the rate increases could potential shift the burden to renters.

Should the surcharge be placed on the property tax rolls, the payment responsibility would be transferred to the parcel owner, who may or may not pass the cost onto tenants in the case they rent their property. That could reduce the burden on renters. However, a downside to this approach is there is no existing Utility Discount Program offered for property tax roll charges. Another downside is that there will be two balloon payments each year on the surcharge through this method, which may impact parcel owners who are on fixed income. City staff are seeking input from the various advisory board/commission members on these options.

2) Implementation of rate increase

The City could choose to implement the rate increase by front loading the increase in year one, or phase in the increases over the period of four years. Front loading the increase will lead to a larger increase in the first year but result in a lower overall rate at year four. A phased in approach would lead to less of an increase in year one but would impact cash flow, meaning there would be less available cash to fund the project on a pay-go basis and ultimately increasing the overall financed amount of the project by approximately $6 million. The proposed front-loaded rate is $191 for the next five years. Under a phased in approach, the year one rate would be $161, or $30 less per month. Under the phased-in approach, the FY 2022/23 rate would grow to $194 per month. The phased in approach of rate increases would result in a higher overall rate in year 5 compared to front loading approach due to the need to finance an additional $6 million of the project which under the front-loaded method would be available as cash on hand.

The following table demonstrates the difference between the two approaches, in terms of combined sewer and water rates for the average rate payer.

	FY 2019/2020	FY 2020/21	FY 2021/22	FY 2022/23
Front load	191.00	191.00	191.00	191.00
Phase In	161.00	172.00	183.00	194.00

Recommended Council Action on WIFIA Application

The WIFIA application deadline is fast approaching and the various city teams have been working diligently to obtain all information necessary to submit a comprehensive application to WIFIA for review and consideration by July 9, 2018. The City first submitted a letter of interest for WIFIA financing on April 10, 2017 and received an invitation to submit a WIFIA application on July 17, 2017. WIFIA Financing is low interest financing, lower interest than bond financing, and obtaining this financing will help to minimize the overall rate impact to customers. However, obtaining WIFIA financing is conditioned upon the City's project being innovative and incorporating a recycled water component. With the WIFIA application submission deadline approaching, staff recommends Council authorize the City Manager to submit the WIFIA application, accompanied by the application fee of $25,000 paid for from the FY 2018/19 WRF Capital Project Budget.

CONCLUSION

The City is proposing an overall $41/month rate increase (for average water and sewer rate payers) that will fund the WRF project, which will provide another source of potable water to residents, and address needed water and sewer capital needs, while funding water and sewer operations and maintenance. While this is a significant rate increase, it does keep the overall rate below $200 for the average rate payers, which is drastic improvement over what the draft rate study conducted in 2017 had determined was necessary to fund the project at that time. Special thanks go out to the Blue Ribbon Commission for their hard work and determination to make the rates as reasonable as possible for the community.

ATTACHMENTS

1. WRF Blue Ribbon Commission Report and Recommendations to City Manager, June 21, 2018
2. Draft Financial Plan & Rate Analysis for a New Water Reclamation Facility (June 26, 2018)

MORRO BAY WATER RECLAMATION FACILITY

BLUE RIBBON COMMISSION

June 21, 2018

Prepared for the City of Morro Bay by Blue Ribbon Commission Members:

Homer Alexander 6/21/2018
Homer Alexander Date

6/21/18
John Martin Date

June 21, 2018
Joan Solu Date

JUNE 21, 2018
Barbara Spagnola Date

TABLE OF CONTENTS

I. INTRODUCTION

Morro Bay City Manager, Scott Collins, appointed four citizens to a Blue Ribbon Commission (BRC) on April 23, 2018 to evaluate the costs and potential user rate increases associated with the Water Reclamation Facility (WRF). Members of the Blue Ribbon Commission are Homer Alexander, John Martin, Joan Solu, and Barbara Spagnola. Mr. Alexander is a former chairperson of the City's Measure Q Citizens Oversight Committee and a retired small business owner. Mr. Martin is a current member of the Citizens Finance Advisory Committee and is a certified public finance officer who brings over twenty-three years of public sector management experience, including eight years as general manager of a water district. Ms. Solu is a former chairperson of the Tourism Business Improvement District Board, who has worked in the hotel industry since 1989, owning and operating several motels in Morro Bay. Ms. Spagnola is chairperson of the Citizens Finance Advisory Committee and a member of the WRF Citizens Advisory Committee, recently retired after spending over twenty-five years in IT management, contract negotiations, and budgeting.

The mission statement for the Blue Ribbon Commission is: "The WRF Blue Ribbon Commission is committed to independently evaluating the costs of the major components of the WRF program and water and sewer capital project needs and provide a recommendation to the City Manager for equitable and reasonable customer rates to pay for those needs."

The Commission met eight times with City staff (Scott Collins, City Manager, Rob Livick, Public Works Director, Jennifer Callaway, Finance Director, and Joe Mueller, Utility Manager) along with Eric Casares of Carollo Engineers, Program Manager and Alex Handlers of Bartle & Wells Associates. Mr. Handlers is a Public Financial Advisor who is helping the City establish the new water and sewer rates. The Commission also met independently several times. The objective of these meetings was to gather and analyze information regarding cost components of the WRF project and recent draft plans for current and future water and sewer non WRF related capital expenses, suggest cost reduction alternatives for both the Water and Sewer Funds, evaluate varying scenarios for financing, and determine the impact of all of the above on future user water and sewer rates. The Commission consistently challenged the City staff and Program Manager on every component of the cost structure used to develop the new rates.

The Commission reviewed and commented on four working drafts of the "Financial & Rate Analysis for a New Water Reclamation Facility" prepared by Bartle Wells Associates. Key points focused in our discussions included challenging the debt coverage ratio assumptions, contingency assumptions, and the accounting separation of water and sewer charges. A summary of the questions and comments raised by the

Commission members, and the associated responses from City staff and consultants, is attached to this report as Appendices A and B. This information in Appendix A and Appendix B is current as of the date of this report and was used for the recommendations provided later in this report by the Blue Ribbon Commission.

II. DISCUSSION OF ISSUES

A. Capital Costs

The Commission recommended to the City that only the following criteria be used for selecting the Capital Cost projects, unrelated to the new WRF, that should be completed:

1. Any project that if not completed could have an immediate adverse effect on the Health and Safety of the Community must be completed.
2. Projects that are absolutely needed to insure an adequate water supply.
3. Projects that are integral to the new Treatment Plant.
4. Projects to replace infrastructure that might fail in the next five years.

The Commission focused a good portion of meeting discussing the recently published draft of the OneWater Plan which addressed immediate and long-term infrastructure needs for the City owned Water and Sewer Utilities that are not related to the new Water Reclamation Facility. The Plan was prepared by a team from Carollo Engineers. These projects will be funded for the next five years by the free cash flow that the Water and Sewer Revenue Funds generate. The projected costs in the report are engineering estimates. They include the cost of construction, a 30% contingency, 10% for engineering, 10% for Construction Management and 7.5% for Project Administration. The cost figures in the report are in today's dollars.

Fire Suppression and the replacement of the Nutmeg water tank constitute a significant portion of the costs in the Water Fund in the next five years. There are certain sections of Morro Bay where the Fire hydrants test below a standard of 20 psi Maximum Day Demand (MDD). The OneWater plan recommends that the pipes in these sections be replaced with pipes that are a larger diameter to ensure that there is more than adequate water capacity for firefighting.

Further, the Commission discussed the need for the City to negotiate for purchase or a long term (50 year) lease for the Nutmeg site and or any space needed to secure the capital improvement needs for the Nutmeg project.

The replacement of the Nutmeg Water Storage Tank is necessary because the existing capacity is not sufficient to supply the Nutmeg zone with consistent MDD. Initially this project was planned to start in the fiscal year 2019-20. After a lengthy discussion it was agreed that the expense be spread over a number of years because there are logistical issues in reaching the tank, along with potential permitting delays.

Other major expenses in the Water Fund include upgrades to the control systems at the brackish water/desal plant and increasing the capacity of the fill line to the Nutmeg water storage tank.

A significant portion of the projected capital costs for Sewer infrastructure improvements in the next five years is the replacement of the gravity main on Main St. that runs from San Joaquin Street to Atascadero Road with pipe that has a capacity that is at least 50% larger. The gravity main along Beachcomber from Toro Lane to Java is scheduled for rehabilitation or replacement. Ongoing, there are capital projects to reduce the amount of infiltration and intrusion (INI) which includes replacing certain pipes that have been identified as the cause of significant INI and also replacing caps and manholes covers.

B. Billing Options for Water and Sewer Charges

The Commission discussed methods that could be utilized for the collection and payment of the capital costs of the proposed new Water Reclamation Facility (WRF). The City currently sends all ratepayers a monthly bill for both the water and sewer services. If the capital costs associated with the new treatment plant were to be included in the combined water and sewer utility bills, the monthly amount will increase significantly for all ratepayers.

An alternate method of recouping a portion of the combined water and sewer capital costs would be to include these costs on the County property tax roll, as opposed to the monthly utility bill. It is our understanding that this process for collection of infrastructure project capital costs is used by many local agencies. With this method, payment responsibility for the water and sewer capital costs ($41 per month as of the date of this report) shifts from the rate payer to the parcel property owner.

Both of the above methods of cost recovery have advantages and disadvantages. The current monthly utility billing process is familiar to everyone and illustrates a direct connection from the cost of the new plant to the ratepayer receiving the service. This method also provides the City timely receipt of water and sewer revenues, since the billing is monthly. Ratepayers who are also property owners do not have to save monthly for a semiannual property tax bill. Billing monthly will also provide more funds for the Utility Discount Program. The major disadvantage of monthly utility bills is the impact such significant increases may have on the low-income ratepayers, and the potential resulting delinquencies which the City has to follow through to collect.

Should the capital cost of the WRF be transferred to the property tax rolls, the payment responsibility would accordingly be transferred from the ratepayer to the property owner. While the overall total costs for the WRF would remain the same, the visibility changes. Additionally, the property owners who are landlords may or may not immediately pass on all of the increased costs to their tenants. Since the completion of a major infrastructure project benefits property owners, it may be appropriate to recover these costs via the property tax rolls. A disadvantage of the property tax method of collection is that there is no existing utility discount program offered for property tax charges.

San Luis Obispo participates in the Teeter Plan, which means the City receives 100% of all assessments placed on the property tax rolls for collection, regardless of any actual delinquencies. The County Assessor's office handles the delinquencies, and retains any penalties collected as well. Thus, the City does not have to collect on delinquent charges for the sewer capital cost. A final advantage of utilizing the property tax rolls for the WRF cost is that there would be a visible termination of the assessment, typically 30 years or whatever time period the capital costs are financed.

Finally, both of the above methods of cost recovery could also be applied to the water service provided by the City. The Commission is not recommending one method over the other, but merely addressing the pros and cons of both methods for consideration and implementation by our elected leaders.

C. Cost Reduction

At each meeting, the Commission challenged the City staff, Program Manager and Rate Advisor on every revenue and expense line item in the cash flow projections used to develop the new rates for the WRF project. All of these ideas were presented during the meetings held with City staff and external personnel currently working with the City on the WRF.

Regarding Table 1 from the "Financial & Rate Analysis for a New Water Reclamation Facility" dated June 21, 2018, the Commission discussed adding a column entitled "Project Reserves," which are placeholder estimates for additional project funding requirements (e.g. outside project scope) with funding subject to City control. The Commission argued successfully to reduce this amount. The current Program manager, Mr. Eric Casares, was uncomfortable totally eliminating it, because the original Request for Proposal (bridging documents) was not prepared by Carollo Engineers. As negotiations with Filanc/Black & Veatch progress, the expense in this column of Table 1 may be reduced.

The Commission questioned whether the new and more automated treatment plant would require the same number of employees as the existing plant, and what reduction in headcount could be anticipated from cross training plant employees. There are currently two vacant authorized positions within the water department. The City's Utility Manager, Mr. Joe Mueller, anticipates not filling these positions resulting in the permanent reduction of these positions in future years.

The Commission also proposed the design of the new operations building be revisited and possibly scaled down to reduce costs. Combining the operations and maintenance buildings was discussed, but the City's Utility Manager presented a number of good reasons to keep them separate. However, he did indicate in the negotiations with the Design/Build team he expected the costs of the operations building to be reduced (apparently the architectural design of the building may be more elaborate than

necessary). We also discussed removing the $ 1.5 million cost for demolition of the existing plant, which was done. Finally, the Commission and the project team reduced the cash funded water and sewer infrastructure capital costs over the first five years by approximately $ 3 million.

The Commission discussed several additional items for potential rate reduction:

- Prioritization for the capital projects identified in the OneWater Plan.
- Questioned the feasibility of projecting savings from a solar leaseback program.
- The Commission recommended that the feasibility of consolidating the pipes to the new plant into a single trench be investigated.
- Scrutinized the fund reserve forecast in the cash flow statements to more closely align with the Council's newly adopted reserve policy. This action has resulted in lower rates.

Many of the ideas presented by the Commission members along with the City staff's responses are documented in Appendices A and B.

D. Financing Options

The initial plan to finance all of the components of the new Water Reclamation Facility project is coming from four sources. They are: (i) accumulated cash; (ii) a ten-year planning loan at a rate of 1.70% from the Clean Water State Revolving Fund Financing Program (SRF) in the amount of $10.3M; (iii) a thirty-five-year loan at an estimated rate of 3.25% from the Federal EPA's Water Infrastructure Finance & Innovation Act (WIFIA) in the amount of $60.2M; and (iv) a thirty-year loan at an estimated rate of 4.75%, financed by issuing bonds in the amount of $28.9M. The Bonds will be structured so in the first ten years the City will only be repaying interest. When matched with the ten-year amortization term of the SRF planning loan the total debt service payments remain constant for the first thirty years.

Because the City does not have a letter of commitment from the managers of the State Revolving Loan program the new rates are being calculated using the $28.9M of bond financing. The City has submitted preliminary application to SRF. When the EIR is certified later this summer the City will be in a position to submit a complete application. It is estimated that the application review process may require up to eighteen months.

The City Staff is optimistic that they will receive a thirty-year SRF loan at an estimated rate of 2.2% for the balance of the principal that is required beyond the WIFIA loan. If that occurs the SRF loan would replace the $28.9M of bond financing. Eliminating the Bond financing would reduce the total annual debt service expenses, which would result in an estimated reduction in the rates of about $6 per month. In addition to the reduction

in interest rates, the $10.3M SRF planning loan will be rolled into a thirty-year SRF loan which would have a positive impact on lowering the annual debt service payments.

If the City is able to secure SRF financing then the elected officials would have the option of either slightly reducing the monthly base water and sewer rates or to accelerate water and sewer infrastructure improvement projects.

E. Conveyance to and from the Plant (Pipes and Lift Stations)

The route of the force main from the existing Atascadero Road Treatment Plant to the new Water Reclamation Facility on South Bay Boulevard will travel along or under the bike/pedestrian path (runs just to the east of the Morro Bay Power Plant to the intersections of Quintana and Main). The force main would then continue south on Quintana to South Bay Boulevard then north to the new plant. In addition to the force main the trench will also include a pipe for the brine discharge and heavy wet weather processed flows to the City's Outfall to the Ocean. The trench will also include a potable water line for fire suppression at the plant.

The design of the route for the pipe to transport the recycled water to the injection well fields in the Morro Valley has not been determined. The two routes that are being considered are on either side of Highway 1. There is a possibility that if the westside route is chosen the pipe to the injection wells could be placed in the same trench as the force main, which would lower the estimated costs and therefore possibly have a positive impact on rates. However, there are concerns that due to other underground utilities in the same area it may not be possible to increase the size of the trench to accommodate the additional pipe.

F. Billing

The Commission discussed the need for the Water and Sewer billing process to be clarified for all rate payers. There is concern by the City that the current bill design is not adequate for the needs of the community. Similar concerns were expressed by the Commission. It was noted that largely, the community refers to the current bill as the "Water Bill" based on the format provided. The City is currently in the process of updating its billing to reflect a clearer, more easily readable water and sewer bill for the rate payer. The Commission suggested that bills should reflect the user category i.e. residential or commercial, with a reference to strength class for sewer charges for the commercial user. Additionally, the bill should reference where the rate tiers and rate structure can be found on the City web site along with any scheduled increases. Further, the Commission believed that it would be good practice for the City to "Audit" the commercial bills against the commercial business licenses and/or commercial public building use to ensure that rate payers are being classified correctly. Many buildings

have changed in use over time therefore there is opportunity for the City to implement best practices to maintain billing integrity. It was also suggested that any future scheduled increases have a notice of said increase included in the water and sewer bill 30 days prior to the increase occurring.

G. Water Independence and the State Water Project (SWP)

Since state water is a major component of the water rates, the Commission spent considerable time analyzing present and future state water impacts to the rate structure. One of the community goals is to achieve local water supply independence through the complete recycling of wastewater by the proposed advanced treatment component of the WRF and the associated indirect potable reuse (IPR) project (off-site improvements). While this is a worthy goal, the Commission concludes that the benefits from this achievement will be limited for the duration of the SWP contract, which expires in 2038. This conclusion is based on the following findings:

- Costs for SWP water are largely fixed and the City will not be able to escape paying them regardless of how much water is delivered.
- Both groundwater basins available to the City are contaminated with nitrates and cannot be delivered directly into the potable water system without treatment.
- Treating the local groundwater is more expensive than the variable charges for SWP water.
- The City has contingent water supplies available.

The City is under contract with the San Luis Obispo Flood Control and Water Conservation District (SLOFC) for its SWP water supply, which comes to the City already treated by the Central Coast Water Authority (CCWA). The City is billed for five different types of charges related to SWP water: (1) Department of Water Resources (DWR) charges, (2) drought buffer, (3) CCWA bonds (Chorro pipeline), (4) CCWA fixed O&M and (5) CCWA variable O&M. All but the last of these charges are fixed. Annually, the City pays approximately $2.2 million in total for SWP water, with less than $80,000 in the form of variable charges. So, the remaining $2.1 million is due and payable even if no water is delivered. The drought buffer, which provides the City additional SWP water during a drought, is under a separate contract and the City can decline this on an annual basis, which would save about $260,000 per year. Final payment on the CCWA bonds will occur in fiscal year 2021/22, which will reduce fixed costs by $670,000 per year. So, beginning in fiscal year 2022/23, the City will have annual SWP fixed costs of $1.2 million (2018 dollars) which will persist until 2038.

Over the past five years, the State Water Project provided 92% of the City's water supply, with the remaining 8% coming from wells in the Morro Valley Groundwater Basin, which is contaminated with nitrates. Its groundwater must be processed through the City's Brackish Water Reverse Osmosis (BWRO) facility. The BWRO has an

operating capacity of 450 GPM, a peak capacity of 900 GPM and delivers 80% of its input water to the potable water system (20% to waste). The City has 581 acre-feet per year (AFY) of water rights in the Morro Basin, which translates to 465 AFY into the system after BWRO treatment. The City also has 1,142 AFY of water rights in the Chorro Valley Groundwater Basin, but it currently lacks a method to treat that water to meet state and federal water quality standards. So, for now, the City effectively has no water available from that source.

The BWRO has sufficient capacity to treat all of the City's groundwater available from Morro Basin, but it will need to be expanded to treat additional water introduced through IPR. The City commissioned GSI Water Solutions to create a groundwater model, which "indicates that it may be possible to achieve the 825 AFY injection goal." Further field studies will be required to test transport times to meet state water quality standards. If IPR is permitted, it is unknown how much of the 825 AFY will become available in the City's wells, as that will be determined by the degree of saltwater intrusion into the well field. Assuming that all of the water will be available, the 825 AFY will be processed by the BWRO into 660 AFY to the potable water system, resulting in 1,125 AFY when added to the Morro Basin supply.

City staff and engineers expressed that the introduction of pure recycled water could clean the Morro Basin over time and that eventually the groundwater will not need to be processed by BWRO. However, the level of nitrate contamination (as much as three times the maximum contaminant level in one well) presents a challenge to this goal. Moreover, the quantity of water introduced through IPR will likely be too small to impact a basin with a storage capacity of up to 33,000 acre-feet (DWR Basin 3-41 Report). So, it appears that all of the water from the WRF that will be injected into the Morro Basin will need to be processed through an expanded BWRO at a much higher cost than taking delivery of SWP water and paying the relatively small variable charge. Therefore, the City is aware that until 2038, it is likely that the most economical way to deal with the water recycled by the WRF will be to inject it into the ground and leave it there.

In addition to its 1,313 AFY of SWP contract water, the City has contracted for a drought buffer of 174% of that amount. In addition, when the City doesn't take its full SWP annual supply, it is stored in the San Luis Reservoir and can be taken in future years. Moreover, the SLOFC can "loan" the City some of its SWP supply that can be paid back later. These provisions enabled the City to survive the most severe drought in California's history. In 2014, the SWP's allocation was only 5%, which would have provided only 180 AF under the City's drought buffer provision, yet the City took delivery of 1,214 AF that year. The following year (2015), the SWP allocation was only 20%, which should have provided only 720 AF, yet the City took delivery of 1,094 AF. The SWP, while unreliable, has been rendered much more reliable by the wise actions already taken by the City. Finally, in the past, the City has established emergency

water supply agreements with the California Men's Colony, Whale Rock and Morro Bay Power Plant to address the unreliability of the SWP.

The Commission concludes that water made available by the WRF should be viewed as an insurance policy rather than as a primary source of water. In the event that there is a catastrophic failure of the SWP south of the San Luis Reservoir (Los Banos), the City could tap the banked recycled water during the emergency. However, during normal times, even during severe droughts, the SWP would provide the lowest-cost water available to the City.

III. BLUE RIBBON COMMISSION RECOMMENDATIONS

The Blue Ribbon Commission has completed their analysis of all cost components of the WRF and the impact of these current and future costs on the water and sewer rates necessary to support this project.

The City of Morro Bay "Financial & Rate Analysis for a New Water Reclamation Facility with WIFIA & Bond Financing Draft" of 06/21/2018 prepared by Bartle Wells Associates proposes a residential combined water and sewer WRF facility surcharge of $41.00 per month to be added to the already adopted rates as of July 1, 2019. As a result, the total rate increase for an average residential rate payer would be approximately 28%. Based on the information provided to the Commission for analysis at the time of this report, the Commission considers the City's rate proposal to be reasonable.

Further the Commission agrees that if the City Staff and Eric Casares, Program Manager were given additional time to begin negotiations with Filanc/Black & Veatch the process could potentially generate additional cost reductions for the WRF which could benefit rate payers. Therefore, the Blue Ribbon Commission suggests that the scheduled City Council meeting of July 10, 2018 to approve the new water and sewer rates be postponed to August 14, 2018 to provide City staff and the Program Manager sufficient time to negotiate any potential additional cost savings.

The Commission also recommends City Council authorize a contract to GSI Water Solutions to proceed with the field work in the Morro Valley to determine the feasibility of ground injection. The results of their analysis have the potential of reducing the advanced treatment processes which could further lower costs.

Regarding the monthly utility billing, it is recommended the WRF surcharge for the new Water Reclamation Facility should appear on the monthly bill as a separate line item.

The Commission requested that Bartle Wells Associates (BWA), the City's rate advisor, provide a rate analysis for the WRF without reclamation, financed at the higher rates for bonds issued by the City. Since the Commission has not received that analysis, we have no comments nor recommendation to offer.

APPENDIX A

Blue Ribbon Commission Questions and Answers

Submitted May 31, 2018

The following questions have been composed by the Blue-Ribbon Commissioners as a group. The questions are divided into the 3 sections based on the project and the goals of the commission as discussed at our third meeting:

Water and Sewer Combined (WS)
Water Only (W)
Sewer Only (S)

Each section is further divided into sub categories that contain questions, ideas and considerations for City Staff and the various firms hired to produce a competitive project that meets the communities needs and is financially responsible.

We believe the answers to our questions will begin the process of providing the information necessary for the Commission to properly evaluate the proposed new sewer and water rates and subsequently make appropriate recommendations.

The name of the individual (s) who supplied the answers is to the right of the heading for each question or group of questions. The answeres were supplied in writing and viewed at our June 6th meeting.

WATER AND SEWER

WS-I. General – Answer - Casares/Handlers

A. Splitting costs accurately and equitably between **Water and Sewer** that are not easily defined (i.e. headworks-defined vs. site prep-not defined) will be key to determining accurate rates. This work must be done in order to provide information to the public for a 218 vote.
   1. Who will be determining ratio? - 1. Carollo as the Program Manager will be determining the split between the Water and Sewer. Costs attributed to both water and sewer will be apportioned as a ratio between water and sewer.
   2. When will this work be done? Ongoing.

3. Will your rate study provide information comparing the proposed rates with EPA's and CalEPA's affordability index for water? We can include whatever is desired. However, the rates will need to recover the costs of service and in some cases, that may result in rates that exceed an index.

WS-II. Finance – Answer -Callaway/Handlers

A. Considering the projects will be financed with, the ten-year planning loan, WIFIA and SRF loans
   1. Who is going to be responsible for blending loan interest rates together to determine the annual debt service? Alex Handlers from Bartle Wells Associates (BWA) is modeling the debt financing. He is a Certified Independent Professional Municipal Advisor with extensive experience structuring debt service and serving as financial advisor on issuance of bonds, COPs, bank loans, lines of credit, State Revolving Fund Loans, and other types of financing. The interest rates will not be "blended", instead each component of the financing will be modeled independently.
   2. Who will be responsible for forecasting the existing cash that is available in both funds? The City's finance department.
   3. What are reserve requirements for the different loans? The reserve requirements for each financing will be modeled independently based on the requirements of each source of financing. For example, a) State Revolving Funds typically require a one-year debt service reserve fund to be funded at least 90 days prior to project completion, b) the reserve requirement for bonds/COPs may need to be cash funded or can potentially be satisfied by a reserve surety bond issued by a bond insurance company, c) the reserve requirement for WIFIA is somewhat negotiable depending on credit quality.
      i. If the reserve requirements are different who will blend them?
   4. How will the City control the amount of principle to be borrowed from either the EPA or SRF loans if one of the lenders has significantly more favorable terms? Who determines which loan gets priority/majority of the debt?

      From the City's perspective, the goal will be to maximize the lowest-cost financing (in this case, first maximize SRF, then maximize WIFIA). However, we may not have this luxury at the end of the day. Also note that WIFIA will only fund up to 49% of the project cost and SRF has not yet provided any funding.

WS-III. Personnel Costs – Answer - Callaway/Mueller

A. Between the three accounting entities--Water, Collections and Treatment---there has been significant turnover of staff in the last three years. Most of the new hires are at the beginning of their step increase process and additionally most of them are at tier 3 CALPERS rates.
   1. We recommend that the City calculate each individual employee's actual salary and benefits separately for each year over the next five years. The City should use 2018 wages and benefits for accurate measurement. The sum of those numbers should be included in the rate study vs. an arbitrary percentage annual increase. The total 2017-18 budget for personnel is $2.475M…. not an insignificant number.

B. Will the new automated plant really need the same number of employees as the existing plant? Over the past two years the existing plant and collections staff have been anticipating an updated facility by planning and par-paring staffing and operations plans. By taking advantage of the efficiency gained by shared department staffing and the anticipation of a new facility two FTE positions that became vacant where not filled.
   1. How many employees are expected to be cross trained- All 15 water, wastewater, and collections staff will have the opportunity to cross train, initially cross training will be focused on the 11 operations staff members with the remaining 4 lead and supervisor positions focusing on their specialized areas.
   2. How many are expected to be phased out through natural attrition such as retirement over the next 5 years? As stated in #2(i) two FTE's where phases out over this past year, current FTE levels are what is anticipated for the operation of current and future facilities.

WS-IV. Buildout Calculations – Answer - Handlers

A. Will the projected numbers that will be used for new customers correspond with the Community Development Department buildout projections? BWA strongly recommends that any financial projections be based on conservative growth assumptions. Revenues from projected growth typically have little impact in the bigger financial picture and are not considered a reliable recurring revenue source for debt repayment.

B. Who is calculating the future impact fees? City's water and sewer impact fees. A few years ago, BWA conducted some initial analysis indicating that the water and sewer impact fees could be increased. Higher impact fees may help offset the need for future rate increases to a small degree, but would only have minimal impact on proposed rate increases at this time as the adopted rates generally

need to be adequate to support debt repayment and associated financial covenants assuming minimal to no future growth.

WS-V. Interest Rates – Answer - Handlers

A. Was the interest rate for the ten-year planning loan locked in when the loan was secured? If so what was the rate? The SRF planning loan has a 1.7% rate and a preliminary repayment schedule that starts in Fiscal Year 2020/21. However, it may possible to roll repayment into a longer-term 30-year SRF Loan. Alternatively, it may be possible to structure the WIFIA loan or potential bonds around the debt repayment schedule for the 10-year planning loan to result in level annual debt service in future years (as opposed to elevated debt repayment for 10 years).

B. How is the WIFIA interest rate going to be determine for the debt service calculation? WIFIA interest rates are based on the US Treasury Department's rate for State & Local Government Securities (SLGS rate) corresponding with the Average Weighted Maturity of the loan. The rate is locked in when the WIFIA loan agreement is finalized. The rate fluctuates daily and is currently right around 3% for a loan with an Average Weighted Maturity anywhere from 20-30 years.

WS-VI. Capital Projects Prioritization – Answer - Casares

A. We believe the capital projects identified in the first five years in the OneWater Plan should be prioritized in the following order:
    1. Any project that if not completed could have an immediate adverse effect on the Health and Safety of the Community must be completed.
    2. Projects that are absolutely needed to insure an adequate water supply.
    3. Projects that are integral to the new Treatment Plant
    4. Projects to replace infrastructure that might fail in the next five years

We are working directly with BWA to move as much of the CIP as possible later in the planning horizon. We agree with your recommendations and are using them to aid in this re-prioritization. In addition, the criteria you are using, we are also considering:

1. Projects that would reasonably be constructed together (i.e., tank as well as pipeline needed to fill the tank).
2. Sequencing (i.e., upsizing gravity sewer lines starting at the downstream end.

B. Other projects should be pushed off into the second five-year period or even into the second ten years. Noted. We will be trying to maintain a consistent spend for capital projects throughout the period.

WATER

W-I. General – Answer - Casaras/Handlers

1. Will Morro Bay's 2015 Urban Water Management Plan inform your water demand forecast in your 2018 rate study? It may potentially provide some useful information for a water rate study. However, the demand projections in the 2015 UWMP were developed for a completely different purpose of evaluating water supply needs, etc. I do not recommend using outdated demand projections for a water rate study, but instead would recommend using slightly conservative demand estimates based on recent historical water use. If water use and water sales revenues were to significantly increase in upcoming years, then that would potentially offset the need for future rate increases.

2. Will your rate study include a robust cost analysis ($/AF) of the City's many water sources, including water delivered through the proposed advanced treatment / indirect potable reuse project? The OneWater Plan includes a robust analysis of the costs associated with various water supply options including several variations of IPR.

3. Is the water reliability analysis in the 2015 UWMP current for the City? If not, have you been assigned to write an update? The UWMP plays a specific role and the information regarding the reliability of the City's water supply has been updated in the OneWater Plan.

W-II. Revenue- Answer - Handlers

A. Interest Income—What rate will be used to calculate future income? BWA is currently assuming an interest rate of 1.5% through year 5, with a future assumed rate of 2.0% in outer years. LAIF's most recently quarterly yield as of March 2018 was 1.51%. Please note that interest earnings are only a very small component of utility revenues, most of the revenues are generated by rate revenues.

B. System Capacity Charge (Meter Size) --- A significant portion of the City's water CIP is for "Fire Flow Improvements." How will these costs be incorporated into your rate recommendation? Would it make sense to add a safety surcharge to every bill to cover the cost of Fire suppression and therefore lower the base charge? There are a number of ways of apportioning costs for fire flow

improvements that can evaluated. I am typically not a fan of trying to break out such costs and separately reallocating, but that is always a possibility.

1.Does the Glendale decision affect this? I am of the understanding that there has not yet been any court decision but we can incorporate any new legal requirements as they are known.

C. We recognize that this is questionable but charges for fire suppression are something that the community might find appealing and could more readily support. Instead of trying to break out a small component of the charge for fire suppression (or any other factor) in the rates, the issue of fire suppression could be discussed as one of the factors impacting rates.

W-III. Expenses – Answer - Casares

A. What are the estimated electricity charges for the new advanced treatment/ RO for the new plant? Based on the anticipated, selected proposer, the estimated electrical cost is $190,000 or $16,000 per month (first year of operation in 2022 presented in 2018 dollars).
B. Is it possible to project savings from the solar lease back program that Mr. Livick has been referring to? If so can the calculated savings be used to lower the new plant's O&M costs that will be used to calculate the new rates? We do anticipate potential cost savings from debt forgiveness through the SWRCB SRF Green Water Reclamation debt forgiveness and through savings in energy costs. Unfortunately, it is too early in the process to identify the costs at this point and use those savings in the rate analysis.

W-IV. State Water – Answer - Callaway

A. Who is going to determine the base year for the pass-through charges from DWR and the O&M costs from the CCWA? State Water costs are based on the latest year with data available with an inflation of 5% for O&M costs annually.
B. What is the exact date of the last bond payment to the CCWA for the Chorro Valley Turnout? June 1, 2021 (last debt service payment is for FY 2021/2022 and the payment is made on June 1st).

W-V. Specific Capital Projects – Answer - Casares

A. Nutmeg Water Tank

1. The replacement should not take place until

i. The land can be purchased and annexed into the City or

ii. A new lease for the land the tank will occupy is signed and at a minimum the new lease should be as long as the useful life of the tank.

Capital cost of the tank should be accrued over a three-year period in anticipation of the community objections and permitting delays. Noted. The Nutmeg Tank project will be pushed-out in the CIP in order to provide sufficient time for these activities to occur.

SEWER

S-I. Revenue – Answer - Handlers

A. Impact Fees-Fee projection should match the Community Development Departments projections to buildout. BWA recommends using conservative growth projections for financial planning and rate setting, particularly since the City's creditworthiness will be a key component for securing financing.

S-II. Expenses – Answer - Mueller/Livick

A. What are the existing electric fees for the existing plant? Current plant electric expenses to date for FY 17/18 average approximately $12,600 per month.

B. Also, see Water Re: Solar lease back. **(W-II. B and B-1.)** We do anticipate potential cost savings from debt forgiveness through the SWRCB SRF Green Water Reclamation debt forgiveness and through savings in energy costs. Unfortunately, it is too early in the process to identify the costs at this point and use those savings in the rate analysis.

S-III. General – Answer - Casares

A. Cayucos

Has anyone talked to Rick Koons or Robert Enns recently to try and pin them down on the quarter and year they anticipate processing their own waste water? I have spoken to my contacts at WSC (SLO Engineering Firm that is working with the Cayucos) and are indicating that the plant should go online in 2020. They are not providing any additional information regarding timing at this time.

S-IV. Existing Plant – Answer - Mueller/Livick

A. Are there any major maintenance and/or major repairs that are beyond normal O&M expenses planned for the Atascadero Road plant between now and

the time the new plant comes on line? No, short of any unforeseen failures, the current operations philosophy of the existing plant is normal routine maintenance and repairs not major rebuilds and/or replacements.

B. Decommissioning and Demolition of the existing plant

1. Consideration should be given to deferring this expense until the second five years. For several reasons:

i. Resolving the issue with the Cayucos Sanitary District on the division of expenses might be contentious and possibly involve litigation.

ii. The City's new General Plan appears to have designated the site the current plant sits on as recreation/open space, therefore waiting a couple of years to demo the plant will not have an adverse effect on any potential new City revenue. Also, in all likelihood the Coastal Commission will not allow any permanent structure built on the site.

Per previous discussion, the City has attractive pricing from the Design Build (DB) proposers for the decommissioning and demolition of the site. Staff believes it is prudent include it as part of the project and use low-interest financing for this aspect of the work. It may be beneficial to remove this from the DB team's scope and bid the work to a local contractor, but still keep it under the program.

APPENDIX B

Blue Ribbon Commission Questions and Answers

Submitted June 18, 2018

Questions to and Answers from Alex Handlers, Rate Advisor:

1. Will Table 2 be modified to show a 5% WRF contingency in the amount of $3,445,000 on a separate line described as "unanticipated change orders / scope changes" or some other appropriate description?

We have modified the costs based on removal of the demolition from the project and other modifications. The total project cost estimate is now approximately $126M. I have performed a detailed cost accounting to more accurately determine project soft costs (i.e., construction management, program management, design, permitting, etc.) and the remaining project costs are $121M (expenditures starting FY 18/19 through FY 21/22). This will be the number used to determine rates ($121M).

2. Can Table 9 be modified to show only sewer-related items, similar to Table 11, but with all of the detail of Table 9? During our last meeting we asked about the potential of reducing Pay-Go CIP and were told that it had to be $1,350,000 because of the 1.25 coverage ratio. But if Table 9 is constructed with only sewer-related items, the coverage would be less than $1 million. Using the figures from Table 11, it appears that the revenue requirement could be reduced by about $400,000, which would leave about $1 million annually for Pay-Go capital.

Yes...already done.

3. Will you be presenting a similar table for water? Table 15 lacks the detail that Table 9 contains.

Yes...already done. I looked back at the pdf and see that I somehow missed including the Water Cash Flow Projections in the prior pdf that I had circulated.

4. Table 15 water cost allocation includes the O&M cost for advanced treatment & recycling from Table 14. Since that is a variable operating cost, why is it being included in the WRF capital cost recovery rate calculation? Should that cost be covered by the existing water volume charges, especially considering that operation won't begin for several years?

It is not...the prior Table 15 had only indicated the water utility's funding allocations related to the WRF and future water recycling.

5. Table 15 shows a 70/30 split between residential and commercial customers. What is the source of this split? Does the City have a more precise split based on their utility billing history?

Yes...that was my preliminary estimate for purposes of determining a proportionate allocation of cost-recovery between residential and commercial/non-residential accounts. I have since acquired data for the past 2+ years and have modified the allocation based on usage over the most recent 12-month period.

6. Table 15 calculates an SFR monthly rate of $23.97 in base year 2022/23, the first full year of debt service payments. What is the nexus between that calculated figure and your recommendation of $25? Is it simply rounding up?

I think that may have been the case in the prior draft you are referring to.

7. Table 15 calculates a water volume charge for commercial customers to recover the water portion of the WRF debt service. Since they already pay a water volume charge per the City's increasing block rate structure, how will this be incorporated and shown on the water bill? As an alternative, what form would a fixed charge take?

This could be treated as a separate line item. Due to the non-homogeneity of commercial accounts, I would generally recommend a volumetric charge for commercial. I would be happy to discuss in more detail.

Questions to and Answers from Eric Casares, Program Manager:

8. Could you provide the coverage ratio requirements for WIFIA and SRF?

Answer not available

9. Do you have any additional information about the feasibility of locating more pipelines in Quintana Road?

We do not have any additional information at this time regarding the potential for routing additional utilities in Quintana. At this time, we believe the best approach is to assume the separate routing of the purified (i.e., IPR) water line.

10. Will you and Alex be providing a rate analysis for bond financing of the WRF without the recycling portion?

Yes. We have a separate cost estimate for the non-IPR project. The total project cost is $105M with $100M left in the program (i.e., $100M is what will go into the rate study).

11. Will demolition of the existing WWTP be removed from the project costs?

Yes, this component of the project has been removed. The recommendation is to keep it as a bid "add alternate" and only have the work done by the design-build contractor if budget permits.

12. Will the WRF use recycled water as process water? Or will potable water be required?

The WRF will use recycled water for process water, but will still require potable water for drinking, fire protection, locker room facilities.

Questions to and Answers from Jennifer Callaway, City Finance Director:

13. Could you send a copy of the CCWA contract provision re: the SWP coverage ratio requirement? What is the denominator of that calculation? Is it the full amount of annual payments to CCWA or some portion thereof?

Attached is the Official Statement from CCWA's most recent Bond refunding. Beginning at the bottom of page ii, under the heading "Rate Covenants", it reads:

"Each San Luis Obispo Purvey or Purchaser has agreed to fix, prescribe and collect rates and charges in connection with its water system which will be at least sufficient to yield each fiscal year net water system revenues equal to 125% of the sum of the Contract Payments required to be made by it in such fiscal year pursuant to its Local Water Treatment Agreement plus debt service with respect to such fiscal year on obligations which are secured by a pledge of a lien on the San Luis Obispo Purveyor Purchaser's net water system revenues and which are on a parity with the obligations of the San Luis Obispo Purveyor Purchaser under the Local Water Treatment Agreement. See "SECURITY FOR THE BONDS Rate Coverage Reserve Fund" below for information with respect to amounts deposited by certain San Luis Obispo Purveyor Purchaser's with the Authority which may be counted as water system revenues for purposes of computing such coverage."

Will keep looking but this is all I can find at this point.

The coverage ratio is the net revenues over expenditures divided by the state water contract amount. The state water contract payment is the denominator. For example, in FY 2016/17 the water fund had revenues over expenditures of $3,743,043 which was divided by the state water payment of $2,010,166 for a coverage ratio of 1.86

14. Will you consider reducing the projected 5% annual increase to SWP expense considering that the bond payment decreased in FY 17/18 from $745K to $666K and other SWP costs are not increasing that fast?

This is referring to the 2015 rate study and again, Alex maybe something we can work through as you do the water study tomorrow. Our FY 2018/19 budget reflects lower

SWP projections and I would be comfortable figuring out a happy medium with Alex Handlers to keep forecasts reasonable in the out years.

15. The final CCWA bond payment is forecast for FY 21/22. Does CCWA hold any reserve against the final payment or is the full amount due from the City?

I am not aware of a reserve and contacted CCWA staff to confirm. The Deputy Controller is also not aware of any. She will confirm this understanding with the Controller upon her return to the office tomorrow.

16. Table 9 includes an interest earnings rate of 1.5% through FY 21/22 and 2% thereafter. Considering that LAIF's current daily rate is already 1.83%, would you consider increasing the forecast? Could you research the Federal Reserve forecast and use that?

Really more of an Alex Handlers question. Given that the Feds are raising rates on a regular basis now I am ok with increasing the projections slightly. The feds are stating that the rates will rise to 2.1% by the end of the year and 2.9% by the end of 2019, 3.4% by end of 2020 – 2.9% long-run. Alex, would you be comfortable increasing interest rates to 2.5% in 2019/20 through 21/22 and 2.9% thereafter?

Questions to and Answers from Scott Collins:

17. How will the City utilize the recycled water when it becomes available and until 2038 when the SWP contract expires?

The City currently relies on groundwater for about 15% (~150 acre-feet/year) of its supply annually. The purified water will be discharged to the Morro sub basin to eliminate/reduce nitrate contamination and augment supply when either State Water is down for maintenance or when the City's peak demands exceeds State Water's capacity.

City of Morro Bay

Financial Plan & Rate Analysis for a New Water Reclamation Facility

Draft 06/26/18

BARTLE WELLS ASSOCIATES
INDEPENDENT PUBLIC FINANCE ADVISORS

Table of Contents

City of Morro Bay
Financial Plan & Rate Analysis for a
New Water Reclamation Facility

1. Background

The City of Morro Bay is located on the Central California coast in San Luis Obispo County, about 12 miles northwest of the City of San Luis Obispo. The City has a population of approximately 10,500. The City provides water and wastewater service to residents and businesses within the City.

The City's existing wastewater treatment plant has reached the end of its useful life and needs to be rebuilt due to a number of factors including age and condition, as well as capacity and regulatory deficiencies. The existing plant was originally built in 1953 and last underwent major upgrades in 1984. The existing plant does not meet current wastewater discharge permit requirements and needs to be rebuilt to comply with the City's new Waste Discharge Permit requirement within a maximum of five years, as required by the Central Coast Regional Water Quality Control Board (RWQCB). Failure to meet the RWQCB's permit requirements can result in substantial fines.

Adding to the City's challenges, the wastewater treatment plant cannot be rebuilt at its current location. The existing plant is located on the coast in a flood plain and tsunami inundation zone. In 2013, the California Coastal Commission denied the City's development permit to build a new treatment plant near the existing site. In 2015 the Commission issued Sea Level Rise Policy Guidance that strongly discourages siting facilities in areas where they could be adversely affected by the impacts of sea level rise over the full life of the structure. The current location is also inconsistent with other provisions of the Coastal Act and Local Coastal Program.

Based on evaluation of a wide range of project and site alternatives, the City is now moving forward with a new Water Reclamation Facility (WRF) at a proposed site near the intersection of South Bay Boulevard and Highway 1, approximately 1 mile east of downtown Morro Bay. In June 2018, pursuant to a competitive proposal process, the City selected a team to construct the new WRF via a design-build process. The City is currently undergoing negotiations with the selected design-build team.

The full WRF project includes a new wastewater treatment plant, pumping facilities, a pipeline to convey wastewater to the new WRF, and water recycling facilities for potable reuse. Water recycling facilities are included in the WRF project for a number of reasons including:

- The City predominantly relies on imported water from the State Water Project for the

community's water supply. Recycled water provides the City with a relatively drought-proof local supply that improves water supply security and reliability.

- While water recycling infrastructure adds significant cost to the WRF project, it also helps make the WRF project eligible and competitive for grants and low-interest-rate loans. Financial analysis indicates that the impact of the added costs of the recycled water facilities would be largely offset by the financial benefits of subsidized financing available with recycling.
- Water recycling was identified as a community goal for the new WRF.

2. Study Overview

Bartle Wells Associates (BWA) was retained to develop a financial plan and rate recommendations to support funding for the new WRF as well ongoing operating and capital improvement needs. This report presents findings and rate recommendations developed under a few financial scenarios. The proposed WRF Facility Surcharges were developed with input from City staff, Carollo Engineers, and the City's Blue Ribbon Commission -- a group of Morro Bay residents with substantial financial and business experience that was established to provide independent review and help evaluate the costs and potential rate increases needed to support the new WRF.

The City's water and sewer utilities are financially self-supporting enterprises funded primarily from monthly service charges. *In order to secure financing for the WRF, the City will need to first adopt utility rates adequate to repay debt service for the new WRF.*

BWA developed financial projections and rate recommendations under four alternative scenarios.

A. **Base Case Scenario**: This scenario assumes the WRF project is funded by a combination of WIFIA financing, revenue bonds, and pay-as-you go cash funding from rates and fund reserves. Under this scenario, the City would levy the full WRF Facility Surcharges beginning fiscal year 2019/20.

B. **Phase-In Scenario**: This scenario is similar to the Base Case Scenario, but assumes the WRF Facility Surcharges would be phased in from fiscal year 2019/20 through 2021/22.

C. **SRF Financing Scenario:** This scenario assumes the City obtains low-rate SRF financing, instead of bonds, to supplement the anticipated WIFIA loan and cash funding.

D. **No Water Recycling Scenario:** This scenario eliminates the water recycling facilities resulting in a reduced-cost, wastewater-only WRF project, and also assumes no WIFIA financing with all project funding from bonds and pay-as-you-go cash contributions.

3. Prior Rate Increases & Need for WRF Surcharges

In 2015, the City adopted 5-years of water and sewer rate increases. The adopted rates were designed to phase in funding to support the cost of providing utility service and help provide funding for capital improvements to aging infrastructure. As of July 1, 2018, the City will have implemented 4 of the 5 years of adopted rate increases. Prior to these rate increases, the City had not adopted any water rate increases in 20 years but had periodically adopted some sewer rate adjustments.

The previously-adopted sewer rates were also designed to help support funding for a new wastewater treatment plant assuming Morro Bay would need to fund approximately $56 million of project costs, equal to 75% of an estimated $75 million wastewater treatment plant that would be jointly owned with Cayucos funding the remaining 25%. The $75 million preliminary cost estimate from 2015 was based on a conceptual design and parametric estimates.

In addition, the adopted rates were not designed to fund recycled water facilities, which were previously expected to be a future phase of the project. The adopted sewer rates also assumed the City would be able to obtain low-rate financing from the State Revolving Fund (SRF) for all debt financing needs of the new treatment plant. SRF financing was previously fairly easy to obtain but is now substantially more difficult to secure.

The adopted rates substantially strengthened the financial condition of the City's water and sewer utilities but do not provide adequate funding to support each utility's share of costs for the new WRF. Additional water and sewer charges are needed to provide adequate funding for each utility's share of debt service for the WRF project.

BWA recommends the City adopt new water and sewer WRF Facility Surcharges to supplement the previously-adopted rates in order to provide adequate funding for WRF-related debt repayment. These would be separate surcharges levied in addition to the City's adopted utility rates.

4. Summary of Proposed WRF Facility Surcharges

Table 1 shows proposed WRF Facility Surcharges for single family residential customers under the four financial scenarios. Note that the surcharges shown under the Phase-In Scenario are maximum surcharges with full phase-in starting 2022/23. Surcharges for residential customers are structured as fixed monthly charges. Surcharges for all customer classes are detailed later in this report.

Table 1 – Summary of Maximum Single Family Residential WRF Facility Surcharges

	Base Case	Phase-In	WIFIA & SRF	No Recycling*
	WRF+Recycling WIFIA+Bonds	Base Case with Rate Phase In	WRF+Recycling WIFIA+SRF	No Recycling All Bonds
WRF Facility Surcharges				
Sewer WRF Facility Surcharge	$25.00	$27.00	$20.00	$44.00
Water WRF Facility Surcharge	16.00	17.00	14.00	-
Total	**41.00**	**44.00**	**34.00**	**44.00***

* Under the No Recycling Scenario, the fifth and final year of the previously-adopted water rate increases would not need to be implemented, resulting in a $4.50 reduction in the monthly water bill for a typical single family home using 5 units of water per month compared to other scenarios. This results in a net reduction of $1.50 per month compared to the Base Case Scenario.

5. Key Alternative for Implementing & Billing WRF Facility Surcharges

The City has options for implementing and billing the proposed WRF Facility Surcharge as discussed below.

Timing of Surcharge Implementation

At this stage, the City is considering two approaches regarding the timing of implementing the WRF Facility Surcharges, including:

- **Front-Load** - Levy the full WRF Facility Surcharges starting fiscal year 2019/20 (Base Case Scenario)
- **Phase-In** - Phase-in the WRF Facility Surcharges in upcoming years (Phase-In Scenario)

The Phase-In Scenario results in a lower level of surcharge revenues than the front-loaded Base Case Scenario until the surcharges are fully phased-in. The Phase-In Scenario results in approximately $4.3 million less of pay-as-you-go cash funding which results in the need for a corresponding increase in debt financing, higher annual debt service, and ultimately a higher surcharge.

Method of Bill Collection

The City currently bills customers monthly via a combined utility bill for water and sewer service. The City is considering two methods of bill collection for recovering the WRF Facility Surcharges, including:

- **Monthly Billing** - Add the WRF Facility Surcharges as a new line-item in the monthly bills.
- **Property Tax Rolls** - Recover the proposed WRF Facility Surcharges on the property tax rolls.

The WRF Facility Surcharges would be the same under both billing alternatives and in many cases would be paid by the same people; only the method of billing and collection would vary. Additional information regarding potential billing on the property tax rolls is included later in this report.

Community & Advisory Board/Committee Input Received

The City conducted a community workshop to discuss the WRF project and proposed rate surcharges on Saturday, June 23, 2018. During the workshop, community members were requested to provide their preferences regarding: a) either phasing in or front-loading the WRF Facility Surcharges, and b) billing the WRF Facility Surcharges as a separate line-item on the monthly utilities bill vs. submitting the surcharges for recovery via the property tax rolls. Community members who participated at the workshop were fairly evenly split regarding their preferences on both the potential phase-in and method of bill collection.

The same feedback was sought from members of the Public Works Advisory Board (PWAB), Water Reclamation Facility Citizens Advisory Committee (WRFCAC), and Citizens Finance Advisory Committee (CFAC) during a joint meeting between these three committees held on June 25, 2018. Advisory board and committee members slightly favored phasing in the surcharges and strongly favored including the surcharges on the monthly utilities bill, not on the property tax rolls.

6. Total Monthly Water & Sewer Charges with WRF Facility Surcharges

Tables 2A and 2B show the total combined monthly water and sewer charges – *including water and sewer service charges and the proposed WRF Facility Surcharges* – for a typical single family home using 5 units (hcf) of water use per month under the Base Case and Phase-In Scenarios. Under the Phase-In Scenario, pay-as-you-go cash funding for the WRF Project generated by the Surcharges would be reduced by approximately $4.3 million compared to the Base Case Scenario. This results in the need for a corresponding amount of additional debt financing which results in slightly higher debt service and a higher maximum surcharge.

Note that monthly single family residential use has averaged about 4.6 units (hcf) over the past year. BWA estimates that roughly 2/3rds of single family residential bills are at or below 5 hcf.

Table 2A – Base Case Scenario: Total Monthly Charges with WRF Surcharges

Typical Single Family Home with 5 Units (hcf) Monthly Water Use

	2018/19	2019/20	2020/21	2021/22	2022/23
Monthly Utility Bill					
Sewer Monthly Charge	$77.00	$83.00	$83.00	$83.00	$83.00
Water Monthly Charge	62.50	67.00	67.00	67.00	67.00
Subtotal Monthly Bill	139.50	150.00	150.00	150.00	150.00
WRF Facility Surcharges					
Sewer WRF Facility Surcharge	-	25.00	25.00	25.00	25.00
Water WRF Facility Surcharge	-	16.00	16.00	16.00	16.00
Subtotal Monthly Bill		41.00	41.00	41.00	41.00
Total Monthly Charges	**139.50**	**191.00**	**191.00**	**191.00**	**191.00**

Table 2B – Phase-In Scenario: Total Monthly Charges with WRF Surcharges

Typical Single Family Home with 5 Units (hcf) Monthly Water Use

	2018/19	2019/20	2020/21	2021/22	2022/23
Monthly Utility Bill					
Sewer Monthly Charge	$77.00	$83.00	$83.00	$83.00	$83.00
Water Monthly Charge	62.50	67.00	67.00	67.00	67.00
Subtotal Monthly Bill	139.50	150.00	150.00	150.00	150.00
WRF Facility Surcharges					
Sewer WRF Facility Surcharge	-	9.00	18.00	27.00	27.00
Water WRF Facility Surcharge	-	8.00	12.00	17.00	17.00
Subtotal Monthly Bill		17.00	30.00	44.00	44.00
Total Monthly Charges	**139.50**	**167.00**	**180.00**	**194.00**	**194.00**

7. WRF Project Costs & Timing

Table 3 shows projected WRF project capital and operating costs based on the winning design-build proposal received by the City (which is subject to final negotiation) and engineering cost estimates provided by Carollo Engineers. The WRF project is currently estimated to cost a total of $122.8 million including all expenses incurred to date.

Table 3 – WRF Project Cost Estimates

	Construction Costs[1]	Soft Costs	Project Reserves[2]	Total Cost
Projected Capital Costs				
Includes permitting, design, procurement, construction, and management.				
Water Reclamation Facility	$62,616,000	$8,489,000	$3,131,000	$74,236,000
Conveyance Facilities	21,086,000	2,820,000	2,343,000	26,249,000
Offsite Recycled Water Facilities[3]	8,592,000	2,648,000	859,000	12,099,000
General Program Implementation	0	5,160,000	0	5,160,000
Subtotal	92,294,000	19,117,000	6,333,000	117,744,000
Prior Project Expenditures	0	5,063,000		5,063,000
Total	92,294,000	24,180,000		122,807,000
Annual Operating & Maintenance Expenses				
Projected online starting January 1, 2022.		2018 Estimate	Cost Inflation	2022 Projection
WRF Wastewater Operations		$2,383,000	$299,000	$2,682,000
Conveyance to WRF		246,000	31,000	277,000
Recycled Water Operations		193,000	24,000	217,000

Source: Carollo Engineers, WRF Program Revised Cost Estimates as of 6/20/18.

1 Construction costs Include estimated cost inflation to construction mid-point where applicable.

2 Project Reserves are placeholder estimates for additional project funding requirements (e.g. outside project scope) with funding subject to City control.

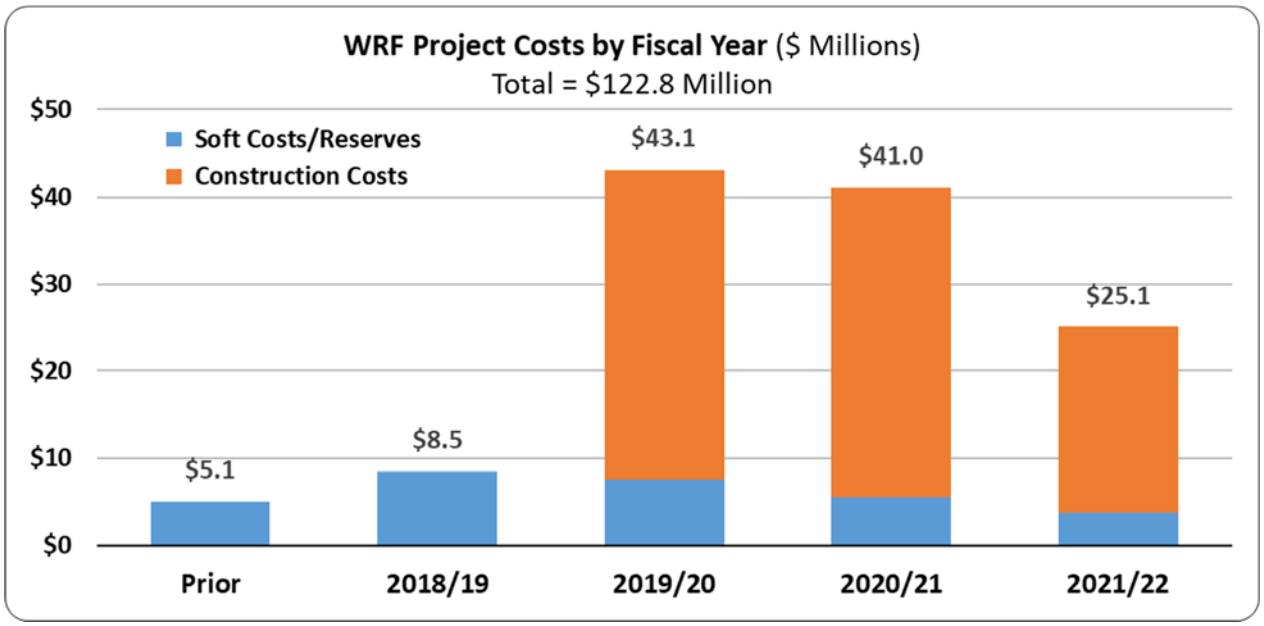
3 Offsite Recycled Water Facilities assume West alternative and include property acquisition estimate.

Without recycled water infrastructure, the total cost of project is reduced by approximately $20 million to an estimated total of $102.2 million. The reduction includes elimination of $12 million of Offsite Recycled Water Facilities, and an $8 million reduction in costs for the wastewater treatment plant. Tables detailing financial projections for a No Water Recycling Scenario are included in the appendix.

Table 4 shows projected WRF costs by fiscal year. The City estimates that a little over $5 million will have been spent by the end of fiscal year 2017/18, with future costs totaling about $117.7 million including estimated cost inflation to the projected mid-point of construction for each project component. The City anticipates incurring costs primarily for design in 2018/19, with construction occurring during the subsequent 3 fiscal years. The new wastewater treatment facility is targeted for completion by October 2021 with operations targeted to start January 2022.

Table 4 – Projected WRF Costs by Fiscal Year

	Prior Costs			Projected Costs			
	Prior	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
Soft Costs	2,800,000	1,423,000	840,000	8,490,000	5,218,000	3,160,000	2,248,000
Construction					35,512,000	35,512,000	21,271,000
Project Reserves					2,377,000	2,377,000	1,579,000
Annual Total	2,800,000	1,423,000	840,000	8,490,000	43,107,000	41,049,000	25,098,000
Subtotal			*5,063,000*				*117,744,000*
Total							*122,807,000*



8. Water vs. Wastewater Cost Allocation

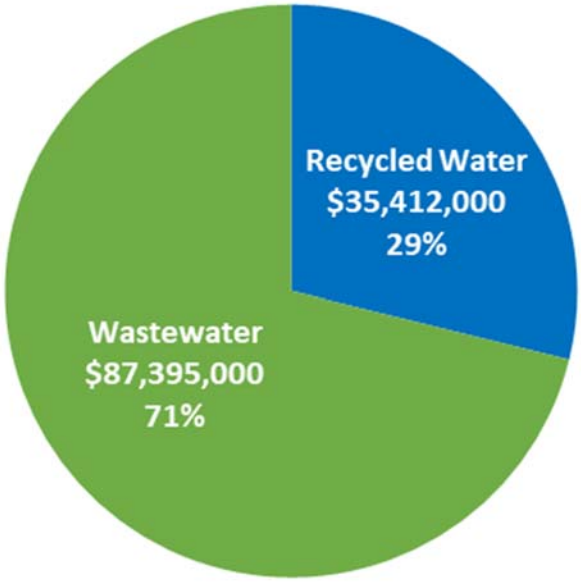
Tables 5 shows an allocation of WRF project costs to water vs. wastewater based on analysis developed by Carollo Engineers. Costs allocated to the water utility include all facility costs related to recycled water production that are in excess of the costs that would be incurred for constructing a new WRF for wastewater only. Each utility is responsible for funding its share of project costs.

Table 5 – WRF Project Cost Allocation to Water vs. Wastewater

Project Component	Total Cost	Water		Wastewater	
Water Reclamation Facility	$74,236,000	$21,528,000	29.0%	$52,708,000	71.0%
Conveyance Facilities	26,249,000	0	0.0%	26,249,000	100.0%
Offsite Recycled Wtr Facilities	12,099,000	12,099,000	100.0%	0	0.0%
General Program Implementation*	5,160,000	1,541,000	29.9%	3,619,000	70.1%
Prior Project Expenditures	5,063,000	244,000	4.8%	4,819,000	95.2%
Total	122,807,000	35,412,000	28.8%	87,395,000	71.2%

* Allocated based on proportionate share of total future facility costs.

Wastewater vs. Recycled Water Costs



9. WRF Project Funding Sources

The City anticipates funding the WRF project via a combination of long-term debt and pay-as-you-go cash funding provided by utility rates and available fund reserves. The Base Case Scenario assumes the City secures WIFIA funding for the maximum allowable 49% of the WRF project cost, with remaining funding provided by cash funding and revenue bonds. Table 6 and the chart below show a breakdown of anticipated funding sources for the WRF project under the Base Case Scenario. For comparison, the Phase-In Scenario results in $4.3 million of reduced cash funding for the WRF and a corresponding $4.3 million increase in Revenue Bond financing.

Table 6A – Base Case: WRF Project Funding Sources

	Total	% of Ttl	Water	% of Source	Wastewater	% of Source
WRF Total Project Costs	$122,807,000		$35,412,000	28.8%	87,395,000	71.2%
Projected Funding Sources						
WIFIA Loan	60,175,000	49.0%	17,352,000	28.8%	42,823,000	71.2%
SRF Planning Loan	10,300,000	8.4%	2,970,000	28.8%	7,330,000	71.2%
Revenue Bonds	24,700,000	20.1%	10,246,000	41.5%	14,454,000	58.5%
Sewer New Cash Funding	17,969,000	14.6%	0	0.0%	17,969,000	100.0%
Water New Cash Funding	4,600,000	3.7%	4,600,000	100.0%	0	0.0%
Prior Cash Contributions	5,063,000	4.1%	244,000	4.8%	4,819,000	95.2%
Total	122,807,000	100.0%	35,412,000	28.8%	87,395,000	71.2%

Base Case: WRF Project Funding Sources

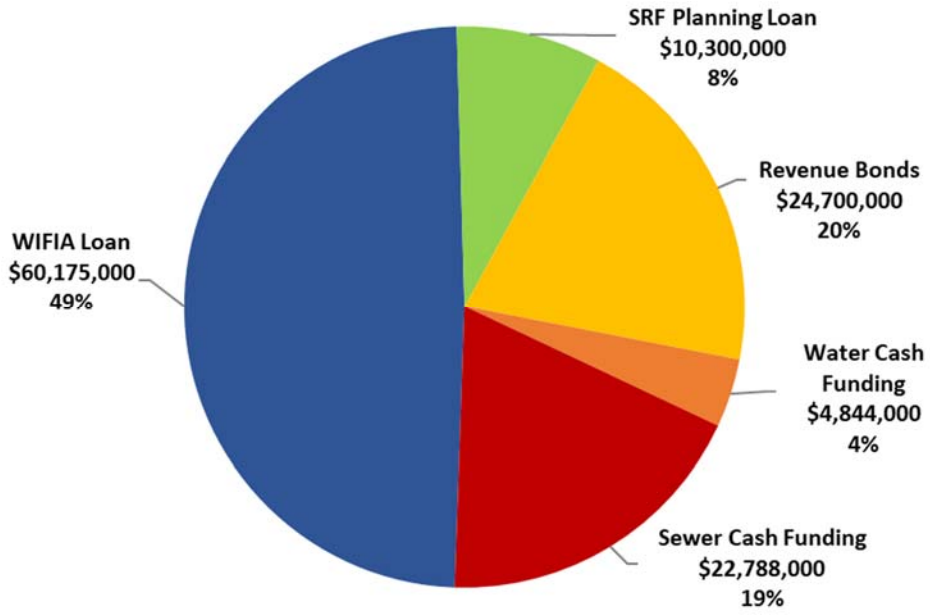


Table 7 shows a breakdown of anticipated funding sources for the WRF Project by fiscal year under the Base Case Scenario.

Table 7 – Base Case: WRF Funding Sources by Year

	Prior	2018/19	2019/20	2020/21	2021/22
WRF Project Costs	$5,063,000	$8,490,000	$43,107,000	$41,049,000	$25,098,000
WRF Funding Sources					
SRF Planning Loan		5,800,000	4,500,000		
WIFIA Loan			31,100,000	29,075,000	
Revenue Bonds				7,400,000	17,300,000
Sewer Cash Contribution	4,819,000	2,390,000	5,307,000	3,374,000	6,898,000
Water Cash Contribution	244,000	300,000	2,200,000	1,200,000	900,000
Total	5,063,000	8,490,000	43,107,000	41,049,000	25,098,000

The City has been pursuing state and federal grants and low-interest-rate loans to help finance the WRF project. The City has been successful in obtaining commitments for a substantial amount of low-interest-rate financing to date and continues to seek additional financial assistance. The City has retained Kestrel Consulting, a grant specialist, to assist in identifying and applying for grants and subsidized financing programs.

- The City was awarded a $10.3 million Planning Loan from California's Clean Water State Revolving Fund (SRF) Financing Program with a subsidized interest rate of 1.7%.
- Morro Bay was as one of 12 communities nationwide invited to apply for low-interest-rate financing from the Water Infrastructure and Financing Innovation Act (WIFIA) funding program administered by the United State Environmental Protection Agency (EPA). WIFIA financing can be used to fund up to 49% of the WRF project cost and has favorable repayment terms including low interest rates. The rate for a long-term WIFIA loan is currently in the 3% range but would not be formally set until final approval is obtained.
- The City was previously awarded a small Recycled Water Planning Feasibility Study Grant.
- The City is pursuing additional financing from Clean Water SRF Financing Program, which offers low-interest-rate loans – currently below 2% -- and repayment terms up to 30 years.
- The City has been pursuing grant financing from the United States Bureau of Reclamation.

Any additional grant or subsidized loan financing received would result in lower future debt service and could reduce annual funding needs from future water and sewer charges.

10.Debt Service Estimates

Tables 8A and 8B show debt service estimates under the Base Case and Phase-In Scenarios. Debt service is partially structured around the 10-year repayment term of the SRF Planning Loan to result in level annual future debt service. The debt service estimates for the anticipated WIFIA Loan and projected Revenue Bonds are based on slightly conservative assumptions of interest rates. Interest rates are currently lower but would be established when the WIFIA financing agreement is finalized and when Revenue Bonds are issued.

Table 8A – Base Case: Debt Service Estimates

	SRF Planning Loan	WIFIA Loan	Revenue Bonds	Total
Project Funding	$10,300,000	$60,175,000	$24,700,000	$95,175,000
Term	10 Years	35 Years	30 Years	All-In TIC
Avg Interest Rate	1.70%	3.25%	4.70%	3.48%
Debt Service				
Through 2029/30	$1,130,000	$2,973,000	$1,190,000	$5,293,000
After 2029/30	-	$3,422,000	$1,871,000	$5,293,000

The Phase-In Scenario generates less cash funding for the WRF Project which results in a corresponding increase in debt financing needs from revenue bonds and a resulting increase in debt financing and debt service.

Table 8B – Phase-In: Debt Service Estimates

	SRF Planning Loan	WIFIA Loan	Revenue Bonds	Total
Project Funding	$10,300,000	$60,175,000	$29,000,000	$99,475,000
Term	10 Years	35 Years	30 Years	All-In TIC
Avg Interest Rate	1.70%	3.25%	4.70%	3.51%
Debt Service				
Through 2029/30	$1,130,000	$3,051,000	$1,396,000	$5,577,000
After 2029/30	-	$3,383,000	$2,194,000	$5,577,000

11.Capital Improvement Plans

The City recently collaborated with Carollo Engineers to evaluate and prioritize capital improvement needs to the City's aging water and sewer infrastructure resulting in the development of updated Capital Improvement Plans (CIPs) for the water and sewer utilities. The CIP projects include replacement and rehabilitation of old water and sewer pipelines, water pump stations, sewer lift stations, and water storage tanks. The CIPs are designed to address the highest priority needs the soonest. The City plans to continue evaluating its capital improvement needs and may re-prioritize projects in future years.

Tables 9 and 10 summarize annual water and sewer CIP funding needs. The City plans to fund these improvements on a pay-as-you-go basis with no additional debt. A detailed list of CIP projects and costs is included in the appendix to this report. Note that costs are shown in current dollars.

Table 9 – Water Capital Improvement Plan Summary

	Near-Term Years 1 - 5	Mid-Term Years 6 - 10	Long-Term Through 2040
CIP Cost Estimates	$6,788,000	$4,977,000	$11,586,000
Average Annual Cost	1,357,600	995,400	965,500

Table 10 – Sewer Capital Improvement Plan Summary

	Near-Term Years 1 - 5	Mid-Term Years 6 - 10	Long-Term Through 2040
CIP Cost Estimates	$5,096,000	$5,726,000	$7,349,000
Average Annual Cost	1,019,200	1,145,200	612,417

12. Financial Projections

BWA developed 10-year water and sewer utility financial projections to evaluate annual revenue requirements and project rate increases under each of the four financial scenarios. The projections are based on reasonable and slightly conservative assumptions including:

- Operating expenses are based on the 2018/19 preliminary budget.
- Operating costs escalate at the annual rate of 4% per year for planning purposes.
- Future costs for a) wastewater treatment at the new WRF and b) wastewater conveyance to the new WRF, and c) recycled water operations are based on engineering estimates developed by Carollo Engineers and account for future cost inflation.
- The projections assume a low-growth scenario of 5 new single family homes or equivalents per year.
- Water and sewer service charge revenues assume monthly water use remains constant based on usage over the past fiscal year. Note that residential sewer rates and all WRF Facility Surcharges are fixed monthly charges that do not vary with changes in water use.
- Sewer financial projections assume that Cayucos Sanitary District funds 25% of the operating costs of the existing wastewater treatment plant for two more fiscal years – through 2019/20 – after which Cayucos anticipates transitioning to its own planned treatment facility. *Note: The reduction in wastewater flow from Cayucos SD is not projected to result in a significant decrease in operating costs. Most of the wastewater treatment plant's operating and maintenance costs are fixed costs (e.g. staffing) that do not vary with changes in wastewater flow.*
- The sewer cash flow projections show how the entire WRF Project is funded and include the full debt service payments which are offset by the debt service paid by the water utility.
- Water and sewer capital improvement plans are funded entirely on a pay-as-you-go basis from revenues generated each year by water and sewer service charges.
- The City has accrued some fund reserves that can eventually be applied toward the WRF Project and anticipates generating additional cash contributions for the project from future rates and WRF Facility Surcharges. BWA recommends the City maintain its water and sewer fund reserves while the WRF Project is being built. The City can draw down a portion of its water and sewer fund reserves during fiscal year 2021/11, the final year of construction. Over the longer-term, the cash flow projections assume the City would maintain at least $4 million in fund reserves for each utility.

Tables 11A and 12A show 10-year sewer cash flow projections and water cash flow projections under the Base Case Scenario. Tables 11B and 12B show financial projections under the Phase-In Scenario.

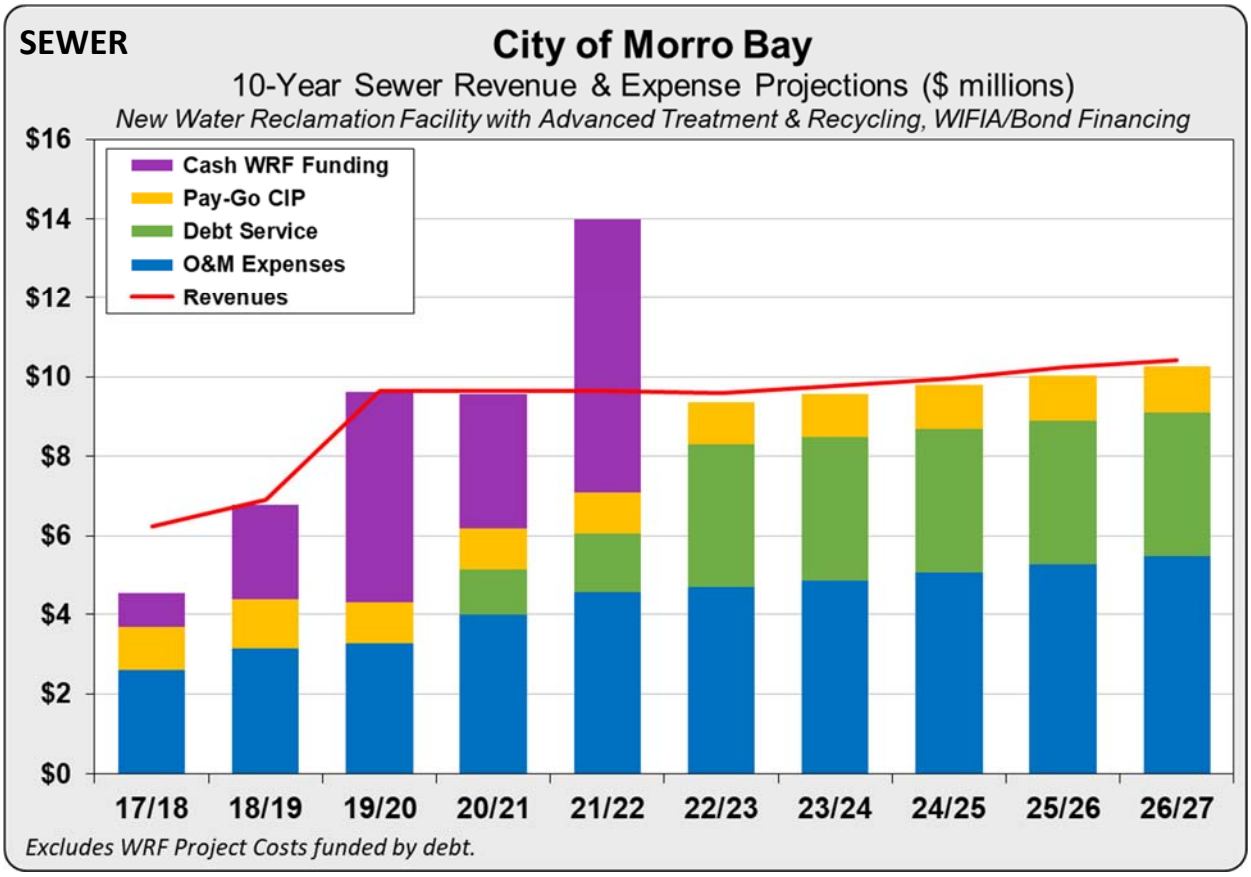
Table 11A - City of Morro Bay - Sewer Cash Flow Projections					Base Case Scenario
	Projected				
Years 1 - 5	2017/18	2018/19	2019/20	2020/21	2021/22
Monthly Single Family Sewer Charge	$70.00	$77.00	$83.00	$83.00	$83.00
Monthly Single Family Surcharge			$25.00	$25.00	$25.00
Beginning Sewer Accounts	5,346	5,351	5,356	5,361	5,366
Growth: Single Family Equivalents	5	5	5	5	5
Growth %	-	0.1%	0.1%	0.1%	0.1%
Sewer Development Impact Fee	$5,445	$5,550	$5,660	$5,770	$5,890
Interest Earnings Rate	1.25%	1.75%	2.0%	2.0%	2.0%
Cost Escalation			4.0%	4.0%	4.0%
Beginning Fund Reserves	$6,402,000	$8,112,000	$8,251,000	$8,274,000	$8,357,000
REVENUES					
Sewer Service Charges	6,100,000	6,716,000	7,246,000	7,253,000	7,260,000
Sewer WRF Facility Surcharges	0	0	2,173,000	2,173,000	2,173,000
Development Impact Fees	30,000	28,000	28,000	29,000	29,000
Interest Earnings	80,000	142,000	165,000	165,000	167,000
Rental Income/Other (Excl Penalties)	25,000	30,000	30,000	30,000	30,000
Subtotal	6,235,000	6,916,000	9,642,000	9,650,000	9,659,000
WRF Debt Financing					
SRF Planning Loan		5,800,000	4,500,000		
WIFIA Loan			31,100,000	29,075,000	
Bond Proceeds				7,400,000	17,300,000
EXPENSES					
Operating & Maintenance	Estimated	Projected			
Sewer Collection	1,100,000	1,480,000	1,539,000	1,601,000	1,665,000
Wastewater Treatment Existing	2,000,000	2,210,000	2,298,000	2,390,000	1,247,000
Wastewater Treatment New WRF	-	-	-	-	1,500,000
Conveyance to New WRF	-	-	-	-	140,000
Less Cayucos SD Reimbursements	*(495,000)*	*(553,000)*	*(575,000)*	*0*	*0*
Subtotal	2,605,000	3,137,000	3,262,000	3,991,000	4,552,000
Debt Service					
SRF Planning Loan	-	-	-	1,130,000	1,130,000
WIFIA Loan	-	-	-	-	-
Revenue Bonds (structured around SRF)	-	-	-	595,000	1,190,000
Less Water Share of WRF Debt	-	-	-	(573,000)	(820,000)
Subtotal	0	0	0	1,152,000	1,500,000
Capital Improvements					
Sewer Cash Contribution to WRF	840,000	2,390,000	5,307,000	3,374,000	6,898,000
Sewer System Pay-Go CIP	630,000	1,200,000	1,000,000	1,000,000	1,000,000
Vehicle/Equipment Replacement	450,000	50,000	50,000	50,000	50,000
Subtotal	1,920,000	3,640,000	6,357,000	4,424,000	7,948,000
Total Sewer Expenses	4,525,000	6,777,000	9,619,000	9,567,000	14,000,000
Revenues Less Expenses	1,710,000	139,000	23,000	83,000	(4,341,000)
Ending Fund Reserves	8,112,000	8,251,000	8,274,000	8,357,000	4,016,000
Debt Service Coverage	-	-	-	4.91	3.40

Table 11A - City of Morro Bay - Sewer Cash Flow Projections					Base Case Scenario
	Projected				
Years 6 - 10	2022/23	2023/24	2024/25	2025/26	2026/27
Monthly Residential Sewer Charge	$83.00	$85.00	$87.00	$90.00	$92.00
Monthly Single Family WRF Surcharge	$25.00	$25.00	$25.00	$25.00	$25.00
Beginning Sewer Accounts	5,371	5,376	5,381	5,386	5,391
Growth: Single Family Equivalents	5	5	5	5	5
Growth %	0.1%	0.1%	0.1%	0.1%	0.1%
Sewer Development Impact Fee	$6,010	$6,130	$6,250	$6,380	$6,510
Interest Earnings Rate	2.0%	2.0%	2.0%	2.0%	2.0%
Cost Escalation	4.0%	4.0%	4.0%	4.0%	4.0%
Beginning Fund Reserves	$4,016,000	$4,245,000	$4,445,000	$4,604,000	$4,802,000
REVENUES					
Sewer Service Charges	7,267,000	7,449,000	7,631,000	7,901,000	8,084,000
Sewer WRF Facility Surcharges	2,173,000	2,173,000	2,173,000	2,173,000	2,173,000
Development Impact Fees	30,000	31,000	31,000	32,000	33,000
Interest Earnings	86,000	91,000	95,000	98,000	102,000
Rental Income/Penalties/Other	30,000	30,000	30,000	30,000	30,000
Subtotal	9,586,000	9,774,000	9,960,000	10,234,000	10,422,000
WRF Debt Financing					
SRF Planning Loan					
WIFIA Financing					
Bond Financing					
EXPENSES					
Operating & Maintenance					
Sewer Collection	1,732,000	1,801,000	1,873,000	1,948,000	2,026,000
Wastewater Treatment Existing	0	0	0	0	0
Wastewater Treatment New WRF	2,682,000	2,789,000	2,901,000	3,017,000	3,138,000
Conveyance to New WRF	277,000	288,000	300,000	312,000	324,000
Less Cayucos SD Reimbursements	*0*	*0*	*0*	*0*	*0*
Subtotal	4,691,000	4,878,000	5,074,000	5,277,000	5,488,000
Debt Service					
SRF Planning Loan	1,130,000	1,130,000	1,130,000	1,130,000	1,130,000
WIFIA Financing	2,973,000	2,973,000	2,973,000	2,973,000	2,973,000
Revenue Bonds (structured around SRF)	1,190,000	1,190,000	1,190,000	1,190,000	1,190,000
Less Water Share of WRF Debt	(1,677,000)	(1,677,000)	(1,677,000)	(1,677,000)	(1,677,000)
Subtotal	3,616,000	3,616,000	3,616,000	3,616,000	3,616,000
Capital Improvements					
Sewer Cash Contribution to WRF	0	0	0	0	0
Sewer System Pay-Go CIP	1,000,000	1,030,000	1,061,000	1,093,000	1,126,000
Vehicle/Equipment Replacement	50,000	50,000	50,000	50,000	50,000
Subtotal	1,050,000	1,080,000	1,111,000	1,143,000	1,176,000
Total Expenses	9,357,000	9,574,000	9,801,000	10,036,000	10,280,000
Revenues Less Expenses	229,000	200,000	159,000	198,000	142,000
Ending Fund Reserves	4,245,000	4,445,000	4,604,000	4,802,000	4,944,000
Debt Service Coverage	1.35	1.35	1.35	1.37	1.36

Table 12A - City of Morro Bay - Water Cash Flow Projections					Base Case Scenario
	Projected				
Years 1 - 5	2017/18	2018/19	2019/20	2020/21	2021/22
Fixed Monthly Water Charge	$28.00	$30.00	$32.00	$32.00	$32.00
Fixed Monthly Single Family WRF Surcharge			$16.00	$16.00	$16.00
Water Rate Adjustment %		7.1%	6.7%	0.0%	0.0%
Growth: Single Family Equivalents	5	5	5	5	5
Growth %	0.1%	0.1%	0.1%	0.1%	0.1%
Change in Water Sales		0.0%	0.0%	0.0%	0.0%
Water Development Impact Fee	$5,392	$5,500	$5,610	$5,720	$5,830
Interest Earnings Rate	1.25%	1.75%	2.0%	2.0%	2.0%
State Water Project Cost Escalation			4.0%	4.0%	4.0%
Operating Cost Escalation			4.0%	4.0%	4.0%
Beginning Fund Reserves	$3,132,000	$4,456,000	$4,537,000	$4,622,000	$4,687,000
REVENUES	Estimated	Projected			
Water Service Charges	5,280,000	5,700,000	6,086,000	6,092,000	6,098,000
Water WRF Facility Surcharges	0	0	1,654,000	1,654,000	1,654,000
Development Impact Fees	30,000	28,000	28,000	29,000	29,000
Interest Earnings	39,000	78,000	91,000	92,000	94,000
Other (Excludes Penalties)	16,000	20,000	20,000	20,000	20,000
Subtotal	5,365,000	5,826,000	7,879,000	7,887,000	7,895,000
EXPENSES					
Operating & Maintenance	Estimated	Projected			
Water System Operations	1,591,000	2,130,000	2,215,000	2,304,000	2,396,000
State Water Project Payments	1,535,000	1,595,000	1,659,000	1,725,000	1,794,000
Share of CCWA 2016 Bonds (Thru Oct-2021)	665,000	670,000	670,000	670,000	670,000
Recycled Water Operations	-	-	-	-	110,000
Subtotal	3,791,000	4,395,000	4,544,000	4,699,000	4,970,000
Debt Service					
SRF Planning Loan: Water Share	-	-	-	326,000	326,000
WRF WIFIA Loan: Water Share	-	-	-	-	-
WRF Revenue Bonds: Water Share	-	-	-	247,000	494,000
Subtotal	0	0	0	573,000	820,000
Capital Improvements					
Water System Pay-Go CIP	250,000	1,000,000	1,000,000	1,300,000	1,800,000
Water Cash Contribution to WRF	0	300,000	2,200,000	1,200,000	900,000
Vehicle/Equipment Replacement	0	50,000	50,000	50,000	50,000
Subtotal	250,000	1,350,000	3,250,000	2,550,000	2,750,000
Total Expenses	4,041,000	5,745,000	7,794,000	7,822,000	8,540,000
Revenues Less Expenses	1,324,000	81,000	85,000	65,000	(645,000)
Ending Fund Reserves	4,456,000	4,537,000	4,622,000	4,687,000	4,042,000
CCWA Bond Debt Service Coverage	1.72	1.63	2.43	2.33	2.19
City Debt Service Coverage	-	-	-	5.56	3.57

Table 12A - City of Morro Bay - Water Cash Flow Projections					Base Case Scenario
	Projected				
Years 6 - 10	2022/23	2023/24	2024/25	2025/26	2026/27
Fixed Monthly Residential Water Charge	$32.00	$32.00	$32.00	$33.00	$34.00
Fixed Monthly Single Family WRF Surchar	$16.00	$16.00	$16.00	$16.00	$16.00
Water Rate Adjustment %	0.0%	0.0%	0.0%	3.1%	3.0%
Growth: Single Family Equivalents	5	5	5	5	5
Growth %	0.1%	0.1%	0.1%	0.1%	0.1%
Change in Water Sales	0.0%	0.0%	0.0%	0.0%	0.0%
Water Development Impact Fee	$5,950	$6,070	$6,190	$6,310	$6,440
Interest Earnings Rate	2.0%	2.0%	2.0%	2.0%	2.0%
State Water Project Cost Escalation	4.0%	4.0%	4.0%	4.0%	4.0%
Operating Cost Escalation	4.0%	4.0%	4.0%	4.0%	4.0%
Beginning Fund Reserves	$4,042,000	$4,031,000	$4,442,000	$4,647,000	$4,825,000
REVENUES					
Water Service Charges	6,104,000	6,110,000	6,116,000	6,313,000	6,510,000
Water WRF Facility Surcharges	1,654,000	1,654,000	1,654,000	1,654,000	1,654,000
Development Impact Fees	30,000	30,000	31,000	32,000	32,000
Interest Earnings	86,000	86,000	94,000	99,000	102,000
Other (Excludes Penalties)	20,000	20,000	20,000	20,000	20,000
Subtotal	7,894,000	7,900,000	7,915,000	8,118,000	8,318,000
EXPENSES					
Operating & Maintenance					
Water System Personnel	2,492,000	2,592,000	2,696,000	2,804,000	2,916,000
State Water Project Payments	1,866,000	1,941,000	2,019,000	2,100,000	2,184,000
Share of CCWA 2016 Bonds (Thru Oct-2021)	0	0	0	0	0
Recycled Water Operations	220,000	229,000	238,000	248,000	258,000
Subtotal	4,578,000	4,762,000	4,953,000	5,152,000	5,358,000
Debt Service					
SRF Planning Loan: Water Share	326,000	326,000	326,000	326,000	326,000
WRF WIFIA Loan: Water Share	857,000	857,000	857,000	857,000	857,000
WRF Revenue Bonds: Water Share	494,000	494,000	494,000	494,000	494,000
Subtotal	1,677,000	1,677,000	1,677,000	1,677,000	1,677,000
Capital Improvements					
Water System Pay-Go CIP	1,600,000	1,000,000	1,030,000	1,061,000	1,093,000
Water Cash Contribution to WRF	0	0	0	0	0
Vehicle/Equipment Replacement	50,000	50,000	50,000	50,000	50,000
Subtotal	1,650,000	1,050,000	1,080,000	1,111,000	1,143,000
Total Expenses	7,905,000	7,489,000	7,710,000	7,940,000	8,178,000
Revenues Less Expenses	(11,000)	411,000	205,000	178,000	140,000
Ending Fund Reserves	4,031,000	4,442,000	4,647,000	4,825,000	4,965,000
CCWA Bond Debt Service Coverage	-	-	-	-	-
Debt Service Coverage	1.98	1.87	1.77	1.77	1.77

Base Case Scenario



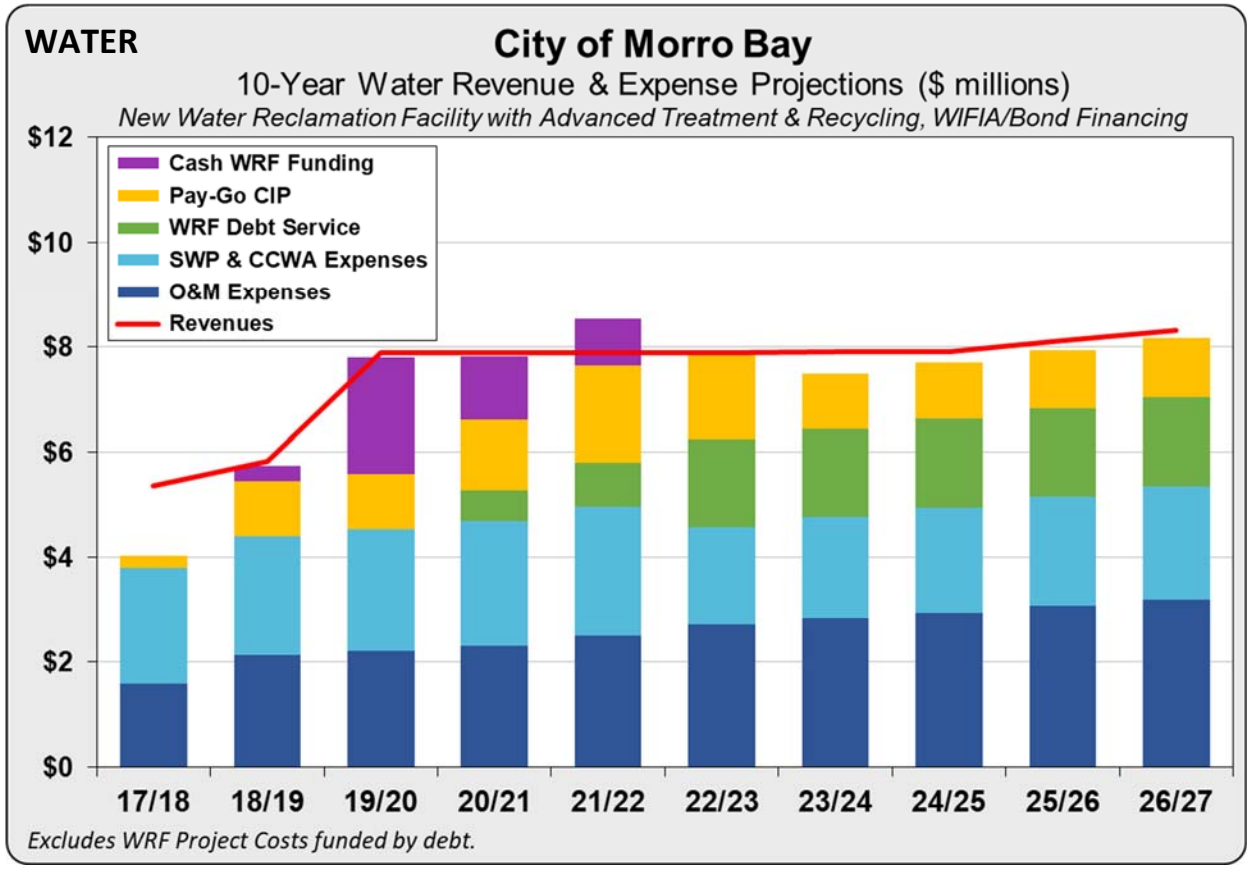


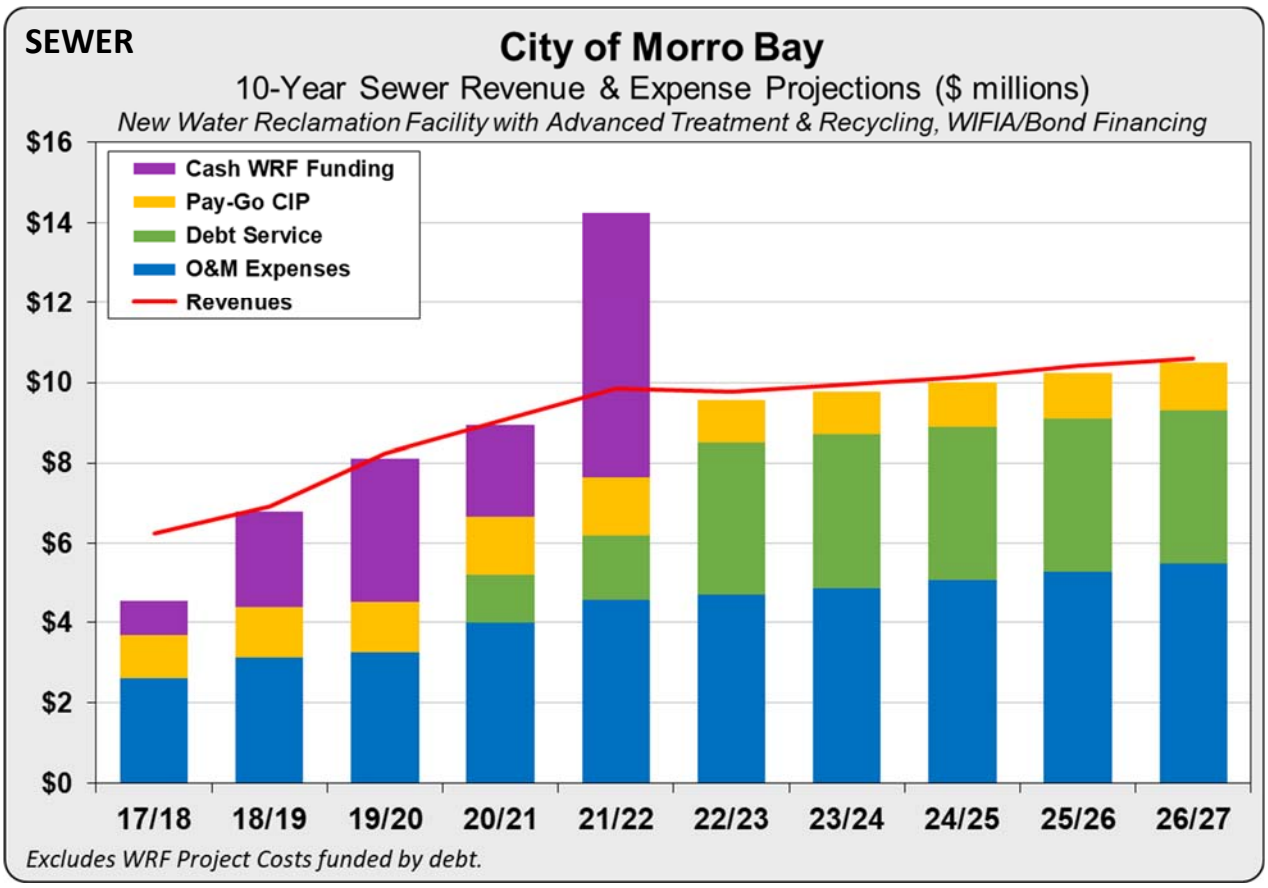
Table 11B - City of Morro Bay - Sewer Cash Flow Projections					Phase-In Scenario
	Projected				
Years 1 - 5	2017/18	2018/19	2019/20	2020/21	2021/22
Monthly Single Family Sewer Charge	$70.00	$77.00	$83.00	$83.00	$83.00
Monthly Single Family Surcharge			$9.00	$18.00	$27.00
Beginning Sewer Accounts	5,346	5,351	5,356	5,361	5,366
Growth: Single Family Equivalents	5	5	5	5	5
Growth %	-	0.1%	0.1%	0.1%	0.1%
Sewer Development Impact Fee	$5,445	$5,550	$5,660	$5,770	$5,890
Interest Earnings Rate	1.25%	1.75%	2.0%	2.0%	2.0%
Cost Escalation			4.0%	4.0%	4.0%
Beginning Fund Reserves	$6,402,000	$8,112,000	$8,251,000	$8,379,000	$8,480,000
REVENUES					
Sewer Service Charges	6,100,000	6,716,000	7,246,000	7,253,000	7,260,000
Sewer WRF Facility Surcharges	0	0	778,000	1,563,000	2,347,000
Development Impact Fees	30,000	28,000	28,000	29,000	29,000
Interest Earnings	80,000	142,000	165,000	168,000	170,000
Rental Income/Other (Excl Penalties)	25,000	30,000	30,000	30,000	30,000
Subtotal	6,235,000	6,916,000	8,247,000	9,043,000	9,836,000
WRF Debt Financing					
SRF Planning Loan		5,900,000	4,400,000		
WIFIA Loan			33,800,000	26,375,000	
Bond Proceeds				11,700,000	17,300,000
EXPENSES					
Operating & Maintenance	Estimated	Projected			
Sewer Collection	1,100,000	1,480,000	1,539,000	1,601,000	1,665,000
Wastewater Treatment Existing	2,000,000	2,210,000	2,298,000	2,390,000	1,247,000
Wastewater Treatment New WRF	-	-	-	-	1,500,000
Conveyance to New WRF	-	-	-	-	140,000
Less Cayucos SD Reimbursements	*(495,000)*	*(553,000)*	*(575,000)*	*0*	*0*
Subtotal	2,605,000	3,137,000	3,262,000	3,991,000	4,552,000
Debt Service					
SRF Planning Loan	-	-	-	1,130,000	1,130,000
WIFIA Loan	-	-	-	-	-
Revenue Bonds (structured around SRF)	-	-	-	698,000	1,396,000
Less Water Share of WRF Debt	-	-	-	(601,000)	(877,000)
Subtotal	0	0	0	1,227,000	1,649,000
Capital Improvements					
Sewer Cash Contribution to WRF	840,000	2,390,000	3,607,000	2,274,000	6,598,000
Sewer System Pay-Go CIP	630,000	1,200,000	1,200,000	1,400,000	1,400,000
Vehicle/Equipment Replacement	450,000	50,000	50,000	50,000	50,000
Subtotal	1,920,000	3,640,000	4,857,000	3,724,000	8,048,000
Total Sewer Expenses	4,525,000	6,777,000	8,119,000	8,942,000	14,249,000
Revenues Less Expenses	1,710,000	139,000	128,000	101,000	(4,413,000)
Ending Fund Reserves	8,112,000	8,251,000	8,379,000	8,480,000	4,067,000
Debt Service Coverage	-	-	-	4.12	3.20

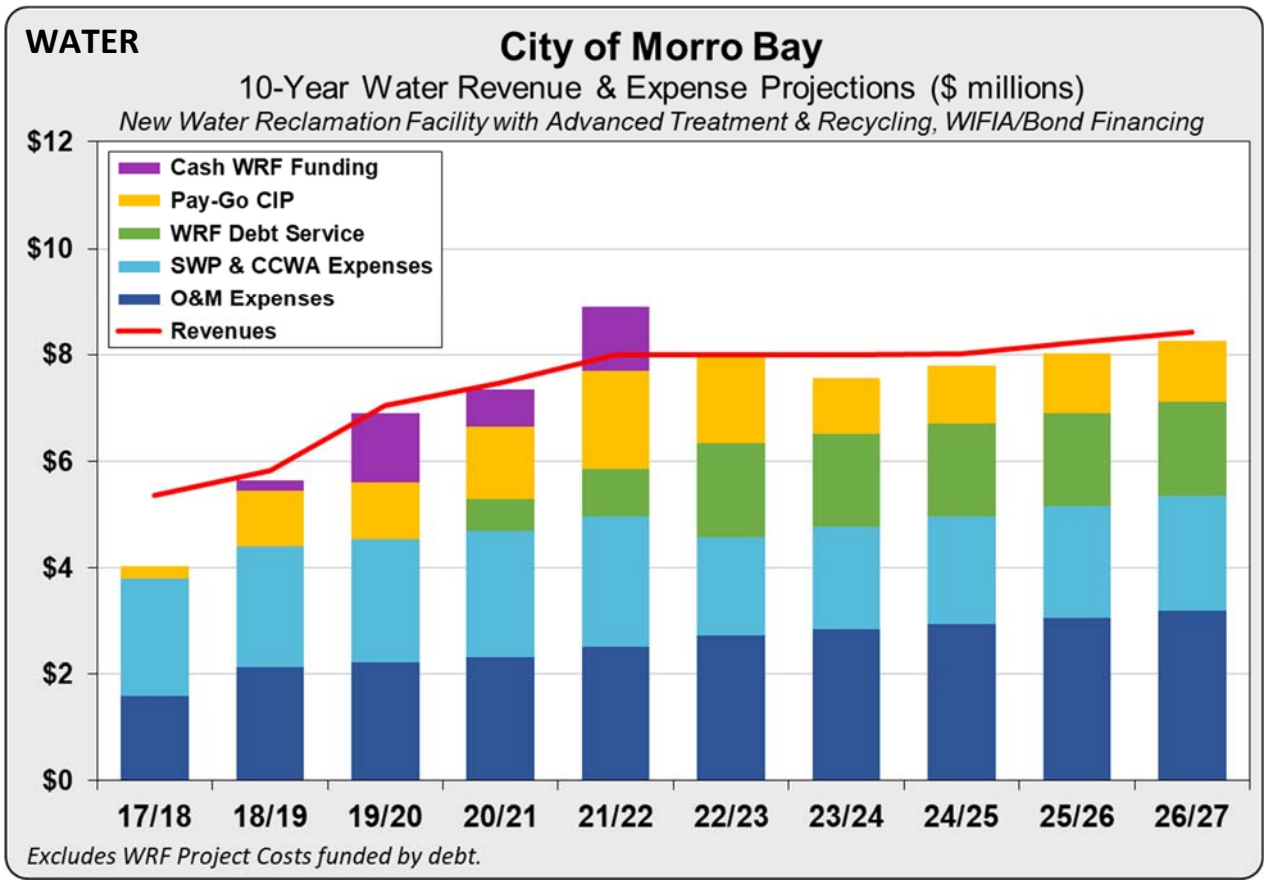
Table 11B - City of Morro Bay - Sewer Cash Flow Projections					Phase-In Scenario
	Projected				
Years 6 - 10	2022/23	2023/24	2024/25	2025/26	2026/27
Monthly Residential Sewer Charge	$83.00	$85.00	$87.00	$90.00	$92.00
Monthly Single Family WRF Surcharge	$27.00	$27.00	$27.00	$27.00	$27.00
Beginning Sewer Accounts	5,371	5,376	5,381	5,386	5,391
Growth: Single Family Equivalents	5	5	5	5	5
Growth %	0.1%	0.1%	0.1%	0.1%	0.1%
Sewer Development Impact Fee	$6,010	$6,130	$6,250	$6,380	$6,510
Interest Earnings Rate	2.0%	2.0%	2.0%	2.0%	2.0%
Cost Escalation	4.0%	4.0%	4.0%	4.0%	4.0%
Beginning Fund Reserves	$4,067,000	$4,267,000	$4,437,000	$4,565,000	$4,732,000
REVENUES					
Sewer Service Charges	7,267,000	7,449,000	7,631,000	7,901,000	8,084,000
Sewer WRF Facility Surcharges	2,347,000	2,347,000	2,347,000	2,347,000	2,347,000
Development Impact Fees	30,000	31,000	31,000	32,000	33,000
Interest Earnings	87,000	91,000	94,000	97,000	100,000
Rental Income/Penalties/Other	30,000	30,000	30,000	30,000	30,000
Subtotal	9,761,000	9,948,000	10,133,000	10,407,000	10,594,000
WRF Debt Financing					
SRF Planning Loan					
WIFIA Financing					
Bond Financing					
EXPENSES					
Operating & Maintenance					
Sewer Collection	1,732,000	1,801,000	1,873,000	1,948,000	2,026,000
Wastewater Treatment Existing	0	0	0	0	0
Wastewater Treatment New WRF	2,682,000	2,789,000	2,901,000	3,017,000	3,138,000
Conveyance to New WRF	277,000	288,000	300,000	312,000	324,000
Less Cayucos SD Reimbursements	*0*	*0*	*0*	*0*	*0*
Subtotal	4,691,000	4,878,000	5,074,000	5,277,000	5,488,000
Debt Service					
SRF Planning Loan	1,130,000	1,130,000	1,130,000	1,130,000	1,130,000
WIFIA Financing	3,051,000	3,051,000	3,051,000	3,051,000	3,051,000
Revenue Bonds (structured around SRF)	1,396,000	1,396,000	1,396,000	1,396,000	1,396,000
Less Water Share of WRF Debt	(1,757,000)	(1,757,000)	(1,757,000)	(1,757,000)	(1,757,000)
Subtotal	3,820,000	3,820,000	3,820,000	3,820,000	3,820,000
Capital Improvements					
Sewer Cash Contribution to WRF	0	0	0	0	0
Sewer System Pay-Go CIP	1,000,000	1,030,000	1,061,000	1,093,000	1,126,000
Vehicle/Equipment Replacement	50,000	50,000	50,000	50,000	50,000
Subtotal	1,050,000	1,080,000	1,111,000	1,143,000	1,176,000
Total Expenses	9,561,000	9,778,000	10,005,000	10,240,000	10,484,000
Revenues Less Expenses	200,000	170,000	128,000	167,000	110,000
Ending Fund Reserves	4,267,000	4,437,000	4,565,000	4,732,000	4,842,000
Debt Service Coverage	1.33	1.33	1.32	1.34	1.34

Table 12B - City of Morro Bay - Water Cash Flow Projections					Phase-In Scenario
	Projected				
Years 1 - 5	2017/18	2018/19	2019/20	2020/21	2021/22
Fixed Monthly Water Charge	$28.00	$30.00	$32.00	$32.00	$32.00
Fixed Monthly Single Family WRF Surcharge			$8.00	$12.00	$17.00
Water Rate Adjustment %		7.1%	6.7%	0.0%	0.0%
Growth: Single Family Equivalents	5	5	5	5	5
Growth %	0.1%	0.1%	0.1%	0.1%	0.1%
Change in Water Sales		0.0%	0.0%	0.0%	0.0%
Water Development Impact Fee	$5,392	$5,500	$5,610	$5,720	$5,830
Interest Earnings Rate	1.25%	1.75%	2.0%	2.0%	2.0%
State Water Project Cost Escalation			4.0%	4.0%	4.0%
Operating Cost Escalation			4.0%	4.0%	4.0%
Beginning Fund Reserves	$3,132,000	$4,456,000	$4,637,000	$4,797,000	$4,924,000
REVENUES	Estimated	Projected			
Water Service Charges	5,280,000	5,700,000	6,086,000	6,092,000	6,098,000
Water WRF Facility Surcharges	0	0	827,000	1,240,000	1,757,000
Development Impact Fees	30,000	28,000	28,000	29,000	29,000
Interest Earnings	39,000	78,000	93,000	96,000	98,000
Other (Excludes Penalties)	16,000	20,000	20,000	20,000	20,000
Subtotal	5,365,000	5,826,000	7,054,000	7,477,000	8,002,000
EXPENSES					
Operating & Maintenance	Estimated	Projected			
Water System Operations	1,591,000	2,130,000	2,215,000	2,304,000	2,396,000
State Water Project Payments	1,535,000	1,595,000	1,659,000	1,725,000	1,794,000
Share of CCWA 2016 Bonds (Thru Oct-2021)	665,000	670,000	670,000	670,000	670,000
Recycled Water Operations	-	-	-	-	110,000
Subtotal	3,791,000	4,395,000	4,544,000	4,699,000	4,970,000
Debt Service					
SRF Planning Loan: Water Share	-	-	-	326,000	326,000
WRF WIFIA Loan: Water Share	-	-	-	-	-
WRF Revenue Bonds: Water Share	-	-	-	275,000	551,000
Subtotal	0	0	0	601,000	877,000
Capital Improvements					
Water System Pay-Go CIP	250,000	1,000,000	1,000,000	1,300,000	1,800,000
Water Cash Contribution to WRF	0	200,000	1,300,000	700,000	1,200,000
Vehicle/Equipment Replacement	0	50,000	50,000	50,000	50,000
Subtotal	250,000	1,250,000	2,350,000	2,050,000	3,050,000
Total Expenses	4,041,000	5,645,000	6,894,000	7,350,000	8,897,000
Revenues Less Expenses	1,324,000	181,000	160,000	127,000	(895,000)
Ending Fund Reserves	4,456,000	4,637,000	4,797,000	4,924,000	4,029,000
CCWA Bond Debt Service Coverage	1.72	1.63	2.08	2.16	2.23
City Debt Service Coverage	-	-	-	4.62	3.46

Table 12B - City of Morro Bay - Water Cash Flow Projections					Phase-In Scenario
	Projected				
Years 6 - 10	2022/23	2023/24	2024/25	2025/26	2026/27
Fixed Monthly Residential Water Charge	$32.00	$32.00	$32.00	$33.00	$34.00
Fixed Monthly Single Family WRF Surchar	$17.00	$17.00	$17.00	$17.00	$17.00
Water Rate Adjustment %	0.0%	0.0%	0.0%	3.1%	3.0%
Growth: Single Family Equivalents	5	5	5	5	5
Growth %	0.1%	0.1%	0.1%	0.1%	0.1%
Change in Water Sales	0.0%	0.0%	0.0%	0.0%	0.0%
Water Development Impact Fee	$5,950	$6,070	$6,190	$6,310	$6,440
Interest Earnings Rate	2.0%	2.0%	2.0%	2.0%	2.0%
State Water Project Cost Escalation	4.0%	4.0%	4.0%	4.0%	4.0%
Operating Cost Escalation	4.0%	4.0%	4.0%	4.0%	4.0%
Beginning Fund Reserves	$4,029,000	$4,041,000	$4,475,000	$4,704,000	$4,906,000
REVENUES					
Water Service Charges	6,104,000	6,110,000	6,116,000	6,313,000	6,510,000
Water WRF Facility Surcharges	1,757,000	1,757,000	1,757,000	1,757,000	1,757,000
Development Impact Fees	30,000	30,000	31,000	32,000	32,000
Interest Earnings	86,000	86,000	95,000	100,000	104,000
Other (Excludes Penalties)	20,000	20,000	20,000	20,000	20,000
Subtotal	7,997,000	8,003,000	8,019,000	8,222,000	8,423,000
EXPENSES					
Operating & Maintenance					
Water System Personnel	2,492,000	2,592,000	2,696,000	2,804,000	2,916,000
State Water Project Payments	1,866,000	1,941,000	2,019,000	2,100,000	2,184,000
Share of CCWA 2016 Bonds (Thru Oct-2021)	0	0	0	0	0
Recycled Water Operations	220,000	229,000	238,000	248,000	258,000
Subtotal	4,578,000	4,762,000	4,953,000	5,152,000	5,358,000
Debt Service					
SRF Planning Loan: Water Share	326,000	326,000	326,000	326,000	326,000
WRF WIFIA Loan: Water Share	880,000	880,000	880,000	880,000	880,000
WRF Revenue Bonds: Water Share	551,000	551,000	551,000	551,000	551,000
Subtotal	1,757,000	1,757,000	1,757,000	1,757,000	1,757,000
Capital Improvements					
Water System Pay-Go CIP	1,600,000	1,000,000	1,030,000	1,061,000	1,093,000
Water Cash Contribution to WRF	0	0	0	0	0
Vehicle/Equipment Replacement	50,000	50,000	50,000	50,000	50,000
Subtotal	1,650,000	1,050,000	1,080,000	1,111,000	1,143,000
Total Expenses	7,985,000	7,569,000	7,790,000	8,020,000	8,258,000
Revenues Less Expenses	12,000	434,000	229,000	202,000	165,000
Ending Fund Reserves	4,041,000	4,475,000	4,704,000	4,906,000	5,071,000
CCWA Bond Debt Service Coverage	-	-	-	-	-
Debt Service Coverage	1.95	1.84	1.75	1.75	1.74

Phase-In Scenario





13. Debt Service Coverage

Tables 13A and 13B show projected debt service coverage independently for the sewer and water utilities as well as combined coverage for both utilities under the Base Case and Phase-In Scenarios. Debt service coverage is calculated based on Net Revenues – defined as total revenues less operating and maintenance expenses – divided by annual debt service. Additional funding generated after paying debt service is available to help fund the City's water and sewer CIP projects.

Table 13A – Base Case: Debt Service Coverage

	2022/23	2023/24	2024/25	2025/26	2026/27
SEWER					
Net Revenues	$4,895,000	$4,896,000	$4,886,000	$4,957,000	$4,934,000
Debt Service	3,616,000	3,616,000	3,616,000	3,616,000	3,616,000
Debt Service Coverage	1.35	1.35	1.35	1.37	1.36
Add'l Funding Generated	1,279,000	1,280,000	1,270,000	1,341,000	1,318,000
WATER					
Net Revenues	$3,316,000	$3,138,000	$2,962,000	$2,966,000	$2,960,000
Debt Service	1,677,000	1,677,000	1,677,000	1,677,000	1,677,000
Debt Service Coverage	1.98	1.87	1.77	1.77	1.77
Add'l Funding Generated	1,639,000	1,461,000	1,285,000	1,289,000	1,283,000
COMBINED					
Net Revenues	$8,211,000	$8,034,000	$7,848,000	$7,923,000	$7,894,000
Debt Service	5,293,000	5,293,000	5,293,000	5,293,000	5,293,000
Debt Service Coverage	1.55	1.52	1.48	1.50	1.49
Add'l Funding Generated	2,918,000	2,741,000	2,555,000	2,630,000	2,601,000

Table 13B – Phase-In: Debt Service Coverage

	2022/23	2023/24	2024/25	2025/26	2026/27
SEWER					
Net Revenues	$5,070,000	$5,070,000	$5,059,000	$5,130,000	$5,106,000
Debt Service	3,820,000	3,820,000	3,820,000	3,820,000	3,820,000
Debt Service Coverage	1.33	1.33	1.32	1.34	1.34
Add'l Funding Generated	1,250,000	1,250,000	1,239,000	1,310,000	1,286,000
WATER					
Net Revenues	$3,419,000	$3,241,000	$3,066,000	$3,070,000	$3,065,000
Debt Service	1,757,000	1,757,000	1,757,000	1,757,000	1,757,000
Debt Service Coverage	1.95	1.84	1.75	1.75	1.74
Add'l Funding Generated	1,662,000	1,484,000	1,309,000	1,313,000	1,308,000
COMBINED					
Net Revenues	$8,489,000	$8,311,000	$8,125,000	$8,200,000	$8,171,000
Debt Service	5,577,000	5,577,000	5,577,000	5,577,000	5,577,000
Debt Service Coverage	1.52	1.49	1.46	1.47	1.47
Add'l Funding Generated	2,912,000	2,734,000	2,548,000	2,623,000	2,594,000

14. Sewer WRF Facility Surcharges

Tables 14A and 14B show proposed sewer WRF Facility Surcharges under the Base Case and Phase-In Scenarios. These surcharges would be levied as separate surcharges in addition to the City's previously-adopted sewer rates. The surcharges maintain the same rate structure as the City's existing sewer rates. Residential surcharges are fixed monthly surcharges and Non-Residential surcharges are volumetric rates applied to monthly water use – with higher charges for customer classes with higher wastewater strength -- subject to a minimum charge as shown.

Table 14A – Base Case: Proposed Monthly Sewer WRF Facility Surcharges

	2018/19	2019/20	2020/21	2021/22	2022/23
RESIDENTIAL					
Charge per residential dwelling unit					
Single Family		$25.00	$25.00	$25.00	$25.00
Multi-Family/Condo		20.00	20.00	20.00	20.00
NON-RESIDENTIAL					
Rate per hcf of metered water use					
Class A - Low Strength		$3.43	$3.43	$3.43	$3.43
Class B - Domestic Strength		4.10	4.10	4.10	4.10
Class C - Moderate Strength		4.77	4.77	4.77	4.77
Class D - Mod-High Strength		5.43	5.43	5.43	5.43
Class E - High Strength		6.77	6.77	6.77	6.77
Minimum Monthly Charge		20.00	20.00	20.00	20.00

Table 14B – Phase-In: Proposed Monthly Sewer WRF Facility Surcharges

	2018/19	2019/20	2020/21	2021/22	2022/23
RESIDENTIAL					
Charge per residential dwelling unit					
Single Family		$9.00	$18.00	$27.00	$27.00
Multi-Family/Condo		7.20	14.40	21.60	21.60
NON-RESIDENTIAL					
Rate per hcf of metered water use					
Class A - Low Strength		$1.24	$2.47	$3.71	$3.71
Class B - Domestic Strength		1.48	2.95	4.43	4.43
Class C - Moderate Strength		1.72	3.43	5.15	5.15
Class D - Mod-High Strength		1.96	3.91	5.87	5.87
Class E - High Strength		2.44	4.87	7.31	7.31
Minimum Monthly Charge		7.20	14.40	21.60	21.60

15. Water WRF Facility Surcharges

Tables 15A and 15B show proposed water WRF Facility Surcharges under the Base Case and Phase-In Scenarios. Again, these surcharges would be levied in addition to the City's previously-adopted water rates. Residential surcharges are fixed monthly surcharges and Non-Residential surcharges are volumetric rates applied to monthly water use, subject to a minimum charge as shown.

Table 15A – Base Case: Proposed Monthly Water WRF Facility Surcharges

	2018/19	2019/20	2020/21	2021/22	2022/23
RESIDENTIAL					
Charge per residential dwelling unit					
Single Family		$16.00	$16.00	$16.00	$16.00
Multi-Family/Condo		12.80	12.80	12.80	12.80
NON-RESIDENTIAL					
Rate per hcf of metered water use					
Surcharge on all water use		$3.64	$3.64	$3.64	$3.64

Table 15B – Phase-In: Proposed Monthly Water WRF Facility Surcharges

	2018/19	2019/20	2020/21	2021/22	2022/23
RESIDENTIAL					
Charge per residential dwelling unit					
Single Family		$8.00	$12.00	$17.00	$17.00
Multi-Family/Condo		6.40	9.60	13.60	13.60
NON-RESIDENTIAL					
Rate per hcf of metered water use					
Surcharge on all water use		$1.82	$2.73	$3.87	$3.87

16. Previously-Adopted Water & Sewer Rates

As of July 1, 2018, the City will have implemented 4 of the 5 years of previously-adopted rate increases. The final rate increase – scheduled to become effective July 1, 2019 – equates to a roughly 7.5% increase for a typical single family home with 5 hcf monthly water use. The adopted rates were originally designed to generate some funding for the WRF Project. Funding from the City's regular water and sewer rates will supplement the WRF Facility Surcharges, which will recover most of the costs for WRF-related debt service. Based on the financial projections, if the WRF Facility Surcharges are adopted, then no additional water or sewer rate increases – above those previously adopted – would likely need to be implemented over at least the next 5 years. However, the City should periodically evaluate its utility rates in future years to ensure future rates continue to recover the cost of providing service and each utility continues to meet its future financial obligations.

Table 16 – Adopted Monthly Water Rates

		2018/19	2019/20	2020/21	2021/22	2022/23
		Adopted	Adopted	No Change Projected		
Fixed Monthly Charge		$30.00	$32.00	$32.00	$32.00	$32.00
Water Quantity Charges						
Billed per 100 cubic feet of metered water use ($/hcf)						
Tier	Use in Tier					
Tier 1	0 - 3 hcf	$5.50	$6.00	$6.00	$6.00	$6.00
Tier 2	4 - 10 hcf	8.00	8.50	8.50	8.50	8.50
Tier 3	11- 50 hcf	10.50	11.00	11.00	11.00	11.00
Tier 4	>50 hcf	13.50	14.00	14.00	14.00	14.00

Table 17 – Adopted Monthly Sewer Rates

	2018/19	2019/20	2020/21	2021/22	2022/23
	Adopted	Adopted	No Change Projected		
RESIDENTIAL					
Charge per residential dwelling unit					
Single Family	$77.00	$83.00	$83.00	$83.00	$83.00
Multi-Family/Condo	61.60	66.40	66.40	66.40	66.40
NON-RESIDENTIAL					
Rate per hcf of metered water use					
Class A - Low Strength	$10.57	$11.40	$11.40	$11.40	$11.40
Class B - Domestic Strength	12.67	13.61	13.61	13.61	13.61
Class C - Moderate Strength	14.89	15.82	15.82	15.82	15.82
Class D - Mod-High Strength	17.13	18.03	18.03	18.03	18.03
Class E - High Strength	21.36	22.46	22.46	22.46	22.46
Minimum Monthly Charge	61.60	66.40	66.40	66.40	66.40

17. Bill Impacts

The following charts and tables show the total combined billing impacts – with full implementation of previously-adopted water and sewer rates and the proposed WRF Surcharges – on single family homes at different levels of monthly water use under the Base Case Scenario. Impacts on a range of other customer classes under the Base Case Scenario are included in the appendix.

Base Case Scenario

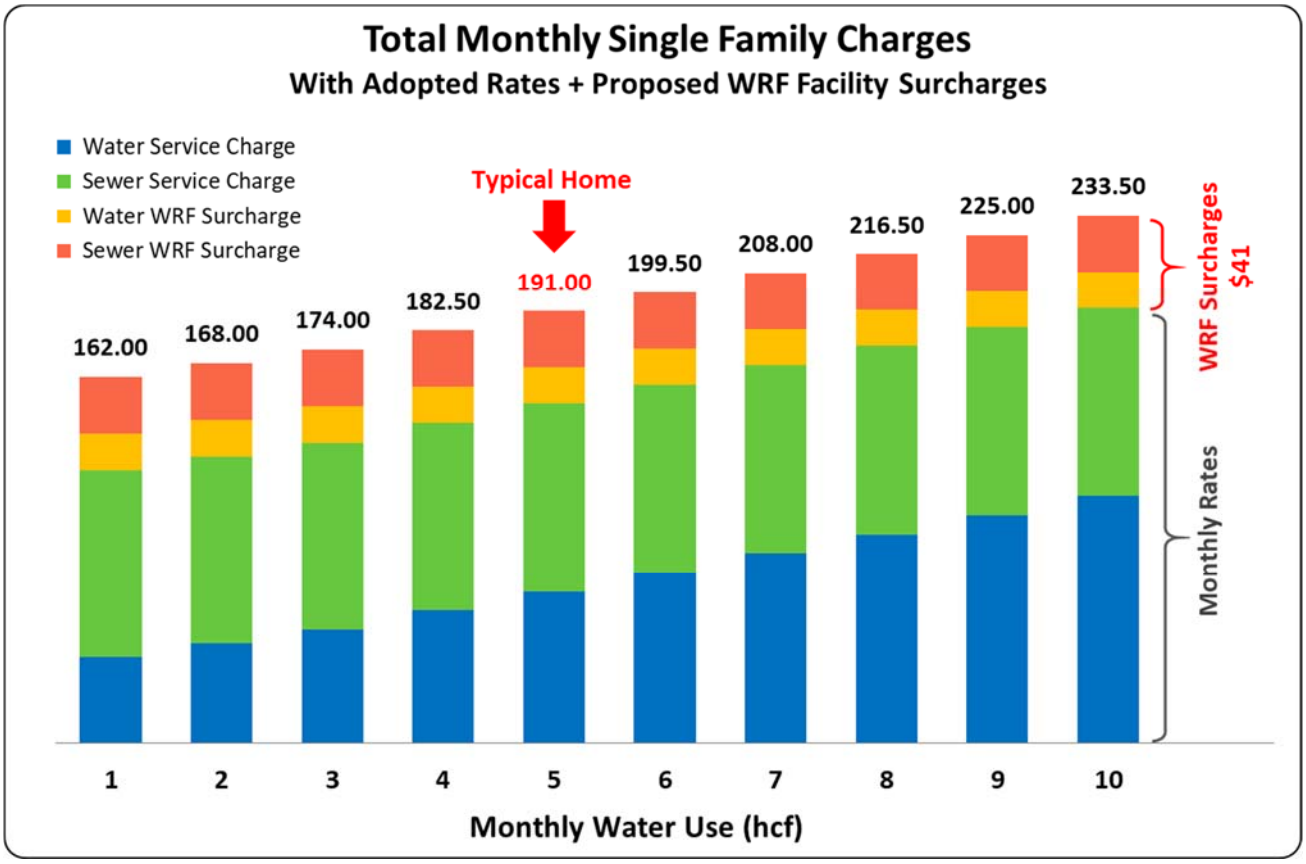


Table 18A – Base Case: Total Combined Bill with Adopted Rates + Proposed WRF Surcharges

Single Family Home at Different Levels of Use

	Monthly Water Use (hcf)									
	1	2	3	4	5	6	7	8	9	10
Water Service Charge	$38.00	$44.00	$50.00	$58.50	$67.00	$75.50	$84.00	$92.50	$101.00	$109.50
Sewer Service Charge	83.00	83.00	83.00	83.00	83.00	83.00	83.00	83.00	83.00	83.00
Subtotal	121.00	127.00	133.00	141.50	150.00	158.50	167.00	175.50	184.00	192.50
Water WRF Surcharge	16.00	16.00	16.00	16.00	16.00	16.00	16.00	16.00	16.00	16.00
Sewer WRF Surcharge	25.00	25.00	25.00	25.00	25.00	25.00	25.00	25.00	25.00	25.00
Subtotal	41.00	41.00	41.00	41.00	41.00	41.00	41.00	41.00	41.00	41.00
Combined Total	**162.00**	**168.00**	**174.00**	**182.50**	**191.00**	**199.50**	**208.00**	**216.50**	**225.00**	**233.50**

The following charts and tables show the total combined billing impacts – with full implementation of previously-adopted water and sewer rates and the proposed WRF Facility Surcharges – on single family homes at different levels of monthly water use under the Phase-In Scenario. Impacts on a range of other customer classes under the Phase-In Scenario are included in the appendix.

Phase-In Scenario

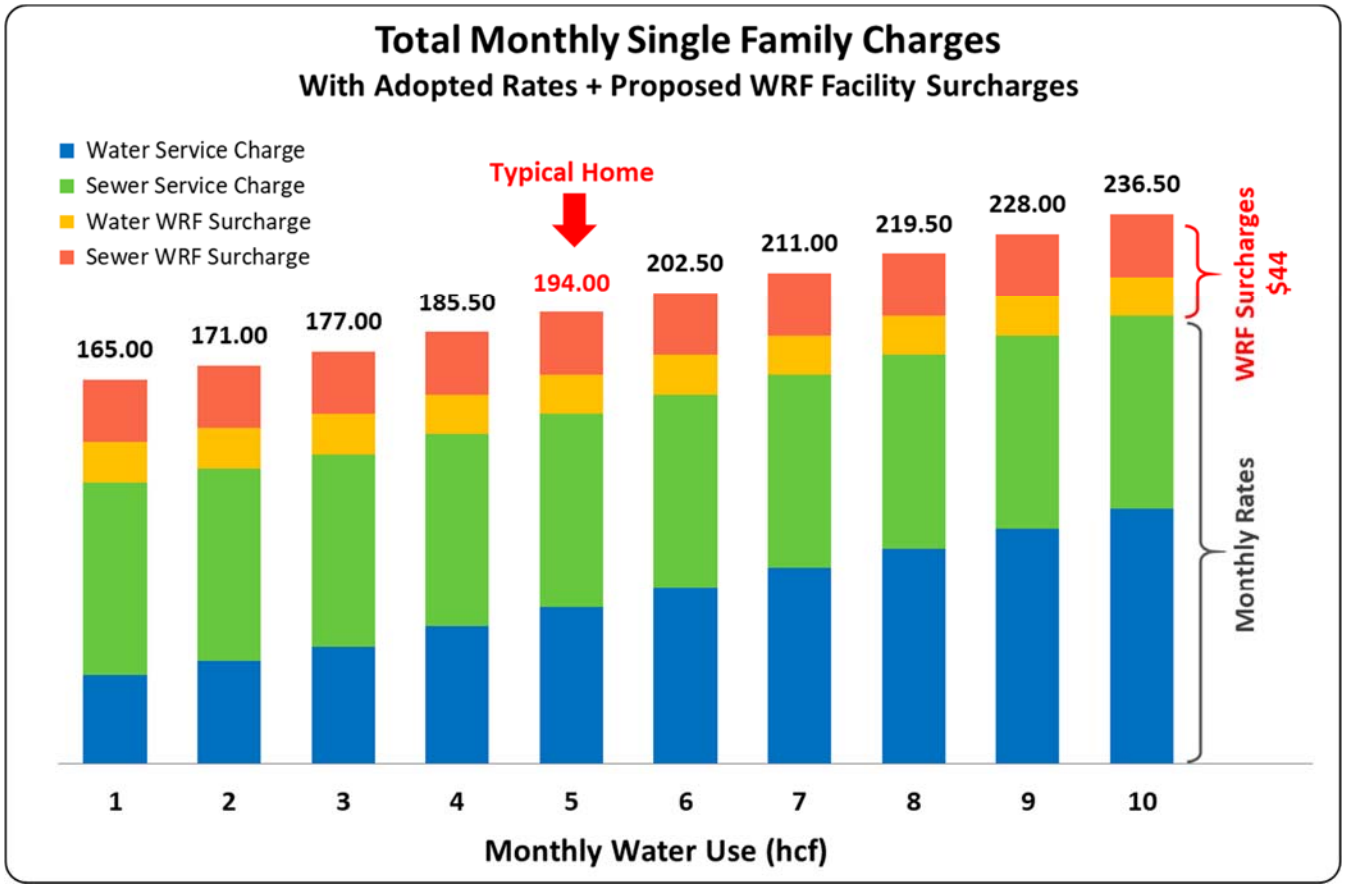


Table 18B – Phase In: Total Combined Bill with Adopted Rates + Proposed WRF Surcharges

Single Family Home at Different Levels of Use

	Monthly Water Use (hcf)									
	1	2	3	4	5	6	7	8	9	10
Water Service Charge	$38.00	$44.00	$50.00	$58.50	$67.00	$75.50	$84.00	$92.50	$101.00	$109.50
Sewer Service Charge	83.00	83.00	83.00	83.00	83.00	83.00	83.00	83.00	83.00	83.00
Subtotal	121.00	127.00	133.00	141.50	150.00	158.50	167.00	175.50	184.00	192.50
Water WRF Surcharge	16.00	16.00	16.00	16.00	16.00	16.00	16.00	16.00	16.00	16.00
Sewer WRF Surcharge	25.00	25.00	25.00	25.00	25.00	25.00	25.00	25.00	25.00	25.00
Subtotal	41.00	41.00	41.00	41.00	41.00	41.00	41.00	41.00	41.00	41.00
Combined Total	**162.00**	**168.00**	**174.00**	**182.50**	**191.00**	**199.50**	**208.00**	**216.50**	**225.00**	**233.50**

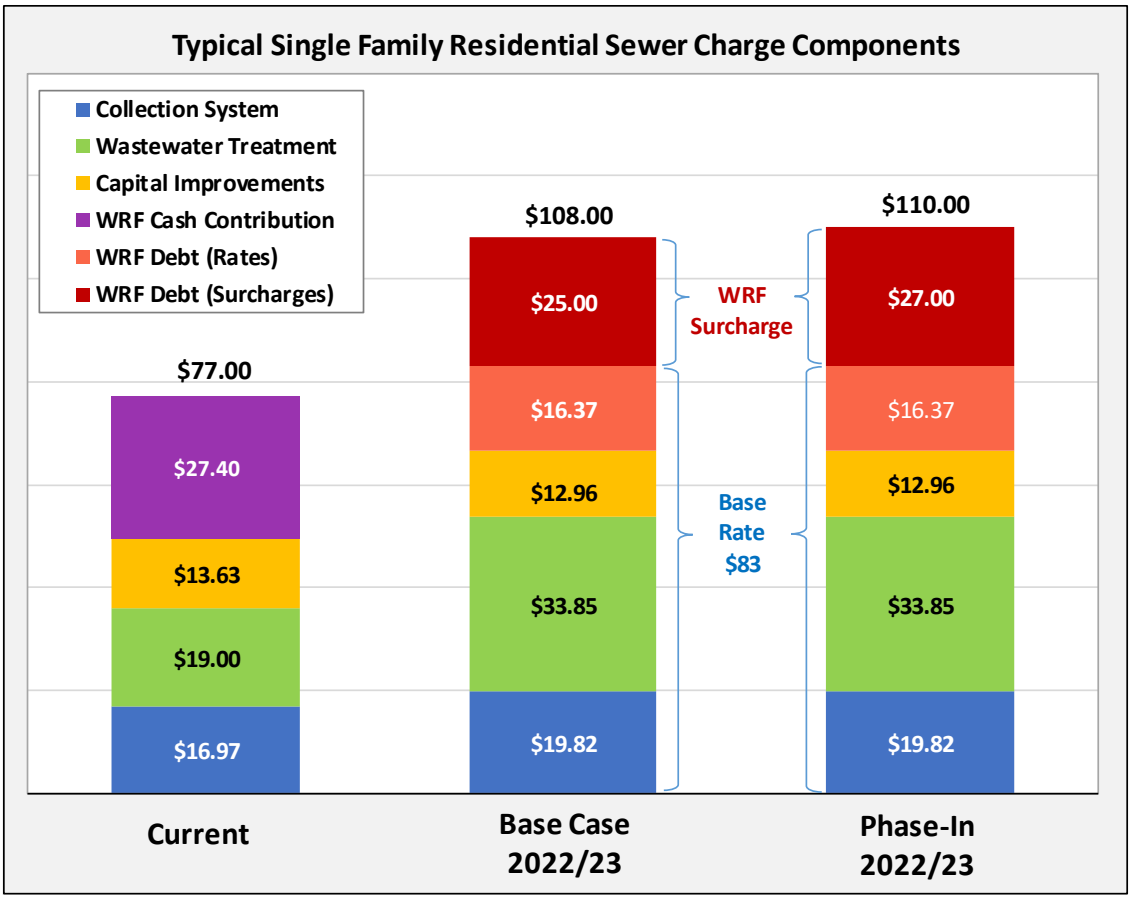
18. Sewer Rate & WRF Surcharge Cost Recovery

Table 19 shows and estimated breakdown of the cost components of monthly sewer charges for a typical single family home with 5 units (hcf) monthly water use. The table compares current charges vs. charges in 2022/23 with full implementation of adopted rates and the WRF Facility Surcharge.

Table 19 – Sewer Rate Components

	Current 2018/19	Base Case 2022/23	Phase-In 2022/23
Base Monthly Sewer Rate			
Sewer Collection System O&M	$16.97	$19.82	$19.82
Wastewater Treatment O&M*	19.00	33.85	33.85
WRF Debt Service: Sewer Rates	0.00	16.37	16.37
Sewer CIP/Equipment/Other	13.63	12.96	12.96
WRF Cash Contribution	27.40	0.00	0.00
Subotal Base Sewer Rate	77.00	83.00	83.00
WRF Surcharge (for WRF Debt Service)	0.00	25.00	27.00
Total	**77.00**	**83.00**	**83.00**

** Current year wastewater treatment O&M is net of 25% cost-sharing by Cayucos SD*



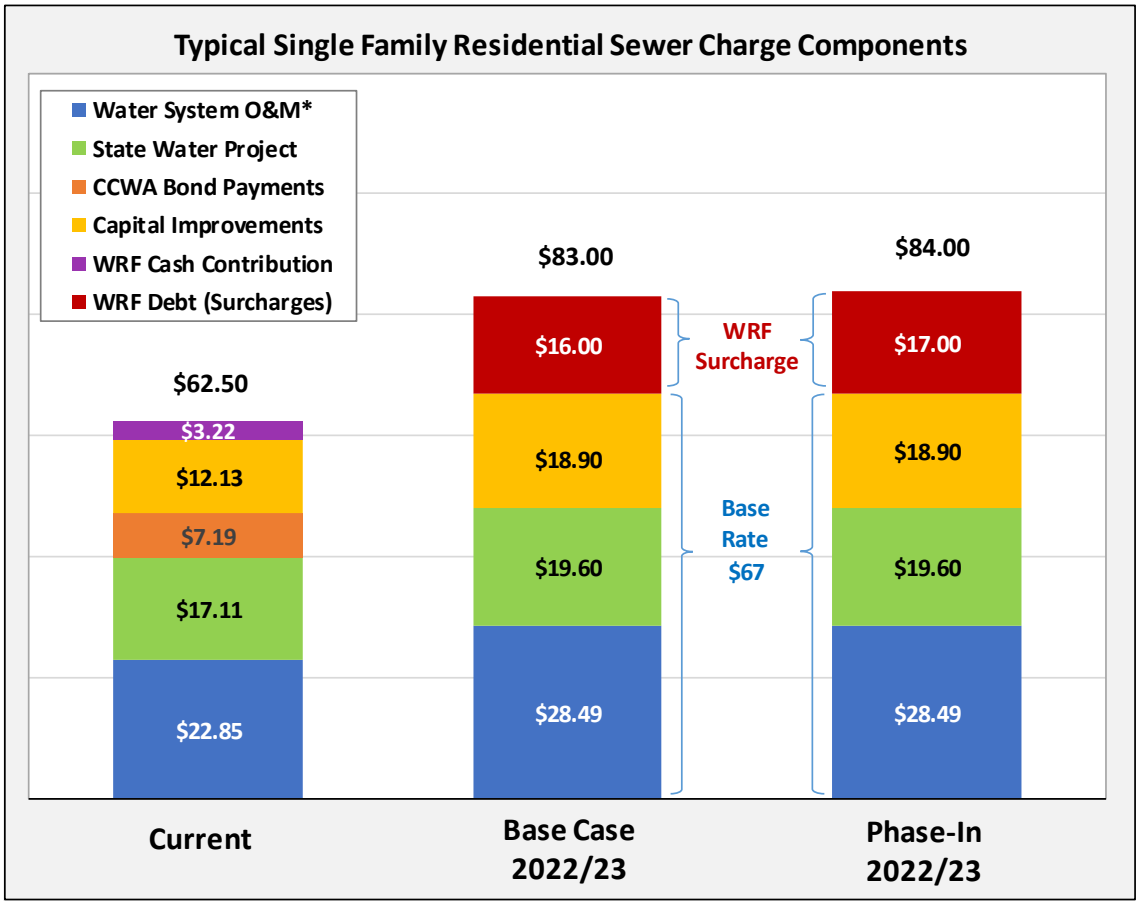
19. Water Rate & WRF Surcharge Cost Recovery

Table 20 shows and estimated breakdown of the cost components of monthly water charges for a typical single family home with 5 units (hcf) monthly water use. The table compares current charges vs. charges in 2022/23 with full implementation of adopted rates and the WRF Facility Surcharge.

Table 20 – Water Rate Components

	Current 2018/19	Base Case 2022/23	Phase-In 2022/23
Base Monthly Water Rate			
Water System O&M*	$22.85	$28.49	$28.49
State Water Project Expenses	17.11	19.60	19.60
CCWA Bond Payments	7.19	0.00	0.00
Water CIP/Equipment/Other	12.13	18.90	18.90
WRF Cash Contribution	3.22	0.00	0.00
Subtotal Water Rate	62.50	67.00	67.00
WRF Surcharge (for WRF Debt Service)	0.00	16.00	17.00
Total	**62.50**	**83.00**	**84.00**

** Water System O&M in 2022/23 includes recycled water operating expenses of $220,000.*



20. Billing Options for WRF Facility Surcharges

The City currently bills customers monthly via a combined utility bill for water and sewer service. The City is considering two methods of bill collection for recovering the WRF Facility Surcharges, including:

- **Monthly Billing** - Add the WRF Facility Surcharges as a new line-item in the monthly bills.
- **Property Tax Rolls** - Recover the proposed WRF Facility Surcharges on the property tax rolls.

The WRF Facility Surcharges would be the same under both alternatives; only the method of billing and collection would vary. For a single family home, adding the surcharges to the property tax rolls, would result in two payments of roughly $250 that would be added to the semi-annual property tax assessments. Table 20 shows the timing of payments for WRF Facility Surcharges under the Base Case and Phase-In Scenarios with full implementation of the surcharges. Non-residential customers could be billed on the property tax rolls based on usage from the immediately-prior 12-month period.

Table 20 – Example of Single Family WRF Surcharges Collected with Property Taxes

	Annual Total	December Installment 1	April Installment 2
WRF Facility Surcharges			
Base Case Scenario	$492.00	$246.00	$246.00
Phase-In Scenario	528.00	264.00	264.00

While there are some administrative differences for billing and collecting the WRF Facility Surcharges under the two billing options, the main difference is who will bear the financial burden of paying the surcharges: ratepayers or property owners. Note than many ratepayers are also property owners and would be the same people paying the same surcharges regardless of billing method. However, the City does serve a number of tenants who currently pay utility bills for their rental units.

Some potential pros, cons, and issues related to collecting the WRF Facility Surcharges on the property tax rolls include:

- In many (but not all) cases, property owners own substantial equity in their homes, whereas many renters do not have such equity and/or may not be able to afford to purchase a home. Hence billing the WRF Facility Surcharges via the property tax rolls would put the burden on a group that generally has more financial asset than renters. At the same time, there are number of homeowners who – although they may have substantial equity in their home – are also living on fixed incomes.

- The new WRF facility benefits homeowners by preserving property value with access to safe and reliable wastewater service.
- Adding the WRF Facility Surcharges to the combined monthly water and sewer bill could potentially result in an uptick in delinquencies. However, delinquencies can be ultimately recovered by placing a lien on the property, which results in the charge being put back on the property tax rolls in case of extreme delinquency.
- San Luis Obispo County is on the Teeter Plan and pays agencies for 100% of assessments or charges placed on the property tax rolls for collection, regardless of actual delinquencies. The County has indicated that if delinquencies exceed 3%, then the County retains the authority to end the Teeter Plan practice and instead provide only actual amounts collected. However, the County has never done this in the past.
- The cost of placing the surcharges on the property tax rolls currently costs $2 per parcel and is roughly estimated to cost a total of about $11,000 per year.
- Placing the surcharges on the tax roll would require the City Council to pass a Resolution adopting a schedule of charges to be levied on all affected properties by Assessor's Parcel Number (APN) each year. If the Resolution was not adopted, the charges could not be assessed on the property tax rolls. However, this does not mean that the City could not recover the charge, it would simply change the method of collection and would require the City to add the surcharges to the monthly bills instead.
- Regardless of the billing approach, the City would be under legal covenant to adopt rates and charges as needed to repay debt service, meet debt service coverage requirements, and meet other legal obligations.
- Collecting sewer charges on the property tax rolls would also result in a change in timing of receiving revenues. The County generally sends agencies payments twice per year (in December and April) based on actual tax collections. Subsequently, at the end of the fiscal year, the County does a true-up and would send the City the remainder of amounts billed on the tax rolls regardless of delinquencies. The County subsequently deals with the delinquencies and keeps any funds recovered from the delinquent properties including any penalties.
- If the City opted to collected the WRF Facility Surcharges on the property tax rolls, due to the change in timing of revenues, the City may need to strategically determine the payment dates for future debt service payments to ensure the debt payments are due after the City receives payment from the County in December and April.

In order to recover the WRF Facility Surcharges via the property tax rolls, the City would need to follow the process identified in the California Health and Safety Code Section 5470 – 5474, attached as an appendix to this report. The process is similar to the Proposition 218 process required for increasing utility rates and could be done concurrently when the City goes through the Proposition 218 rate increase process for potential water and sewer rate increases.