

PROPOSED WATER RATE INCREASE Bear Valley Community Services District

At their meeting on January 10th, the Bear Valley Community Services Board of Directors received a draft Water Rate Study prepared by Willdan Financial Services and provided direction on public outreach to the community to explain the Study's findings and recommendations.

Last fall, the Board approved a Professional Services Agreement with Willdan Financial Services (Willdan) to prepare what was described as an "interim water rate study" to address the critical revenue needs for the District's water system and lack of reserves for both current maintenance and long-term capital repairs and replacement. Their recommendations will be considered at the February 14th meeting. Upon approval of the final report, a public hearing will be set and a notice will be sent to all property owners.

Background

In 2017, the District initiated a planned three phase effort involving a comprehensive review and restructuring of the District's rates and charges related to water, sewer and solid waste service. The first phase of this effort was to conduct a survey of the applicable facilities, as particularly with respect to the District's water system, no such inventory exists. The information from Phase 1 would then be incorporated into Phase 2 as part of a Capital Improvement Plan (CIP) that would identify and prioritize infrastructure needs and develop a multi-year capital planning model. The third phase of the work is a comprehensive rate study to establish rates which would encompass the capital expenditures and possible debt service arising from the CIP, as well as implement rates to cover existing operations and maintenance and provide appropriate reserves.

The first phase of the project has taken longer than anticipated, in part, due to the need to survey the scope of the District's existing water system from scratch. While this effort is nearly complete, in light of the Water Department's existing revenue needs and lack of reserves, and the anticipated time needed to complete Phase 2, the Board determined it was prudent to proceed with an interim water rate study that would provide recommendations for the next three to five years so that, at minimum, water rates would cover operating expenses and the District could begin to develop operating reserves.

The Study

While initially referred to as an "interim" study because further analysis will need to be done when the CIP is completed, this Study involved a comprehensive review of past five fiscal years (2013-2017) of actual operating expenses and revenues for the Water Department along with detailed budget projections for the next five fiscal years (2019-2023), and laid the foundation for the proposed revised rate schedule. As summarized in the report, expenditures have generally been exceeding water system revenues for the past five fiscal years. The Study

results confirm the District's own analysis that without any rate increase action, projected operating expenses will continue to exceed revenues and the Water Department will deplete its cash reserves in FY 2020

The Need

The following outlines the primary financial management goals that the District sought to establish, and the proposed revised rate structure was designed to satisfy:

A. Minimum Working Capital Balance - In order to maintain a certain level of liquidity, the rates are premised upon a goal of maintaining working capital reserves in an amount greater than or equal to approximately 120 days of operating expenses.

B. Debt Service Coverage - The District currently has outstanding water-related debt obligations which require the District to set rates and charges to maintain a debt service coverage ratio, defined as Current Year Net Revenues divided by Current Year Debt Service, at a minimum ratio of 1.10x. The District has not been meeting this coverage requirement even though the District has been meeting its annual loan obligation of approximately \$160,000 in principal and interest payments. As a result, the lender requested, and at the December meeting the Board approved, the establishment of a rate stabilization fund.

C. Funding of Capital Improvements - This goal is to fund the Water Department's current capital improvement requirements including incremental costs associated with eliminating the existing backlog of repair, maintenance and replacement needs.

D. To Stabilize Revenues - The District's current rate structure provides approximately 40% of revenues through the base charge and 60% of revenues based on usage (called the volumetric rate). As a result, when usage drops, such as during the drought years of 2016 and 2017 (when the District imposed conservation measures), revenue significantly decreased even though the fixed costs to operate the system remained constant. A more stable long-term rate structure would generate 60% of revenues from the base charge and 40% from the volumetric rate.

Rate Changes

Another change that will result from the recommended new rates is the replacement of the current seven volumetric tiers with a two-tier structure. Consistent with State law provisions to promote water conservation, the existing rate structure imposes higher costs with higher usage. Recent court decisions, however, require that while conservation is a desirable goal, water rates must still reasonably reflect the cost of service. Accordingly, the District is proposing to shift to a two-tiered rate structure. The first tier reflecting the cost to pump and provide groundwater from within the District, and the second tier reflecting the incremental cost to purchase additional water from the Tehachapi-Cummings County Water District. The incremental cost of this purchased water has been determined to be \$1.56/HCF, which amount would be added to all usage above 5 HCF in any month.

The Willdan study recommends the following rate structure that addresses the above-stated goals:

Monthly Rates	<u>Current</u>	<u>2019</u>	<u>2020</u>	<u>2021</u>	<u>2022</u>	<u>2023</u>
Fixed rate	\$25.33	\$43.06	\$73.20	\$76.86	\$80.71	\$84.74
Volumetric rate						
1 to 5 HCF	\$2.00	\$2.80	\$3.78	\$3.78	\$3.78	\$3.78
6+ HCF	\$2.85	\$4.36	\$5.34	\$5.34	\$5.34	\$5.34

The District is keenly aware that the revised rate structure will result in substantial increases in customers' monthly bills, and has reviewed and refined the operating projections of the Water Department to the point where even with the proposed increases, the District is not projected to maintain the desired operating reserve equal to 120 days of annual operating and maintenance expenses until fiscal year 2023. This is primarily due to the fact that for over a decade, the District's rates have barely changed and certainly have not kept pace with inflation. For example, the fixed rate for a residential customer in 2007 was \$24.22 (currently \$25.33) and the usage rate for 10 HCF (an average household) was \$3.15 (currently \$2.85).

To ensure that the community understands the District's critical need for the proposed rate increases and to provide opportunities for discussion and feedback before the required 45-day public hearing notice is issued, the Board directed staff to share the information with the community and to solicit and consider community input prior to finalizing the rates to be implemented.