



Agenda Report

May 6, 2024

TO: Honorable Mayor and City Council
FROM: Department of Public Works
SUBJECT: PUBLIC HEARING TO APPROVE SEWER USE FEE RATE STRUCTURE AND RATE ADJUSTMENTS (CONTINUED)

RECOMMENDATION:

It is recommended that the City Council:

1. Find that the proposed action is not a project as defined in the California Environmental Quality Act (CEQA) Public Resources Code Section 21065, 21080(b)(8) and State CEQA Guidelines Sections 15378(a) and (b)(4), and that even if it were a project, the proposed sewer use fee increases are statutorily exempt pursuant to Section 15273 (Rates, Tolls, Fares, and Charges) under State CEQA Guidelines and as such, is not subject to environmental review;
2. Conduct a Public Hearing to receive public comment on the adjustments to the Sewer Use Fee rate structure proposed to be implemented for the Fiscal Years (FY) 2025 through FY 2029 rates effective July 1, 2024 or as soon as practicable thereafter;
3. Consider all protests against the proposed Sewer Use Fee rate adjustments in accordance with Proposition 218;
4. Close the Public Hearing and approve Revised Proposed Sewer Use Fee rate structure and rate adjustments or provide alternate direction; and
5. Direct the City Attorney to prepare an amendment to the Sewer Use Charge Ordinance (Ordinance) implementing the changes to the approved Sewer Use Fee rate structure and rate adjustment described herein.

EXECUTIVE SUMMARY

The operations, ongoing maintenance, and needed capital improvements of the City-owned sewer collection system is funded by the City's Sewer Use Fee. Currently, the Sewer Use Fee does not generate sufficient revenue to cover the cost of providing

adequate operation and maintenance of the City's sewer system. To address these funding needs, the City contracted with an experienced rate consultant, Raftelis, who prepared an evaluation of the Sewer Use fee rates and structure.

This report is in response to City Council's request for additional clarification and information as discussed at the public hearing on April 8, 2024. This report includes further explanations regarding the sewer program financials, four rate scenarios and a rate smoothing option. The scenarios divide the sewer rates into categories or "buckets" to illustrate ways the operations, capital improvements and reserves could be funded for: 1) operations only; 2) operations plus capital (no reserves); 3) Revised Proposed – operations plus capital plus reserves; and 4) operations, increased capital plus reserves. The Smoothing Option includes elements from the various rate scenarios and will provide appropriate funding for operations and allow for construction of previously deferred CIP projects; however, it is not ideal as it will result in some continued deferral and reduced scope of forecasted CIP projects. Furthermore, while it offers a modest level of financial relief for the first three years, the Smoothing Option rates in the final two years exceed those in the recommended Revised Proposed scenario.

BACKGROUND:

The operations, ongoing maintenance, and needed capital improvements of the City-owned sewer collection system is funded by the City's Sewer Use Fee. Revenue generated by the current Sewer Use Fee structure is insufficient to cover current and future operating and capital improvement program (CIP) costs. Currently, the Sewer Fund is unable to maintain a minimum Fund Balance equal to one-month of current operating appropriations per City's Fund Balance Policy. It is crucial that sufficient revenue is generated to cover the cost of providing this essential service to the community and to sustain the integrity of the City's sewer system. Without a fee increase, the City would be unable to adequately operate and maintain the sewer system. This could lead to dangerously and costly sewage spills as well as higher future costs for repairs and replacement.

To address these funding needs, the City contracted with an experienced firm, Raftelis, and initiated an evaluation of the Sewer Use Fee structure in June 2023. Staff presented the findings to the Municipal Services Committee on January 23, 2024, and a public hearing date was set by City Council on February 5, 2024. On April 8, 2024, the City Council opened the public hearing and received public comment on the noticed Sewer Use Fee rate adjustments. During the hearing, the City Council requested additional information and clarification regarding the City's Sewer Fund balance and relevant CIP costs and directed staff to model additional rate adjustment scenarios. City Council continued the public hearing to May 6, 2024.

Sewer Use Fee Revenues, Costs and Fund Balance Clarifications

The Sewer Fund, as presented in both the Operating Budget and CIP Budget, includes revenues and expenditures related to both Sewer Use Fees and Storm Drain Use Fees. In the Operating Budget, operational expenditures are generally split 75% / 25% with 75% of expenses being budgeted and charged for Sewer Use Fee related operations. The CIP Budget and the projects within it are allocated internally to either Sewer Use Fees or Storm Drain Use Fees based on the scope of the project; they are not allocated on a percentage basis. The amounts referenced in the fee study are specific to operational and capital improvement costs for only the Sewer Use Fee funded expenditures.

The amounts presented by the consultant during the prior meeting on April 8, 2024, regarding revenues and expenditures were a forecast developed by the consultant based on year-to-date actuals as of April 2023. The consultant made assumptions on revenue and expenditures for the remainder of Fiscal Year 2023 and all the forward years. A major assumption that resulted in showing expenditures of \$6.1 million in FY 2023 was that Public Works would spend \$1.75 million of the CIP allocated to the Pump Station projects included in the approved CIP Budget. Additionally, the consultant assumed the remaining funding for those projects would be expended in FY 2024, also driving those expenditures figures higher. The two pump station projects had \$2.77 million appropriated but not yet spent when actuals were provided to the consultant in April 2023. Therefore, the consultant's expenditure forecast included that amount spread across FY 2023 and 2024 along with assumptions related to revenue and operating expenses that did not tie directly to the budget nor the subsequent actuals.

Expenditures in a fiscal year may exceed revenues in a fiscal year due to the timing of capital improvement project work; however, the cumulative revenues and expenditures related to the Sewer Use Fees has not gone into the negative from a cash position. In FY 2023, operating expenditures did exceed revenues by more than \$400,000 due to rising costs and lower actual revenues; however, the fund had unassigned cash of approximately \$800,000 at the start of FY 2024.

Proposed Capital Improvement Programs

The City owns and operates a sewer wastewater collection system that serves approximately 140,000 residents and the City's commercial users. The sewer system includes approximately 325 miles of sewer pipelines, three pump stations, and approximately 7,430 manholes. To help balance the fund and maintain service levels over the last few years, needed capital improvements have been deferred and the Sewer Fund operating reserve balance has been depleted.

Citywide, approximately 80% of the City's sewer pipelines are over 80 years old and most of the system, 89%, is constructed of Vitrified Clay Pipe (VCP). The estimated lifespan of VCP pipe is anywhere from 60 to 100 years and is primarily a function of proper and timely maintenance. The City's Sewer Master Plan indicated a priority for

replacement or rehabilitation of any sewer pipeline over 100 years of age. Using these criteria, over 60% of the City’s sewer collection system is recommended for lining or replacement, while approximately 10% of the system has been lined to date. In general, trenchless sewer lining extends pipeline life by approximately 60 years and generally costs less than 10% of trenched sewer replacement while also eliminating the inconvenience caused by trench construction.

Based on Best Management Practices for capital and preventative maintenance of the sewer collection system, Public Works staff, with guidance from sewer consultants, determined an “Optimum” sewer capital program with an estimated annual cost of \$5.15 million, as indicated on the Annual Sewer System Improvements & Capacity Upgrades project sheet in the FY24 CIP Budget. Given a forecast of limited Sewer Fund revenues and in an effort to reduce fee increases to residents, Public Works staff established an “Acceptable” sewer capital program with an estimated annual cost of \$3.5 million. In doing so, staff weighed risk exposure against lower program cost and was comfortable with this level of expenditure because the scope still included a significant amount of preventive maintenance and condition assessment. This would allow problems to be identified and prioritized for repair before they become larger issues, minimizing the risk of sewer backups and overflows while addressing systemwide needs, albeit over a longer period of time.

The key scope of work and difference in level of effort between each proposed CIP program – “Acceptable” and “Optimum” are shown below:

Proposed Capital Improvement Programs (CIP)		
KEY SCOPE OF WORK	ACCEPTABLE	OPTIMUM
Reline 325 miles of Sewer main pipes (80% over 80 years old)	40 years	30 years
Rehabilitate manhole (MH) structures (7,430 systemwide)	25% of MH in 40 years	60% of MH in 30 years
Televise & inspect system; flow monitor & heavy clean-out where needed	7-year cycle	5-year cycle
Dig-up & repair sewer pipes (unable to reline)	50% of Optimum	-
Pump station upgrades	10-year cycles	10-year cycles
EST. TOTAL ANNUAL PROGRAM COST	\$3.5M	\$5.15M

Sewer Use Fee Rate Adjustment Scenarios & “Smoothing” Options

The proposed new Sewer Use Fee rate calculation recommends a fixed charge plus a volumetric rate based on water consumption for both residential and commercial customers. This option allows the City to recover a portion of the fixed costs of

operating the sewer collection system while still encouraging water conservation efforts by charging customers in proportion with their burden on the sewer system as measured by water usage.

Rates Proposed in Public Hearing Notice & Revised Proposed Rates

The Proposed rates in the Public Hearing Notice for single-family residence is a fixed monthly rate of \$6.16 plus a volumetric rate of \$0.65/hundred cubic feet (hcf) of water used. Under the Proposed rates, single family residence water use is capped at 13 hcf per month, which assumes that water usage above 13 hcf is for irrigation and, therefore, does not go into the sewer collection system. The average single family residence monthly fee would increase from \$4.55 to \$11.37 in FY 2025, which is an increase of \$6.82 monthly. Commercial customers would have a fixed rate of \$6.16 plus a volumetric rate of \$1.24/ hcf. The average commercial customer discharges more wastewater into the system, so the volumetric rate reflects commercial customers' share of cost in proportion to flow. Commercial customers' sewer use will be estimated by taking 90% of water use. A copy of the public hearing notice is included as Attachment A.

Subsequent to the April 8, 2024 City Council meeting, a small revision was made to the Proposed rates. The rates were revised to account for a zero-dollar starting reserve in FY 2025 and increasing to the target reserve through FY 2029. Attachment B charts the Proposed rate structure in the Public Hearing Notice and the Revised Proposed rate structure. The Revised Proposed rate structure has a single family residential fixed monthly rate of \$6.00 plus a volumetric rate of \$0.63/hcf, while commercial customers would have a fixed rate of \$6.00 plus volumetric rate of \$1.21/hcf. The Revised Proposed rate structure will also cap residential use at 13/hcf monthly. Under this rate structure, the average residential monthly fee would increase from \$4.55 to \$11.05.

Rate Scenarios

Per City Council's direction, additional rate adjustment scenarios have been modeled by the City's consultant, Raftelis, to address the three funding "buckets" in the sewer program, including Operations, CIP and Reserves. Attachment C separately charts each of the scenarios noted above, distinguishing between Operating and CIP rates, as well as Reserve Balance thru FY 2029. Attachment C also shows the projected monthly increase to the Average Single-Family Bill for each FY. The following scenarios were developed for discussion and consideration:

Scenario 1: Operations Only (no CIP, no reserve) – *Not Recommended*

- Unable to complete two deferred CIP projects
 - Sewer pump stations rehabilitation and Civil Defense septic upgrades
- Unable to reline sewer pipes & extend life of over 80-year-old pipes
- No funding for emergency repairs
- Risk sewer back-ups & overflows due to lack of CIP
 - Contamination of stormwater channels/creeks
 - Claims due to sewer back-up into homes/facilities

- Fines by Regional Water Quality Control Board
- Unable to sustain the integrity of the sewer system

Scenario 2: Operations + \$3.5M CIP + No Reserve – *Not Recommended*

- Funds “Acceptable” level of CIP to extend life of sewer system (see table above)
- Funds two deferred CIP projects
- No funding for emergency repairs
 - Defer implementation of CIP projects to pay for emergency work
- Minimizes risk for sewer back-ups & overflows

Scenario 3 – Revised Proposed: Operations + \$3.5M CIP + Reserve Starting at \$0 in FY 2025 – **Recommended**

- Funds “Acceptable” level of CIP to extend life of sewer system (see table above)
- Funds two deferred CIP projects
- Reserve fund available for emergency repairs
- Minimizes risk for sewer back-ups & overflows

Scenario 4: Operations + \$5.15M CIP + Reserve Starting at \$0 in FY 2025 – *Not Recommended*

- Funds “Optimum” level of CIP to extend life of sewer system (see table above)
- Funds two deferred CIP projects
- Reserve fund available for emergency repairs
- Minimizes risk for sewer back-ups & overflows

Rate Smoothing Option

Raftelis has also modeled a “Smoothing” option with incremental increases in CIP funding, based on staff’s current CIP expenditure projections for FY 2025 & FY 2026. Attachment D charts the Smoothing Option thru FY 2029 and includes the monthly increase to the Average Single-Family Bill for each FY.

Smoothing Option: Operations + Reduced FY 2025 (\$1.33M) & FY 2026 (\$2.5M) CIP + Reserve

- Allows construction of two deferred active CIP projects in FY 2026
- Postpones implementation of “Acceptable” CIP projects by 2 years, to FY 2028
- Reserve fund available for emergency repairs
- Offers financial relief first three years

A comparison table for an average single-family resident bill, indicating the monthly cost and rate increase for each of the rate models discussed above, is shown in Attachment E.

In conclusion, after review of the information presented in this report, staff recommends City Council approve the Revised Proposed Sewer Rates to provide appropriate funding for operations, acceptable level of CIP, and targeted reserves as noted. Although the Smoothing Option will provide appropriate funding for operations and allow for

construction of previously deferred CIP projects, it is not ideal as it will result in some continued deferral or reduced scope of forecasted CIP projects.

Proposition 218 Noticing & Compliance

In accordance with Proposition 218, 45-day notices were mailed on February 21, 2024, to all property owners/customers of record for the public hearing on the proposed Sewer Use Fee rate structure and rate adjustments. A total of 29,197 hard copies of the notices were mailed via United States Postal Service presorted First Class Mail. Due to the required 45-day notice and the bi-monthly billing schedule of Pasadena Water & Power bills, staff did not have a sufficient window of time to include notification with the billing statements.

In addition, a press release was issued by the City's Public Information Officer on March 6, 2024, regarding the April 8, 2024, public hearing and the two March community meetings. The public hearing notice was also posted on the Public Works website www.cityofpasadena.net/public-works with both Spanish and Mandarin translations, as well as English and Spanish versions of the frequently asked questions.

Notification of the March 19 and March 20, 2024, community meetings was also posted on the City's Public Works Department webpage in both English and Spanish, and shared on the City's social media channels such as Facebook and Twitter. Information was also provided in the City Manager's Newsletter and to Council district liaisons.

The City must consider all protests and counts one written protest per parcel, filed by an owner or tenant of the parcel, in calculating a majority protest. There are a total of 29,197 sewer parcels in the City, which means at least 14,599 protests would need to be received in order to constitute as a majority protest. As of April 29, 2024, the City Clerk's office has received 300 protest letters and one letter of support for the Sewer Rate adjustments.

New Rate Implementation

Upon City Council's approval of a Sewer Use Fee rate structure and rate adjustment, a First and a Second Reading of the Updated Sewer Use Charge Ordinance will be scheduled. Staff recommends new Sewer Use Fee Rates to become effective July 1, 2024, or as soon as practical thereafter.

COUNCIL POLICY CONSIDERATION:

The recommendation is consistent with the City Council's goals to maintain fiscal responsibility and stability; and improve, maintain, and enhance public facilities and infrastructure.

ENVIRONMENTAL ANALYSIS:

The implementation of a sewer use fee increase is an administrative action that would not cause either a direct physical change in the environment or a reasonably foreseeable indirect physical change in the environment. Therefore, the proposed action is not a "project" subject to CEQA, as defined in Section 21065 of CEQA and Sections 15378(a) and (b)(4) of the CEQA Guidelines. Since the action is not a project subject to CEQA, no environmental document is required.

Furthermore, the recommended sewer use fee increases are determined to be statutorily exempt from CEQA under Public Resources Code Section 21080(b)(4) and Section 15273 (Rates, Tolls, Fares, and Charges) of the State CEQA Guidelines.

Under Section 15273, CEQA does not apply to the establishment, modification, structuring, restructuring, or approval rates, tolls, fares, or other charges by public agencies which the public agency finds are for the purpose of:

1. Meeting operating expenses, including employee wage rates and fringe benefits,
2. Purchasing or leasing supplies, equipment, or materials,
3. Meeting financial reserve needs and requirements,
4. Obtaining funds for capital projects, necessary to maintain service within existing services areas, or
5. Obtaining funds necessary to maintain such intra-agency transfers are authorized by city charter.

The rate increase falls within these parameters and therefore is exempt from CEQA.

FISCAL IMPACT:

The City currently collects an average of \$3.9 million each year in Sewer Use Fees. If the Revised Proposed Sewer Use Fee Rates are approved, an additional \$3.9 million in revenue is expected to be generated in FY 2025 to address the cost of service and to start building reserves. However, the exact amount of revenue generated, and the fiscal impact will be dependent on the Sewer Use Fee Rate approved by City Council.

Respectfully submitted,



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Approved by:



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- Attachment A – Published Public Hearing Notice
- Attachment B – Proposed and Revised Proposed Rates
- Attachment C – Rate Scenarios
- Attachment D – Rate Smoothing Option
- Attachment E – Rate Comparison Tables