

TO: BOARD OF DIRECTORS  
FROM: BRUCE BUEL *BB*  
DATE: NOVEMBER 9, 2007

**AGENDA ITEM  
E-1  
NOV. 14, 2007**

**TENTATIVELY APPROVE COMBINED WATER SYSTEM FINANCIAL PLAN**

**ITEM**

Tentatively approve Town and Blacklake Combined Water System Financial Plan and rate structure and authorize notice for January 23, 2008 hearing [RECOMMEND APPROVAL].

**BACKGROUND**

In 2005, your Honorable Board determined that the Blacklake Water Booster Station was failing and needed to be replaced and NCSD retained Boyle Engineering to design a replacement Booster Station. Boyle submitted its design in October 2006 and your Honorable Board then retained Dee Jaspar and Associates to render a second opinion. In November 2006, your Honorable Board formed a committee to explore the possibility of merging the Blacklake Water Fund with the Town Water Fund to avoid the cost of replacing the Blacklake Water Booster Station. Dee Jaspar's design memorandum was received in December 2006, at which time your Honorable Board retained Boyle to prepare a memo comparing the two designs with the concept of merging the two Water Funds. Boyle submitted their Comparative Analysis in February 2007, which summarized the two cost opinions and the likely cost of a temporary fix until the decision could be made on the merger. In March 2007, your Board received Boyle's Interconnection Schematic memo and authorized staff to install a transfer pump to replace the old Booster Station on an interim basis pending closure on the merger proposal. In April 2007, your Honorable Board retained Bob Reed of the Reed Group to prepare an equity analysis to evaluate the equity payment necessary for Blacklake Water Fund customers to pay to the Town Water Fund if a merger of the funds was to occur. Mr. Reed's initial report was received in July and your Honorable Board ordered Mr. Reed to edit the original draft report and directed staff to notify the Blacklake Customers of their choices and to hold a briefing regarding these choices. Bob Reed submitted the attached Final Report on September 14, 2007 including a section of the calculation of the equity payment. Staff mailed notice of the informational hearing on September 13, 2007 and conducted the briefing on September 25, 2007. Your Board then discussed the merger at your October 10, 2007 and October 24, 2007 Board meetings.

At the October 10, 2007 meeting, President Winn advised interested parties that they could submit alternate proposals for calculation of the equity surcharge at or by October 24, 2007, for staff analysis prior to the November 14, 2007 Board meeting. Two proposals were received at the October 24, 2007 Board Meeting – Mr. Bill Nelson submitted a Listing of Points and Mrs. Pat Eby submitted a letter questioning the validity of any equity payment. Additionally, your Honorable Board directed staff to provide the Board with a history of annexations; with a history of the Blacklake Annexation; with a discussion of precedents for an equity surcharge; with a legal opinion regarding the defensibility of an equity payment; and a comparison of charges with and without the merger.

Attached is a copy of Mr. Nelson's Listing of Points. Attached behind Mr. Nelson's Listing of Points is a reprint of these points with Staff's responses. In sum, staff disagrees with Mr.

Nelson's proposal to eliminate the cash component of the equity calculation and with Mr. Nelson's proposal to adjust the equity payment to reflect the potential production capacity of Blacklake Water System's Wells.

Next, staff has attached Mrs. Eby's letter. Although staff agrees with Mrs. Eby that Blacklake was annexed into the District and that the District owns the Blacklake Water System assets, staff disagrees with Mrs. Eby's position that an equity surcharge should have been assessed at the time of the annexation, since these assets were not co-mingled with the Town System assets. NCSD has maintained two separate funds and there was no need for the Blacklake Customers to pay an equity surcharge as long as there were two separate funds. The need for an equity surcharge arose out of the proposal to merge the funds and as set forth in the attached legal opinion; state law prohibits such a merger without a reconciliation of impacts. In other words, state law prohibits the District from using Town Assets to subsidize the merger of the two funds. The Blacklake Customers could choose to retain the existing fund structure, but if this is their choice, they will also need to pay the cost of upgrading their independent system to Title 22 Standards.

Also attached is a history of annexations; a history of the Blacklake Annexation; and a memo from Bob Reed regarding the comparison of charges with and without the merger. It should be noted that the attached legal opinion speaks to precedents.

In September, your Honorable Board directed Bob Reed to develop a two-tiered inclining block rate structure for Multi-Family Housing and to submit an addendum to the previously submitted Combined Water Systems Financial Plan. Mr. Reed's addendum, which proposes to use the same user fees per block as single-family with a lower threshold for charging the higher user fees in the second tier per apartment, was received on October 15, 2007 and reviewed by the Board at your October 24, 2007 Meeting. The Board agreed, by consensus, to delay implementation of the rates proposed in the addendum until the next rate increase.

### **RECOMMENDATION**

Staff recommends that your Honorable Board first review the attached material and listen to any public input on this issue at the hearing. Following closure of the hearing, staff recommends that the Board discuss the various proposals and information and then consider adoption of the attached Combined Water System Financial Plan. If the Board wishes to pursue the merger, staff believes that the only defensible approach is to propose an equity payment that avoids a subsidy from the Town Customers to the Blacklake Customers and staff recommends that the Board tentatively adopt the attached Financial Plan and direct staff to provide notice to the Blacklake Customers of the proposed surcharge to be considered for adoption at the Board's January 23, 2008 Meeting.

If the Board can not reach closure on this issue at this meeting or if the Board wishes to make edits to the Financial Plan, then it will not be possible to satisfy the state's requirements for noticing for a January 23, 2008 Hearing and the Board will need to reset all of the user fee, surcharge, and capacity charge hearings previously set for the January 23, 2008 Hearing.

If the Board determines that it does not wish to merge the two water systems at this time, staff respectfully requests authorization to retain Bob Reed to prepare revised Financial Plans for the two systems for subsequent Board review.

**ATTACHMENTS**

- September 14, 2007 Combined Water System Financial Plan
- Listing of Points from Bill Nelson
- Reprint of Mr. Nelson's Points with Staff Responses
- District Legal Counsel's Opinion regarding the validity of the equity payment
- History of Annexations
- History of the Blacklake Annexation
- Memo from Bob Reed regarding rates with and without merger.

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**Nipomo Community Services District  
COMBINED WATER SYSTEM  
FINANCIAL PLAN AND  
USER RATES  
FINAL REPORT**

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**Sept 14, 2007**



**THE REED GROUP, INC.**

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## I. Executive Summary

### Introduction

In 2005, The Reed Group, Inc. assisted the Nipomo Community Services District with the development of five-year financial plans for the District's water and sewer utilities. In the spring of 2007 the Nipomo Community Services District retained The Reed Group, Inc. to update financial plans and water and sewer rate recommendations for the District's Town and Blacklake Divisions. The District is considering merging the two water divisions together. This report presents analyses related to combined merging the Town and Blacklake water systems and presents a combined financial plan and water rate recommendations for the combined water systems, as well as recommends an equity surcharge for customers of the Blacklake Division that would make their investment in the water system equivalent to that already made by customers of the Town Division. Finally, this report also presents an analysis of alternative water rate structures intended to help the District meet water conservation and other objectives through refinements to the rate structure. Financial plans and sewer rate recommendations for the Town and Blacklake sewer systems are presented in separate reports.

The District is committed to securing supplemental water to mitigate the impacts groundwater usage has on the underlying groundwater basin. In September 2004, the District signed a Memorandum of Understanding (MOU) with the City of Santa Maria to acquire up to 3,000 acre-feet (AF) of water per year. In order to use water from the City of Santa Maria the District will need to construct transmission facilities to convey water to the District's service area. Plans for the most cost-effective means of conveying supplemental water are still in development. However, the financial plan presented herein includes the District's best current estimates for the cost of the project and the manner in which it may be financed. Water system buy-in and supplemental water capacity charges are not updated in this report. However, the District should consider updating these charges once plans for the supplemental water project are firmed up.

It is anticipated that a portion of the supplemental water project will need to be financed. However, the amount appears to be relatively small (less than \$1 million). As a result, the financial plan presented herein assumes that an internal loan (from the Water Funded Replacement Fund to the Supplemental Water Fund) would be utilized. The loan would be repaid from future supplemental water capacity charges. In addition to ensuring that each of the combined water system is covering appropriate operating costs and capital program needs, the financial analysis also addresses the need to meet debt service obligations, including debt service coverage.

During workshops held with the Board of Directors, we were asked to explore various rate structure alternatives. This report describes rate structure analyses performed. However, as described below, no changes to the rate structure are being made at this time. Instead, it is recommended that the District implement previously adopted water rates for 2008 and 2009. This will provide the District more time to more fully explore rate structure alternatives (for new rates that will need to be adopted in 2010 and beyond).

The remainder of this Executive Summary presents findings and recommendations related to the (1) Blacklake equity surcharge, (2) combined water system financial plan, and (3) water rates for both the combined water system. Section II provides details on the financial plans. Section III presents water rate calculations, including the equity surcharge, and discussion of alternative water rate structures.

**Equity Surcharge**

Existing customers of the Town and Blacklake water systems have each contributed to the construction, operation, and maintenance of their respective water systems based on the requirements of each system. In considering the merger of the two water systems, the District's Board of Directors requested an analysis of the relative investment made, per customer<sup>1</sup>, in both the Town and Blacklake water systems. The objective is to require whichever customers have a lesser investment in the water systems to make an additional contribution to establish equity and parity for all customers of the combined system. To achieve this, the book value of water system assets, as well as financial reserves, based the last audited financial statements (as of June 30, 2006) were expressed on a per customer basis. Then, an equity surcharge was calculated based on the difference between the relative investments within each water system.

Customers of the Town water system have a current investment of about \$4,272 per equivalent meter, whereas customers of the Blacklake water system have a current investment of about \$2,600. Therefore, to establish equity between customers in a combined water system an equity surcharge of \$1,672 per 1" equivalent meter paid by Blacklake customers is appropriate. The equity surcharge includes both investments in water system facilities, as well as cash reserves. About 20 percent of the equity surcharge reflects differences in capital investments and 80 percent is associated with differences in cash reserves.

**Exhibit I-1** summarizes the results of this calculation. The proposed equity surcharge is presented either as a lump sum amount or as a bi-monthly payment that would be imposed for a one-, two-, five-, or ten-year period. A five percent interest rate is included on any equity surcharge payments to be made over time. Details of the Blacklake equity surcharge are included in Section III of this report.

**Exhibit I-1  
Nipomo Community Services District  
Proposed Blacklake Equity Surcharges**

	Meter Size		
	Up to 1"	1 1/2"	2"
<b>Lump Sum Payment</b>	\$ 1,672	\$ 5,015	\$ 8,025
<b>Alternative Bi-Monthly Payments</b>			
For 1-Year	\$ 286.82	\$ 860.45	\$ 1,376.72
For 2-Years	\$ 146.98	\$ 440.93	\$ 705.49
For 5-Years	\$ 63.21	\$ 189.64	\$ 303.42
For 10-Years	\$ 35.52	\$ 106.56	\$ 170.50

**Combined Water System Financial Plan**

The financial plan for the combined water system was developed to cover a five-year planning period from FY 07-08 through FY 11-12. The financial plan includes estimated operating and

<sup>1</sup> The number of customers is expressed in terms of the number of equivalent 1" meters, which takes into account the higher relative demands that can be placed on the water system by customers with large meters.

maintenance costs, anticipated debt service obligations, and capital program needs, including requirements for implementing the supplemental water project.

The financial plan model was used to identify annual water rate revenue requirements for each year of the planning period. The revenue requirement is the amount needed to cover operating costs, debt obligations, and capital program needs with consideration of other revenues and financial reserves. Annual rate increases are based on the estimates of current and future costs provided by the District. Analyses sought to develop a financial strategy that would help to minimize the magnitude of annual water rate increases, while still meeting financial obligations.

The financial plan model is intended to serve a planning and management tool to assist the District in evaluating the current and future needs of the water utility. Underlying assumptions, financial objectives, and the proposed financial strategies are described in Section II of this report. Significant findings and recommendations resulting from the financial planning efforts are presented below.

- Current revenues exceed current expenditures and capital program transfers, which results in an increasing Operating Fund balance. However, this situation will change with the implementation of the supplemental water project.
- The beginning-of-year (FY 07-08) Operating Fund balance is about \$1,570,000 with a target Operating Reserve of \$1,160,000.
- The District continues to annually transfer an amount equal to depreciation into the Funded Replacement Fund. The fund has adequate cash for planned replacement and upgrade projects for the five-year planning period, and can also fund a loan in support of the financing of the supplemental water project.
- Previously adopted water rates for 2008 and 2009 appear adequate to meet the combined water system's financial needs for the next two years. Additional rate increases will be needed in 2010.
- Two remaining installment payments under the Memorandum of Understanding with the City of Santa Maria for supplemental water totaling \$525,000 will likely to become due in FY 10-11.
- The cost of supplemental water will increase operating costs and water rates when it becomes available in 2011. Increased costs will be associated with supplemental water purchases, pumping, and treatment. These increased costs are reflected in the financial plan beginning in 2011.

The proposed financial strategy for the combined water system reflects the following changes:

- The proposed Blacklake equity charge is assumed to be paid by existing customers of Blacklake through bi-monthly service charges paid over a ten-year period. Revenues from the equity surcharge accrue to the Funded Replacement Fund.
- The supplemental water project is assumed to have a total cost of \$7.5 million. It is also assumed that other water purveyors will contribute one-third (about \$2.5 million) the cost of the project. It is recommended that the remaining \$5 million in costs be funded as follows:



- o \$4.25 million from Supplemental Water Fund reserves
  - o \$0.75 million from a loan from the Funded Replacement Fund
- Supplemental water capacity charge revenue should be sufficient to cover annual debt service payments. However, the District should update the supplemental water capacity charges once a project is sufficiently defined and costs have been updated. Annual debt service is estimated to be about \$97,000 per year for ten years based on the supplemental water project assumptions contained herein.
- Water rates for the combined water system should be increased as shown below. Required water rates for 2008 and 2009 are the same as those previously adopted for the Town water system. With the merger of the two water systems, the Town water rates would also apply to customers in Blacklake. The rates for 2008 and 2009 are lower than the water rates previously adopted for Blacklake. As a result, the only rate action related to the combined water system required for the next two years is the adoption of the Blacklake equity surcharge. Because the water rates in Blacklake would effectively be reduced (relative to previously approved water rates for both 2008 and 2009), this will offset the effects of the Blacklake equity surcharge. The litigation charges should not change, but should continue until resolution of groundwater litigation issues.

January 2008	10%
January 2009	8%
January 2010	11%
January 2011	11%
January 2012	12%

**Proposed Water Rate Schedules**

This study included exploring specific water rate structure changes for the combined water system. However, because no rate increases over previously approved water rates are required for the next two years, and because rate structure analyses have not resulted in consensus on appropriate new rate structures, no rate structure changes are recommended at this time. Previously adopted rate schedules for 2008 and 2009, and well as potential future water rate schedules covering the three-year period from 2010 through 2012 without a rate structure change, are presented in **Exhibit I-2** for information purposes. The rates are estimated to generate the revenues reflected in financial plan analyses. In addition, it is recommended that the District continue to explore water rate structures changes over the next two years, and that any change be implemented beginning in 2010.

Details of the water rate structure analyses developed as part of this study are described in Section III of this report.

**Exhibit I-2  
Nipomo Community Services District  
Current and Estimated Future Water Rates**

	Current Rates (1)		Prev. Adopt. Rates (2)		Est. Future Water Rates (3)			Litigation Charge (4)
	Town	Blacklake	Jan. 2008	Jan. 2009	Jan. 2010	Jan. 2011	Jan. 2012	
<b>Bi-Monthly Service Charges</b>								
Up to 1"	\$ 20.64	\$ 22.08	\$ 22.71	\$ 24.52	\$ 27.22	\$ 30.21	\$ 33.84	\$ 6.32
1 1/2"	\$ 58.60	\$ 61.09	\$ 64.46	\$ 69.61	\$ 77.27	\$ 85.77	\$ 96.06	\$ 14.36
2"	\$ 92.81	\$ 96.24	\$ 102.09	\$ 110.25	\$ 122.38	\$ 135.84	\$ 152.14	\$ 19.92
3"	\$ 172.68	\$ 178.33	\$ 189.95	\$ 205.15	\$ 227.72	\$ 252.77	\$ 283.10	\$ 27.92
4"	\$ 286.77	\$ 295.58	\$ 315.45	\$ 340.68	\$ 378.15	\$ 419.75	\$ 470.12	\$ 36.00
6"	\$ 571.73	\$ 588.42	\$ 628.91	\$ 679.22	\$ 753.93	\$ 836.86	\$ 937.28	\$ 59.58
8"	\$ 913.83	\$ 939.98	\$ 1,005.21	\$ 1,085.63	\$ 1,205.05	\$ 1,337.61	\$ 1,498.12	\$ 68.08
<b>Water Usage Rates (\$/HCF)</b>								
Single Family Residential								
Tier 1 (0-40 HCF)	\$ 1.38	\$ 1.42	\$ 1.52	\$ 1.64	\$ 1.82	\$ 2.02	\$ 2.26	
Tier 2 (>40 HCF)	\$ 2.35	\$ 2.49	\$ 2.59	\$ 2.80	\$ 3.11	\$ 3.45	\$ 3.86	
Non-Residential (5)								
All Usage	\$ 1.74	\$ 1.73	\$ 1.91	\$ 2.06	\$ 2.29	\$ 2.54	\$ 2.84	

**Notes:**

- (1) Effective January 1, 2007 as adopted with Ordinance 2005-103.
- (2) Previously adopted with Ordinance 2005-103. No change is required at this time. Would also apply within Blacklake with merger.
- (3) Estimated future water rates to meet revenue needs. These rates assume no change in the rate structure.
- (4) No changes are proposed for the litigation charge, which applies to all water connections until resolution of groundwater litigation.
- (5) Includes multi-family, commercial, irrigation, agricultural, industrial, and construction.

**Customer Bills Impacts of Proposed Rates**

With the exception of the new equity surcharge for customers of Blacklake, no changes to previously adopted water rates are recommended at this time. Exhibit I-3 shows the change in typical single family water bills for various levels of water use in 2008. The bill calculations assume merger of the two water systems, application of previously approved Town water rates for 2008 to the combined service area, and implementation of the Blacklake equity surcharge to Blacklake customers.

While Blacklake customers will be offered the opportunity to pay the equity surcharge with a lump sum payment of \$1,672, the table below assumes the alternative \$35.52 bi-monthly surcharge would apply. It should be noted that analyses of water rates in Blacklake, without the merger of the two water divisions, would be higher than the water rates with the merger (including the equity surcharge) by 2009.

**Exhibit I-3  
Nipomo Community Services District  
Typical Single Family Water Bill Changes with 2008 Water Rates**

	Bi-Monthly Water Bills					
	Current		Proposed for 2008			
	Town	Blacklake	Town	Blacklake (1)	Change for Town	Change for Blacklake
Low Use (24 HCF)	\$ 60.08	\$ 62.48	\$ 65.51	\$ 101.03	\$ 5.43	\$ 38.55
Median Use (34 HCF)	\$ 73.88	\$ 76.68	\$ 80.71	\$ 116.23	\$ 6.83	\$ 39.55
High Use (64 HCF)	\$ 176.16	\$ 184.80	\$ 193.43	\$ 228.95	\$ 17.27	\$ 44.15
Very High Use (120 HCF)	\$ 270.16	\$ 284.40	\$ 297.03	\$ 332.55	\$ 26.87	\$ 48.15

**Notes:**

(1) Includes bi-monthly equity surcharge of \$35.52.

## II. Five-Year Financial Plan

This section of the report describes the combined water system five-year financial plan prepared for the Nipomo Community Services District. This section includes a description of fund and reserve structures and cash flows, financial plan assumptions including the capital improvement program and debt financing assumptions for capital projects, and a summary of the financial plan. Detailed exhibits of combined water system financial plan model are included in **Appendix A**, at the end of this report.

The financial plan is used to determine annual water rate revenue requirements. The annual rate revenue requirement is the amount of revenue needed from user rates to cover planned operating, maintenance, debt service, and capital program costs with consideration of other revenues, including capacity charges, as well as financial reserves.

### Fund and Reserve Structures and Cash Flows

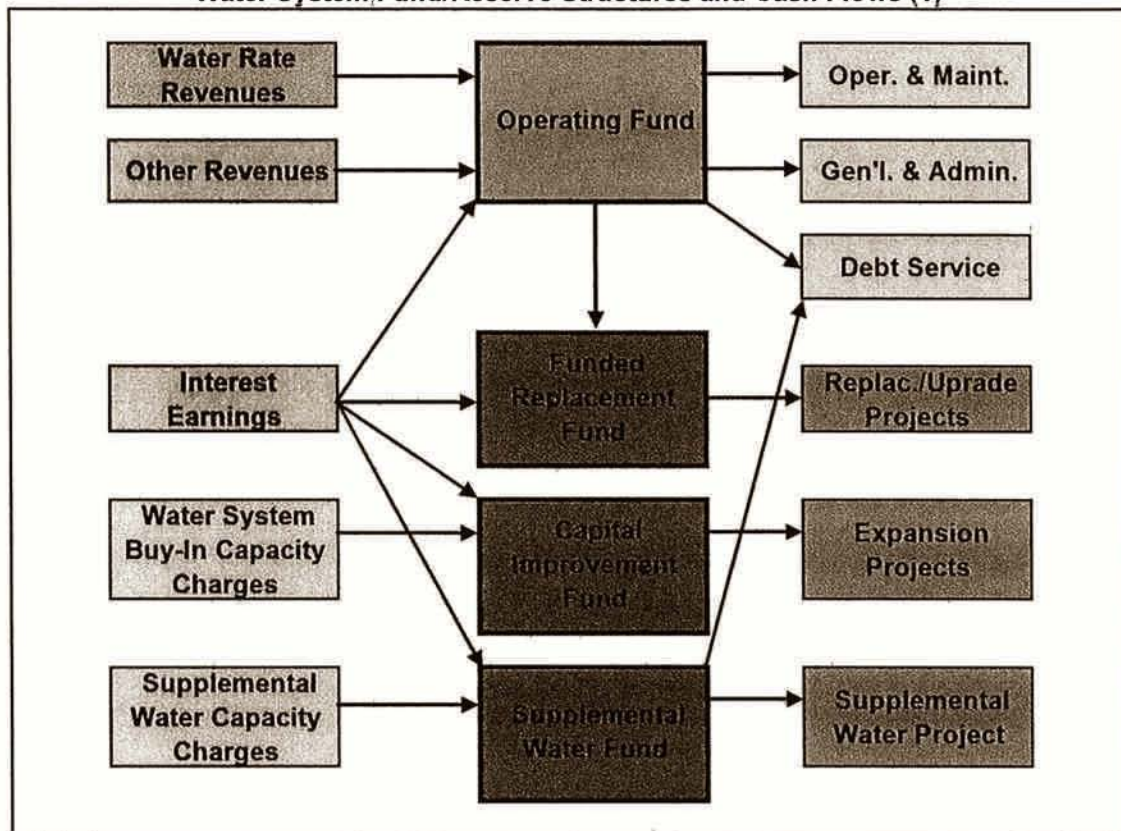
The financial plan is an annual cash flow model. As a cash flow model, it differs from standard accounting income statements and balance sheets. The financial plan models sources and uses of funds into, out of, and between the various funds and reserves of the water utility.

The financial plan model is based on the fund, reserve, and account structures currently used by the District. **Exhibit II-1** is a schematic diagram of the funds/reserves and major cash flows associated with the financial plan model.

An understanding of the fund/reserve structure is helpful in understanding the financial plan worksheets that model annual cash flows through the water utility from one year to the next. The fund/reserve structure is comprised of:

- **Operating Fund** – The Operating Fund is the primary fund within the water utility. Most of the water system's revenues, including rate revenues, flow into the Operating Fund and all operating and maintenance costs, including capital outlay items and debt service payments, are paid out of this fund. Funds are also transferred from the Operating Fund to the Funded Replacement Fund to help pay for capital projects intended to rehabilitate and upgrade facilities.
  - **Operating Reserve** – The District currently has a policy goal to maintain Operating Reserves within the Operating Fund equal to 50 percent of annual operating and maintenance costs for the water system. The purpose of the Operating Reserve is to provide working capital and funds for unplanned operating and maintenance expenditures. The balance in the combined water system Operating Fund is currently above the minimum target Operating Reserve.
  - **Uncommitted Fund Balance** – The balance in the Operating Fund in excess of the target amount for the Operating Reserve is shown in the financial plan exhibits (see Appendix A) as Uncommitted Fund Balance. After all other obligations are met the Uncommitted Fund Balance is available to offset rate increases, and the financial plan model generally seeks to reduce any Uncommitted Fund Balance over time.

Exhibit II-1  
Nipomo Community Services District  
Water System Fund/Reserve Structures and Cash Flows (1)



**Notes:**

(1) Excludes funds related to the 2003 COP proceeds and property taxes.

- **Funded Replacement Fund** – The Funded Replacement Fund is used to account for capital projects intended to rehabilitate or upgrade the water system. The primary source of money for the Funded Replacement Fund is a transfer from the Operating Fund. The District currently transfers an amount equal to annual depreciation into the Funded Replacement Fund.
- **Capital Improvement Fund** – The Capital Improvement Fund is used to account for revenues and expense related to the water system buy-in capacity charges. Capital projects funded from the Capital Improvement Fund are those needed for system expansion and to accommodate the needs of new development.
- **Supplemental Water Project Fund** – A separate fund was created by the District to account for supplemental water capacity charges and expenditures related to implementing the supplemental water supply. Proceeds from the anticipated COPs to be issued for the supplemental water pipeline project will be deposited into this fund. Supplemental water capacity charges will be applied against project costs and related debt service.
- **Property Tax and 2003 COP Funds** – The District also maintains funds to account for proceeds from the issuance of Certificates of Participation (COPs) in 2003 and also to

account for property tax revenues. Property taxes have been pledged for payment of debt service related to the 2003 COPs. While property taxes and the 2003 COPs were considered in financial analyses, they are independent of general operations and are not reflected in the exhibits contained in Appendix A.

### **Financial Plan Assumptions**

The financial plan was created to reflect the proposed FY 07-08 budget and financial condition as of the beginning of the fiscal year. The financial plan also reflects planned capital improvement program expenditures, as identified by staff for the five-year planning period.

The process used to develop the financial plan involved estimating future revenues and expenditures based on growth projections, inflation and interest rates, anticipated capital improvement needs, and other information. The District does not have formal estimates of future operating and maintenance costs, and capital improvement needs are defined at a planning level. The financial plan is based on the best available information and assumptions are believed to be reasonable; however, no assurance can be provided as to the accuracy and completeness of the estimates.

### **Basic Assumptions**

**Exhibit II-2** summarizes the basic assumptions reflected in the financial plan model, as described below.

- *Inflation Rates* – Operating costs are inflated largely based on a factor for general inflation. An annual inflation rate of 3.0 percent was used for operational costs.
- *Interest Rates* – The District earns interest on its fund and reserve balances. Most of the District's available cash is invested in the Local Agency Investment Fund (LAIF). An annual return on fund and reserve balances is assumed to be 4.5 percent per year estimated on the beginning-of-year balances. The current interest earnings on funds deposited with LAIF is about 5.2 percent, however, the 4.5 percent assumption is more consistent with long-term averages. The assumption reflected herein is therefore somewhat conservative. The District also pays interest on debt obligations within the water utility. Interest rates and payments on existing obligations are those contained in existing contracts and repayment schedules.
- *Growth Projections* – For purposes of financial planning, a conservative annual customer growth rate of 1.0 percent is assumed for the Town Division and zero percent for the Blacklake Division. Actual growth is expected to be about 2.3 percent. However, because financial performance (in particular capacity charge revenue) is sensitive to the growth assumption, a lower assumption was used herein.
- *Water Conservation* – Average water use per account is assumed to decrease by 0.5 percent each year of the planning period. That is, customers will use, on average, slightly less water each year. Reduced water usage is expected to result from increased water conservation efforts (public education and outreach) as well as increased costs associated with water and sewer services.

Exhibit II-2  
Nipomo Community Services District  
Summary of Financial Plan Assumptions

Interest Earnings	4.5%					
General Inflation Rate	3.0%					
Operating Reserve - Water	50% of operating expenditures					
Customer Growth Rate						
Town Division	1.0% per year					
Blacklake Division	0.0% per year					
Water Conservation Factor	0.5% per year					
	FY 06-07	FY 07-08	FY 08-09	FY 09-10	FY 10-11	FY 11-12
<b>No. of Accounts</b>						
Town - Water	3,428	3,462	3,497	3,532	3,567	3,603
Blacklake - Water	589	589	589	589	589	589
Water System - Combined	4,017	4,051	4,086	4,121	4,156	4,192
Equivalent Meters	4,215	4,257	4,300	4,343	4,386	4,430
<b>Water Sales</b>						
Combined Water Sales (HCF)	1,137,593	1,143,000	1,149,000	1,155,000	1,161,000	1,167,000
Combined Water Sales (AF)	2,612	2,624	2,638	2,652	2,665	2,679
Sales per Acct. (AF)	0.65	0.65	0.65	0.64	0.64	0.64
<b>Water Production by Source (AF)</b>						
Mesa Groundwater	2,902	2,916	2,931	2,946	2,298	1,310
Supplemental Water	-	-	-	-	663	1,667
Total Water Production	2,902	2,916	2,931	2,946	2,961	2,977
Production per Acct.						
Unaccounted for Losses	10%	10%	10%	10%	10%	10%
<b>Variable Water Supply Costs (\$/AF)</b>						
Groundwater Pumping	\$ 175	\$ 180	\$ 185	\$ 191	\$ 197	\$ 203
Supplemental Water					\$ 1,200	\$ 1,200
Supplemental Water Pumping					\$ 96	\$ 99
Supplemental Water Treatment					\$ 13	\$ 13
<b>Capacity Charges</b>						
Water Buy-In	\$ 2,599	\$ 2,713	\$ 2,794	\$ 2,878	\$ 2,965	\$ 3,054
Supplemental Water	\$ 11,556	\$ 12,062	\$ 12,424	\$ 12,797	\$ 13,180	\$ 13,576
<b>Supplemental Water Project Loan from Replacement Fund (FY 08-09)</b>						
Amount of Debt	750,000					
Interest Rate	5.0%					
Term	10 years					
Annual Payment	97,128					

- *Customer Account and Water Use Data* – In developing the financial plan model, detailed customer account and water use data were obtained for the period from June 2006 through May 2007. Additional information on the current number and type of customers is provided in Sections III of this report.
- *Water Production* – Water sales are based on past sales and growth and conservation assumptions described above. Water production is greater than water sales due to unaccounted for system losses, which is typically in the range of 6 to 12 percent. While losses may vary, a loss rate of 10 percent has been assumed in the financial plan models. Currently groundwater comprises 100 percent of water supplies of the District's water supplies. The District is working to obtain supplemental water from the City of Santa Maria in order to mitigate impacts of groundwater withdrawals on the groundwater basin. The financial plan model reflects an assumption that by January 2011 about 56 percent of the District's water supplies will come from supplemental water, with 44 percent from the existing groundwater basin.

- *Capacity Charge Revenues* – Capacity charge revenues reflected in the financial plans are based on the current capacity charge schedules, as well as customer growth and annual inflationary fee increases. The District annually increases capacity charges by the average change to the Consumer Price Indices for the San Francisco bay area and the Los Angeles area. Inflationary increases of 3.0 percent per year for capacity charges are included in this study.
- *Loan for Supplemental Water Project* – As described in greater detail below, a \$750,000 loan from the Funded Replacement Fund to the Supplemental Water Fund is assumed to provide adequate funds for the supplemental water project. This loan is assumed to have a 10-year term and interest rate of 5.0 percent. It would be repaid from future supplemental water capacity charges.

**Water Supplies**

Currently the District obtains 100 percent of its water supply from groundwater from the Nipomo hydrologic sub-area of the greater Santa Maria groundwater basin. However, the District's use of groundwater is limited to having no impact on the basin's water supplies. As a result of recent legal actions to adjudicate the groundwater basin, the District has initiated steps to acquire supplemental water to mitigate the effects of groundwater withdrawals.

In September 2004, the District and City of Santa Maria entered into a Memorandum of Understanding (MOU) to establish terms and conditions for a contract for up to 3,000 AF per year of supplemental water from the City. Under the terms of the MOU the District must pay a \$750,000 reservation fee in installments as presented below.

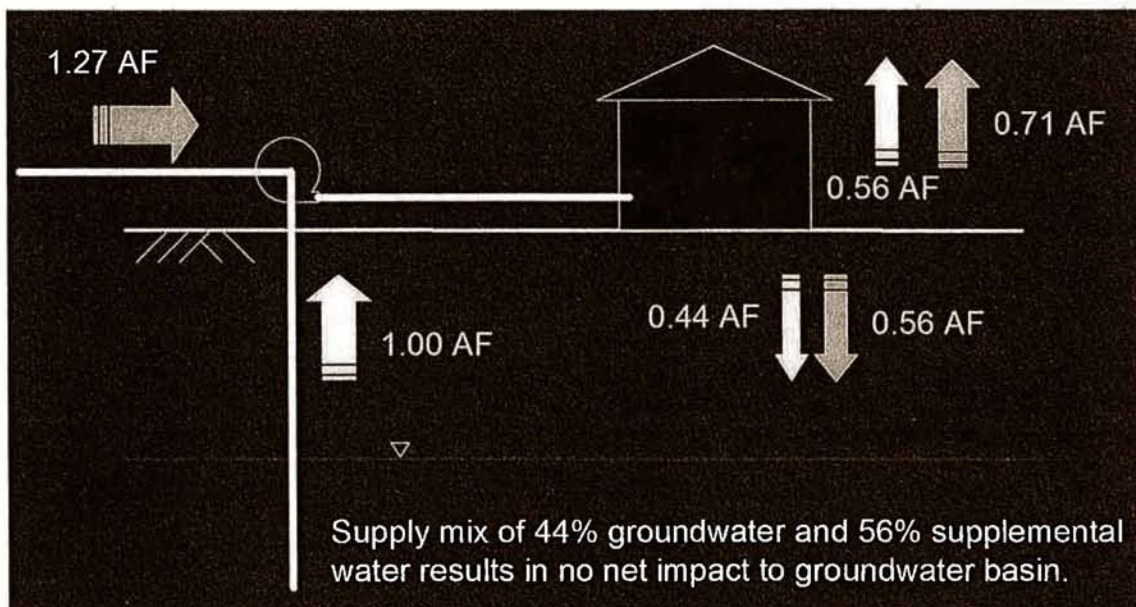
<u>Installment</u>	<u>Amount</u>	<u>Est. Date</u>
MOU Date	\$37,500	Sept. 2004
Contract Date (after CEQA)	\$187,500	Fall 2005
Construction Complete	\$225,000	Fall 2010
First 300 AF Delivered	\$300,000	Spring 2011

Water delivered under the agreement will cost \$1,250 per AF, although the reservation fee will be credited back at \$50 per AF over the first 15,000 AF delivered. The District needs to construct a transmission pipeline to convey water from the City to the District's service area.

In order to mitigate any impacts on the groundwater basin the District estimates that it will need a water supply mix of 44 percent groundwater and 56 percent supplemental water. As shown graphically in **Exhibit II-3**, for each AF of groundwater extracted from the basin an estimated 44 percent returns to the basin while 56 percent is consumed or otherwise leaves the basin. Each AF of imported supplemental water will add 44 percent to the basin, while 56 percent is consumed. The financial analyses presented herein assume that the District will utilize a 44 percent groundwater and 56 percent supplemental water supply mix beginning in January 2011.



**Exhibit II-3  
Nipomo Community Services District  
Groundwater and Supplemental Water Supply Strategy**



### Capital Improvement Program

At present, the District is nearing completion of a 20-year water system master plan and details for implementing the supplemental water project. For purposes of this study, District staff prepared a five-year capital improvement plan for the combined water system. Financial plan exhibits contain in Appendix A list each project, estimated cost, year of construction, and fund from which each project will be funded. Replacement/upgrade project costs are assigned to the Funded Replacement Fund, expansion costs are assigned to the Capital Improvement Fund, and supplemental water project costs are reflected in the Supplemental Water Fund.

### Supplemental Water Project Costs

As described above, the District is currently working to obtain 3,000 AF per year of supplemental water through a contract with the City of Santa Maria. A Memorandum of Understanding (MOU) calls for payments totaling \$750,000 in several installments to solidify the contractual arrangement. In addition, the District has estimated that it may cost about \$7.5 million to construct needed transmission facilities to convey supplemental water from the City to the District's service area. Water under the contract with Santa Maria would cost the District \$1,250 per AF. This cost of water will be reduced by \$50 per AF for the first 15,000 AF of water delivered as reimbursement of initial installment payments. Supplemental water pumping and treatment costs are estimated to add about \$109/AF to the cost of supplemental water when deliveries begin in 2011.

In 2005 the District adopted a supplemental water capacity charge to provide funds for the supplemental water project. As of the beginning of FY 07-08 the Supplemental Water Fund has about \$2.3 million. Annual supplemental water capacity charge and interest revenue is estimated to exceed \$500,000 per year.

While the District is still developing plans for constructing needed facilities to convey supplemental water to the District's service area, the financial plan presented herein assumes a \$7.5 million project cost, which will be financed as follows:

- \$2.5 million paid by other water purveyors for 1,000 AF of the 3,000 AF capacity in the supplemental water pipeline
- \$4.25 million from current Supplemental Water Fund reserves and anticipated future revenues
- \$0.75 million from a loan of available reserves in the water system Funded Replacement Fund.

After construction of the supplemental water project future supplemental water capacity charge revenues are to be applied towards supplemental water loan repayment, and to offset a portion of the cost of supplemental water purchases.

While not included within the scope of this project, the District should update the supplemental water capacity charge calculation once the supplemental water project is more clearly defined and more accurate cost estimates obtained. Current capacity charges are based on a project cost of about \$6 million, with no debt financing.

As with the previous financial plan, the financial strategy herein assumes that the District will make 1,000 AF/year of conveyance capacity in the planned transmission facilities available to other purveyors, and that the purveyor(s) would pay a proportionate share of transmission facility costs. Details of any arrangement with other purveyors are unknown at this time and beyond the scope of this study.

### **Financial Plan Findings and Conclusions**

The preceding portion of this section describes the basic framework and assumptions underlying financial analyses. Specific findings and conclusions pertaining to the combined water system is presented below, beginning with a description of the current situation.

Proposed increases to water rates are the same as those previously adopted for the Town Division water system. The current financial condition of the combined water utility is stronger than previously estimated at this point in time with the previous financial plan. This is largely due to the fact that the prior financial plan had assumed that the supplemental water project would be completed by now, with supplemental water deliveries beginning in FY 07-08.

Currently, the combined water system has:

- Budgeted expenditures and transfers that exceed current revenues, which results in a slightly growing Operating Fund balance.
- A beginning-of-year (FY 07-08) Operating Fund balance of about \$1,570,000, with a target Operating Reserve of \$1,160,000.
- The combined water system Funded Replacement Fund has adequate cash for planned replacement and upgrade projects for the five-year planning period, and can also provide \$0.75 million in a loan to help finance the supplemental water project.

Water rates and other Operating Fund revenues should normally cover all operating and maintenance costs, plus providing ongoing support for capital replacement and upgrade needs through annual transfers to the Funded Replacement Fund. Current water rates and other revenues meet this requirement. However, once the District begins receiving supplemental water from the City of Santa Maria annual operating costs will increase significantly. In addition, the District will need to maintain water rates and other revenues at levels sufficient to meet debt service requirements. As a result, continued annual water rate increases are needed and recommended.

The proposed overall average annual rate increases needed to meet estimated financial obligations are shown below. The increases for 2008 and 2009 are the same as those previously approved by the District (with rates already adopted). The increases for 2010 through 2012 are estimates.

	<u>Overall Average</u> <u>Rate Increase</u>
January 2008	10%
January 2009	8%
January 2010	11%
January 2011	11%
January 2012	12%

At present, water rates generate about \$2.6 million annually. Future supplemental water costs including pumping and treatment will total about \$2.2 million annually, representing a potential increase in the annual water rate revenue requirement approaching 100 percent. However, the proposed supplemental water capacity charge (see Section V) should reduce the net cost of supplemental water to about \$200,000 to \$300,000 per year (after paying related supplemental water debt service), and groundwater pumping costs will be reduced more than \$300,000 annually with reduced groundwater pumping. Therefore, the proposed rate increases should be sufficient to cover the added cost of supplemental water through the planning period.

**III. Water Rates**

This section of the report describes proposed water rates for the combined water system. A five-year rate plan is presented. This section also includes information on the current water rates, customer account and water use data, the proposed Blacklake equity surcharge, evaluation of potential rate structure changes, and the impact of proposed rates on typical water bills.

**Current Water Rates**

**Exhibit III-1** summarizes the current water rates of both the District's Town and Blacklake Divisions. Water rates include a fixed bi-monthly service charge based on the size of the water meter. Single family residential customers are subject to a two-tier commodity rate structure, while other customer classes are subject to a uniform commodity rate. In addition, the District maintains a litigation charge applicable to all water customers to help defray the costs of litigation regarding the adjudication of the groundwater basin. Current water rates became effective in January 2007.

**Exhibit III-1  
Nipomo Community Services District  
Current (2007) Water Rates**

	Town Division	Blacklake Division	Litigation Charge (2)
<b>Bi-Monthly Service Charges</b>			
Up to 1"	\$ 20.64	\$ 22.08	\$ 6.32
1 1/2"	\$ 58.60	\$ 61.09	\$ 14.36
2"	\$ 92.81	\$ 96.24	\$ 19.92
3"	\$ 172.68	\$ 178.33	\$ 27.92
4"	\$ 286.77	\$ 295.58	\$ 36.00
6"	\$ 571.73	\$ 588.42	\$ 59.58
8"	\$ 913.83	\$ 939.98	\$ 68.08
<b>Water Usage Rates (\$/HCF)</b>			
Single Family Residential			
Tier 1 (0-40 HCF)	\$ 1.38	\$ 1.42	
Tier 2 (>40 HCF)	\$ 2.35	\$ 2.49	
Non-Residential (3)			
All Usage	\$ 1.74	\$ 1.73	

**Notes:**

- (1) Effective January 1, 2007 as adopted with Ordinance 2005-103.
- (2) Applies to all water connections in both the Town and Blacklake Divisions.
- (3) Includes multi-family, commercial, irrigation, agricultural, industrial, and construction

Average bi-monthly water use for single family customers is 46 HCF<sup>2</sup> and median usage is 34 HCF. A typical water bill (with median usage) for single family customer within the Town with a meter size 1" or less is currently \$73.88, including the litigation charge. A single family customer using the same amount of water in Blacklake would pay \$76.68 under current water rates.

**Current Customer Accounts and Water Use Data**

The District currently provides water service to about 4,000 customers. **Exhibit III-2** summarizes the current number of customer accounts by meter size for both divisions. The Town Division includes about 3,400 customers and the Blacklake Division includes about 600 customers.

Exhibit III-2  
Nipomo Community Services District  
Summary of Combined Water System Accounts

	5/8"	3/4"	1"	1 1/2"	2"	3"	4"	Total
<b>Combined Water System</b>								
Single Family	2,341	13	1,090	1	3	-	-	3,448
Multi-Family	240	1	147	-	-	1	2	391
Commercial	32	2	32	13	10	1	-	90
Irrigation	4	-	51	19	7	1	-	82
Agricultural	-	1	-	-	1	-	-	2
Outside	1	3	-	-	-	-	-	4
<b>Total</b>	<b>2,618</b>	<b>20</b>	<b>1,320</b>	<b>33</b>	<b>21</b>	<b>3</b>	<b>2</b>	<b>4,017</b>
Equiv. Mtrs.	2,618	20	1,320	99	101	27	30	4,215
Hydr. Cap. Factor	1.0	1.0	1.0	3.0	4.8	9.0	15.0	

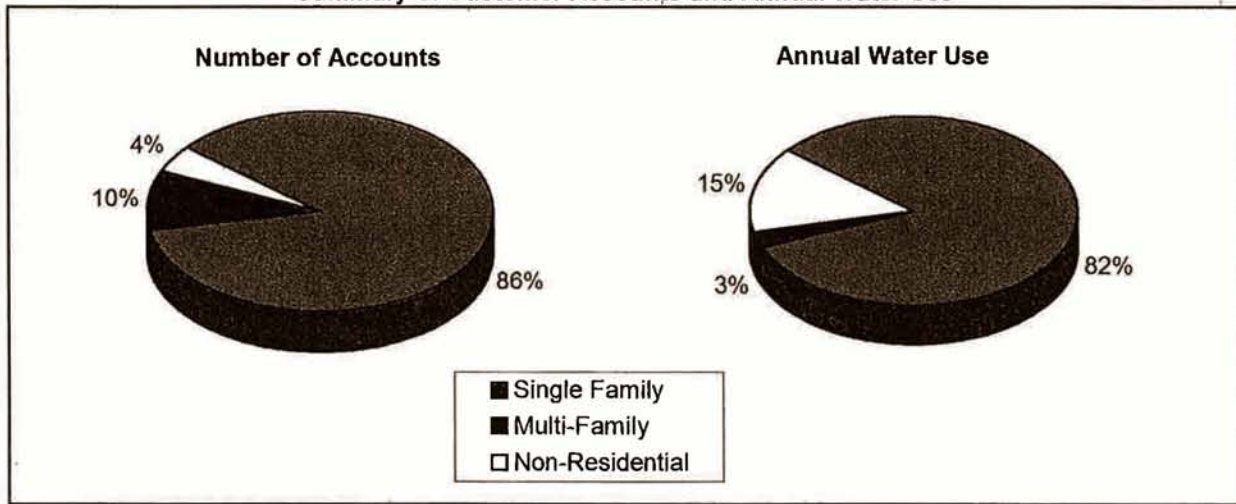
**Exhibit III-3** graphically summarizes the number of customer accounts and annual water use by customer class.

Critical to the analysis of any tiered rate structure is the analysis of water use characteristics. The amount of revenue generated from each tier is related to each customer's bi-monthly water usage. Therefore, tier rate analysis required obtaining detailed water use information for each customer account.

The District's current water rates include tiers for single family residential customers because this customer class exhibits fairly homogeneous water use characteristics. Other customer classes exhibit diverse water use patterns and tiered rate structures are less effective as a conservation tool in such cases. Tiered rates can be developed for multi-family residential customers on a per-dwelling-unit basis, and a growing number of utilities are using water budget-based tier structures for irrigation accounts. Water budget-based rates, however, require determining a water budget based on irrigated area, evapotranspiration data, and potentially plant types. The additional administrative complexity of such structures must be weighed with other considerations when considering tier structures for non-single family customer classes.

<sup>2</sup> 1 HCF = 100 cubic feet = 748 gallons.

Exhibit III-3  
Nipomo Community Services District  
Summary of Customer Accounts and Annual Water Use



Single family water use varies throughout the year based on seasonal irrigation demands. Water use also varies for other reasons as well including number of people per household, landscape characteristics, parcel size, personal habits, and other factors. Even with this variation, single family water usage characteristics are more homogeneous than other customer classes.

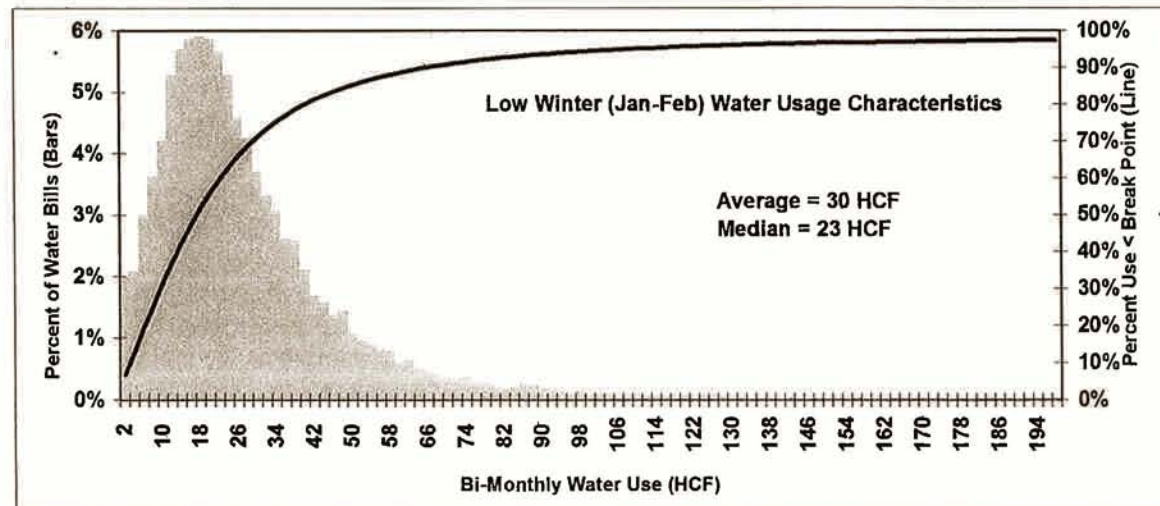
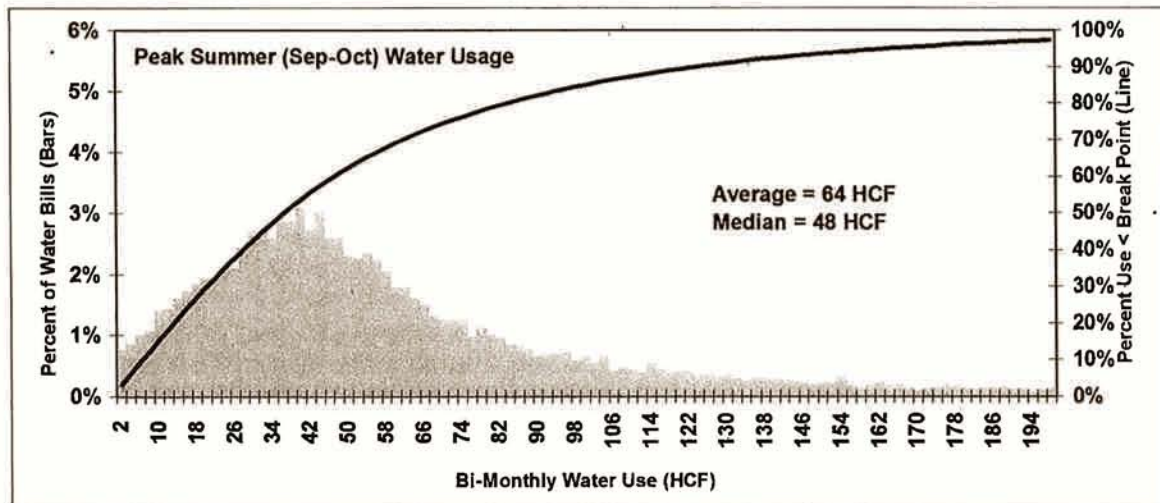
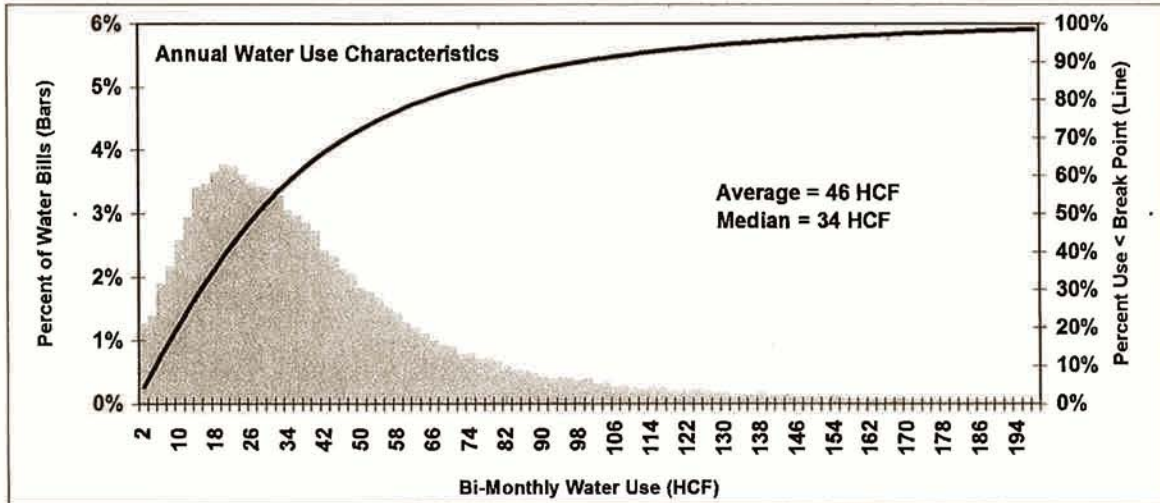
**Exhibit III-4** provides water use frequency distributions for single family customers in the combined water system. Individual graphs summarize bi-monthly water use on an annual basis, during the peak summer billing period (September-October) and during the low use winter billing period (January-February). Average and median use is shown for each graph. The bell-shaped shaded region of each graph provides a histogram showing the number of customer bills with various levels of water usage. The curved line indicates the percentage of water use below a specified level of use. The line in the top (annual) graph is critical to tier rate design in that it indicates that amount of water that would be sold within any tier once tier break points are established. This information is used later in this section in the development of the proposed tiered water rates for single family customers.

The data presented in Exhibit III-4 reflects water use characteristics for the past 5 years.

**Blacklake Equity Surcharge**

As the District is considering the merger of the water systems for the Town and Blacklake Divisions, one unresolved issue is the relative difference in the investment made into the respective water systems by existing customers of the two systems. Customers of each system have contributed to the construction and investments made into each water system, but the relative investments in each system vary. This study included evaluating the value of water system assets within each water system, as well as financial reserves, as reflected in audited financial statements and expressing this information on a per-account basis. The difference in the value of water system assets and financial resources between the two water systems would be the basis for an equity surcharge to be paid by the customers than have made a lesser relative investment.

Exhibit III-4  
Nipomo Community Services District  
Water Use Characteristics for Single Family Residential Customers



Financial information used in preparing the District's audited financial statements ending June 30, 2006 was used for the equity analysis. **Exhibit III-5** presents asset and financial resource information and the resulting calculation of a proposed equity surcharge.

Exhibit III-5  
Nipomo Community Services District  
Summary of Water System Assets and Financial Reserves as of June 30, 2006

	Town Division				Blacklake Division		
	Water Operating Town (Fund 120)	Water Capacity (Fund 700)	Funded Depreciation Town Water (Fund 800)	Town Division Totals	Water Operating Blacklake (Fund 140)	Funded Depreciation Blacklake Water (Fund 820)	Blacklake Division Totals
<b>Water System Assets</b>							
1520 Water - Pumping	\$ 1,598,264	\$ 774,742	\$ 192,373	\$ 2,565,379	\$ 1,576,268	\$ 39,670	\$ 1,615,938
1525 Water - Transmission	\$ 1,157,964	\$ 1,238,291		\$ 2,396,255			\$ -
1530 Water - Distribution	\$ 475,714	\$ 79,385	\$ 116,603	\$ 671,682	\$ 88,047	\$ 2,749	\$ 70,798
1535 Water - Contributed	\$ 6,147,216			\$ 6,147,216	\$ 505,732		\$ 505,732
1540 Buildings	\$ 55,188			\$ 55,188			\$ -
1545 Machinery & Equipment	\$ 82,129		\$ 126,822	\$ 208,951	\$ 9,800	\$ 30,845	\$ 40,445
1550 Computer Equipment	\$ 65,759			\$ 65,759	\$ 7,442		\$ 7,442
1555 Office Furniture & Fixtures	\$ 9,310			\$ 9,310			\$ -
1560 Land and Land Rights	\$ 43,500	\$ 235,739		\$ 279,239			\$ -
1570 Vehicles	\$ 102,507			\$ 102,507	\$ 15,667		\$ 15,667
1590 Work In Progress		\$ 30,125		\$ 30,125		\$ 13,593	\$ 13,593
1595 Accumulated Depreciation	\$ (4,396,254)	\$ (371,827)	\$ (33,851)	\$ (4,801,932)	\$ (1,103,130)	\$ (4,104)	\$ (1,107,234)
<b>Book Value of Water System Assets</b>	<b>\$ 5,341,297</b>	<b>\$ 1,986,435</b>	<b>\$ 401,947</b>	<b>\$ 7,729,679</b>	<b>\$ 1,079,826</b>	<b>\$ 82,553</b>	<b>\$ 1,162,379</b>
<b>Financial Reserves</b>							
1099 Cash Balance	\$ 899,909	\$ 4,654,295	\$ 1,776,215	\$ 7,330,419	\$ (25,287)	\$ 491,609	\$ 466,322
1210 A/R - Utility Billing	\$ 36,852			\$ 36,852	\$ 30,479		\$ 30,479
1220 Unbilled A/R - Utility Billing	\$ 331,000			\$ 331,000	\$ 29,000		\$ 29,000
1240 Receivable - Other	\$ 9,902			\$ 9,902			\$ -
2135 Accrued Interest Receivable	\$ 10,750	\$ 51,732	\$ 19,919	\$ 82,401	\$ 90	\$ 5,514	\$ 5,604
2100 Accounts Payable	\$ (47,143)	\$ (4,594)		\$ (51,737)	\$ (11,333)	\$ (2,160)	\$ (13,493)
2110 Refunds Payable - MQ	\$ (939)			\$ (939)			\$ -
2120 Construction Meter Deposits	\$ (11,500)			\$ (11,500)			\$ -
2130 Compensated Absences Payable	\$ (23,005)			\$ (23,005)	\$ (2,397)		\$ (2,397)
2320 Accrued Wages	\$ (4,352)			\$ (4,352)	\$ (968)		\$ (968)
2450 Deposit - Pomeroy Water Line				\$ -	\$ (24,170)		\$ (24,170)
2510 Revenue Bonds - Current Portion	\$ (9,000)			\$ (9,000)			\$ -
2610 Revenue Bonds Payable	\$ (129,000)			\$ (129,000)			\$ -
<b>Financial Reserves</b>	<b>\$ 1,063,474</b>	<b>\$ 4,701,433</b>	<b>\$ 1,796,134</b>	<b>\$ 7,561,041</b>	<b>\$ (4,586)</b>	<b>\$ 494,963</b>	<b>\$ 490,377</b>
<b>Total of Assets and Reserves</b>	<b>\$ 6,404,771</b>	<b>\$ 6,687,868</b>	<b>\$ 2,198,081</b>	<b>\$ 15,290,720</b>	<b>\$ 1,075,240</b>	<b>\$ 577,516</b>	<b>\$ 1,652,756</b>
No. of Equivalent Meters				3,579			636
Water System Assets per Equivalent Meter				\$ 2,160			\$ 1,829
Financial Reserves per Equivalent Meter				\$ 2,112			\$ 772
<b>Total Assets and Reserves per Equivalent Meter</b>				<b>\$ 4,272</b>			<b>\$ 2,600</b>
	<b>Alternative Bi-Monthly Payments Over:</b>						
	<b>Lump Sum</b>	<b>1 Year</b>	<b>2 Years</b>	<b>5 Years</b>	<b>10 Years</b>	<b>Interest</b>	
<b>Blacklake Equity Surcharge (\$/ Eq. Mtr.)</b>	\$ 1,672	\$ 286.82	\$ 146.98	\$ 63.21	\$ 35.52	5.0%	
<b>Annual Revenue from Each Alternative</b>	\$ 1,062,594	\$ 1,093,801	\$ 560,514	\$ 241,069	\$ 135,462		

The book value (original cost less accumulated depreciation) of water system assets of the Town Division totals about \$7.73 million. The book value of water system assets of the Blacklake Division totals about \$1.16 million. Cash reserves, adjusted for short term receivables, short term payables, deposits, and outstanding long-term debt, for the Town Division totals about \$7.56 million. Adjusted cash reserves for the Blacklake Division totals about \$490,000.

The denominator used to determine the equity surcharge is the number of 1" equivalent meters. This is similar to the number of accounts, but reflects the relative capacities of different meter sizes.



The Town Division has 3,579 equivalent meters and the Blacklake Division has 636 equivalent meters.

The relative investment in water system assets and financial resources of customers in the Town and Blacklake Divisions is \$4,272 and \$2,600 per 1" equivalent meter, respectively. The difference between these two amounts is \$1,672 and represents the amount that customers of Blacklake should make to establish equity and parity in a combined water system.

Conceivably the equity surcharge could be paid by Blacklake water system customers in a single lump sum payment. However, alternative payment approaches are possible, which would allow the surcharge to be paid over time. At the request of the District, bi-monthly payments that would last for one, two, five, or ten years were developed for the Board of Director's consideration. Bi-monthly payment alternatives all assume a 5.0 percent interest rate.

If paid entirely in a lump sum, the Blacklake equity surcharge would provide about \$1.06 million for the combined water system. The District could potentially allow each customer to elect whether to pay the lump sum amount or one or more of the bi-monthly surcharge approaches. For purposes of preparing the financial plan included in Section II of this report, it was assumed that the equity surcharge would be paid over ten years by all Blacklake customers. This is the most financially conservative assumption for planning purposes. Any other payment approach would result in the District receiving equity surcharge revenues sooner. The bi-monthly equity surcharge paid over a ten year period would be \$35.52 for water meters up to 1". A complete equity surcharge schedule for different meter sizes and payment periods is included in Exhibit I-1, in the Executive Summary of this report.

## **Water Rate Calculations**

Because the financial plan analyses presented in Section II indicate that previously adopted water rates are sufficient to meet the combined water utilities needs for the next two years, no further water rate changes are recommended at this time. However, the study did include exploring other water rate structures (which might have been adopted had previously adopted water rates been shown to be insufficient for near-term needs), and the results of those analyses are described herein.

The calculation of water rates involves a three-step process. First, the annual water rate revenue requirement must be determined. The water rate revenue requirement is that amount of revenues to be generated annually to meet operating and capital program needs with consideration of other water system revenues and reserves. Annual water rate revenue requirements were determined using the five-year financial plan model described in the previous section. The second step in the rate setting process is a cost of service analysis accomplished by the allocation of water system costs to rate components. Finally, the third step in the process is rate design and the development of water rate schedules.

### **Annual Water Rate Revenue Requirement**

The annual water rate revenue requirements were determined for each fiscal year of the planning period using the five-year financial planning model. Because the District has adjusted water rates at the beginning of each calendar year, fiscal year revenue requirements were converted into calendar year revenue requirements. Estimated current calendar year water rate revenues as well as future water rate requirements for the next five years are summarized below. The percentage change in the rate revenue requirement differs from the percentage change in overall level of rates

due to the merger of the two divisions and rates (in 2008), growth in the customer base, and estimated increased water conservation.

	<u>Water System</u> <u>Rate Rev. Reqmt.</u>	<u>Percent</u> <u>Change</u>
2007	\$2,656,000	
2008	\$2,911,000	9.6%
2009	\$3,151,000	8.2%
2010	\$3,502,000	11.1%
2011	\$3,893,000	11.2%
2012	\$4,368,000	12.2%

Current water rates differ for the Town and Blacklake Divisions, but this study assumes they will be consolidated in 2008. The previously adopted water rate schedules for the next two years, as well as estimated rate increases for the following three years, are estimated to generate the amount of revenue listed above. Annual rate calculations also reflect assumptions for new development and increased water conservation, both of which have an impact on rate revenues separate from the rate structures themselves.

### **Cost of Service Analysis**

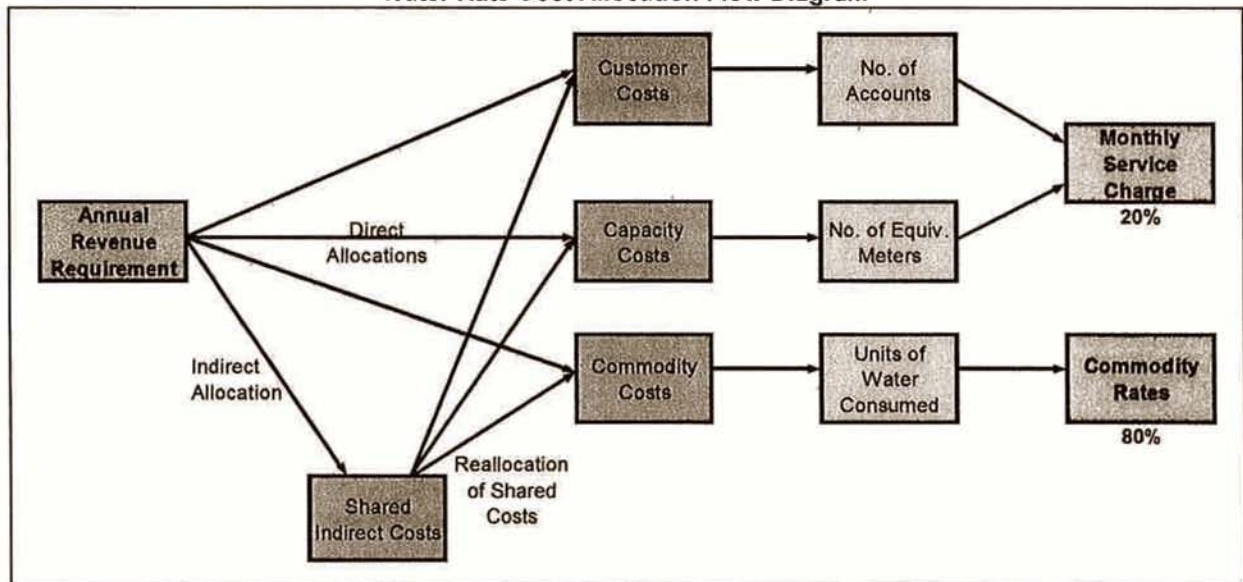
Cost allocation is the method by which the annual water rate revenue requirement is recovered from each customer class based on the cost of providing water service. The cost allocation process is shown schematically in **Exhibit III-6**. There are a number of ways to allocate costs for rate setting purposes. Some are rather complex and require detailed knowledge of water system costs, cost drivers, and customer water use characteristics (including peaking characteristics). Others are somewhat simpler to understand and administer. The approach used herein is commensurate with available data that categorizes water system costs into three specific categories. These include:

- *Customer Costs* – Customer costs such as meter reading, billing, and customer service are fixed costs that tend to vary as the function of the number of customers served. Customer costs are allocated equally to all customers based on the total number of accounts, and are included in the bi-monthly service charge.
- *Capacity Costs* – Capacity costs are also fixed costs. However, they tend to vary in relation to the capacity of the water system. Customers that can place greater or lesser demands on the water system should bear greater or lesser shares of these costs. The water system is sized to meet peak demands. The demand that each customer could potentially place on the water system is reflected in the size and capacity of the water meter. Capacity costs include fixed operating costs, water system maintenance, and debt service. Capacity costs are allocated to each customer based on the size and capacity of the water meter, and are included in the bi-monthly service charge calculation.
- *Commodity Costs* – Commodity costs include those costs that vary with the amount of actual water usage. Water treatment and pumping costs are the most significant examples. In addition, other costs that may not be truly variable are often allocated based on water usage because allocating these costs to each customer based on water usage is an equitable basis. Commodity costs are used to determine the commodity rates of the rate structure. Many utilities also place what may be considered fixed costs into the variable commodity component as a means of encouraging water conservation. It is fairly typical for commodity rates to account for 65 to 90 percent of water rate revenues, even

when a majority of costs might be considered fixed. The recently adopted water conservation best management practice regarding water conservation requires water rates to recover 70 percent of water rate revenue from commodity charges<sup>3</sup>.

- *Shared (Indirect) Costs* – Some cost items are not directly allocated to any of the three components identified above. Instead these costs are first allocated as shared (indirect) costs, and subsequently reallocated to each of the three components based on the percentage of costs that were directly allocated to these components.

**Exhibit III-6  
Nipomo Community Services District  
Water Rate Cost Allocation Flow Diagram**



The allocation of costs to each of the cost components occurs at the individual line-item level of detail in the District's budget and account structure. Most costs are allocated directly to the customer, capacity, or commodity components, although some are categorized as shared costs then reallocated indirectly. As shown in Exhibit III-6, the cost allocation results in about 20 percent of costs to be recovered from service charges and 80 percent to commodity rates. This is a slightly greater allocation to commodity charges than the current rates, and is intended to help improve the water conservation incentive embodied in the water rates.

**Water Rate Structure Design**

Water rate design and the development of rate schedules take place after the annual water rate revenue requirement is determined and after the cost of service analysis has been performed. Based on discussions with District staff, the District seeks to increase the water conservation incentives embodied in the rate structure. After discussing a variety of alternatives with the Board during recent workshops, the Board asked that we develop water rates with the following characteristics:

<sup>3</sup> California Urban Water Conservation Council (CUWCC) Best Management Practice (BMP) #11 – Retail Conservation Pricing, adopted in June 2007.

- A lowering of the bi-monthly service charges, with commensurate increase in commodity rates to improve the conservation incentive and mitigate impact of other rate structure changes on customer water bills.
- A two-tier single family water rate structure similar to the current two-tier structure with slight adjustments based on evaluation of water use characteristics to improve the conservation incentive.
- Change to the current uniform commodity rate for multi-family and non-residential customers to a two-tier rate structure with similar characteristics of the single family structure.

In addition, the Board asked that the rate structure evaluation be based on water use data covering a five-year period. It was believed that the most recent year (FY 06-07) included anomalous usage during winter months due to unusually dry winter conditions.

Based on this direction from the Board of Directors, the following water rates were developed. These rates, if implemented, would meet the 2008 revenue needs of the combined water system.

Service Charges

Exhibit III-7 presents the bi-monthly service charge calculations for the combined water system for 2008. The service charges recover customer and capacity costs from each customer. Customer costs are allocated equally to all customers, and capacity costs are allocated based on the hydraulic capacity associated with each meter size. The service charges, including the litigation charge (which would be unchanged), would generate about 20 percent of total annual water rate revenues.

Exhibit III-7  
Nipomo Community Services District  
Calculation of Water Service Charges for the Town Division

	Meter Size							Total
	1" or Less	1 1/2"	2"	3"	4"	6"	8"	
<b>Customer Accounts</b>								
No. of Customers	3,958	33	21	3	2	-	-	4,017
No. of Equivalent Meters	3,958	99	101	27	30	-	-	4,215
Hydraulic Capacity Factor (1)	1.0	3.0	4.8	9.0	15.0	30.0	48.0	
<b>Bi-Monthly Service Charges</b>								
Customer Cost	\$ 1.74	\$ 1.74	\$ 1.74	\$ 1.74	\$ 1.74	\$ 1.74	\$ 1.74	
Capacity Cost	\$ 14.99	\$ 44.96	\$ 71.94	\$ 134.88	\$ 224.80	\$ 449.56	\$ 719.32	
<b>Total Service Charges</b>	<b>\$ 16.73</b>	<b>\$ 46.70</b>	<b>\$ 73.68</b>	<b>\$ 136.62</b>	<b>\$ 226.65</b>	<b>\$ 451.30</b>	<b>\$ 721.07</b>	
Litigation Charge (2)	\$ 6.32	\$ 14.36	\$ 19.92	\$ 27.92	\$ 36.00	\$ 59.58	\$ 68.08	
<b>Combined Service Charges</b>	<b>\$ 23.05</b>	<b>\$ 61.06</b>	<b>\$ 93.60</b>	<b>\$ 164.54</b>	<b>\$ 262.55</b>	<b>\$ 510.88</b>	<b>\$ 789.15</b>	
<b>Annual Service Charge Revenue</b>								
Single Family	\$ 476,294	\$ 366	\$ 1,685	\$ -	\$ -	\$ -	\$ -	\$ 478,345
Multi-Family	\$ 53,659	\$ -	\$ -	\$ 987	\$ 3,151	\$ -	\$ -	\$ 57,797
Non-Residential	\$ 17,425	\$ 11,724	\$ 10,109	\$ 1,975	\$ -	\$ -	\$ -	\$ 41,233
<b>Total Srv. Chrg. Revenue</b>	<b>\$ 547,379</b>	<b>\$ 12,091</b>	<b>\$ 11,794</b>	<b>\$ 2,962</b>	<b>\$ 3,151</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ 577,375</b>
<b>Water Rate Revenue Requirement</b>								
Customer Costs	\$	42,000	1.5%					
Capacity Costs	\$	379,000	13.0%					
Commodity Costs (3)	\$	2,332,000	80.1%					
Litigation Charge	\$	158,000	5.4%					
<b>Total Revenue Requirement</b>	<b>\$</b>	<b>2,911,000</b>						

**Notes:**  
 (1) See text of report for discussion of capacity factors.  
 (2) Litigation charges remain unchanged.  
 (3) Commodity costs recovered through commodity rates. See Exhibit III-8.

Each meter type and size has a rated maximum flow capacity. Hydraulic capacity factors are determined by taking the ratio of the rated capacity for each meter size to that of the standard meter size (typically a 3/4" or 1" meter). Because the District treats all meters up to 1" as equivalent, the standard rated capacity was determined by calculating the weighted average capacity of all existing meters up to 1" in size. This resulted in a standard rating of 33 gpm. Capacity factors for meters larger than 1" were determined by taking the ratio of each meter size's rated capacity to the standard of 33 gpm. For example, the capacity factor of a 1 1/2" meter is 3.0 (100 gpm / 33 gpm).

The District's litigation charge associated with groundwater management issues is proposed to be continued, without change, until resolution of those issues. The litigation charge is also shown in Exhibit III-7. The charge is expected to remain through the planning period as certain legal and groundwater monitoring costs are expected to continue. However, the Board of Directors has indicated that the charge will be removed when the litigation issues are resolved and associated costs end.

Commodity Rates

**Exhibit III-8** presents the commodity rate calculations for the combined water system for 2008 based on direction from the Board of Directors during the workshop held on August 15, 2007. The two tier rate structure was derived as described below, and has the following characteristics (which are both positive and negative):

**Exhibit III-8  
Nipomo Community Services District  
Calculation of Water Commodity Rates for the Town Division**

No. of Accts.	Customer Class	Ann. Water Use (HCF)	FIRST TIER		Break Point	SECOND TIER		Annual Revenue
			Rate (\$/HCF)	Revenue		Rate (\$/HCF)	Revenue	
3,448	Single Family % of Water Use --> % of Water Bills -->	939,041	\$ 1.58	\$ 898,124 60.5% 53.8%	36	\$ 2.77	\$ 1,026,856 39.5% 46.2%	\$ 1,924,980
391	Multi-Family	32,088	\$ 1.58	\$ 30,690	(1)	\$ 2.77	\$ 35,089	\$ 65,779
178	Non-Residential	166,464	\$ 1.58	\$ 159,211	(1)	\$ 2.77	\$ 182,031	\$ 341,242
<b>4,017</b>	<b>TOTALS</b>	<b>1,137,593</b>						<b>\$ 2,332,000</b>
<b>Summary of Commodity Costs</b>								
Total Commodity Costs		<b>\$ 2,332,000</b> (from Exhibit III-7)						

**Notes:**

(1) Tier break points for multi-family and non-residential customers would vary with meter size, as shown below:

Up to 1" meter	36	CCF
1 1/2" meter	240	CCF
2" meter	340	CCF
3" and 4" meter	1,900	CCF

- The two-tier rate structure for single family customers includes a tier break point that is slightly lower than the current rate structure (36 CCF rather than 40 CCF). The first tier is intended to represent reasonable water needs for indoor water use for domestic purposes. This amount is equivalent to about 450 gallons per day, which should be ample for domestic purposes (many utilities use about 250 gpd for indoor single family needs). The

36 CCF break point represents the 75<sup>th</sup> percentile of winter water use (using five years of data). That is, 75 percent of all single family customers use less than this amount during the winter months. With this tier structure, about 60 percent of the single family water usage would be at the first tier rate and 40 percent at the second tier rate. Typically, customers would have no second tier usage during winter months and some second tier usage during summer months. During the peak summer use period, a median customer would have about 12 CCF at the second tier, while a customer at the 75<sup>th</sup> percentile would have 42 CCF at the second tier in the peak use period.

- The increase in the commodity rate from Tier 1 to Tier 2 (\$1.58/CCF to 2.77/CCF) is a 75 percent increase. It is also slightly greater than the step increase in the current rate structure.
- Three- and four-tier rate structures were considered in earlier analyses presented to the Board of Directors. Such rate structures may still have merit, however, consensus on the rationale and specific design of these structures was not obtained with the limited time spent on this topic during the study. Typically, a third (or fourth) tier is intended as an excess use rate that applies only to water use beyond a recognized "norm" for single family customers. Often the highest tier only applies to a small portion of consumption (less than 5 percent).
- Two-tier water rates were also developed for multi-family and non-residential customers (currently charged for water usage with a uniform rate). The tier structure was developed for each meter size. For multi-family and non-residential customers tier break points would be as follows:
  - Up to 1" meter                      36 CCF
  - 1 ½" meter                            240 CCF
  - 2" meter                                340 CCF
  - 3" and 4" meters                    1,900 CCF

The above tier break points would result in about 60 percent of the multi-family and non-residential water usage being priced at the first tier and about 40 percent at the second tier. This is intended to serve to maintain equity between the customer classes. The break points are based on analysis of water usage by meter size over the past five years. However, there are only 5 accounts with 3" or 4" water meters (3 multi-family, 1 commercial, and 1 irrigation). These accounts exhibit very different water usage patterns, and with the 1,900 CCF break point four of the customers would never come close to entering the second tier, while the fifth would seldom avoid it. This illustrates the problem of tier structures for customer classes with non-homogeneous water use characteristics. Similar results occur in the smaller meter sizes, although the problem is masked by the larger number of accounts in each meter size. In our opinion, this rate structure would fail to effectively achieve water conservation objectives, and could unfairly penalize some customers.

It is our recommendation, that if the District wants to develop a tier structure for multi-family and non-residential customer classes it should take a different approach for each user group. Multi-family tier structures can be effectively developed on a per-dwelling-unit basis, since water use per-dwelling-unit exhibits a homogeneous pattern (similar, though more condensed, to single family customers). Water budget tier structures could be an effective approach for landscape irrigation accounts. This would entail developing a customized rate structure for each of 82 irrigation accounts based on irrigated area. While administratively burdensome, these structures have been

effectively used to encourage water conservation in other jurisdictions throughout the state. An effective tier structure for commercial accounts may be more problematic. Water budget tier structures based on each customer's needs (based on a review of historical usage and assessment of water needs for the type/size of business) are possible, but obviously administratively burdensome. Tiers based on meter size may be possible, though the problems identified above would need to be addressed (possibly with less aggressive tier steps).

### **Water Rates Schedules**

Because financial plan analyses indicate that water rates do not need to be raised above previously approved levels, and because the two-tier structure developed at the Board's request exhibits some problems (for multi-family and non-residential customers), it is recommended that the District simply implement the previously approved water rates for the next two years. This will allow the District more time to consider water conservation objectives, other water conservation measures, and additional rate structure alternatives. By 2010, the District will likely need to take action to adjust water rates to meet revenue needs, and at that time could implement a new water rate structure.

**Exhibit III-10** presents the water rate schedules for the combined water system for 2008 through 2012. The water rates for 2009 and 2010 are the same as those previously approved, and the rates for 2010 through 2012 are simply an extension of the current rate structures to meet the revenue needs identified in the financial plan for those years. The rate schedules for these later years are provided for information purposes.

**Exhibit III-10  
Nipomo Community Services District  
Current and Estimated Future Water Rates**

	Current Rates (1)		Prev. Adopt. Rates (2)		Est. Future Water Rates (3)			Litigation Charge (4)
	Town	Blacklake	Jan. 2008	Jan. 2009	Jan. 2010	Jan. 2011	Jan. 2012	
<b>Bi-Monthly Service Charges</b>								
Up to 1"	\$ 20.64	\$ 22.08	\$ 22.71	\$ 24.52	\$ 27.22	\$ 30.21	\$ 33.84	\$ 6.32
1 1/2"	\$ 58.60	\$ 61.09	\$ 64.46	\$ 69.61	\$ 77.27	\$ 85.77	\$ 96.06	\$ 14.36
2"	\$ 92.81	\$ 96.24	\$ 102.09	\$ 110.25	\$ 122.38	\$ 135.84	\$ 152.14	\$ 19.92
3"	\$ 172.68	\$ 178.33	\$ 189.95	\$ 205.15	\$ 227.72	\$ 252.77	\$ 283.10	\$ 27.92
4"	\$ 286.77	\$ 295.58	\$ 315.45	\$ 340.68	\$ 378.15	\$ 419.75	\$ 470.12	\$ 36.00
6"	\$ 571.73	\$ 588.42	\$ 628.91	\$ 679.22	\$ 753.93	\$ 836.86	\$ 937.28	\$ 59.58
8"	\$ 913.83	\$ 939.98	\$ 1,005.21	\$ 1,085.63	\$ 1,205.05	\$ 1,337.61	\$ 1,498.12	\$ 68.08
<b>Water Usage Rates (\$/HCF)</b>								
Single Family Residential								
Tier 1 (0-40 HCF)	\$ 1.38	\$ 1.42	\$ 1.52	\$ 1.64	\$ 1.82	\$ 2.02	\$ 2.26	
Tier 2 (>40 HCF)	\$ 2.35	\$ 2.49	\$ 2.59	\$ 2.80	\$ 3.11	\$ 3.45	\$ 3.86	
Non-Residential (5)								
All Usage	\$ 1.74	\$ 1.73	\$ 1.91	\$ 2.06	\$ 2.29	\$ 2.54	\$ 2.84	

**Notes:**

- (1) Effective January 1, 2007 as adopted with Ordinance 2005-103.
- (2) Previously adopted with Ordinance 2005-103. No change is required at this time. Would also apply within Blacklake with merger.
- (3) Estimated future water rates to meet revenue needs. These rates assume no change in the rate structure.
- (4) No changes are proposed for the litigation charge, which applies to all water connections until resolution of groundwater litigation.
- (5) Includes multi-family, commercial, irrigation, agricultural, industrial, and construction.



**Appendix A – Financial Plan Exhibits**

The following exhibit summarizes the combined water system five-year financial plan developed for the District and described in Section II of this report.

Appendix A  
Nipomo Community Services District  
Combined Water Divisions Financial Plan

	FY 05-06 Actual	FY 06-07 Estimate	FY 07-08 Budget	FY 08-09	FY 09-10	FY 10-11	FY 11-12
<i>Proposed CY Rate Increases --&gt;</i>			10%	8%	11%	11%	12%
<b>OPERATING FUND (FUNDS 120 &amp; 140)</b>							
<b>Beginning Balance</b>	162,967	778,298	1,574,000	1,631,982	1,855,882	2,225,854	2,181,199
<b>Revenues</b>							
Water Availability Charges	566,648	620,000	709,000	763,000	829,000	912,000	1,008,000
Water Usage Charges	1,619,511	1,955,000	2,055,000	2,249,000	2,470,000	2,756,000	3,086,000
Fees and Penalties	49,703	40,000	42,200	42,600	43,000	43,400	43,800
Meter & Connection Fees	10,905	5,300	6,875	6,900	7,000	7,100	7,200
Plan Check & Insp. Fees	100	-	-	-	-	-	-
Miscellaneous Income	39,793	25,000	25,000	25,300	25,600	25,900	26,200
Interest Earnings	31,630	61,200	78,300	73,400	83,500	100,200	98,200
Transfer from Suppl. Wtr. Fund	-	-	-	-	37,500	43,073	577,918
<b>Total Revenues</b>	<b>2,318,290</b>	<b>2,706,500</b>	<b>2,916,375</b>	<b>3,160,200</b>	<b>3,495,600</b>	<b>3,887,673</b>	<b>4,847,318</b>
<b>Expenditures</b>							
<b>Operations &amp; Maintenance</b>							
Wages	169,710	169,500	222,500	302,700	311,800	321,200	330,800
Wages - Overtime	30,130	34,500	36,025	37,100	38,200	39,300	40,500
Payroll Taxes	4,528	5,250	4,720	4,900	5,000	5,200	5,400
Retirement	48,504	41,600	60,300	62,100	64,000	65,900	67,900
Medical and Dental	38,996	40,800	60,345	62,200	64,100	66,000	68,000
Workers Comp Insur.	15,681	13,400	15,000	15,500	16,000	16,500	17,000
Electricity - Pumping	264,294	390,000	410,000	426,500	443,700	372,000	294,000
Natural Gas - Pumping	65,252	117,000	135,000	140,400	146,100	152,000	158,100
Supplemental Water	-	-	-	-	-	796,000	2,000,000
Chemicals	2,908	5,150	16,000	16,600	17,300	18,000	18,700
Lab Tests and Sampling	20,203	20,200	31,000	32,200	33,500	34,900	36,300
Operating Supplies	44,062	46,000	56,000	58,300	60,600	63,000	65,500
Outside Services	39,208	52,000	70,000	72,100	74,300	76,500	78,800
Permits & Operating Fees	5,083	8,600	9,820	10,100	10,400	10,700	11,000
Repairs & Maintenance	103,791	140,000	150,000	154,500	159,100	163,900	168,800
Repairs & Maint - Vehicles	12,594	8,100	12,600	13,000	13,400	13,800	14,200
Engineering	9,614	-	10,500	10,800	11,100	11,400	11,700
Fuel	15,582	19,760	24,480	25,500	26,500	27,600	28,700
Paging and Cellular Service	3,512	3,400	4,215	4,300	4,400	4,500	4,600
Meters - New Installations	7,549	6,000	15,000	15,500	16,000	16,500	17,000
Meters - Replac. Program	5,302	18,000	22,000	22,700	23,400	24,100	24,800
Uniforms	2,630	3,800	4,490	4,600	4,700	4,800	4,900
Wtr Conserv/Recycl Prog.	2,234	7,500	53,700	55,300	57,000	58,700	60,500
Oper. Transfer Out - Replac.	93,678	88,000	392,000	403,800	415,900	428,400	441,300
<b>Total Oper. &amp; Maint.</b>	<b>1,005,045</b>	<b>1,238,560</b>	<b>1,815,695</b>	<b>1,950,700</b>	<b>2,016,500</b>	<b>2,790,900</b>	<b>3,968,500</b>
<b>General &amp; Administrative</b>							
Wages	94,509	87,700	190,425	196,100	202,000	208,100	214,300
Payroll Taxes	1,864	1,900	3,390	3,500	3,600	3,700	3,800
Retirement	25,828	23,800	53,000	54,600	56,200	57,900	59,600
Medical and Dental	19,355	20,100	38,490	39,600	40,800	42,000	43,300
Workers Comp Insur.	922	900	1,735	1,800	1,900	2,000	2,100

Appendix A -- Continued  
Nipomo Community Services District  
Combined Water Divisions Financial Plan

	FY 05-06	FY 06-07	FY 07-08	FY 08-09	FY 09-10	FY 10-11	FY 11-12
	Actual	Estimate	Budget				
Audit	-	2,412	4,560	4,700	4,800	4,900	5,000
Bank Charges & Fees	429	500	660	700	700	700	700
Computer Expense	18,625	11,400	18,240	18,800	19,400	20,000	20,600
Director Fees	8,721	10,820	13,680	14,100	14,500	14,900	15,300
Dues & Subscriptions	3,854	6,000	5,530	5,700	5,900	6,100	6,300
Education & Training	1,692	1,800	3,135	3,200	3,300	3,400	3,500
Elections	-	2,378	-	2,500	-	2,500	-
Insurance - Liability	17,293	18,200	19,095	19,700	20,300	20,900	21,500
Landscape and Janitorial	4,977	5,200	5,550	5,700	5,900	6,100	6,300
Legal - Gen. & Spec. Counsel	42,194	76,200	100,000	103,000	106,100	109,300	112,600
Legal - Water Counsel	267,312	135,000	100,000	103,000	106,100	109,300	112,600
Professional Services	-	49,000	111,040	114,400	117,800	121,300	124,900
Miscellaneous	10	1,500	2,000	2,100	2,200	2,300	2,400
Newsletter and Mailers	-	-	1,740	1,800	1,900	2,000	2,100
Office Supplies	7,098	10,600	8,265	8,500	8,800	9,100	9,400
Outside Services	3,380	2,150	5,510	5,700	5,900	6,100	6,300
Postage	9,338	9,000	15,070	15,700	16,300	17,000	17,700
Public Notices	489	-	3,400	3,500	3,600	3,700	3,800
Repairs & Maint. - Office Equip	958	800	2,280	2,300	2,400	2,500	2,600
Property Taxes	663	815	830	900	900	900	900
Telephone	2,411	2,900	2,985	3,100	3,200	3,300	3,400
Travel & Mileage	3,824	5,100	5,700	5,900	6,100	6,300	6,500
Oper. Transfer Out - Admin.	129,371	152,483	178,299	183,600	189,100	194,800	200,600
<b>Total Gen'l &amp; Admin.</b>	<b>665,117</b>	<b>638,658</b>	<b>894,609</b>	<b>924,200</b>	<b>949,700</b>	<b>981,100</b>	<b>1,008,100</b>
<i>Other Expenditures</i>							
Wtr Rev Bond DS - Interest	7,300	6,900	6,775	6,000	5,500	5,000	4,500
Wtr Rev Bond DS - Principal	9,000	9,000	9,000	10,000	10,000	10,000	11,000
Suppl Wtr Debt Service - Int.					37,500	34,519	31,388
Suppl Wtr Debt Service - Prin.					59,628	62,610	65,740
Fixed Asset Purchases	16,497	17,680	132,314	45,400	46,800	48,200	49,600
<b>Total Other Expenditures</b>	<b>32,797</b>	<b>33,580</b>	<b>148,089</b>	<b>61,400</b>	<b>159,428</b>	<b>160,328</b>	<b>162,228</b>
<b>Total Expenditures</b>	<b>1,702,959</b>	<b>1,910,798</b>	<b>2,858,393</b>	<b>2,936,300</b>	<b>3,125,628</b>	<b>3,932,328</b>	<b>5,138,828</b>
<b>Ending Balance</b>	<b>778,298</b>	<b>1,574,000</b>	<b>1,631,982</b>	<b>1,855,882</b>	<b>2,225,854</b>	<b>2,181,199</b>	<b>1,889,689</b>
Oper. Resrv. (50% of Expend.)	788,000	895,000	1,159,000	1,236,000	1,275,000	1,672,000	2,268,000
Uncommitted Fund Balance	(9,702)	679,000	472,982	619,882	950,854	509,199	(378,311)
DS Coverage (Min. 1.15 w/ CCs) -->					19.21	14.13	7.42
DS Coverage (Min. 1.00 w/o CCs) -->					13.28	8.00	1.13
<b>FUNDED REPLACEMENT - COMBINED WATER (FUNDS 800 &amp; 820)</b>							
<b>Beginning Balance</b>	2,256,277	2,259,000	2,361,000	2,255,500	2,089,800	2,678,700	3,306,600
<b>Revenues and Transfers</b>							
Interest Earnings	87,005	114,000	106,500	101,500	94,000	120,500	148,800
Blacklake Equity Surcharge	-	-	60,000	121,000	121,000	121,000	121,000
Operating Transfers In	93,678	88,000	392,000	403,800	415,900	428,400	441,300
<b>Total Revs. and Trans.</b>	<b>180,683</b>	<b>202,000</b>	<b>558,500</b>	<b>626,300</b>	<b>630,900</b>	<b>669,900</b>	<b>711,100</b>
<b>Expenditures</b>							
Previous Expenditures	177,960	100,000					
Fire Hydrant Replac.			50,000	-	-	-	-
Well Refurbishment			45,000	-	-	-	-
Quad Tank Coating & Maint.			75,000	-	-	-	-
BL Shop Construction			68,000	-	-	-	-
BL Bstr Sta Rebuild or Merge			112,000	-	-	-	-
BL Well #3 Casing Rehab.			20,000	-	-	-	-
GIS Upgrades			15,000	15,000	15,000	15,000	15,000
SCADA Upgrades			15,000	15,000	15,000	15,000	15,000
Reset Mains - Drainage			100,000	-	-	-	-
Reset Mains - Roads			50,000	10,000	10,000	10,000	10,000
Security			100,000	-	-	-	50,000
Contingency (5%)			14,000	2,000	2,000	2,000	4,500
Loan to Suppl. Wtr. Fund			-	750,000	-	-	-
<b>Total Expenditures</b>	<b>177,960</b>	<b>100,000</b>	<b>664,000</b>	<b>792,000</b>	<b>42,000</b>	<b>42,000</b>	<b>94,500</b>
<b>Ending Balance</b>	<b>2,259,000</b>	<b>2,361,000</b>	<b>2,255,500</b>	<b>2,089,800</b>	<b>2,678,700</b>	<b>3,306,600</b>	<b>3,923,200</b>

Appendix A -- Continued  
Nipomo Community Services District  
Combined Water Divisions Financial Plan

	FY 05-06 Actual	FY 06-07 Estimate	FY 07-08 Budget	FY 08-09	FY 09-10	FY 10-11	FY 11-12
<b>SUPPLEMENTAL WATER FUND (FUND 500)</b>							
<b>Beginning Balance</b>			2,300,000	2,268,500	5,140,144	6,688	-
<b>Revenues and Transfers</b>							
Suppl. Wtr. Capac. Charges			465,000	528,877	544,744	561,086	577,918
Interest Earnings			103,500	102,100	231,300	300	-
Loan from Replac. Fund			-	750,000	-	-	-
Purveyor Contributions			-	2,490,667	-	-	-
Total Revs. and Trans.			568,500	3,871,644	776,044	561,386	577,918
<b>Expenditures</b>							
Suppl. Water Project Planning			600,000	1,000,000	400,000	-	-
Suppl. Water Project Constr.			-	-	5,472,000	-	-
MOU Installment Payments			-	-	-	525,000	-
Trans. for COP DS & Credit			-	-	37,500	43,073	577,918
Total Expenditures			600,000	1,000,000	5,909,500	568,073	577,918
<b>Ending Balance</b>			<b>2,268,500</b>	<b>5,140,144</b>	<b>6,688</b>	-	-
<b>COMBINED WATER CAPITAL FUND (FUND 710)</b>							
<b>Beginning Balance</b>			4,750,000	2,904,310	3,153,966	3,418,390	2,753,390
<b>Revenues and Transfers</b>							
Capacity Charges			103,960	118,956	122,524	126,200	129,986
Interest Earnings			237,500	130,700	141,900	153,800	123,900
Other Funding Source - TBD			-	-	-	-	-
Total Revs. and Trans.			341,460	249,656	264,424	280,000	253,886
<b>Expenditures</b>							
W&S Master Plan			25,000	-	-	50,000	50,000
Shop Upgrade			308,000	-	-	-	-
Mains - West Side			500,000	-	-	500,000	500,000
Mains - East Side			250,000	-	-	250,000	250,000
Storage			950,000	-	-	-	-
Looping			50,000	-	-	100,000	100,000
Contingency (5%)			104,150	-	-	45,000	45,000
Total Expenditures			2,187,150	-	-	945,000	945,000
<b>Ending Balance</b>			<b>2,904,310</b>	<b>3,153,966</b>	<b>3,418,390</b>	<b>2,753,390</b>	<b>2,062,276</b>

I would like you to consider a proposal that I made some time ago about the water system surcharge proposed for Black Lake customers being unfair. Your consultant has consistently stated that the book value per equivalent customer in the Town system must equal that in the Black Lake system before you can merge the financial accounts of the two systems. Please consider the following instead.

1. Black Lake is not being given credit for the water it has been furnishing to the Town System. 29% of the Sundale well water belongs to Black Lake and has been used by the Town System for a number of years without reimbursement. Credit should be given.
2. I believe Black Lake water from wells 3, 4, and 29% of the Sundale well is more than adequate for Black Lake customers on an annual basis and brings more water to the merged system than it uses. The Town System charged \$13,000 from a new single family customer for service to expand its capacity and I believe that Black Lake should be given credit for the extra capacity it brings to the merge.
3. The cash reserves in the Town System Water Capacity Fund (700) had been collected from new customers in the Town System before the merge to provide them with capacity in the Town System. These funds should not be used in the equalization because they cannot be used to improve service in and are not needed by the Black Lake Community. I believe this because of the definition of Capacity Charges the District approved in Section V of the Reed report dated 25 May 2005.
4. The cash reserves in the Town System Equipment Replacement Fund (800) should not be used in the equalization because they represent the value of equipment wear out on only the Town System before the merge. The District should have collected sufficient fees from Black Lake customers before the merge to replace the worn out Black Lake equipment however, the District did not collect such funds but relied on the fact that the merged system does not require replacement of the worn out Black Lake equipment. Black Lake will pay for future equipment wear out in the merged system through its water rates.
5. The cash reserve in the Black Lake Equipment Replacement Fund (820) was used to cover the cost of merging the systems. The merge was done at no cost to the Town.
6. Because these funds were collected for use after the merge, the cash reserves in the Operating Funds (120 & 140) as of 30 June 2006 should be equalized. I believe this would result in a charge to Black Lake of \$305 per equiv customer. Also the physical assets in each system at the merge as determined by audit should be equalized. I believe this would result in a charge to Black Lake of \$331 per equiv customer.
7. With the charges in item 6 imposed and then reduced by credit given for items 1 and 2 above the result would be a reduction in the surcharge. The revenue projected in the financial plan for the Merged System would be less. This should have minimal effect on the plan since it has been determined that a \$750,000 surplus would exist in the merged Equipment Replacement Fund in FY 08/09 under the Book Value system of equalization.

Request you consider the above before approving the surcharge on Black Lake customers for merging the two systems.

1. Black Lake is not being given credit for the water it has been furnishing to the Town System. 29% of the Sundale well water belongs to Black Lake and has been used by the Town System for a number of years without reimbursement. Credit should be given.

*Prior to annexation, the County imposed a condition on developers in Blacklake to build a third well prior to the tracts that were built in the 1990's for peaking and meeting Title 22. In lieu of building a third well, Blacklake bought into the Sundale well. In 2000, the emergency intertie was built to supply Blacklake with the Sundale well water. Over the years, Blacklake has only paid for the operational costs of the Sundale well for the actual water delivered to them via the intertie.*

*The Sundale well, 29% of the original cost, is included as an asset of Blacklake.*

*In the equity calculation, neither Division is given credit for their respective water production capacity.*

2. I believe Black Lake water from wells 3, 4, and 29% of the Sundale well is more than adequate for Black Lake customers on an annual basis and brings more water to the merged system than it uses. The Town System charged \$13,000 from a new single family customer for service to expand its capacity and I believe that Black Lake should be given credit for the extra capacity it brings to the merge.

*An engineer should address peaking and Title 22 capacity issues.*

*The Town Capacity Charge is currently:*

<i>Capacity Charge</i>	<i>\$ 2,713</i>
<i>Supplemental Water Charge</i>	<i><u>\$12,062</u></i>
<i>TOTAL</i>	<i><u>\$14,775</u></i>

3. The cash reserves in the Town System Water Capacity Fund (700) had been collected from new customers in the Town System before the merge to provide them with capacity in the Town System. These funds should not be used in the equalization because they cannot be used to improve service in and are not needed by the Black Lake Community. I believe this because of the definition of Capacity Charges the District approved in Section V of the Reed report dated 25 May 2005.

*All customers benefit from system improvements and expansion. In addition, rates and charges are used to maintain and replace all system assets.*

4. The cash reserves in the Town System Equipment Replacement Fund (800) should not be used in the equalization because they represent the value of equipment wear out on only the Town System before the merge. The District should have collected sufficient fees from Black Lake customers before the merge to replace the worn out Black Lake equipment however, the District did not collect such funds but relied on the fact that the merged system does not require replacement of the worn out Black Lake equipment. Black Lake will pay for future equipment wear out in the merged system through its water rates.

*If NCSD did not maintain a Replacement Fund, all reserves that are currently in Fund 800 would be in Fund 120 (Town Water). The same is said for Blacklake. If NCSD did not maintain Fund 820, all reserves that are currently in Fund 820 would be in Fund #140.*

*Rates and charges are used to fund replacement. If the rates and charges are not sufficient to cover funded replacement, then funded replacement does not occur.*

5. The cash reserve in the Black Lake Equipment Replacement Fund (820) was used to cover the cost of merging the systems. The merge was done at no cost to the Town.

*Yes, the cost of the second intertie was paid for out of Blacklake funds. This was an expense paid out of the FY06-07 budget and documented in the FY06-07 Audit as a Blacklake Water System Asset. Should Blacklake wish to use the FY06-07 audit as the basis for the equity surcharge instead of the FY05-06 Audit, this could be considered.*

6. Because these funds were collected for use after the merge, the cash reserves in the Operating Funds (120 & 140) as of 30 June 2006 should be equalized. I believe this would result in a charge to Black Lake of \$305 per equiv customer. Also the physical assets in each system at the merge as determined by audit should be equalized. I believe this would result in a charge to Black Lake of \$331 per equiv customer.

*See combined response to #6 and #7 below.*

7. With the charges in item 6 imposed and then reduced by credit given for items 1 and 2 above the result would be a reduction in the surcharge. The revenue projected in the financial plan for the Merged System would be less. This should have minimal effect on the plan since it has been determined that a \$750,000 surplus would exist in the merged Equipment Replacement Fund in FY 08/09 under the Book Value system of equalization.

*Although Blacklake Water Fund 140 started in 1993 following the merger, Town Water Fund 120 has functioned since 1966, so they do not have the same term. Additionally, omission of the cash portion Town Funds 700 and 800 and the cash portion of Blacklake*

*Fund 820 inappropriately distorts the equity position of the Two funds making the comparison invalid. If the two funds are merged, the previous customers of Blacklake will enjoy these assets and should they should pay an equity surcharge that recognizes their existence. Thus, even though the dollar value of Mr. Nelson's equalization calculation is mathematically correct, staff can not recommend that the Board agree to use Mr. Nelson's proposal as the basis for the determination of the equity surcharge.*

T:\FINANCE\FUNDACTG\BLACKLAKE\Bill Nelson Proposal.doc



TO: NCSO District Manager Bruce Buel and  
NCSO Board Members

FROM: Black Lake Ad-Hoc Committee on Water "Equity Surcharge"

DATE: October 24, 2007

By a Certificate of Completion recorded on Jan. 19, 1993 by Paul L. Hood, Deputy Executive Officer of the Local Agency Formation Commission (LAFCo), and recorded with San Luis Obispo County as Doc. No. 1993-002864, the Nipomo Community Services District (NCSO) annexed the Black Lake Golf Course and Country Club. A copy of the recording, the LAFCo Resolution No. 92-19 dated October 15, 1992, and Exhibit A, Proposed NCSO Annexation No. 7 is attached.

Those documents, and the references therein, clearly state that the Black Lake community, including the appurtenant water and sewer facilities were annexed to NCSO and are therefore owned by NCSO. Frequent statements made by NCSO management and Board further substantiates the fact that the Black Lake water facilities are owned by NCSO.

Any "equity surcharge" should have been proposed at the time of annexation. Black Lake's assets at that time accounted for ~30% of NCSO's assets while its system connections comprised ~10%. Therefore, NCSO's other customers could have been assessed an "equitable surcharge" to match Black Lake's share.

Currently, there are ongoing discussions regarding a fair and equitable method of "balancing the equities" between the NCSO and Black Lake water systems. This appears to be a moot point since Black Lake does not own any water facilities and therefore has no equity in the water system supplying Black Lake. Further, it also appears that NCSO has an obligation to continue to operate and maintain the Black Lake water system, or, as it is presently, provide a water supply from the town system augmented by Black Lake wells #3 and #4, and the Sundale well.

NCSO must take responsibility for failing to maintain the wells and equipment at Black Lake and allowing the water facilities to fall into disrepair. NCSO has the further responsibility of providing water service to Black Lake in the future absent the suggested "balancing of equities".

Signed: *Patricia Ely, Ad-Hoc Committee Representative*

Recording Requested by & mail to:
Deputy Executive Officer - LAFCo
County Government Center
San Luis Obispo, CA 93408

Official Records
San Luis Obispo Co.
FRANCIS M. COONEY
Recorder
Jan 19, 1993
Time: 16:42

NF 0.00
TOTAL 0.00

@@ [ 6 ]

CERTIFICATE OF COMPLETION

Pursuant to Government Code Section 57200, this Certificate is hereby issued by the Executive Officer of the Local Agency Formation Commission of San Luis Obispo County, California.

1. Short-form designation, as designated by LAFCo is LAFCo File No. 2-R-92:
Annexation No. 7 to the Nipomo Community Services District (Black Lake Golf Course and Country Club)

2. The name of each district or city involved in this change of organization or reorganization and the kind or type of change of organization ordered for each city or district are as follows:

Table with 2 columns: City or District, Type of Change of Organization. Row 1: Nipomo Community Services District, Annexation.

3. The above listed cities and/or districts are located within the following county(ies): San Luis Obispo County

4. A description of the boundaries of the above cited change of organization or reorganization is shown on the attached map and legal description, marked Exhibit A and by reference incorporated herein.

5. The territory involved in this change of organization or reorganization is Inhabited (Inhabited/uninhabited)

6. This change of organization or reorganization has been approved subject to the following terms and conditions, if any:

7. The date of adoption of the Resolution ordering this change of organization or reorganization without election, or the Resolution confirming an order for this change of organization or reorganization after confirmation by the voters was ... A certified copy of the ordinance or resolution approving this proposal by the ... is attached hereto marked Exhibit ... and by reference incorporated herein.

I hereby certify that I have examined the above cited ordinance or resolution for a change in organization or reorganization and have found this document to be in compliance with Resolution No. 92-19 approving said change of organization or reorganization and adopted by the Local Agency Formation Commission of the County of San Luis Obispo on October 15, 1992.

Dated: 1/17/93
LAFCo File No.: 2-R-92

Paul L. Hood
PAUL L. HOOD, Deputy Executive Officer

IN THE LOCAL AGENCY FORMATION COMMISSION  
COUNTY OF SAN LUIS OBISPO, STATE OF CALIFORNIA

Thursday, October 15, 1992

PRESENT: Commissioners, Duane Picanco, Alternate Craig Pritchard, Chairman  
Chuck Comstock

ABSENT: Commissioners David Blakely, Laurence L. Laurent, Alternate Evelyn Delany

RESOLUTION NO. 92-19

RESOLUTION MAKING DETERMINATIONS APPROVING THE  
REORGANIZATION INVOLVING DETACHMENT OF TERRITORY FROM  
COUNTY SERVICE AREA NO. 1-G AND  
ANNEXATION NO. 7 TO THE NIPOMO COMMUNITY SERVICES DISTRICT  
(BLACK LAKE GOLF AND COUNTRY CLUB)

The following resolution is now offered and read:

**WHEREAS**, on September 22, 1992 there was filed with this Commission a proposal for Detachment of territory from County Service Area No. 1-G and Annexation of territory to the Nipomo Community Services District (Black Lake Golf Course and Country Club); and

**WHEREAS**, the Executive Officer has given the notices required by law and has forwarded copies of his report to officers, persons, and public prescribed by law; and

**WHEREAS**, the matter was duly set for public hearing at 9 a.m. on August 20, 1992 and continued to October 15, 1992, and the public hearing was duly conducted and determined and decision made on October 15, 1992; and

**WHEREAS**, at said hearing, this Commission heard and received all oral and written protests, objections, and evidence, which were made, presented, or filed, and all persons present were given the opportunity to hear and be heard in respect to any matter relating to said proposal and report; and

**WHEREAS**, the Commission duly considered the negative declaration approved for this project, and reviewed and considered the information contained therein and all comments received during the public hearing process; and

**WHEREAS**, the Commission duly considered the proposal and finds that the territory proposed to be annexed is uninhabited; that the distinctive short form designation of the territory proposed to be annexed is "Reorganization involving detachment of territory from CSA No. 1-G and Annexation No. 7 To The Nipomo Community Services District (Black Lake Golf Course and Country Club); that the territory proposed for annexation is located within the sphere of influence and sphere of service of the Nipomo Community Services District; and that the proposed reorganization should be approved

**NOW, THEREFORE, BE IT RESOLVED AND ORDERED** by the Local Agency Formation Commission of the County of San Luis Obispo, State of California, as follows:

1. That the recitals set forth hereinabove are true, correct, and valid.
2. That the legal description approved by this Commission is attached thereto,



Revised  
2/15/12  
PB

PROPOSED NIPOMO COMMUNITY SERVICES DISTRICT  
ANNEXATION NO. 7

Those portions of Division A of Pomeroy's Resubdivision of a Part of the Los Berros Tract as shown in Map Book A, Page 109, on file in the Recorder's Office of the County of San Luis Obispo, State of California, which County Recorder's Office contains the Official Record Books, Map Books and Parcel Map Books hereinafter referenced, more particularly described as follows.

Beginning at the easterly corner of Parcel 1 of COAL 87-124 as shown in Parcel Map Book 45 Page 45, which corner is on the southwesterly line of a 60 foot road (Pomeroy Road) of said Division A, and which corner is in Lot 33 of said Division A;

CALL 1:

Thence northwesterly along the southwesterly line of said 60 foot road (Pomeroy Road) to an angle point in said 60 foot road (Pomeroy Road);

thence N. 71° 45' E., 5.27 feet more or less to the point on the southwesterly end of the course recited as "South 71° 45' West, 26.32 feet..." in Grant Deed recorded in Official Record Book 217, Page 154 et seq. on May 17, 1937;

thence N. 0° 24' W. along the easterly part of Parcel 1 of said COAL 87-124 to the intersection with the line between Lots 33 of said Division A and Lot 42 of Division C of said Pomeroy's Resubdivision, which point is also on the northerly line of Parcel 1 as shown in said COAL 87-124.

CALL 2:

Thence westerly, northwesterly and westerly along the northerly lines of Lots 33, 34, 35, 32 and 31 of said Division A, which line is also the northerly line of Parcel 1 of said COAL 87-124, to the northwesterly corner of said LOT 31, which corner is the northwesterly corner of Parcel 1 of said COAL 87-124.

CALL 3:

Thence southerly along the westerly line of Lot 31 of said Division A, which line is also the westerly line of Parcel 1 of said COAL 87-124, 914.95 feet to the northwesterly corner of Lot 174 of Tract 1542 as shown in Map Book 15, Page 10;

thence southerly along the westerly line of said Lot 174 to a point in the northerly line of a 60 foot road (Black Lake Canyon Drive) as shown on said Tract 1542;

thence westerly and southerly along the northerly and westerly lines of 30 foot right-of-way (Via Concha), as described in



document # 21361 recorded in Official Records Book 3295, Page 769 et seq., to a point at the intersection of the northerly line of a 60 foot road (Callender Road), with the northerly extension of the westerly line of a 60 foot road (Via Concha), which point is in Lot 30 of said Division A.

CALL 4:

Thence southerly along the westerly line of said 60 foot road (Via Concha) through Lots 38 and 45 of said Division A, which line is also through Parcels A, B and C as shown in Parcel Map Book 16, Page 35 and through Parcel 4 as shown in Parcel Map Book 11, Page 76 to the intersection with the southerly line of a 60 foot road (Willow Road) as shown in said Division A, which point is in Lot 58 of said Division A.

CALL 5:

Thence easterly along the southerly line of said 60 foot road (Willow Road) through Lots 58, 57, 56, 55, 54 and 53 of said Division A, which line is also the northerly line of Parcels 2 and 3 as shown in Parcel Map Book 8, Page 54, and also through Parcels 1 and 2 as shown in Parcel Map Book 2, Page 89, and also through Parcels 1 and 2 as shown in Parcel Map Book 13 page 35, to the intersection with the line between said Lot 53 and Lot 52 of said Division A, which line is also the westerly line of NCSD Annexation No.2 as described in Official Records Book 1493, Page 744 et seq.;

thence northerly along the line between said Lots 53 and 52 to the northwesterly corner of said Lot 52;

thence easterly along the northerly line of said Lot 52 to the northeasterly corner of said Lot 52, which corner is on the centerline of a 60 foot road (Pomeroy Road).

CALL 6:

Thence northerly along the easterly line of Lot 51 of said Division A, which line is also the westerly line of Lot 58 of Division B of said Pomeroy's Resubdivision and which line is also a westerly line of said NCSD Annexation No.2, to an angle point in the center of said 60 foot Road (Pomeroy Road).

CALL 7:

Thence S. 71° 45' W., 31.59' to an angle point on the westerly line of said 60 foot road (Pomeroy Road), which point is in said Lot 51.

CALL 8:

Thence N. 36° 30' W. along the southwesterly line of said 60 foot road (Pomeroy Road) through said Lots 51 and 33 to the Point of Beginning, containing 535 acres more or less.

JON S. SEITZ  
MICHAEL W. SEITZ

SHIPSEY & SEITZ, INC.  
A LAW CORPORATION  
1066 PALM STREET  
POST OFFICE BOX 953  
SAN LUIS OBISPO, CALIFORNIA 93406  
(805) 543-7272 FAX (805) 543-7281  
JON S. SEITZ  
District Legal Counsel  
Nipomo Community Services District

JOHN L. SEITZ  
(1924-1986)  
GERALD W. SHIPSEY  
(RETIRED)

## MEMORANDUM

TO: BOARD OF DIRECTORS  
NIPOMO COMMUNITY SERVICES DISTRICT

RE: BLACK LAKE WATER DIVISION/TOWN DIVISION MERGER

FROM: JON S. SEITZ, DISTRICT LEGAL COUNSEL

DATE: NOVEMBER 2, 2007

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### SUMMARY

Black Lake water and sewer systems were operated as independent zones by the County of San Luis Obispo prior to annexation, and have been operated by the Nipomo Community Services District as independent zones subsequent to the annexation.

If the Black Lake Water Division and the Town Division are merged, the District Board of Directors must consider and prorate the capital contribution that the two systems would contribute to the merged water system.

### BACKGROUND

Prior to annexation, the Black Lake Golf Course area was a separate self supported community subject to its own adopted Specific Plan. County Service Area Zone 1-G (CSA 1-G) provided water and sewer service within the Black Lake Specific Plan as follows:

- Sewer Service: sewer service is provided by a wastewater treatment plant that discharges disinfected effluent to holding ponds where the effluent is mixed with groundwater to provide limited irrigation to the Black Lake Golf Course.
- Water Service: water service included two (2) wells that pumped water from the underlying groundwater basin to a water tank constructed at ground level. The water from the tank is pressurized and transmitted through water pipes to the residents within the Black Lake Specific Plan.

At the time the District provided sewer service to its residents by a ponding system commonly known as the Southland Wastewater Treatment Plant that discharged effluent through settling ponds back to the groundwater basin. The District's water system used groundwater that was pumped to elevated tanks and then supplied to its residents under pressure by use of gravity.

## **ANNEXATION**

In 1992, the Black Lake Golf Course area was annexed to the District pursuant to LAFCO Resolution 92-19, attached hereto as Exhibit "A". Paragraph 3 of the LAFCO Resolution placed conditions on the annexation (see Exhibit "A", paragraph 3 (a-i)). Paragraph 3(g) authorized the District to continue to levy service charges and rates that were fixed and collected by CSA 1-G within the Black Lake Specific Plan after annexation. The LAFCO approval further provided that water and sewer service not be exported from the Black Lake area except in the event of an emergency.

## **RATE SETTING**

Because of the different operational requirements of the two different wastewater treatment plants and water systems along with the prohibition on exporting water or sewer service outside the Black Lake Specific Plan, the District has operated the two systems as independent zones (with separate accountings), commonly known as the Town Division and the Black Lake Division with independent bi-monthly rates and charges to support water and sewer operations.

Through the years the Town Water Division has constructed a number of new water tanks (paid in part by Town Division capacity charges) and has developed excess capacity in its water transmission lines. On the other hand, the Black Lake water system is beginning to fail. Principally, the system requires at least one well to be completely reconstructed and new pressure tanks and pumps to pressurize the water for service at Black Lake.

By way of background, the purpose of water rate charges are defined in Water Code § 71616 as follows:

*A district, so far as practicable, shall fix such rates for water in the district, and in each improvement district therein, as will result in revenues which will:*

- (a) Pay the operating expenses of the district and the improvement district.*
- (b) Provide for repairs and depreciation of works.*
- (c) Provide a reasonable surplus for improvements, extensions, and enlargements.*
- (d) Pay the interest on any bonded debt.*

*(e) Provide a sinking or other fund for the payment of the principal of such bonded*



*debt as it becomes due.*

*(f) Repay advances, together with interest at a rate not to exceed the interest value of money to the district, made from the district to an improvement district.*

The District's authority to adopt rates is found in Government Code §§61120 and 61123 of the Community Services District law, as follows:

**§ 61120. Authority to raise alternative revenues**

Whenever the board of directors determines that the amount of revenue available to the district or any of its zones is inadequate to meet the costs of operating and maintaining the facilities, programs, and services authorized by this division, the board of directors may raise revenues pursuant to this chapter or any other provision of law.

**§ 61123. Service fees**

(a) A board of directors may charge a fee to cover the cost of any service which the district provides or the cost of enforcing any regulation for which the fee is charged. No fee shall exceed the costs reasonably borne by the district in providing the service or enforcing the regulation for which the fee is charged.

(b) Before imposing or increasing any fee for property-related services, a board of directors shall follow the procedures in Section 6 of Article XIII D of the California Constitution. - - -

**CALIFORNIA CONSTITUTION ARTICLE XIII (D) AND RATE SETTING**

In 1998, the California voters adopted Proposition 218 which amended the California Constitution that among other things added Articles XIII (D) that provides a substantive and procedural requirement to adopt new or increased water rates (also applies to sewer rates).

Pursuant to Article XIII (D) water rate increases must meet the following substantive requirements:

(a) Revenue derived from the fee or charge must not exceed the funds required to provide the property-related service.

(b) Revenue from the fee or charge must not be used for any purpose other than that for which the fee or charge was imposed.

**(c) The amount of the fee or charge imposed upon any parcel or person as an incident of property ownership must not exceed the proportional cost of the service attributable to the parcel. [Emphasis added]**

(d) The fee or charge may not be imposed for service unless the service is actually used by or immediately available to the owner of the property in question.

Fees or charges based upon potential or future use of a service are not permitted. Stand-by charges must be classified as assessments and must not be imposed without compliance with the proportionality requirements for assessments.

(e) No fee or charge may be imposed for general governmental service such as police, fire, ambulance or libraries where the service is available to the public in substantially the same manner.

Article XIII(D) also mandates procedural requirements that the District must meet in setting water rate increases as follows:

- A. The District must identify the parcels upon which a fee or charge is proposed for imposition.
- B. The amount of the fee or charge proposed to be imposed upon each parcel must be calculated by the District.
- C. The District must provide written notice by mail of the proposed fee or charge to the record owner of each identified parcel upon which the fee or charge is proposed for imposition.
- D. The notice to record owners of property must contain all of the following:
  - 1) The amount of the fee or charge proposed to be imposed upon each parcel;
  - 2) The basis on which the amount of the proposed fee or charge was calculated;
  - 3) The reason for the fee or charge;
  - 4) The date, time and location of a public hearing on the proposed fee or charge.
- E. The District must conduct a public hearing on the proposed fee or charge at least 45 days after mailing the notice described above. The hearing is to be conducted in the following manner:
  - 1) At the public hearing, the District must consider all written protests against the fee or charge.
  - 2) If a written protest against a proposed fee or charge is presented by a majority of owners of the identified parcels, the District may not impose the fee or charge.

## BLACK LAKE WATER DIVISION IMPROVEMENTS

District engineering studies identify the following required system improvements and estimated costs:



The Black Lake replacement account (2005-2006 Fiscal Year Audit) is funded at four hundred ninety-six thousand six hundred ninety-one dollars (\$496,691) (approximate), thereby necessitating a rate increase to fund the improvements. The rate increase would be implemented pursuant to Article XIII (D) of the California Constitution (above) including a requirement that the District conduct a protest hearing.

## COMBINED WATER SYSTEM ALTERNATIVE

The District Board of Directors is considering merging the Town Division water system with the Black Lake water system thereby eliminating the requirement for construction of the new booster station and reconstruction of the four hundred gallon reservoir improvements. The net result would be operating both systems from the Town Division water tanks (combined gravity system).

## EQUITABLE CONTRIBUTION

The District's 2005-2006 capacity charge for a one inch meter (residential) to connect the Town Division water system is two thousand five hundred and one dollars (\$2,501) (capital contribution to water storage tanks, wells and transmission lines). The District recognizes that if both systems were merged that the Black Lake division would be contributing significant capital to the merged system. Therefore, the District commissioned Bob Reed to provide the District with analysis and equities of merging the two systems. Bob Reed has published a report that concludes that each Black Lake residential water account should be required to contribute one thousand six hundred seventy-two dollars (\$1,672) to match, on a prorated basis, the Town Division's contribution to the merged system<sup>1</sup>. The equitable contribution would have

to be approved by the Black Lake customers (property owners) pursuant to Article XIII (D) above, including the protest hearing.

## BLACK LAKE CONCERNS

- 
1. (a) The District Board is considering giving Black Lake customers the option of paying the equity buy-in at a lump sum payment or payment over time as part of the bi-monthly water bill;
  - (b) non residential water accounts (water meters that exceed one (1) inch) require a larger equitable contribution.

A number of Black Lake residents have expressed concerns related to the equitable contribution referenced above, summarized as follows:

1. That the Annexation was a de facto merger of the two systems, therefore eliminating the requirement of an equitable surcharge as the systems are already combined.

**Response:** The cases cited for this proposition involve a different factual scenario. The Black Lake water and sewer systems were independent zones administered by CSA 1-G at the time of annexation and were subject to independent rates and charges as referenced in the LAFCO Resolution (Exhibit "A"). Further, see Government Code §§ 61123, 61120, above, and Article XIII (D) of the California Constitution.

2. That the District owns the systems and therefore there can be no equitable buy-in.

**Response:** The District owns and operates its service systems based on rates and charges it collects from its customers (see Government Code §61120 and 61123, above).

The bottom line regarding these types of concerns and by way of analogy, the District cannot require Black Lake sewer customers to subsidize the Southland Treatment Project Upgrade currently estimated at twelve million (\$12M) (approximate). Likewise, the District cannot ask the Town Division water customers to subsidize the water system merger. Both scenarios would violate Article XIII (D) of the California Constitution because in both cases there would be no benefit to the Division providing the subsidy.

3. That the equitable contribution proposed by the Reed Report overestimates the equitable contribution.

**Response:** The equitable contribution must be "rationally based" and must be approved by the Black Lake customers (property owners) pursuant to Article XIII (D) protest procedures (above).

**END OF MEMORANDUM**

IN THE LOCAL AGENCY FORMATION COMMISSION  
COUNTY OF SAN LUIS OBISPO, STATE OF CALIFORNIA

Thursday, October 15, 1992

PRESENT: Commissioners, Duane Picanco, Alternate Commissioner Craig Pritchard,  
and Chairman Chuck Comstock.

ABSENT: Commissioners David Blakely, Laurence L. Laurent, Alternate Commissioner  
Evelyn Delany

RESOLUTION NO. 92-19

RESOLUTION MAKING DETERMINATIONS APPROVING THE  
REORGANIZATION INVOLVING DETACHMENT OF TERRITORY FROM  
COUNTY SERVICE AREA NO. 1-G AND  
ANNEXATION NO. 7 TO THE NIPOMO COMMUNITY SERVICES DISTRICT  
(BLACK LAKE GOLF AND COUNTRY CLUB)

The following resolution is now offered and read:

WHEREAS, on September 22, 1992 there was filed with this Commission a proposal for Detachment of territory from County Service Area No. 1-G and Annexation of territory to the Nipomo Community Services District (Black Lake Golf Course and Country Club); and

WHEREAS, the Executive Officer has given the notices required by law and has forwarded copies of his report to officers, persons, and public prescribed by law; and

WHEREAS, the matter was duly set for public hearing at 9 a.m. on August 20, 1992, and the public hearing was duly conducted and continued until October 15, 1992, and the public hearing was duly conducted and determined and decision was made on October 15, 1992; and

WHEREAS, at said hearing, this Commission heard and received all oral and written protests, objections, and evidence, which were made, presented, or filed, and all persons present were given the opportunity to hear and be heard in respect to any matter relating to said proposal and report; and

WHEREAS, the Commission duly considered the Negative Declaration approved for this project reviewed and considered the information contained therein and all comments received during the public hearing process; and

WHEREAS, the Commission duly considered the proposal and finds that the territory proposed to be annexed is uninhabited; that the distinctive short form designation of the territory proposed to be annexed is "Reorganization Involving detachment of territory from CSA No. 1-G and Annexation No. 7 To The Nipomo Community Services District (Black Lake Golf Course and Country Club); that the territory proposed for annexation is located within the sphere of influence and sphere of service of the Nipomo Community Services District; and that the proposed annexation should be approved.

NOW, THEREFORE, BE IT RESOLVED AND ORDERED by the Local Agency

Formation Commission of the County of San Luis Obispo, State of California, as follows:

1. That the recitals set forth hereinabove are true, correct, and valid.
2. That the legal description approved by this Commission is attached thereto, marked Exhibit "A", and incorporated by reference herein as though set forth in full.
3. That the Reorganization involving Detachment from CSA No. 1-G and Annexation No. 7 To The Nipomo Community Services (Black Lake Golf Course and Country Club), being further identified in the files of this Commission as file No. 2-R-92, is hereby approved and the Board of Directors of the Nipomo Community Services District is authorized to complete proceedings to annex such territory, after notice and hearing, subject to the following conditions:

- A. That the NCSD provide all three services currently provided by CSA No. 1-G: water, sewer, and street-lighting; and
  - B. That the NCSD complete the transfer of sewer service responsibilities from CSA No. 1-C, Montecito Verde by executing the transfer agreement sent to the NCSD by the County in October 1990; and
  - C. That the NCSD offer one Water System Worker position to any County Employee that is laid off because of the proposed reorganization, and who voluntarily chooses to be employed by the NCSD instead of the County; and
  - D. That all property real and personal of CSA No. 1-G, be transferred to the Nipomo Community Services District upon the effective date of the reorganization; and
  - E. That all funds of CSA No. 1-G, including cash on hand and money due but uncollected, together with all obligations due CSA No. 1-G be transferred to the NCSD; and
  - F. That the NCSD succeed to all rights, duties and obligations of CSA No. 1-G with respect to the enforcement of performance or payment of any outstanding contracts and obligations of CSA No. 1-G; and
  - G. That the NCSD be authorized to impose upon the entire territory included in CSA 1-G, liability for payment of all principal and interest and other amounts which will become due on account of any outstanding contract or obligations of CSA No. 1-G; and
  - H. That the NCSD be authorized to continue to levy, fix and collect any special, extraordinary or additional taxes, assessments, service charges and rates which were levied, fixed and/or collected by CSA No. 1-G;
  - I. That the NCSD submit a map and legal description of the revised boundaries of the reorganization proposal certified by the County Surveyor.
4. That the Executive Officer of this Commission is authorized and directed to mail certified copies of this resolution in the manner provided by law.

Upon motion of Commissioner Pritchard, seconded by Commissioner Picanco, and on the following roll call to wit:

AYES: Commissioners Pritchard, Picanco, Chairman Comstock

NOES:

ABSENT:

ABSTAINING:

the foregoing resolution is hereby adopted.

Chuck Comstock  
Chairman of said Local Agency  
Formation Commission

ATTEST

Paul K. Hood  
Deputy Executive Officer

APPROVED AS TO FORM AND LEGAL EFFECT:

JAMES B. LINDHOLM, JR.  
County Counsel

By: A. J. C.  
Deputy County Counsel

STATE OF CALIFORNIA )  
 ) ss.  
COUNTY OF SAN LUIS OBISPO )

I, Robert E. Hendrix, Executive Officer of the Local Agency Formation Commission said County and State, do hereby certify the foregoing to be a full, true and correct copy of the original on file in my office, and I have carefully compared the same with the original.

WITNESS my hand this 17<sup>th</sup> day of MAY, 1993.

ROBERT E. HENDRIX  
Executive Officer

By: Paul K. Hood  
Deputy Executive Officer

History of Annexations

TOWN DIVISION	BLACK LAKE DIVISION								
<p>Property owners request annexation to NCSD in order to receive water or water and sewer services. Prior to annexation, these properties are either vacant land or are using private wells for water service. The conditions of annexation include:</p> <ol style="list-style-type: none"> <li>1. Pay Annexation Fee of \$500 per acre</li> <li>2. Property Owner builds the infrastructure to serve the properties</li> <li>3. Pay Water and Sewer Capacity Fees</li> </ol> <p>All annexations approved by NCSD have connected to the Town Division Water and Sewer infrastructure.</p> <p>No annexation has ever connected to the Blacklake Water and Sewer infrastructure.</p>	<p>At inception, Black Lake Golf Course development was operated by SLO County as County Service Area 1-G (approx 1985-1993). The developers of Black Lake Golf Course built the water and sewer infrastructure and dedicated it to County Service Area 1-G. The water and sewer system was a fully operational and independent system. CSA 1-G had its own set of water and sewer rates set by the County. The County accounted for CSA 1-G revenues and expenses as a separate CSA Fund within the County Budget.</p> <p>Upon annexation in 1992:</p> <ol style="list-style-type: none"> <li>1. County dedicated CSA 1-G infrastructure to NCSD</li> <li>2. CSA 1-G reserves were transferred to NCSD.</li> </ol> <p>NCSD placed these reserves in the following funds:</p> <table style="margin-left: 40px;"> <tr> <td>Blacklake Water</td> <td style="text-align: right;">\$105,159</td> </tr> <tr> <td>Blacklake Sewer</td> <td style="text-align: right;">\$ 35,586</td> </tr> <tr> <td>Blacklake Street Lighting</td> <td style="text-align: right;"><u>\$ 24,365</u></td> </tr> <tr> <td style="text-align: right;">TOTAL</td> <td style="text-align: right;"><u>\$165,110</u></td> </tr> </table> <ol style="list-style-type: none"> <li>3. No Annexation Fee was collected</li> <li>4. No Water and Sewer Capacity Fees were collected</li> </ol>	Blacklake Water	\$105,159	Blacklake Sewer	\$ 35,586	Blacklake Street Lighting	<u>\$ 24,365</u>	TOTAL	<u>\$165,110</u>
Blacklake Water	\$105,159								
Blacklake Sewer	\$ 35,586								
Blacklake Street Lighting	<u>\$ 24,365</u>								
TOTAL	<u>\$165,110</u>								

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Why does NCSD maintain separate Funds?

TOWN DIVISION	BLACKLAKE DIVISION
<p>NCSD utilizes the Fund Accounting Method for all of its funds. A fund is defined as a fiscal and accounting entity with a self-balancing set of accounts recording cash and other financial resources, together with all related liabilities and residual equities, or balances, and changes therein, which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions or limitations.</p> <p>The water and sewer funds are considered "Enterprise Funds". The purpose of enterprise funds is to account for operations in a manner similar to private business enterprises. The costs of providing the services should be financed or recovered through user charges.</p>	<p>Blacklake was a fully operational and independent water and sewer system when it was annexed to NCSD. The Specific Plan stated that the water and sewer infrastructure was designed and built (or to be built out in the late 1990's) to serve only those homes within the Blacklake Specific Plan. Since the system was designed and built to serve only those residences, it was appropriate that their systems be accounted for separately and their rates and charges cover the costs of doing business.</p> <p>The Specific Plan states that the funding for operation and maintenance costs will be obtained through agency assessments and/or service charges.</p> <p>The Blacklake Water and Sewer funds were determined to be "Enterprise Funds" and the cost of providing the services should be financed or recovered through user charges.</p>

DR.

History of Water Rates

BLACKLAKE RATES (Residential)

San Luis Obispo County (CSA 1-G) – October 1991 (billed monthly)

First 10 units	\$9.50 per month
11-20 units	\$0.80 per unit
21-30 units	\$1.00 per unit
31 + units	\$1.15 per unit

Nipomo Community Services District annexed Blacklake in 1993 (billed monthly)

Monthly Minimum Charge (Residential)

SIZE OF METER	1993	1994	1995	1996	1997	1998
1 INCH OR LESS	\$ 6.50	\$ 6.50	\$ 6.50	\$ 6.50	\$ 6.50	\$ 6.50

Monthly Commodity Charge (Residential)

UNITS	1993	1994	1995	1996	1997	1998
0-20 Units	\$0.75	\$0.75	\$0.75	\$0.75	\$0.75	\$0.75
21 + Units	\$1.15	\$1.15	\$1.15	\$1.15	\$1.15	\$1.15

Bi-Monthly Minimum Charge (Residential)

SIZE OF METER	1999	2000	2001	2002	2003	2004	2005	8/1/05	2006	2007
1 INCH OR LESS	\$13.00	\$13.00	\$13.00	\$13.00	\$13.00	\$16.22	\$17.86	\$21.41	\$24.42	\$28.40

Bi-Monthly Commodity Charge (Residential)

UNITS	1999	2000	2001	2002	2003	2004	2005	8/1/05	2006	2007
0-40 Units	\$0.75	\$0.75	\$0.75	\$0.75	\$0.75	\$0.75	\$0.75	\$0.97	\$1.16	\$1.42
41 + Units	\$1.15	\$1.15	\$1.15	\$1.15	\$1.15	\$1.15	\$1.15	\$1.70	\$2.04	\$2.49

Note: All rates in effect as of January 1 of each year unless otherwise noted

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History of Water Rates

TOWN RATES (Residential)

Monthly Minimum Charge (Residential)

SIZE OF METER	1993	1994	1995	1996	1997	1998
1 INCH OR LESS	\$ 6.50	\$ 6.50	\$ 6.50	\$ 6.50	\$ 6.50	\$ 6.50

Monthly Commodity Charge (Residential)

UNITS	1993	1994	1995	1996	1997	1998
0-20 Units	\$0.75	\$0.75	\$0.75	\$0.75	\$0.75	\$0.75
21 + Units	\$1.15	\$1.15	\$1.15	\$1.15	\$1.15	\$1.15

Bi-Monthly Minimum Charge (Residential)

SIZE OF METER	7/1/99	2000	2001	2002	2003	2004	2005	8/1/05	2006	2007
1 INCH OR LESS	\$17.50	\$17.50	\$17.50	\$17.50	\$17.50	\$19.26	\$21.04	\$23.08	\$24.75	\$26.96

Bi-Monthly Commodity Charge (Residential)

UNITS	7/1/99	2000	2001	2002	2003	2004	2005	8/1/05	2006	2007
0-40 Units	\$0.80	\$0.75	\$0.85	\$0.90	\$0.95	\$1.01	\$1.07	\$1.12	\$1.23	\$1.38
41 + Units	\$1.15	\$1.15	\$1.24	\$1.33	\$1.42	\$1.51	\$1.64	\$1.91	\$2.10	\$2.35

Note: All rates in effect as of January 1 of each year unless otherwise noted

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**Bruce Buel**

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**From:** Bob Reed [Bob@TheReedGroup.org]  
**Sent:** Monday, October 29, 2007 11:29 AM  
**To:** Bruce Buel  
**Subject:** RE: Sept 26 Reed Presentation Question

Bruce,

The financial plan model for the combined water system recognizes the revenue that would come from the Blacklake Equity Surcharge. The model includes it as revenue to the Water Funded Replacement Fund, and the money is available for capital projects of the combined water system. Water rate calculations are based on the annual water rate revenue requirement, which is comprised of operating costs, including debt service, and a transfer from the Operating Fund to the Funded Replacement Fund based on depreciation. Non-rate revenues of the Operating Fund, as well as operating reserve requirements also have a bearing on the annual water rate revenue requirement. In answering Mr. Eby's question, it is important to recognize that Blacklake Equity Surcharge (as revenue to the Funded Replacement Fund) does not have a direct bearing on the water rate revenue requirement or the water rates. The financial plan model assumes that since the equity surcharge is related to capital investment, it should accrue to the Replacement Fund and used for capital project purposes. I suppose that the revenue could accrue to the Operating Fund and be used to lower the water rates, but that was not done. Alternatively, I suppose that we could have reduced the transfer from Operations to the Replacement Fund by the amount of Equity Surcharge Revenue. However, because it is a policy to "fund depreciation" from water rates, that also was not done.

The advantage of the Equity Surcharge revenue to the combined water system is the availability of \$1+ million in additional money for capital improvement purposes. We did not apply the revenue to reduce the water rates that would otherwise be required. Hope that this helps address Mr. Eby's question.

--Bob

The Reed Group, Inc.

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**From:** Bruce Buel [mailto:bbuel@ncsd.ca.gov]  
**Sent:** Monday, October 29, 2007 7:13 AM  
**To:** Bob Reed; Celeste Whitlow  
**Subject:** FW: Sept 26 Reed Presentation Question

Bob

See below to review Ed Eby's information request. This is agenda item #2 for our 10am phone call.

Thanks

Bruce

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**From:** edeby@charter.net [mailto:edeby@charter.net]  
**Sent:** Friday, October 26, 2007 8:18 AM  
**To:** Bruce Buel  
**Cc:** Lisa Bognuda  
**Subject:** Re: Sept 26 Reed Presentation Question

Partially correct. Page 11 of the September Powerpoint handout showed Water Bill Comparisons With and Without Merger that included the surcharge to Blacklake customers. I asked for the same chart if the equity charge to Blacklake customers were zero (as they want it). In other words I wanted to see the

benefit/disadvantage comparison to each class of customers in Blacklake did not pay a surcharge. I suspect the Town rates will go up and Blacklake will go down.

Ed

On Oct 26, 2007, at 6:56 AM, Bruce Buel wrote:

Ed

At Wednesday's NCSD Board Meeting, you requested that staff revise a figure from the 9/26 Reed Presentation to show what the Town System Rates would be without the merger with Blacklake. Please confirm that you were looking at page 11 of the presentation at the Slide labeled "Water Rates – Combined Water System"

Thanks

Bruce Buel