TO: BOARD OF DIRECTORS

FROM: BRUCE BUEL

DATE: AUGUST 8, 2008

AGENDA ITEM
E-5
AUGUST 13, 2008

REVIEW TOWN WATER CAPACITY CHARGES

ITEM

Receive presentation from rate consultant re potential increases in Town Water Capacity Charges for new development's share of Waterline Intertie Project and set hearing for adoption [RECOMMEND ADOPTION].

BACKGROUND

Attached is the Reed Group report entitled "Capacity Charges for Town Water System and For Supplemental Water". Bob Reed will present the report to the Board at the Board Meeting.

As detailed in the Report, the Reed Group is recommending increases in both the Town Water System Capacity Charge and the Supplemental Water Charge. Adoption of these new charges would entail the scheduling of a noticed hearing and the adoption of a resolution at that hearing. Staff recommends that the Board set this hearing for September 10, 2008.

RECOMMENDATION

Staff recommends that your Honorable Board review the report; ask any questions of Mr. Reed, set the hearing and direct staff to provide notice for that hearing.

ATTACHMENTS

- Reed Group Report

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Nipomo Community Services District

CAPACITY CHARGES FOR THE TOWN WATER SYSTEM AND FOR SUPPLEMENTAL WATER

REVISED DRAFT REPORT

July 18, 2008

THE REED GROUP, INC.

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I. Executive Summary

Introduction

Since 2005, The Reed Group, Inc. has assisted the Nipomo Community Services District with the development of five-year financial plans, water and sewer rates, and capacity charges 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.

This report presents analyses and recommendations for updating (1) the buy-in water capacity charge for the Town water system, and (2) the supplemental water capacity charge. These capacity charges were last comprehensively reviewed in 2005. The remainder of this Executive Summary presents primary findings and recommendations related to the two water capacity charges. Section II provides details regarding methodology, assumptions and information, calculations, and recommended fee schedules.

Proposed Water Capacity Charges

Exhibit I-1 summarizes current and proposed Town water system buy-in capacity charges. The Town water system buy-in capacity charge reflects the estimated cost of capacity in the distribution system, exclusive of water supply facilities. The cost of water supply capacity is reflected in the supplemental water capacity charge. New development will use and benefit from the District's past investments in the water distribution system. Revenue collected from this capacity charge should be used to rehabilitate, upgrade, and expand the distribution system for the benefit of all customers. The proposed Town water system buy-in capacity charge of $3,022 for a new connection with a 1" water meter represents an 8 percent increase from the charges adopted in July 2008.

Exhibit I-1
Nipomo Community Services District
Current and Proposed Town Water Capacity Charges

	Current (1)	Proposed
Town Water System Capacity Charge		
Up to 1" meter	$ 2,800	$ 3,022
1 1/2" meter	$ 8,392	$ 9,065
2" meter	$ 13,432	$ 14,503
3" meter	$ 25,200	$ 27,194
4" meter	$ 42,009	$ 45,323
6" meter	$ 83,993	$ 90,646

Notes:
(1) Effective July 1, 2008 based on Ordinance 2005-101.

Exhibit I-2 presents the current and proposed supplemental water capacity charges. The supplemental water capacity charge reflects the cost of water supply capacity associated with both the Nipomo Waterline Intertie project and associated water supply from the City of Santa Maria, as well as the proposed desalinization project. The supplemental water capacity charge should be charged to all new development within the District's service area, including both the Town and Blacklake divisions. The proposed capacity charge of $13,404 for a new connection with a 1" meter is an 8 percent increase over the current charge. Revenues collected from the supplemental water capacity charge should be used to help pay for supplemental water supply projects, including potential debt service.

Exhibit I-2
Nipomo Community Services District
Current and Proposed Supplemental Water Capacity Charges

	Current (1)	Proposed
Supplemental Water Capacity Charge		
Up to 1" meter	$ 12,452	$ 13,404
1 1/2" meter	$ 37,320	$ 40,211
2" meter	$ 59,735	$ 64,337
3" meter	$ 112,071	$ 120,632
4" meter	$ 186,823	$ 201,054
6" meter	$ 373,534	$ 402,108

Notes:
(1) Effective July 1, 2008 based on Ordinance 2005-101.

II. Water System Capacity Charges

The section of the report describes the calculation of water system buy-in capacity charges for the Town water system, as well as the supplemental water capacity charge. Capacity charges are one-time charges paid at the time of connection to the water system, and represent the estimated reasonable cost of providing system capacity to new development. The calculation of capacity charges is consistent with the statutory requirements contained in Government Code Section 66013.

Current Capacity Charges

The District currently charges developers or other new customers connecting to the Town water system a one time charge for capacity in the water distribution system. In addition, a supplemental water capacity charge was originally developed in 2005. The supplemental water capacity charge is intended to reflect the estimated cost of new supplemental water supply projects. Current water capacity charge schedules are summarized below in **Exhibits II-1 and II-2**. Water system capacity charges are based on meter size and reflect the potential demand on the water system that each new connection could impose. The current capacity charges for the Town water distribution system are based on the system buy-in methodology. The current supplemental water capacity charge was based on the costs related to the water supply Memorandum of Understanding with the City of Santa Maria and preliminary estimates of the cost of a pipeline to convey supplemental water from the City to the District's service area.

Exhibit II-1
Nipomo Community Services District
Current Town Water Capacity Charges

		Current (1)
Town Water System Capacity Charge		
Up to 1" meter	$	2,800
1 1/2" meter	$	8,392
2" meter	$	13,432
3" meter	$	25,200
4" meter	$	42,009
6" meter	$	83,993

Notes:
(1) Effective July 1, 2008 based on Ordinance 2005-101.

Exhibit II-2
Nipomo Community Services District
Current Supplemental Water Capacity Charges

	Current (1)
Supplemental Water Capacity Charge	
Up to 1" meter	$ 12,452
1 1/2" meter	$ 37,320
2" meter	$ 59,735
3" meter	$ 112,071
4" meter	$ 186,823
6" meter	$ 373,534

Notes:
(1) Effective July 1, 2008 based on Ordinance 2005-101.

Legal Requirements for Capacity Charges

The District has broad authority to charge users for capital facilities. The limitations of that authority are encompassed by the requirement that charges on new development bear a *reasonable relationship* to the needs created by and the benefits accruing to that development. California courts have long used the *reasonableness* standard to evaluate the constitutionality of exactions, including capacity charges.

During the 1988 session of the California Legislature sections of the Government Code were added to codify constitutional and decisional law related to fees imposed on new development. Assembly Bill 1600 (AB 1600) enacted Government Code Sections 66000-66003 related to development fees. These code sections generally contain three requirements:

1. Local agencies must follow a process set forth in the statutes and make certain determinations regarding the purpose and use of the fee and to establish a nexus or connection between a development project and the public improvement being financed with the fee.
2. The fee revenue must be segregated from the general fund in order to avoid commingling of development fees and the general fund.
3. If a local agency has unspent or uncommitted development fees for five years or more, then it must make annual findings describing the continuing need for that money, or it must refund the fees.

Since the passage of AB 1600 various code sections have been added and modified to further clarify and expand the requirements related to developer fees. In particular, Government Code Section 66013 contains requirements specific to water and sewer connection fees and capacity charges. The most pertinent part of Section 66013 states:

> ...when a local agency imposes fees for water connections or sewer connections, or imposes capacity charges, those fees or charges shall not exceed the estimated reasonable cost of providing the service for which the fee or charge is imposed...

The key to the statutory requirements for water and sewer capacity charges is that they shall not exceed the *estimated reasonable cost* of providing service. The District's water and sewer system

capacity charges should also meet the reasonable relationship standard mentioned earlier and should reflect consideration of the following criteria, which would likely be considered by a court in evaluating the validity of capacity charges:

Need – Water and sewer capacity charges should only be imposed on development that will need capacity in facilities provided by the District (i.e., development with a connection to the water and/or sewer system).

Benefit – Improvements to be funded (or reimbursed) by capacity charges should satisfy the service needs related to the development on which the charges are imposed (i.e., new development is served by the facilities paid for by the charges).

Amount – The amount of the capacity charges should reflect the estimated reasonable cost of providing service capacity, and the share of the costs attributable to the service needs of new development (i.e., the charges should reflect a proportionate share of costs).

Earmarking – Revenue from water and sewer capacity charges should be segregated from other funds and used solely to pay for the facilities for which the charges re imposed.

Timely Expenditure – Revenue from water and sewer capacity charges should be expended within a reasonable time after it is collected.

Applying these criteria to the District's situation requires an understanding of how improvement needs are established, how capacity is provided to new development, how costs are estimated and allocated, and how fee revenues are accounted for and spent.

Town Water System Buy-In Capacity Charge Methodology

There are numerous methodologies for calculating capacity charges. The number has proliferated with the growing popularity of this type of charge. Various methodologies have evolved to meet changing public policy, legal requirements, and the unique or special circumstances of each local agency. The capacity charge methodology developed for the Town water system in 2005 was based on the system buy-in methodology.

The buy-in methodology is based on the current customers' average investment in the water system. Under this approach, capacity charges are based upon the buy-in concept that existing users through service charges, past up-front charges, and other contributions have developed a valuable public capital facility. The charge is computed by establishing the current value of the system and dividing this by the number of existing customers to arrive at an average investment per customer. By paying the buy-in capacity charge new customers buy into the existing water system on par with existing customers. Responsibility for new capital improvements is then shared equally by all customers.

The basic equation for buy-in capacity charges is:

$$\frac{\text{Value of Existing System}}{\text{No. of Existing Customers}}$$

At this time, the District anticipates a number of capital improvements to rehabilitate, upgrade and expand the water distribution system. Existing water supply facilities (i.e., groundwater wells) have been excluded from the Town water system capacity charge calculation. This is because water supply facilities are included in the supplemental water capacity charge. Including groundwater

facilities in the buy-in capacity charge could be a form of double charges, which needs to be avoided.

The water system buy-in capacity charge reflects the current value of the water distribution system, pumps (other than wells), storage facilities, buildings, and land. The capacity charge is calculated in the same manner as the current capacity charge, and reflects the value of water system assets from the District's fixed asset records.

The incremental cost methodology is a fairly common approach for capacity charges, particularly for communities experiencing new growth or making significant new capacity additions to their utility systems. The approach is based on the cost of new or planned facilities. The cost of growth-related facilities is allocated to new development to be served by the facilities. Under this approach, new development pays for the incremental investment necessary for system expansion. The incremental cost approach is most commonly applied when new facilities are required to provide capacity for new development.

The basic equation for incremental cost capacity charges is:

$$\frac{\text{Cost of System Expansion}}{\text{No. of New Customers}}$$

The incremental cost methodology is not recommended for the sewer collection system. This is because new development will largely utilize the existing collection system network. Extensions of the existing collection system will likely be similar to existing system costs (on a per customer basis). Continuing to use the system buy-in approach for the collection system is reasonable.

Town Water System Buy-In Capacity Charge Calculations

Capacity charge calculations are described in greater detail below. The calculations for the Town water system capacity charge is summarized in **Exhibit II-3**.

In calculating buy-in capacity charges, the value of the water system assets were determined using fixed asset accounting records obtained from the District. Several adjustments to these records were made, as described below. In addition to fixed assets, the valuation includes the funds available in the Town Division's Funded Replacement and Capital Improvement funds for capital improvements. These funds include money intended for improvements to the water system. Finally, the valuation also reflects interest paid on long-term debt as well as a reduction for outstanding principal related to long-term debt.

Fixed Asset Records

Central to the buy-in capacity charge calculation is the District's water system fixed asset records. A complete listing of the Town Division's water system fixed assets was obtained and used for the buy-in charge calculations. The following adjustments were made to these asset records for purpose of the capacity charge calculation:

- *Groundwater Well Facilities Omitted* – Groundwater wells are excluded from the Town water system fixed asset records for capacity charge calculations because water supply costs are included in the supplemental water capacity charge.

Exhibit II-3
Nipomo Community Services District
Town Water -- Distribution System Buy-In Capacity Charge

	Original Cost	Depreciated Cost	Replacement Cost	Depreciated Replacement Cost
Town Water System Assets (1)				
Pumping (1520)	$ 3,037,252	$ 1,190,838	$ 4,669,744	$ 1,573,811
Less Groundwater Wells	$ (1,144,571)	$ (421,073)	$ (1,887,580)	$ (573,584)
Transmission (1525)	$ 3,184,957	$ 2,426,781	$ 5,143,842	$ 3,487,122
Distribution (1530)	$ 634,953	$ 228,818	$ 1,305,365	$ 349,357
Buildings (1540)	$ 55,187	$ 29,433	$ 84,628	$ 45,135
Land and Land Rights (1560)	$ 279,973	$ 267,098	$ 391,118	$ 373,955
Less COP Financed Facilities	$ (1,458,339)	$ (1,332,611)	$ (1,733,002)	$ (1,583,136)
Water System Asset Total				**$ 3,672,660**
Adjustments to Valuation				
Plus Replacement Fund (800) (2)				$ 2,235,000
Plus Capacity Charge Fund (700) (2)				$ 4,713,000
Plus Past Interest on Long-Term Debt (3)				$ 323,000
Less Outstanding Principal on Long-Term Debt (3)				$ (129,000)
Total Town Water System Valuation				**$ 10,814,660**
Current 1" Equivalent Meters (4)				3,579
Town Water System Buy-In Capacity Charge (up to 1" meter)				**$ 3,022**

Notes:

(1) Excludes groundwater wells, machinery/equipment, office furniture, vehicles, computer equipment, water meters, facilities financed with 2003 COPs, and contributed facilities.
(2) As of July 1, 2008 from FY 08-09 budget.
(3) Related to $270,000 Water Revenue Bonds as of January 1, 2008.
(4) Based on customer account data as of June 2007.

- *Short-Lived Assets Omitted* – Assets with useful lives of less than 10 years were excluded from the buy-in calculations. Short-lived assets typically include vehicles, equipment, machinery, computers, office furnishings, etc. While these assets make up part of the overall value of the water utility, they are generally not part of the service delivery systems. Arguably short-lived assets could be included in the buy-in charge calculation, however excluding them is conservative. New customers will pay for short-lived assets as ratepayers.

- *Developer Contributed Facilities Omitted* – Fixed asset records include a variety of water assets that were contributed by developers. Most of these facilities are likely in-tract or development project-specific improvements (e.g., water distribution lines within a subdivision). In tract facilities are appropriately excluded from the buy-in charge calculation because they may not provide system-wide benefits. In some cases developer contributed facilities may include some system improvements with broad system-wide benefits. However, such facilities are not readily identifiable from the fixed asset listing, and omitting all contributed facilities is conservative.

Escalation and Depreciation

The value of water system assets was adjusted from original cost to current value by (1) escalating historical costs to replacement cost in current dollars using the *Engineering News Record* 20-cities construction cost index (20-cities CCI), and (2) depreciating from the date of construction to 2008 based on the service life of each asset. Both of these adjustments are typical (though not required) in buy-in charge calculations. Historical costs were escalated to replacement value using the 20-cities CCI value of 8,293 for July 2008.

Service lives for fixed asset depreciation are the same as those used for accounting depreciation. Water system assets have service lives of up to 50 years. Straight-line depreciation is used. The last column in Exhibit II-3 shows the value of water system assets based on the depreciated replacement cost.

Capital Fund Balances

At the end of FY 07-08 the Town Division had about $2.235 million in the Funded Replacement Fund and about $4.713 million in the Capital Improvement Fund of the Town water system. While these funds are not capital facilities, they are intended to be used for capital projects that will rehabilitate, upgrade, and/or expand the water distribution system. Cash in capital funds are appropriately included in the buy-in charge calculation.

Debt Service Adjustments

As of January 2008, the District has $129,000 outstanding on water revenue bonds issued in 1978 related to water facilities in the Town Division. Outstanding principal is deducted from the water system valuation. Past debt issuance and interest costs on long-term debt can be added to the value of the water system. Financing costs are real costs associated with acquiring and constructing facilities and can be added to the valuation. Past interest on the water revenue bonds now total about $323,000.

Existing Customers (Equivalent Dwelling Units)

The system buy-in method for calculating capacity charges for new development bases the charges on the average value of the water distribution system for existing customers. Hence, once the value of the systems have been determined it is necessary to divide this amount by the number of customers, or more appropriately, the number of 1" equivalent meters. The number of existing 1" equivalent meters was determined from customer account information obtained from the billing system in June 2007. The number of existing water service customers, expressed in 1" equivalent meters, is 3,579.

As shown in Exhibit II-3, the water distribution system buy-in capacity charge, based on the buy-in methodology, has been calculated to be $3,022 for a 1" meter.

Proposed Town Water System Buy-In Capacity Charges

A complete fee schedule for the Town water distribution system buy-in capacity charge is shown in **Exhibit II-4**. The base capacity charge should apply to all new water connections in the Town Division that have water connections with meters of up to 1". Above 1" the water capacity charge should be as shown in Exhibit II-4.

Exhibit II-4
Nipomo Community Services District
Current and Proposed Town Water Capacity Charges

	Current (1)	Proposed
Town Water System Capacity Charge		
Up to 1" meter	$ 2,800	$ 3,022
1 1/2" meter	$ 8,392	$ 9,065
2" meter	$ 13,432	$ 14,503
3" meter	$ 25,200	$ 27,194
4" meter	$ 42,009	$ 45,323
6" meter	$ 83,993	$ 90,646

Notes:
(1) Effective July 1, 2008 based on Ordinance 2005-101.

Supplemental Water

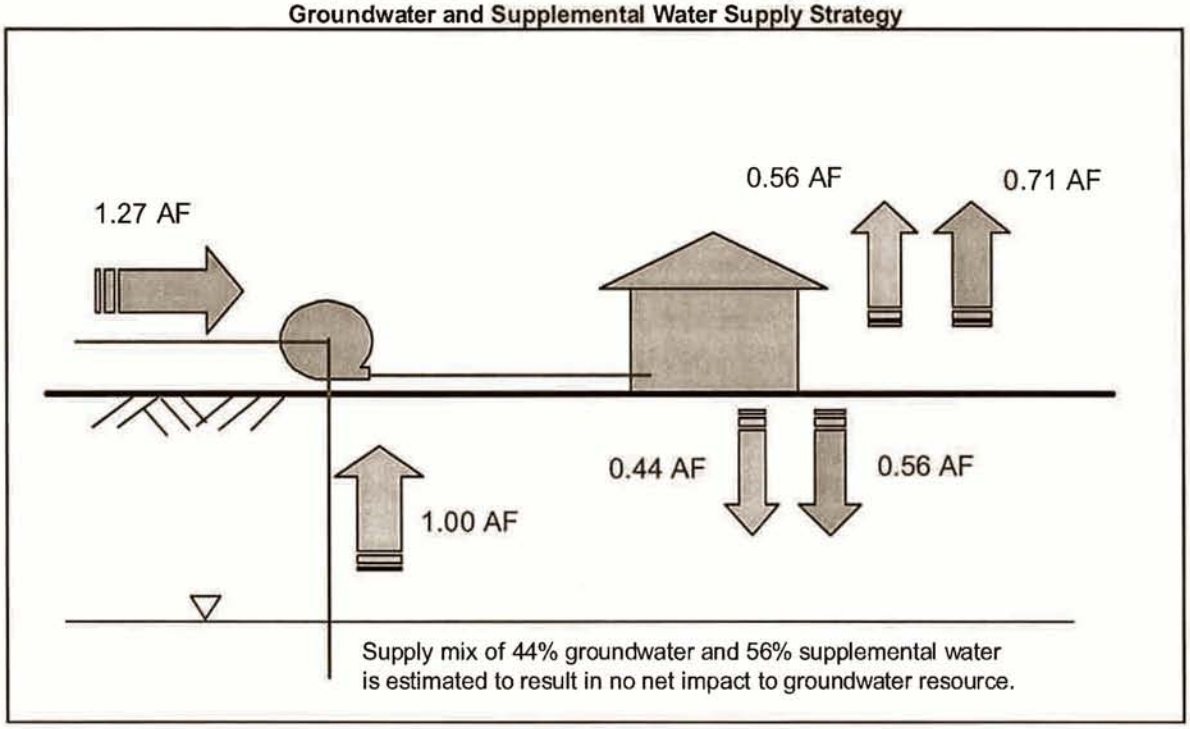
Currently the District obtains 100 percent of its water supply from groundwater from the Nipomo hydrologic sub-area of the greater Santa Maria groundwater basin. The District has been mandated by a stipulated judgment to develop alternative water supplies to reduce demand on groundwater resources. As a result, the District is developing supplemental water supply projects to help offset existing groundwater use and to meet future needs.

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-5**, for each AF of groundwater extracted from the basin and 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 or otherwise leaves the basin. Providing 1.27 AF of supplemental water for each 1.00 AF of groundwater is estimated to result in no net impact to the groundwater resource. The water supply mix is used in capacity charge analyses.

In September 2004, the District and the 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 water from the City. Under the MOU water delivered under the agreement will cost $1,250 per AF. The District needs to construct a transmission pipeline and related pumping facilities to convey water from the City to the District's service area. In April 2008, Boyle Engineering prepared a preliminary engineering memorandum on the *Nipomo Waterline Intertie Project*[1]. This report provides estimates of the cost of constructing conveyance facilities for use of supplemental water provided the City. In addition, the District's *Water and Sewer Master Plan Update*[2] includes costs of additional facilities needed to accommodate supplemental water within the distribution system. These documents provide information used in capacity charge analyses.

[1] *Draft Nipomo Waterline Intertie Project – Preliminary Engineering Memorandum*, prepared by Boyle Engineering Corporation, April 2008.
[2] *Water and Sewer Master Plan Update*, prepared by Cannon Associates, December 2007.

Exhibit II-5
San Luis Obispo County
Nipomo Mesa Supplemental Water Capacity Charge
Groundwater and Supplemental Water Supply Strategy



The District is also exploring a desalinization project to provide an additional source of supplemental water for the Nipomo Mesa. The Evaluation of Supplemental Water Alternatives: Desalinization Option[3] provides costs estimates for constructing a desalinization facility with a capacity of 6,300 AF per year including intake, treatment, and outfall facilities. The report identifies estimated costs to develop and construct the facility. Information in that report is used in capacity charge calculations. It should be noted that current studies do not include costs associated with transmission, pumping, and storage of supplemental water produced at a desalinization facility. Since those costs are not yet known, they are not included in the capacity charge analyses presented in this report.

Supplemental water that may be made available through the Nipomo waterline intertie and the desalinization project would exceed the water needed by the District, and cost sharing arrangements with other water purveyors and water users may be considered.

Supplemental Water Capacity Charge Methodology

The supplemental water capacity charge is based on the cost of capacity associated with the District's potential supplemental water supply projects. The methodology for calculating the supplemental water capacity charge is generally referred to an incremental cost methodology. In

[3] *Evaluation of Supplemental Water Alternatives: Desalinization Option, Administrative Draft Technical Memorandum 2, Work Plan for Project Implementation*, prepared by Boyle Engineering Corporation, September 24, 2007.

short, the cost of capacity in future facilities is divided by the units of capacity to be provided to arrive at a cost per unit of capacity.

Because the District is pursuing two supplemental water supply projects in order to meet long-term water needs, the capacity charge methodology takes a weighted average of the cost of capacity in each project to arrive at the proposed capacity charge. In effect, each new unit of new development would be paying for a portion of capacity in both projects.

The incremental cost methodology often requires more detailed analyses in order to satisfy nexus requirements. First, the capacity requirements of new development must be defined. Second, the amount of capacity provided by new facilities must be determined, and capacity enhancements required to address existing deficiencies should be considered. To the extent that existing capacity does not provide the specified level of service to existing development, new facilities must be identified to correct these deficiencies, and fees paid by new development can not be used to correct existing deficiencies. As a result, it is fairly common for only a portion of new capacity facilities costs to be included in fee calculations.

Supplemental Water Capacity Charge Calculations

The supplemental water capacity charge is calculated in several steps. First, it is necessary to identify the capital costs associated with each supply project.

Santa Maria MOU

The MOU with the City of Santa Maria calls for the District to pay a $750,000 reservation fee in installments to secure a long-term contract for water. Water delivered under the contract will cost $1,250 per AF and be available until 2065 (the MOU allows for a potential adjustment to the rate for water in 2036). The $1,250 per AF cost for water from Santa Maria is based on the cost of State Water Project (SWP) water obtained by the City through the Central Coast Water Authority (CCWA)[4]. The rate for water also reflects both capital and operating costs associated with CCWA delivery of SWP water to the City. In effect, capital costs associated with the SWP have been amortized into the commodity rate.

Based on information presented in the 2005 calculation of the supplemental water capacity charge[5], approximately 69 percent of the rate for water reflects capital costs of providing water. On this basis, the supplemental water capacity charge included 69 percent of the $1,250 per AF water rate as an amortized capital cost, which can be included in capacity charge calculations.

Exhibit II-6 summarizes the estimated capital cost reflected in the rate for water contained in the MOU with the City of Santa Maria. This capital cost of $16,071 per AF is one component of the cost of capacity associated with the Nipomo Waterline Intertie project. This cost is slightly lower than the estimate in 2005 because of the later date assumed for when the District would begin taking water under the agreement with the City.

[4] The MOU does not specify SWP water (the City also has groundwater resources), but the cost of SWP water is the basis for the rate.

[5] See pages 55-57 of the Water and Sewer Financial Plans, User Rates, and Capacity Charges – Final Report, prepared by The Reed Group, Inc., May 25, 2005.

Exhibit II-6
Nipomo Community Services District
Santa Maria MOU Capital Cost Estimate

Supplemental Water from City of Santa Maria			
Water rate per MOU	$	1,250	
Portion of rate associated with capital costs (1)		69%	
Amortized capital cost of water supply	$	862.50	
Term of water deliveries under contract (2)		55	
Assumed discount rate on future costs		5.0%	
Net present value of capital cost for 1 AF/yr	$	16,071	per AF

Notes:

(1) From 2005 supplemental water capacity charge analysis.
(2) Assumes water deliveries begin in 2010 with contract through 2065.

Nipomo Waterline Intertie Project

The Nipomo Waterline Intertie Project would provide the conveyance capacity to use the 3,000 AF available under the MOU with the City of Santa Maria. **Exhibit II-7** summarizes the estimated capital cost associated with the project. In addition to the costs included in the Preliminary Engineering Memorandum, Exhibit II-7 includes the cost of transmission facilities needed with the District's water distribution system to utilize supplemental water. Costs have been adjusted using the Engineering News Record's 20-Cities Construction Cost Index for July 2008. Total costs are currently estimated at about $31.72 million. These facilities, in conjunction with the MOU with the City of Santa Maria, would provide the District with 3,000 AF of supplemental water.

Desalinization Project

Exhibit II-8 summarizes the estimated capital cost associated with the proposed desalinization project, which would provide up to 6,300 AF of supplemental water annually. Costs have been adjusted to July 2008 using the 20-Cities CCI. The adjusted cost to develop and construct the desalinization facility is $88.6 million.

Estimated Future Demands and Supplemental Water Supply Requirements

The District's most recent water demand projects are reflected in the *2005 Urban Water Management Plan*[6] and the *Water and Sewer Master Plan Update*. The District's total water demand in 2030 is estimated to be 5,226 AF based on land use. Assuming an 8 percent unaccounted for water loss rate, total water production of 5,680 AF will be required to meet the 2030 water demand.

Exhibit II-9 summarizes current and future (2030) water demands. Current water demands are based on water sales during FY 06-07, adjusted for an assumed 8 percent unaccounted for loss rate. Current water demands are almost exactly the future projection for 2030. Exhibit II-9 also summarizes how current and future water demands would be met with a water supply mix comprised of 44 percent groundwater and 56 percent supplemental water. Using this supply mix, the District will need about 3,181 AF of supplemental water by 2030.

Exhibit II-10 summarizes how the District's need for supplemental water may be met using both water from Santa Maria and desalinization. At present, the District plans to reserve 2,000 AF of Santa Maria water for its own use and to provide 1,000 AF to other purveyors. Therefore, 2,000 AF of the 3,181 AF supplemental water requirement would be met with water from Santa Maria. This leaves 1,181 AF to be provided from the desalinization project. The remaining 5,119 AF of water from the desalinization project would be available to other water users.

Based on the preceding assumptions, the District's total water supply mix in 2030 would be:

Groundwater	2,499 AF	44%
Santa Maria water	2,000 AF	35%
Desalinization water	1,181 AF	21%
Total	5,680 AF	100%

[6] *Urban Water Management Plan 2005 Update*, Nipomo Community Services District, Adopted January 25, 2006.

Exhibit II-7
Nipomo Community Services District
Nipomo Waterline Intertie Project Cost Estimates

Nipomo Waterline Intertie Project (1)		
Alignment #1 - Western River Crossing		
Phase I - 1,300 gpm, 2000 AF/yr		
Mobilization	$	541,615
Santa Maria System Upgrade		1,235,000
Waterline Intertie - Western Alignment		8,663,800
Nipomo System Upgrades		933,500
Sub-Total		11,373,915
Adjustment for Constr. Cost Inflation (2)		591,565
Adjusted Sub-Total		11,965,480
Engr. & Constr. Mgmt. (20%)		2,393,096
Contingency (30%)		3,589,644
Total Nipomo Intertie Project	$	17,948,220
NCSD Master Planned Improvements	$	1,806,327
Phase I Total	$	19,754,546
Phase II - 1,860 gpm, 3000 AF/yr		
Mobilization	$	28,620
Upgrade Capacity of Pump Station No. 2		68,000
12" Upgrade on Orchard, Southland to Division		504,400
Sub-Total		601,020
Adjustment for Constr. Cost Inflation (2)		31,259
Adjusted Sub-Total		632,279
Engr. & Constr. Mgmt. (20%)		126,456
Contingency (30%)		189,684
Phase II Total	$	948,419
Water Master Plan Projects to Accommodate New Supply (3)		
Near-Term Improv. at Thompson & Mehlschau	$	5,500,000
Willow Road Extension Improvements		3,252,000
Interim-Term Improv. at Willow & Highway 1		1,770,000
Sub-Total		10,522,000
Adjustment for Constr. Cost Inflation (4)		494,153
Total Mstr. Plan Projects to Accom. New Supply	$	11,016,153
Total Nipomo Intertie Project	**$**	**31,720,000**

Notes:

(1) From Draft Nipomo Waterline Intertie Project - Preliminary Engineering Memorandum by Boyle Engineering, April 2008 (as revised on 4/23/2008).
(2) Adjusted from October 2006 to July 2008 using the ENR 20-Cities Construction Cost Index.
(3) From Water and Sewer Master Plan Update prepared by Cannon Associates, December 2007.
(4) Adjusted from May 2007 to July 2008 using the ENR 20-Cities Construction Cost Index.

Exhibit II-8
Nipomo Community Services District
Nipomo Mesa Desalinization Project Cost Estimates

Nipomo Mesa Desalinization Project (1)		
Terrestrial and Freshwater Impact Studies	$	30,000
Phase 1 Marine Impact Studies		110,000
Cultural Resource Studies		24,000
Phase 1 Hydrogeologic Field Study		360,000
Test-Scale Feasibility Study		2,320,000
Phase 2 Hydrogeologic Field Study		180,000
Preliminary Engineering		210,000
CEQA/NEPA		240,000
Public Outreach		1,310,000
Design and Permitting		2,870,000
Construction		46,090,000
Project Management		1,500,000
Total Before Contingency	$	55,267,000
Contingency		17,202,000
Cost Escalation (to Sept. 2007)		13,540,000
Total Desalinization Project	$	86,010,000
Total Adjusted to July 2008 (2)	**$**	**88,600,000**

Notes:
(1) From Evaluation of Supplemental Water Alternatives: Desalinization Option - Administrative Draft Technical Memorandum - Work Plan for Project Implementation, prepared for Nipomo Community Services District by Boyle Engineering, September 24, 2007.
(2) Adjusted from September 2007 to July 2008 using the ENR 20-Cities Construction Cost Index.

Exhibit II-9
Nipomo Community Services District
Current and Projected Water Demands (AF)

	Water Demand	Supply Goals (4) Groundwater	Suppl. Wtr.
		44%	56%
Current (1)	2,839	1,249	1,590
Future Growth (2)	2,841	1,250	1,591
Total Demand in 2030 (3)	5,680	2,499	3,181

Notes:
(1) Based on FY 06-07 water sales and assumed unaccounted for losses of 8% of production.
(2) Derived from total future demand minus current demand.
(3) From Table 2-3 of the Water and Sewer Master Plan Update adjusted for an assumed 8% unaccounted for losses.
(4) The District has estimated that a supply mix of 44% groundwater and 56% supplemental water will result in no net impact to the groundwater basin.

Exhibit II-10
Nipomo Community Services District
NCSD Supplemental Water Requirements (AF)

	Total Capacity	NCSD	Other Purveyors
NCSD Intertie Project (1)	3,000	2,000	1,000
Desalinization Project (2)	6,300	1,181	5,119
Total Supplemental Water	9,300	3,181	6,119

Notes:
(1) NCSD plans to utilize 2,000 AF with 1,000 AF for other purveyors.
(2) Assumes NCSD participates in capacity to meet water needs through 2030.

The District, and existing customers, has made the investment in the District's current groundwater production facilities. The 2005 supplemental water capacity charges were based on requiring new development to pay for water supply capacity based on meeting 100 percent of new demands with supplemental water. As customers, however, new development would receive the same blended water supply as all other customers, and water rates would reflect the blended water supply cost. The approach for the supplemental water capacity charge is reasonable and consistent with the water resource management framework controlling activity in the region.

Supplemental Water Supply Capacity Charge Calculation

Exhibit II-11 summarizes the calculation of the proposed supplemental water capacity charge. The calculation reflects the cost of each supplemental water supply project, and weights the calculation based on the proportion of supplemental water estimated to be derived from each source.

The capital cost of water under the MOU with Santa Maria and conveyance to the District with the Nipomo Waterline Intertie project is calculated to be $26,644 per AF. The capital cost of water from a desalinization project is calculated to be $14,063 per AF. This cost, however, does not include the yet-to-be-determined cost of pumping, transmission, storage, and distribution of desalinized water.

Using 2,000 AF of water from Santa Maria and 1,181 AF of desalinized water to meet the District's future water demands, the cost of supplemental water capacity is calculated to $21,973 per AF. Based on current water demands characteristics of single family customers, the District will need to produce about 0.61 AF of water for each residential customer. Using this as the basis for the supplemental water capacity charge for a 1" water meter, the proposed supplemental water capacity charge is $13,404.

The supplemental water capacity charge calculations shown in Exhibit II-11 do not include the costs associated with debt financing. Financing costs, including issuance and interest costs, are costs associated with constructing facilities using debt financing, and these costs can be included in capacity charge calculations. Financing costs are not included herein because the District has not yet committed to debt financing. At such time as the District issues debt to financing projects (or is initiating the issuance process) then financing costs should be added to the capacity charge calculation. If the District were to finance the Nipomo Waterline Intertie project and the

desalinization project the proposed supplemental water capacity charge might increase from $13,404 to $18,834 for a 1" water meter.

Proposed Supplemental Water Capacity Charges

Exhibit II-12 presents a complete schedule for the proposed supplemental water capacity charge for each meter size. The fees increase across meter sizes based on the hydraulic capacity associated with each size meter. This relationship is indicative of the potential demand that each new customer (each meter size) could place on the water system. Proposed supplemental water capacity charges are about 8 percent higher than the current charges, which were implemented in July 2008.

Exhibit II-11
Nipomo Community Services District
Supplemental Water Capacity Charge Calculation

Unit Cost of Supplemental Water from NCSD Intertie Pipeline			
Intertie Pipeline Capital Cost	$	31,720,000	
Financing Costs	$	-	
Total Cost	$	31,720,000	
Pipeline Capacity		3,000	AF
Pipeline Capacity Cost	$	10,573	per AF
Water Supply Capital Cost	$	16,071	per AF
Unit Cost of Intertie Project Supply	$	26,644	per AF
Unit Cost of Supplemental Water from Desalinization Project			
Desalinization Project Capital Cost	$	88,600,000	
Financing Costs	$	-	
Total Cost	$	88,600,000	
Project Capacity		6,300	AF
Unit Cost of Desalinization Project	$	14,063	per AF

NCSD Supplemental Water Capacity Charge

	Unit Cost ($/AF)	NCSD Capacity (AF)	Capacity Cost	
Intertie Project	$ 26,644	2,000	$ 53,288,000	
Desalinization Project	$ 14,063	1,181	$ 16,608,403	
Totals		3,181	$ 69,896,403	
			3,181	AF
Supplemental Water Capacity Charge -->			$ 21,973	per AF
Water required for single family (basis for 1" meter charge) -->			0.61	AF
Supplemental Water Capacity Charge for 1" meter -->			**$ 13,404**	

Exhibit II-12
Nipomo Community Services District
Current and Proposed Supplemental Water Capacity Charges

	Current (1)	Proposed
Supplemental Water Capacity Charge		
Up to 1" meter	$ 12,452	$ 13,404
1 1/2" meter	$ 37,320	$ 40,211
2" meter	$ 59,735	$ 64,337
3" meter	$ 112,071	$ 120,632
4" meter	$ 186,823	$ 201,054
6" meter	$ 373,534	$ 402,108

Notes:
(1) Effective July 1, 2008 based on Ordinance 2005-101.

Accounting for Capacity Charge Revenues and Expenditures

Under Government Code Section 66013(c) the District is required to separately account for capacity charge revenues in a manner that avoids commingling of capacity charge revenues with other revenues and to expend capacity charge revenues solely for the purpose for which the charges have been collected.

Under Government Code Section 66013(d), within 180 days after the end of each fiscal year, the District is required to make the following information related to capacity charges publicly available for the prior fiscal year:

- A brief description of the type of capacity charge in each account or fund
- The amount of the capacity charges
- The beginning and ending balance of the account or fund
- The amount of the capacity charges collected and the interest earned
- Identification of each capital improvement on which capacity charges were expended and the amount of the expenditures on each improvement, including the total percentage of the cost of the improvement that was funded with the charges
- Identification of each capital improvement on which capacity charges were expended that were completed during the fiscal year
- Identification of each capital improvement that is anticipated to be undertaken in the following fiscal year
- Description of any interfund transfers or loans made from capacity charge accounts or funds, including the capital improvement on which the transferred or loaned funds will be expended, and in the case of a loan the date on which the loan will be repaid, and the interest to be received

Capacity Charge Updates

At a minimum, it is recommended that the District's capacity charges be adjusted annually for inflation based on the 20-cities CCI. This is a common means of updating capacity charges and

works reasonably well for a few years. A more comprehensive and accurate way to update the capacity charges is to recalculate them using the same calculation methodologies used in this report and then-current information. It is recommended that a comprehensive update be performed at least every 3 to 5 years.

The buy-in methodology used to calculate the Town water system capacity charges is relatively simple to update once the procedures are put in place. The recalculation of capacity charges entails making the following updates to the calculations:

- Add new water distribution facilities included in fixed asset records, and delete those taken out of service.
- Update the fixed asset valuation for inflation (using the 20-cities CCI) and depreciation. The fees proposed herein have been indexed to the 20-cities CCI value for July 2008 of 8,293.
- Update cash balance information in capital funds.
- Adjust historical debt service costs for inflation, recent interest payments, and any new debt issuance costs.
- Update the current number of equivalent meters included in the existing water/sewer systems.

The supplemental water capacity charge calculation can be updated by following these steps:

- Update cost estimates for each project included in the capacity charge analysis, or use actual cost information once projects are completed.
- Update demand projections and capacity information.
- Include debt financing costs if and when long-term debt is issued to help finance the supplemental water projects.

Appendix A – Government Code Sections 66013, 66016, 66022, and 66023

66013. (a) Notwithstanding any other provision of law, when a local agency imposes fees for water connections or sewer connections, or imposes capacity charges, those fees or charges shall not exceed the estimated reasonable cost of providing the service for which the fee or charge is imposed, unless a question regarding the amount of the fee or charge imposed in excess of the estimated reasonable cost of providing the services or materials is submitted to, and approved by, a popular vote of two-thirds of those electors voting on the issue.

(b) As used in this section:

(1) "Sewer connection" means the connection of a structure or project to a public sewer system.

(2) "Water connection" means the connection of a structure or project to a public water system, as defined in subdivision (f) of Section 116275 of the Health and Safety Code.

(3) "Capacity charge" means a charge for facilities in existence at the time a charge is imposed or charges for new facilities to be constructed in the future that are of benefit to the person or property being charged.

(4) "Local agency" means a local agency as defined in Section 66000.

(5) "Fee" means a fee for the physical facilities necessary to make a water connection or sewer connection, including, but not limited to, meters, meter boxes, and pipelines from the structure or project to a water distribution line or sewer main, and that does not exceed the estimated reasonable cost of labor and materials for installation of those facilities.

(c) A local agency receiving payment of a charge as specified in paragraph (3) of subdivision (b) shall deposit it in a separate capital facilities fund with other charges received, and account for the charges in a manner to avoid any commingling with other moneys of the local agency, except for investments, and shall expend those charges solely for the purposes for which the charges were collected.

Any interest income earned from the investment of moneys in the capital facilities fund shall be deposited in that fund.

(d) For a fund established pursuant to subdivision (c), a local agency shall make available to the public, within 180 days after the last day of each fiscal year, the following information for that fiscal year:

(1) A description of the charges deposited in the fund.

(2) The beginning and ending balance of the fund and the interest earned from investment of moneys in the fund.

(3) The amount of charges collected in that fiscal year.

(4) An identification of all of the following:

(A) Each public improvement on which charges were expended and the amount of the expenditure for each improvement, including the percentage of the total cost of the public improvement that was funded with those charges if more than one source of funding was used.

(B) Each public improvement on which charges were expended that was completed during that fiscal year.

(C) Each public improvement that is anticipated to be undertaken in the following fiscal year.

(5) A description of each interfund transfer or loan made from the capital facilities fund. The information provided, in the case of an interfund transfer, shall identify the public improvements on which the transferred moneys are, or will be, expended. The information, in the case of an interfund loan, shall include the date on which the loan will be repaid, and the rate of interest that the fund will receive on the loan.

(e) The information required pursuant to subdivision (d) may be included in the local agency's annual financial report.

(f) The provisions of subdivisions (c) and (d) shall not apply to any of the following:

(1) Moneys received to construct public facilities pursuant to a contract between a local agency and a person or entity, including, but not limited to, a reimbursement agreement pursuant to Section 66003.

(2) Charges that are used to pay existing debt service or which are subject to a contract with a trustee for bondholders that requires a different accounting of the charges, or charges that are used to reimburse

the local agency or to reimburse a person or entity who advanced funds under a reimbursement agreement or contract for facilities in existence at the time the charges are collected.

(3) Charges collected on or before December 31, 1998.

(g) Any judicial action or proceeding to attack, review, set aside, void, or annul the ordinance, resolution, or motion imposing a fee or capacity charge subject to this section shall be brought pursuant to Section 66022.

(h) Fees and charges subject to this section are not subject to the provisions of Chapter 5 (commencing with Section 66000), but are subject to the provisions of Sections 66016, 66022, and 66023.

(i) The provisions of subdivisions (c) and (d) shall only apply to capacity charges levied pursuant to this section.

66016. (a) Prior to levying a new fee or service charge, or prior to approving an increase in an existing fee or service charge, a local agency shall hold at least one open and public meeting, at which oral or written presentations can be made, as part of a regularly scheduled meeting. Notice of the time and place of the meeting, including a general explanation of the matter to be considered, and a statement that the data required by this section is available, shall be mailed at least 14 days prior to the meeting to any interested party who files a written request with the local agency for mailed notice of the meeting on new or increased fees or service charges. Any written request for mailed notices shall be valid for one year from the date on which it is filed unless a renewal request is filed. Renewal requests for mailed notices shall be filed on or before April 1 of each year. The legislative body may establish a reasonable annual charge for sending notices based on the estimated cost of providing the service. At least 10 days prior to the meeting, the local agency shall make available to the public data indicating the amount of cost, or estimated cost, required to provide the service for which the fee or service charge is levied and the revenue sources anticipated to provide the service, including General Fund revenues. Unless there has been voter approval, as prescribed by Section 66013 or 66014, no local agency shall levy a new fee or service charge or increase an existing fee or service charge to an amount which exceeds the estimated amount required to provide the service for which the fee or service charge is levied. If, however, the fees or service charges create revenues in excess of actual cost, those revenues shall be used to reduce the fee or service charge creating the excess.

(b) Any action by a local agency to levy a new fee or service charge or to approve an increase in an existing fee or service charge shall be taken only by ordinance or resolution. The legislative body of a local agency shall not delegate the authority to adopt a new fee or service charge, or to increase a fee or service charge.

(c) Any costs incurred by a local agency in conducting the meeting or meetings required pursuant to subdivision (a) may be recovered from fees charged for the services which were the subject of the meeting.

(d) This section shall apply only to fees and charges as described in Sections 51287, 56383, 57004, 65104, 65456, 65863.7, 65909.5, 66013, 66014, and 66451.2 of this code, Sections 17951, 19132.3, and 19852 of the Health and Safety Code, Section 41901 of the Public Resources Code, and Section 21671.5 of the Public Utilities Code.

(e) Any judicial action or proceeding to attack, review, set aside, void, or annul the ordinance, resolution, or motion levying a fee or service charge subject to this section shall be brought pursuant to Section 66022.

66022. (a) Any judicial action or proceeding to attack, review, set aside, void, or annul an ordinance, resolution, or motion adopting a new fee or service charge, or modifying or amending an existing fee or service charge, adopted by a local agency, as defined in Section 66000, shall be commenced within 120 days of the effective date of the ordinance, resolution, or motion.

If an ordinance, resolution, or motion provides for an automatic adjustment in a fee or service charge, and the automatic adjustment results in an increase in the amount of a fee or service charge, any action or proceeding to attack, review, set aside, void, or annul the increase shall be commenced within 120 days of the effective date of the increase.

(b) Any action by a local agency or interested person under this section shall be brought pursuant to Chapter 9 (commencing with Section 860) of Title 10 of Part 2 of the Code of Civil Procedure.

(c) This section shall apply only to fees, capacity charges, and service charges described in and subject to Sections 66013 and 66014.

66023. (a) Any person may request an audit in order to determine whether any fee or charge levied by a local agency exceeds the amount reasonably necessary to cover the cost of any product or service provided by the

local agency. If a person makes that request, the legislative body of the local agency may retain an independent auditor to conduct an audit to determine whether the fee or charge is reasonable.

(b) Any costs incurred by a local agency in having an audit conducted by an independent auditor pursuant to subdivision (a) may be recovered from the person who requests the audit.

(c) Any audit conducted by an independent auditor to determine whether a fee or charge levied by a local agency exceeds the amount reasonably necessary to cover the cost of providing the product or service shall conform to generally accepted auditing standards.

(d) The procedures specified in this section shall be alternative and in addition to those specified in Section 54985.

(e) The Legislature finds and declares that oversight of local agency fees is a matter of statewide interest and concern. It is, therefore, the intent of the Legislature that this chapter shall supersede all conflicting local laws and shall apply in charter cities.

(f) This section shall not be construed as granting any additional authority to any local agency to levy any fee or charge which is not otherwise authorized by another provision of law, nor shall its provisions be construed as granting authority to any local agency to levy a new fee or charge when other provisions of law specifically prohibit the levy of a fee or charge.