



## THE CITY OF SAN DIEGO

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### OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

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# IBA Review of the Public Utilities Department FY 2022-2026 Five-Year Financial Outlook

## OVERVIEW

The [\*Public Utilities Department Fiscal Year 2022-2026 Five-Year Financial Outlook\*](#) (PUD Outlook) was released on November 4, 2020, concurrent with the release of the General Fund Fiscal Year 2022-2026 Five-Year Financial Outlook (General Fund Outlook). Similar to the General Fund, [\*Council Policy 000-02: Budget Policies\*](#) states that the PUD Outlook is intended “to guide long-range planning and serve as the framework for the development of the next year’s Proposed Budget for the Water and Sewer Enterprise Funds”. While the General Fund Outlook has been an annual report since 2006, this is only the second PUD Outlook and the first to be presented at a meeting of the full City Council. The first PUD Outlook was released two years ago, in January 2019, and was only presented to the Budget and Government Efficiency Committee. In addition to projecting what may be included in future proposed budgets, the PUD Outlook also serves as the first look at expenditure projections and revenue needs for the next set of water and sewer rates anticipated to come to City Council in calendar year 2021.

As discussed in our review of the General Fund Outlook ([IBA Report 20-25](#)), the Office of the Independent Budget Analyst (IBA) is charged with providing the City Council with review and analysis of all major budget reports, including financial outlooks, quarterly budget monitoring reports, the Mayor’s Proposed Budget, the Mayor’s May Revision to the Proposed Budget, and Capital Improvements Program budget reports. While the City Council cannot change this PUD Outlook, City Council is the ultimate budget authority and can make changes following the release of the Proposed Budget in April 2021. City Council will also review any proposed water and sewer rate cases, ultimately approving changes following the Proposition 218 process. As such, with this report, our Office provides additional context, history and topics for Council to consider as it reviews the PUD Outlook and future review, modification and approval of the FY 2022 Budget and anticipated water and sewer rate adjustments.

# FISCAL/POLICY DISUSSION

The Public Utilities Department operates two major systems, the City’s water system and the wastewater (sewer) system. The PUD Outlook is broken up into these two major functions which are accounted for in separate funds and budgeted separately. Water rate revenues must be used to support activities of providing water while sewer rate revenues are used to support the operations of the collection, treatment and disposal of wastewater<sup>1</sup>.

The PUD Outlook projects expenditures of \$1.8 billion combined in FY 2022 for operations, capital, debt service and reserve requirements of both systems as reflected in the table below. Expenditure projections decline each year primarily due to the Capital Improvements Program (CIP) which captures both fluctuations in the expenditures anticipated for the Department’s baseline CIP and the wind-down of the Pure Water Phase I project.

<b>Summary of Public Utilities FY 2022-2026 Five-Year Financial Outlook (in millions)</b>						
	<b>FY 2021 Adopted</b>	<b>FY 2022 Projection</b>	<b>FY 2023 Projection</b>	<b>FY 2024 Projection</b>	<b>FY 2025 Projection</b>	<b>FY 2026 Projection</b>
Water Fund	\$ 731.4	\$ 1,083.6	\$ 1,039.8	\$ 986.4	\$ 880.5	\$ 844.8
Wastewater Funds	512.2	723.5	713.8	667.6	587.4	545.6
<b>COMBINED</b>	<b>\$ 1,243.6</b>	<b>\$ 1,807.1</b>	<b>\$ 1,753.6</b>	<b>\$ 1,654.0</b>	<b>\$ 1,467.9</b>	<b>\$ 1,390.4</b>

In contrast to the General Fund Outlook, there is no gap projected in the PUD Outlook. Instead, the PUD Outlook projects sufficient revenue to support anticipated expenditures. While the General Fund is constrained by available tax revenues to support expenditures, the water and sewer systems are supported primarily by rates paid by customers using the systems. The PUD Outlook focuses first on projecting the costs of maintaining and operating the water and sewer systems and then estimates the revenue increase needed in order to fund those expenditures. In other words, rather than projecting a gap, we note the need and expectation of rate increases to support the water and wastewater systems over the next five years. Those projected system-wide rate increases are reflected in the following table. *Note that these percentages are at the aggregate, summary level for each system and do not reflect how costs will be allocated to different customer groups. That level of detail will be included in the cost of service study and could reflect higher percentage increase for some customers and lower increases for others.*

<b>Summary of PUD Outlook Projected Rate Increases Needed</b>					
	<b>FY 2022</b>	<b>FY 2023</b>	<b>FY 2024</b>	<b>FY 2025</b>	<b>FY 2026</b>
Water	4.3%	4.9%	4.9%	4.8%	4.6%
Sewer	5.0%	4.0%	4.0%	3.0%	3.0%

<sup>1</sup> Note that sewer operations are further broken down into separate funds for 1) the collection of wastewater from municipal customers in the City of San Diego and 2) the treatment and disposal of wastewater which is provided for City of San Diego customers as well as other agencies in the region that utilize our sewer system. For the purposes of the PUD Outlook, the two sewer funds have been combined.

## Looking Ahead: Cost of Service Study

The PUD Outlook is a first look at the inputs required to build a cost of service study. All the expenditure components are reflected in the PUD Outlook, as well as projections of revenues, which lead to calculating the rate increase need that is reflected on the table on the previous page. However, the PUD Outlook stops there. A cost of service study will take it a step further and break down the needed rate increase into specific amounts for unique customer classes, while meeting all legal requirements of Proposition 218.

As noted in the PUD Outlook, the last set of water rate increases was approved by City Council in November 2015 and authorized rate increases for 2016-2020. The aggregate rate increases for each of those five years ranged from 5.0% to 9.8%. There was no water rate increase in calendar year 2020. The last set of sewer rate increases was approved in 2006 and covered the years of 2007-2010. There have been no sewer rate increases in the past ten years. The Public Utilities Department has indicated that the sewer rates are more critical at this time and need an increase approved for implementation in calendar year 2021.

During discussion and review of the last set of water rate increases in 2015, the City Council, our Office and the public had several questions and concerns that were brought to the Public Utilities Department. While the Public Utilities Department responded to those questions and concerns and agreed to conduct two reviews of funds during the period covered by the water rate increases, there were sentiments that additional expertise for the City Council would be valuable in reviewing a future rate case.

The Utility Consumers' Action Network (UCAN) followed with a recommendation to the Environment Committee in October 2016 that our Office be authorized to hire an outside consultant to evaluate future water rate proposals. We issued a report in February 2017 ([\*IBA Report 17-06: Review of UCAN Proposal for an Independent Water Rate Consultant\*](#)) supporting UCAN's recommendation. Then in June 2017 the City Council adopted [\*Resolution R-311180: A resolution of the Council of the City of San Diego directing the Independent Budget Analyst to include as a budget priority, the hiring of a consultant to advise the City Council and the Independent Rates Oversight Committee on water and wastewater cost of service studies and rate design\*](#) directing our Office "to include the engagement of an as-needed consultant to review the water and wastewater cost of service studies and rate designs, under the direction of the IBA and funded by the Water and Sewer Funds . . . for the fiscal year when the City anticipates bringing forward the next cost of service studies."

As such and in anticipation of the upcoming cost of service study, our Office has hired Stantec, a consulting firm with expertise in rate development and evaluation, to conduct an in-depth review of the cost of service study and proposed rate increases. The results of which will provide insight and additional information for the City Council, Independent Rates Oversight Committee (IROC), and the public. Stantec met with IROC at their November 2020 meeting to gather preliminary input on IROC's areas of interest for evaluating the upcoming cost of service study. Our Office is also working with Stantec to organize a training for City Council on the process of reviewing and approving rate increases.

## Evaluating the Framework for Water and Wastewater Projections

Stantec and our Office are reviewing the PUD Outlook and identifying areas for further research and evaluation in preparation for the cost of service study. These include assumptions, trends and policies used by the Public Utilities Department and their consultant, Raftelis Financial Consultants, Inc. in development of the PUD Outlook projections and cost of service study. Examples are discussed below.

### Water Demand Assumptions

The PUD Outlook indicates that the Public Utilities Department delivered an average of 180,000 acre-feet of water per year from FY 2015-2019. This is a reduction from an average of 200,000 acre-feet per year over the previous five years. The PUD Outlook also notes that the San Diego Association of Governments (SANDAG) projects population growth of approximately 22% over the next 20 years. Meanwhile, customers continue water conservation efforts. Given the combined impacts to rate revenues and water purchase costs, this demand projection is an important component of the financial plan and should be evaluated to fully understand the impact of changes on the financial outlook.

### Water Purchase Assumptions

The PUD Outlook states that the City purchases 85-90% of its water from the County Water Authority (CWA) and this makes up roughly half of the operating expense for the water system. The Public Utilities Department assumes using 10% of our own water, from rainfall and runoff that flows into the City's reservoirs, in each of the PUD Outlook years. Rainfall is also difficult to predict, fluctuating from 3.3 inches in water year 2018 to 12.9 inches in water year 2019. The PUD Outlook assumes average rainfall from FY 2022 and on. The amount of water to be purchased is projected to decrease in FY 2025 and FY 2026 when the Pure Water Phase I comes online. The Department has also accounted for estimated rate increases from CWA when calculating the cost to purchase water. All of these factors go into developing the estimates in the PUD Outlook of the amount of water to be purchased, which are summarized in the table below.

<b>Water Purchases Estimated in PUD Outlook</b>						
	<b>FY 2021</b>	<b>FY 2022</b>	<b>FY 2023</b>	<b>FY 2024</b>	<b>FY 2025</b>	<b>FY 2026</b>
Acre Feet to Purchase	143,000	161,000	162,000	162,000	145,000	129,000
Estimated Cost ( <i>in Millions</i> )	\$ 239.0	\$ 271.6	\$ 285.5	\$ 300.1	\$ 292.9	\$ 284.5

The projected water supply could be influenced by a number of factors, including rainfall, regional demands, and the completion schedule for phase I of the Pure Water Program. Related to the water demand assumptions discussed above, demand and supply uncertainty and the associated costs of each source of water supply have a meaningful impact on the financial outlook. A review and evaluation of potential changes to the projected amounts and timing of supply from each source will help to understand the financial consequences of deviations from this plan.

### Debt Service Coverage Levels

The Public Utilities Department uses a combination of cash funding (such as revenue from rate payers) and debt financing to support the ongoing Capital Improvements Program for water and sewer assets. Note that debt payment obligations extend well beyond the period covered in the

PUD Outlook. In order to maintain a favorable credit rating and continue to receive low interest rate financing, the Department monitors its debt service coverage ratio. The debt service coverage ratio is a fund's revenues net of operating expenses divided by the total debt service owed. A debt service coverage ratio less than 1.0 would indicate that the organization did not have enough revenues to support its debt payments through annual cash flows and would need to draw from fund balance or reserves or borrow additional funds in order to make the payments.

$$\text{Debt Service Coverage Ratio} = \frac{\text{Net System Revenue}}{\text{Debt Service}}$$

The PUD Outlook states that existing bond covenants require minimum debt service coverage ratios of 1.2x for its senior debt or 1.1x for its aggregate debt. The Public Utilities Department indicates that they generally target a debt service coverage ratio of 1.5x for both water and sewer.

### Reserve Requirements

The water and sewer funds are included in the City's [Council Policy 100-20: Reserve Policy](#). The policy calls for the following reserves, both for water and sewer (unless otherwise noted).

- Emergency Operating Reserves equivalent to 70 days of operations<sup>2</sup>
- Emergency Capital Reserves of \$5 million each (total \$10 million for Public Utilities) budgeted in the Capital Improvements Program each year
- Rate Stabilization Fund Reserves equivalent to 5% of prior year's operating revenue
- Secondary Purchase Reserve (water only) equivalent to 6% of the annual water purchase budget

The PUD Outlook includes projections for these required reserves and notes that the Rate Stabilization Reserves for both water and sewer are higher than the targets and can be used to provide some relief towards the next set of rate increases. We note that at the end of the outlook period, in FY 2026, the PUD Outlook projects the Rate Stabilization Reserves at \$28.3 million and \$32.5 million higher than the targets for water and sewer, respectively, as reflected in the following table.

<b>Rate Stabilization Fund Reserves in PUD Outlook (in millions)</b>						
	<b>FY 2021</b>	<b>FY 2022</b>	<b>FY 2023</b>	<b>FY 2024</b>	<b>FY 2025</b>	<b>FY 2026</b>
<b>Water</b>						
Reserve Target	\$ 33.3	\$ 35.5	\$ 36.7	\$ 38.4	\$ 40.1	\$ 42.3
Estimated Funding Level	115.6	100.6	85.6	75.6	65.6	70.6
<b>Amount Above Target</b>	<b>\$ 82.3</b>	<b>\$ 65.1</b>	<b>\$ 48.9</b>	<b>\$ 37.2</b>	<b>\$ 25.5</b>	<b>\$ 28.3</b>
<b>Sewer</b>						
Reserve Target	18.3	18.9	19.4	20.1	20.8	21.3
Estimated Funding Level	81.3	63.8	41.3	46.3	53.8	53.8
<b>Amount Above Target</b>	<b>\$ 63.0</b>	<b>\$ 44.9</b>	<b>\$ 21.9</b>	<b>\$ 26.2</b>	<b>\$ 33.0</b>	<b>\$ 32.5</b>

Before approving the next set of rate increases, it would be worthwhile to review the reserve balances and minimum targets to ensure customers are not being overcharged and, conversely, that reserves are sufficient to provide stable, reliable operations and meet debt financing requirements.

<sup>2</sup> For the water, this is 70 days of operations less water purchase costs.

### Infrastructure Maintenance and Replacement Schedules and Funding

The water and sewer systems are reliant on properly functioning, critical assets. We have all seen the headlines when a pipe breaks and it causes damage to private property, service outages, traffic congestion, etc. It is important to include projections of regular, ongoing capital maintenance and replacements to keep the water and sewer systems running smoothly. It is more cost effective to maintain assets and replace them at the end of their useful life, before they break and cause damage or an emergency situation. A couple areas to evaluate are historical trends for emergency work and benchmarking based on investment plans, depreciation, and asset useful lives.

The PUD Outlook includes a detailed summary of the capital funding plan to meet system needs. Capital investments are a key driver of costs in the PUD Outlook over the next five years with construction of phase I of the Pure Water Program reflecting the bulk of the costs, as well as ongoing investments in infrastructure repairs, replacements and improvements. The funding mechanisms (cash, commercial paper/bonds or loans) used to fund needed capital improvements should align with the anticipated useful life and expected benefit of each improvement project. The optimal combination of debt and cash funding can help balance the near and long-term impacts to ratepayers while meeting the Public Utilities Department's financial targets and ratings agencies' benchmarks.

### Additional Topics of Interest for Review

The inputs, assumptions, and decisions included in the PUD Outlook provide the overall revenue requirements used to calculate new water and sewer rates. In addition to the financial topics discussed above, Stantec intends to review a number of additional factors as part of the cost of service and rate design analyses. A few examples of these topics include, but are not limited to, the following:

- Industrial Wastewater Control Program costs and associated fee calculation methodology (an update is provided later in this report)
- Evaluating costs and non-rate revenues by function within the water and sewer systems
- Cost allocation factors and methodologies
- Customer water demand and peaking characteristics
- Customer wastewater return flows and loading/strength characteristics

### **Significant Projects/Activities of the Public Utilities Department**

The following section discusses projects and activities of the Public Utilities Department that have been of particular interest to the City Council and public that we continue to monitor for operational and fiscal impacts.

#### Pure Water Program

The Pure Water Program will use purification to produce potable water from recycled water while also reducing discharge into the ocean from the Point Loma Wastewater Treatment Plant. By implementing the Pure Water Program, the Public Utilities Department will avoid having to complete over \$1.8 billion of upgrades to the Point Loma Wastewater Treatment Plant. Phase I of the Pure Water Program is estimated to cost approximately \$1.4 billion, with costs supported by both water and wastewater funding.

The PUD Outlook provides a brief status update on phase I. The City Council had authorized the Department to proceed with construction in November 2018. However, construction was delayed by a Court injunction stemming from a lawsuit initiated by the Association of General Contractors regarding apprenticeship requirements that the City had placed in the bid. This dispute has since been resolved with State Legislation that now requires project labor agreements for Pure Water projects which use State funding. City Council approved the necessary changes in contract language in November 2019, allowing the Department to proceed with the project. According to the PUD Outlook, this caused a delay of 18 months.

The Public Utilities Department anticipates construction will begin in the first half of calendar year 2021 and phase I to be operational in 2025. The PUD Outlook includes the projected staffing and non-personnel support needed for the new and expanded facilities for the Pure Water Program, as reflected in the table on the following page. Positions are being added gradually so that staff can come on board and be trained prior to the facilities going operational. A total of 67.00 FTE positions across the water and wastewater systems will be needed by FY 2024. The PUD Outlook projections also include non-personnel costs for chemicals, energy and other expenses related to running the facilities. A total of \$45.5 million in annual expense will be needed by FY 2026.

<b>Projected Staffing &amp; Support for Pure Water Operations</b>					
	<b>FY 2022</b>	<b>FY 2023</b>	<b>FY 2024</b>	<b>FY 2025</b>	<b>FY 2026</b>
FTE Positions	20.00	44.00	67.00	67.00	67.00
Expense (in Millions)	\$ 2.4	\$ 5.2	\$ 9.3	\$ 19.7	\$ 45.5

The last comprehensive report on the Pure Water Program was presented to the Environment Committee over two years ago. **The City Council may want to request a Pure Water Program update be presented to the Environment Committee which would include an updated project schedule, cost estimates, financing, and projections of future operating needs.** The plans for phase II of the Pure Water Program could also be highlighted.

Advanced Metering Infrastructure

Advanced Metering Infrastructure (AMI) allows water meters to be read remotely, rather than in-person by a meter reader. If fully implemented throughout the system, it is anticipated to result in more accurate data collection. In 2012, the Public Utilities Department implemented AMI for a small portion of customers (approximately 11,000), as a pilot project. In 2015, the Department began implementing AMI Citywide, intending to address the remaining 270,000 metered connections. In July 2019, the Office of the City Auditor issued the [\*Performance Audit of the Public Utilities Department’s Advanced Metering Infrastructure Implementation\*](#) which found that “significant management deficiencies, staffing issues, and implementation of a new work order tracking system, EAM, all contributed to delays in implementing AMI Citywide.”

At the time the audit was released, the Public Utilities Department stated that they would dedicate staff to manage the implementation effort and hire a third-party to install the equipment at the water meters. The request for proposal to hire an installer was target for January 2020; however, this did not occur. The Department indicates that they are currently waiting to meet and confer with the impacted City employee labor organization before they can put the work out to bid.

A timeline for complete implementation of AMI is not known at this time. However, the PUD Outlook does program in the staffing and non-personnel support that will be needed, assuming full implementation by FY 2025, as reflected in the following table. Since the timing of implementation is still to be determined, these estimates may shift to earlier or later years.

<b>Projected Staffing &amp; Support for Advanced Metering Infrastructure</b>					
	<b>FY 2022</b>	<b>FY 2023</b>	<b>FY 2024</b>	<b>FY 2025</b>	<b>FY 2026</b>
FTE Positions	0.00	5.00	10.00	21.00	21.00
Expense (in Millions)	\$ 0.1	\$ 0.4	\$ 0.8	\$ 1.6	\$ 1.6

We note that the Public Utilities Department has not estimated any reductions in meter reading staff during the PUD Outlook periods as a result of full AMI implementation. The goal of AMI is to receive accurate and timely data which can assist both users (such as through the identification of leaks and meeting conservation goals) and the Public Utilities Department (with data to assist with decision-making and development of future cost of service studies and rate allocations), not to reduce costs. However, once fully implemented and operational, the Department should need fewer meter readers in the field.

#### Industrial Wastewater Control Permit Audit

The Public Utilities Department’s Industrial Wastewater Control Program issues discharge permits, performs inspections, conducts wastewater monitoring and enforces sewer discharge standards for businesses and industries based on the U.S. Environmental Protection Agency’s restrictions on pollutants that can be discharged into the sewer system. In July 2020, the Office of the City Auditor issued a [\*Follow-up Performance Audit of the Public Utilities Department’s Industrial Wastewater Control Program \(July 2020\)\*](#). This follow-up audit found that issues the Office of the City Auditor had identified in the 2013 audit had not been entirely resolved with regards to proper cost recovery for industrial users of the wastewater system. The bottom-line is that costs had been passed on to other customers who are not part of the Industrial Wastewater Control Program.

The Public Utilities Department immediately mobilized to address the concerns of the follow-up audit and have updates at both the Audit and Environment Committees of the City Council as well as to the Independent Rates Oversight Committee. The Department is reviewing the fees charged to those in the Program and has begun discussions with the other local agencies using the City’s wastewater system (participating agencies) that will be impacted by a fee change. The Department anticipates bringing the results of the fee study to the Environment Committee in early calendar year 2021. Any fee changes will require approval from the City Council as well as the participating agencies.

The Industrial Wastewater Control Program represents a small portion (around 1%) of revenues for the sewer system. The change in fees will not impact the total revenue received but will shift costs to the correct customers. As a result, resolution of this issue does impact the development of customer rates in the cost of service study.



## **Future Financial Challenges and Risks**

There are a variety of financial challenges and risks that could impact the projections contained in the PUD Outlook and future years. The discussion below is not an all-inclusive list but highlights some of the more significant factors on the horizon.

### City Personnel Expenses

Consistent with the General Fund Outlook, the PUD Outlook does not contain estimates for any potential new negotiated compensation increases for Department employees. Salary increases were provided for all City employees in FY 2019 and FY 2020; however, recent compensation surveys have shown that the City's compensation levels for many employees are lower than comparable California public agencies. The Public Utilities Department is in an even more unique situation in that it competes with other local water agencies, many of which are independent districts, for qualified and talented employees. The Department has indicated that staff salaries and benefits are not competitive which results in a higher rate of attrition and difficulties in recruiting for skilled and technical positions.

The PUD Outlook does not contain the most recent estimates for the City's actuarially determined contribution (i.e., retirement payment) for the City's defined benefit pension. While the General Fund Outlook was updated based on recent information provided by the San Diego City Employees' Retirement System's (SDCERS) actuary, the PUD Outlook was not revised. The FY 2022 contribution should be available in January 2021 and will be incorporated in the Proposed Budget.

### County Water Authority Rates

The Public Utilities Department purchases the majority of City water from the County Water Authority. The City of San Diego is also the largest user of County Water Authority water, accounting for about 40% of their system usage. The PUD Outlook accounts for rate increases that are currently known/anticipated; however, additional rate adjustments could occur during the PUD Outlook period. The Public Utilities Department indicated that roughly half of the anticipated water rate increase needs are due to increased rates from the County Water Authority.

There are also projects on the horizon that will impact costs from the County Water Authority. The County Water Authority is currently studying the feasibility of building a pipeline to the Colorado River. If they choose to proceed, this will be at a significant capital cost, with roughly 40% of that cost potentially being passed on to the City and therefore to the City's water customers. This is likely to occur outside of the PUD Outlook period. The County Water Authority has also discussed shifting their rates to have a larger portion of fixed costs, versus variable use-based costs, which the Public Utilities Department estimates would increase costs to the City, and therefore the City's water customers.

Concurrently, the Public Utilities Department is building the Pure Water Program to reduce the City's reliance on purchased water. This should reduce the portion of the County Water Authority's system that is supported by the City's water users. The Public Utilities Department noted that once the Pure Water program is operational, they will need to work to reduce the City's contributions to the County Water Authority.

### Public Utilities Infrastructure Needs

The Public Utilities Department has indicated that major infrastructure requirements for the dams, such as retrofits and repairs that go beyond routine capital maintenance, are currently not included in this PUD Outlook. The Department has identified a gap in infrastructure planning and intends to initiate condition assessments for water and sewer assets. The plan is to dedicate a team of engineers to oversee the work and hire consultants to conduct the assessments. They will not only consider the size and costs of the assets but also the number of people served and the criticality of the assets. The final product will be a master plan for water and sewer infrastructure which will include a financing plan, identification of staffing needs, and ways to better align between the water and sewer systems. The results of this work are not available for this PUD Outlook or the upcoming cost of service study and rate design. The Department anticipates this work will take two or three years and would like to have the master plan completed in time to be incorporated into the next rate case.

The PUD Outlook includes the projected contract expense to conduct the condition assessments, although the resulting capital expenses are unknown at this time. The contract expense projection is shown in the following table.

<b>Projected Contract for Infrastructure Condition Assessments</b>					
	<b>FY 2022</b>	<b>FY 2023</b>	<b>FY 2024</b>	<b>FY 2025</b>	<b>FY 2026</b>
Expense (in Millions)	\$ 4.2	\$ 4.0	\$ 3.5	\$ 2.5	\$ 1.0

### Pure Water Program Phase II

Phase I of the Pure Water Program is expected to become operational during the PUD Outlook period and full costs are included in the PUD Outlook projections. The second phase of Pure Water will primarily occur after this timeframe. There is some initial consulting work occurring now and the demonstration facility for phase II should start in FY 2024. The largest costs, construction, for phase II will be later, with phase II implementation expected by FY 2035. Once phase II is operational, the Pure Water Program is expected to provide a third of the City's water needs.

### Water Conservation


Continued water conservation efforts reduce the Public Utilities Department's need to purchase water from outside sources. However, a significant portion of the costs of operating the water system, remain largely unchanged regardless of how much less water is being circulated. This is further compounded when customer rates are set based on water usage, and usage goes down, resulting in less revenues to operate the system. To some extent, this will be need to be addressed in the upcoming cost of service and rate design but will likely continue to be an issue beyond that timeframe.

## **CONCLUSION**

The PUD Outlook projects needed water and sewer rate increases for FY 2022-2026. In order to effectuate these rate increases, the Public Utilities Department will need to bring forward the results of the cost of service study in calendar year 2021. Our Office has hired Stantec to assist Council, the Independent Rates Oversight Committee, and the public by conducting an in-depth review of the cost of service study and proposed rate increases. In the meantime, our Office

recommends that the Environment Committee request updates and/or briefings on high-profile projects and other areas of interest that will impact the proposed rate increases and our Office is working with Stantec to schedule a training for City Council on the process of reviewing and approving rate increases.

  
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