

## Agenda Report

**DATE:** December 15, 2015

**TO:** The Mayor and City Council

**FROM:** David A. White, City Manager DW  
Fred Marsh, Director of Finance and Technology FM

**SUBJECT:** Review of Financial Status of the City's Water Utility Fund

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### **RECOMMENDED ACTION**

- (1) Receive Report; and
- (2) Receive direction from City Council.

### **STATEMENT OF ISSUE**

At the May 19, 2015 City Council Meeting, City Council reaffirmed approved Ordinance 2013-10B, which increased water rates by 2.5% per year for four years through Fiscal Year 2016-17. This report includes an attached presentation on the financial condition of the Water Utility. This presentation provides a five year forecast for the Water Utility, recent rate increases enacted by nearby water utility agencies, fiscal impacts of the recent drought on the water utility, and options to address future water fund deficits.

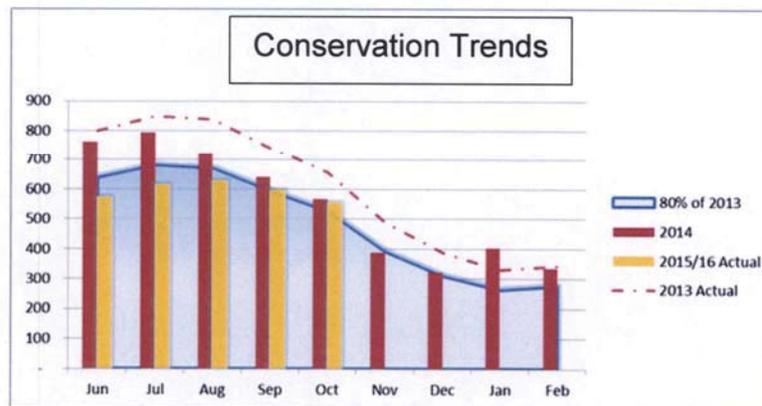
### **DISCUSSION**

The Fairfield Municipal Water Utility (FMU) continues to be in good physical condition overall. In addition to operating the utility to provide water to the community on a continuous basis, staff is responsible for maintaining infrastructure, valued at over \$500 million, in the form of two water treatment plants, 12 concrete and steel reservoirs, 16 treated water pump stations and over 370 miles of transmission and distribution pipelines, including all appurtenances (hydrants, valves, etc.), and approximately 30,000 water service accounts. In order for these extremely valuable community assets to remain in good condition, on-going investment in the proper maintenance and repair of the water infrastructure is critical.

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Proper operation and management of the utility allows water delivery to customers 24 hours per day, 7 days per week, 365 days per year, reduces fire risk and related insurance costs, and keeps bond ratings high to minimize borrowing costs for large capital investments when needed. In addition, Fairfield's excellent planning has resulted in a diverse water supply portfolio that improves reliability and is attractive to water intensive industries such as Anheuser-Busch, Frank-Lin Distillery and Heretic Brewing.

The financial health of the FMU has been good up until these last couple of years of the current drought. Even though Fairfield's water supplies are adequate to withstand the drought's impacts so far, the State Water Resources Control Board (State Board) has mandated several water conserving actions for all water utilities, which has resulted in even greater conservation levels. Drops in consumption associated with these conservation measures have adversely impacted the finances of the FMU. The increases in conservation observed in response to the latest State Board mandates will result in reduced revenue collections for the FMU. The chart below shows the recent conservation trends in the City.



The attached presentation shows the projected deficits for FMU for the next five years. FMU will need to implement a proactive strategy in order to continue to adequately fund operations, maintenance and necessary plant improvements. This strategy includes:

- Legal and Political Advocacy;
- Cost Structure Changes and Additional Cost Savings;
- Economic Development and;
- Rate Increases

City staff has worked hard to ensure efficient operations and continued improvement when it comes to controlling costs, which are primarily driven by power, chemical and personnel costs, as detailed on the attached presentation.

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Just as important to the FMU is continued investment in the physical infrastructure, which has an estimated replacement value exceeding \$500 million (which includes the cost of the North Bay Regional Treatment Plant (NBR). Capital projects are continually needed to replace aging infrastructure, maintain system reliability, and improve operational efficiency, all of which actually help lower the long-term cost of managing the utility. Economic side benefits of these projects are the local jobs that are created for the construction industry.

The City has a long history of modest annual water rate increases. This policy was put in place following years of under-investment in the utility in the late 1970's/early 1980's, which resulted in rate hikes of 71% in 1984 and 38% in 1985. Large spikes in rates are extremely difficult for all customers. The most recently approved four-year, 2.5% per year increase continued the utility management policy of the last 30 years, while being sensitive to the economic impacts to the community of the Great Recession.

#### **FINANCIAL IMPACT**

Without additional rate increases, the City's water utility (accounted for in the City's Water Funds (Funds 461 and 462) is projected to have annual deficits ranging from \$4.5 million to \$6.9 million through Fiscal Year 2019-20.

#### **PUBLIC CONTACT/ADVISORY BODY RECOMMENDATION**

N/A.

#### **ALTERNATIVE ACTION**

N/A.

#### **DOCUMENTS ATTACHED**

Attachment 1: Update on Financial Status of Water Fund  
Attachment 2: City Letter to State Water Resources Board

#### **STAFF CONTACT**

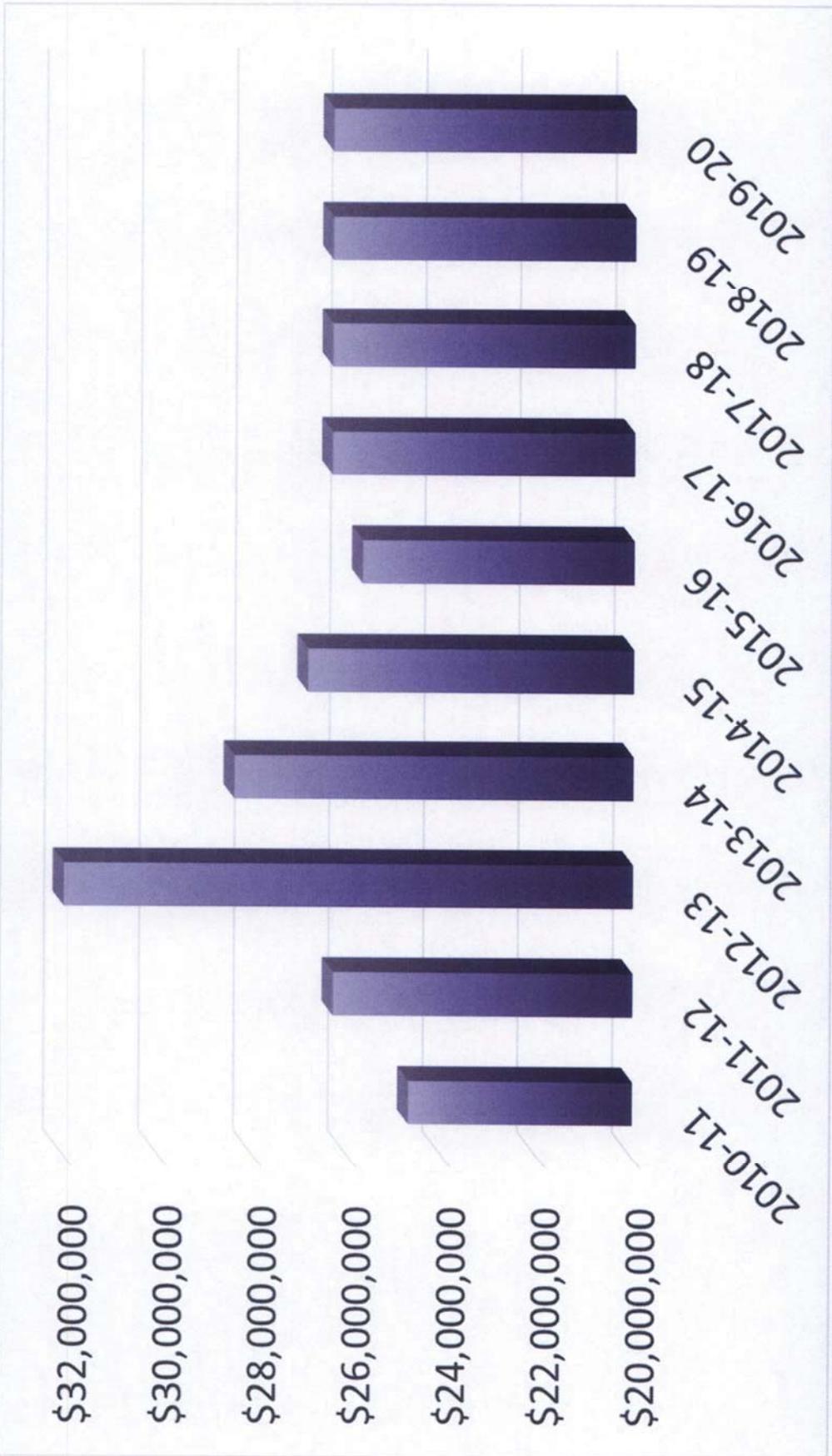
Fred Marsh, Director of Finance and Technology  
707- 428-7495  
fmarsh@fairfield.ca.gov

Coordinated with: Public Works

**City of Fairfield  
Update on Financial Status of Water Fund  
December 15, 2015**

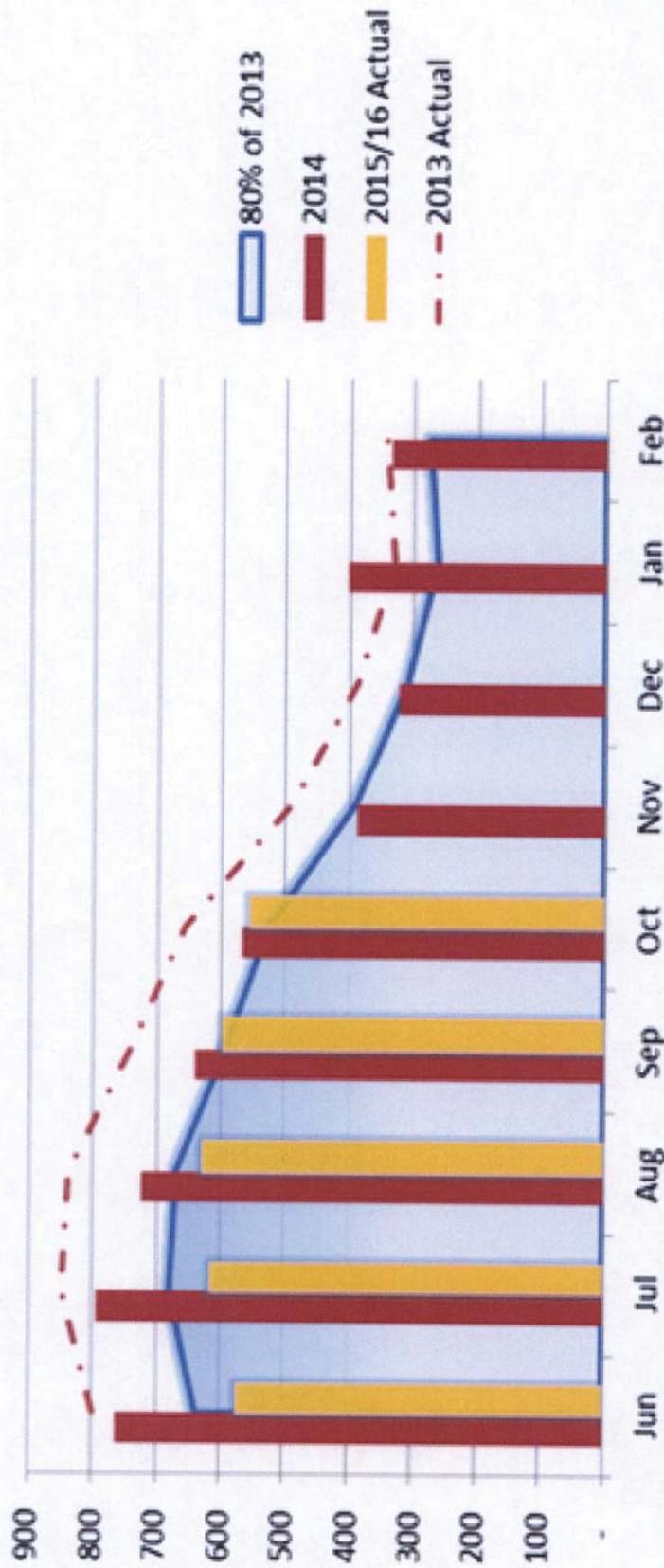


# Impacts of the Drought on Water Revenues



# Impacts of the State Water Conservation Mandates on Production

Conservation Trends



## Recent Cost Saving Measures Implemented by Staff

- Refunded 2005 Water Bonds, resulting in savings of \$400K
- Installation of solar power at NBR resulting in an estimated \$4.8 Million savings over the 20 year life of the agreement
- Chemical Optimization – saving \$100,000 per year since FY 11/12 at Waterman and NBR (combined)



## Recent Cost Saving Measures Implemented by Staff (Continued)

- Retrofitted water meters to radio read heads that allow for time efficiencies in drive-by data gathering
- Participate in local agency chemical purchase pools to get better prices based on economy of scale
- Favorable Energy Rate Structure - \$60K annual savings for NBR Water Treatment Plant



## Capital Projects Planned for Water Fund for FY 2015-16 through 2019-20

- Waterman Treatment Maintenance Projects - \$1.35 million
- Design of East West Transmission System - \$400,000
- Water Main Replacements - \$10 million
- East West Transmission Segments 3-6A - \$10.8 million
- Pump Stations and Reservoirs - \$6.8 million

### **Total Needed Capital Investment**

**or 5 Years - \$29.4 million**



# Assumptions Used in 5 Year Forecast

- Connection Fees from New Development remain at annual average of \$3.5 million of the last five years thru FY 19-20 (Approximately 10% of annual revenues)
- 2.5% Rate increases approved by Council for Fiscal Years 2015-16 and 2016-17; with no rate increases thereafter. Total revenues projected to remain flat after FY 16-17
- Reduced adopted CIP expenses by \$10.2 million – Postponed construction of Red Top Zone 2 and Noonan Reservoirs and reduced some water main replacements scheduled for FY 17-18 to later years.

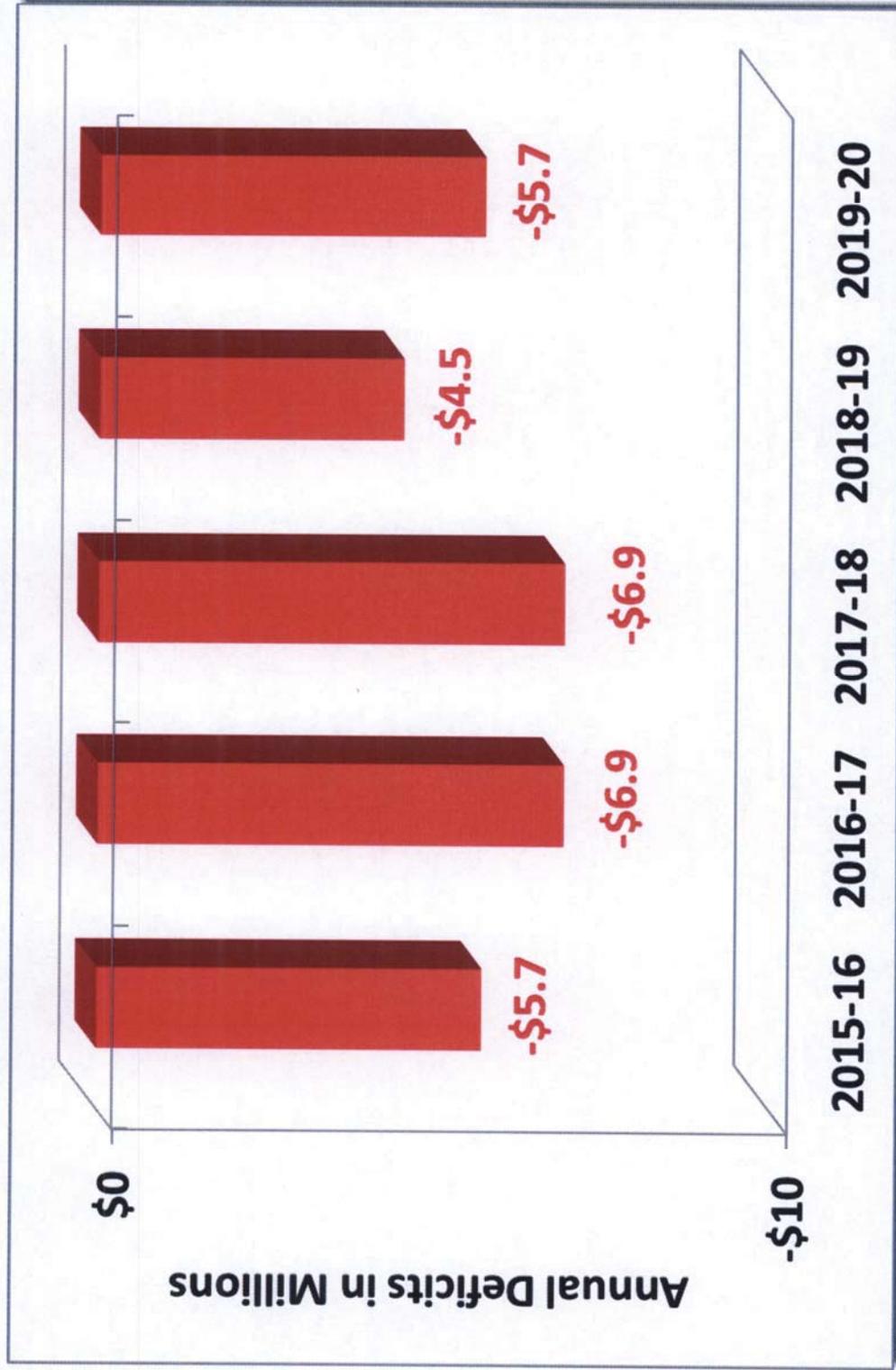


# Assumptions Used in 5 Year Forecast (Continued)

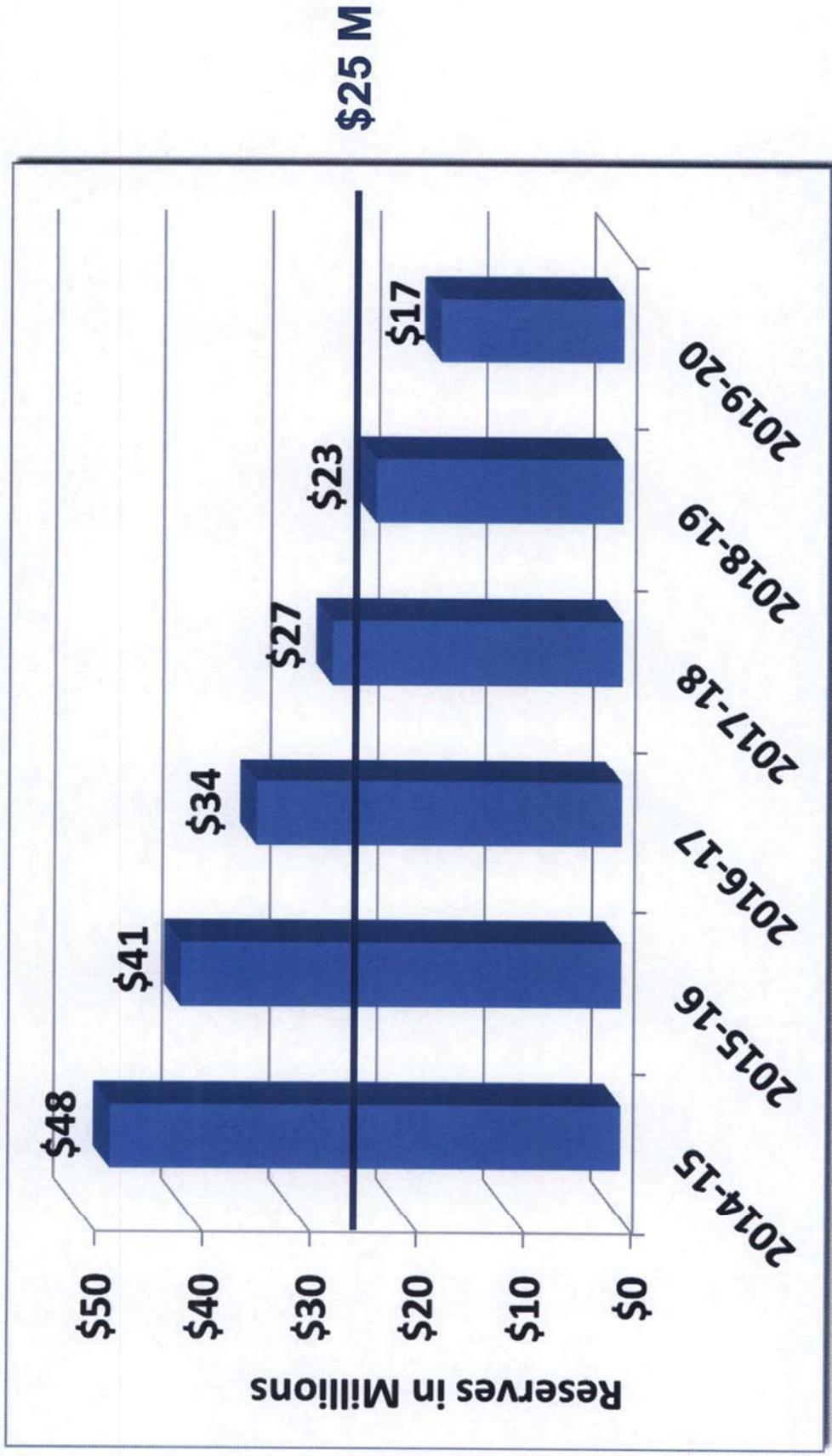
- Includes additional personnel costs resulting from the recent adoption of new MOUs and adjustments to employee classifications relating to employees funded by the Water Fund. No additional COLAs assumed past FY 16-17
- 3% increases in operating costs (excluding personnel) beginning in FY 17-18. Revenues increasing



# Five Year Revised Forecast of Deficits - Water Fund



# Five Year Revised Forecast Reserves Water Fund



# Comparison of Funding of Water Capital Replacement with Other Cities

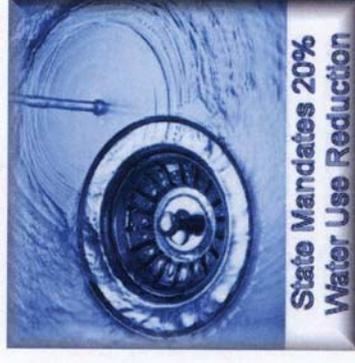
City	Estimated Reserves 6/30/2015 (Millions)	% of Net Book Value Capital Assets
Vacaville	\$17	28%
Vallejo	\$24	29%
Napa	\$20	20%
Pittsburg	\$17	24%
Antioch	\$23	29%
Davis	\$17	19%
Pleasanton	\$23	33%
Livermore	\$17	40%
<b>Average</b>	<b>\$20</b>	<b>28%</b>

## **Recent Rate Increases implemented by Other Water Agencies**

- Vacaville – 28% over 5 years through 19-20 (Proposed)
- Suisun City – 49% over 5 years through 19-20
- Benicia – 49% over 5 years through 16-17
- Napa – 36% over 5 years through 2016
- Pittsburg – 18% over 4 years through 2018
- EBMUD – 24-42% for FY 15-16 (with drought surcharge)
- Contra Costa Water District – 10% FY 15-16
- Livermore – 34% over six years through 20-21
- Zone 7 (Tri Valley) 30% over 3 years through 17-18

## Strategies to Address Water Fund Deficits

- Pursue Legal and Political Options to address State Conservation Mandates
- Address Cost Structure and Implement Cost Savings Measures
- Generate More Revenue for Water Fund:
  - Economic Development
  - Water Rate Increases



# WATER-READY FOR BREWERIES

*Great Water Makes Great Beer*



City of  
**FAIRFIELD** California

- High quality, abundant water
- State-of-the-art sewer treatment facilities
- Strategic location on major transportation routes
- Affordable real estate

[businessinfofairfield.com/water](http://businessinfofairfield.com/water)  
707-428-7462  
[econdev@fairfield.ca.gov](mailto:econdev@fairfield.ca.gov)

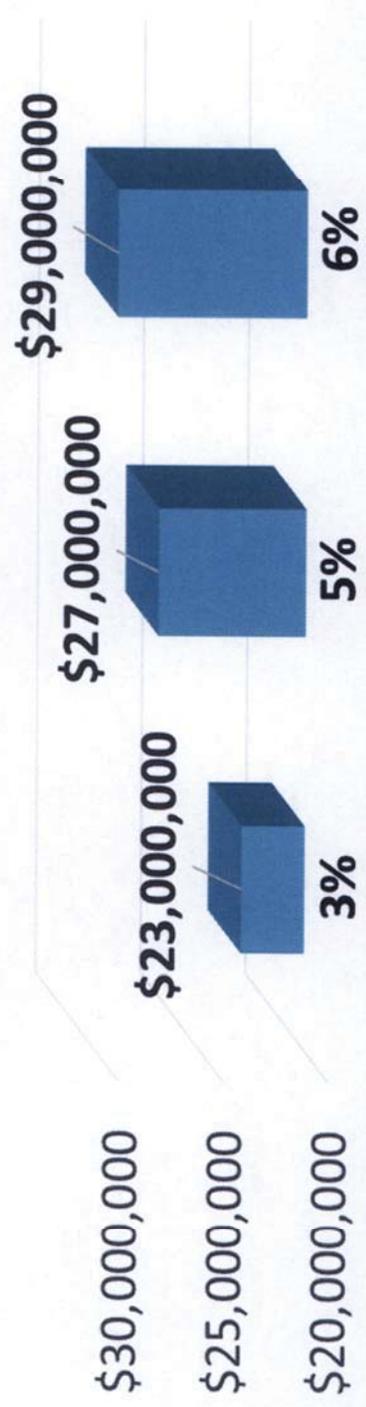


# Rate Options to Address Water Fund Deficits (Annual Rate Increases Proposed to begin in 2017)

Projected Deficit / Surplus FY 19-20



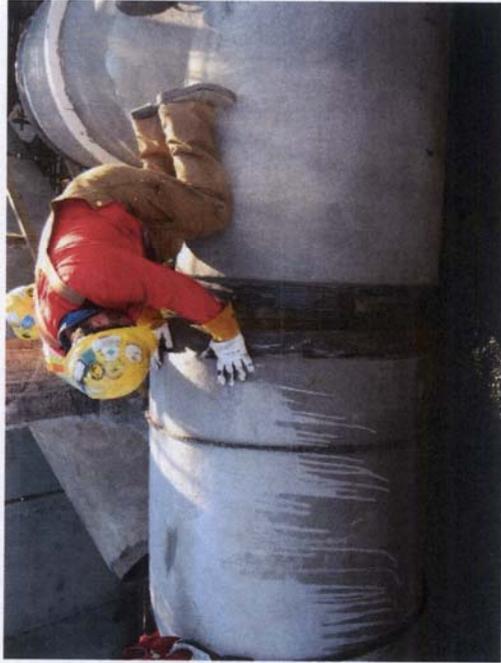
Projected Ending Reserves FY 19-20



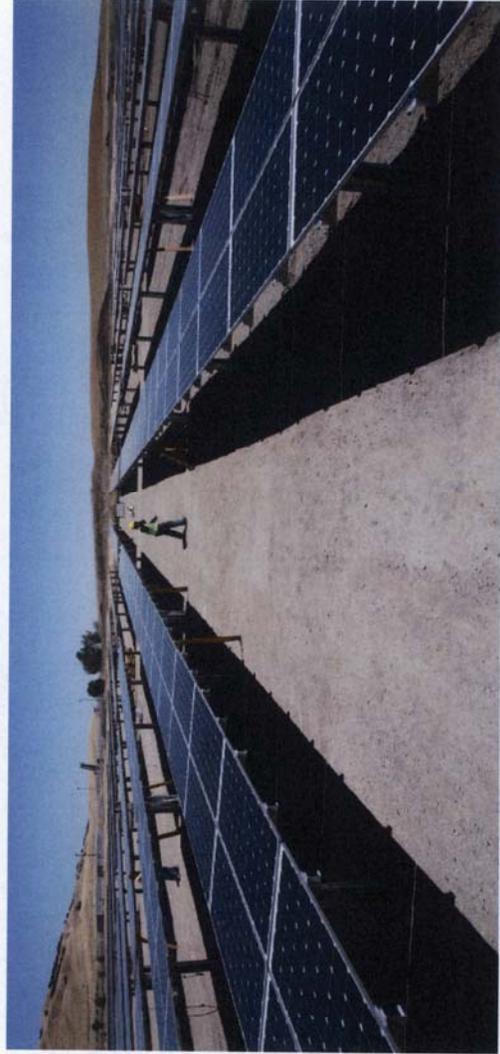
# Recommendations

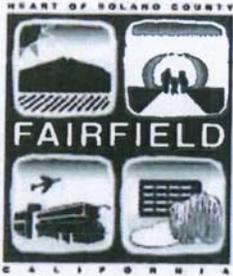
- Accept the Report
- Provide Direction to Staff Regarding Proposed Strategies for the Water Fund





# Questions?





# CITY OF FAIRFIELD

Founded 1856

Incorporated December 12, 1903

December 1, 2015

Home of  
Travis Air Force Base

## COUNCIL

### Mayor

Harry T. Price  
707.428.7395

Vice-Mayor  
Chuck Timm  
707.428.6298

Councilmembers  
707.428.6298

Pam Bertani

Catherine Moy

Rick Vaccaro

\*\*\*

City Manager  
David A. White  
707.428.7400

\*\*\*

City Attorney  
Gregory W. Stepanicich  
707.428.7419

\*\*\*

City Clerk  
Karen L. Rees  
707.428.7384

\*\*\*

City Treasurer  
Oscar G. Reyes Jr.  
707.428.7498

## DEPARTMENTS

City Manager's Office  
707.428.7400

\*\*\*

Community Development  
707.428.7481

\*\*\*

Community Resources  
707.428.7465

\*\*\*

Finance  
707.428.7498

\*\*\*

Fire  
707.428.7375

\*\*\*

Police  
707.428.7362

\*\*\*

Public Works  
707.428.7485

***Via email to [commentletters@waterboards.ca.gov](mailto:commentletters@waterboards.ca.gov)***

State Water Resources Control Board  
Jeanine Townsend, Clerk to the Board  
1001 I Street  
Sacramento, CA 95814

Re: Comment Letter – Urban Water Conservation Workshop

Dear Ms. Townsend, Chair Marcus, and Board Members:

The City of Fairfield (Fairfield) has several concerns about the current Emergency Water Conservation Regulations and any plans to continue these regulations into the future. Comments to the specific questions that the State Water Resources Control Board (SWRCB) has sought input on are provided below.

1. *What elements of the existing emergency regulation, if any, should be modified in an extended emergency regulation.*

The water use reduction mandates should be eliminated. These requirements for every water agency in the State to meet a prescribed conservation target, regardless of their individual water supply situation is arbitrary and does not fairly take into account good preparation, planning, investment and management by agencies such as Fairfield.

Fairfield recognizes and appreciates the severity of the multi-year drought plaguing much of California. Fairfield has achieved significant water-use savings in 2015 in response to the SWRCB's conservation mandates, which the City remains fundamentally opposed to and continues to question the legality of such action by the SWRCB. Fairfield, like other water suppliers, has developed drought strategies and made significant financial investments to prepare for a multi-year drought. In fact, Fairfield's past investments in securing back up water supplies have put Fairfield in a position to provide adequate water supplies to its residents without any reduction in water use even if the current drought extended for several more years. The SWRCB's Emergency Conservation Regulations caused substantial economic losses to the City in 2015 by reducing water consumption revenues and discouraging water intensive industry from locating in Fairfield. Fairfield was denied the benefit of its sound water management practices, long-term planning and financial investment and was effectively forced to forego utilizing its drought water supply.

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- 2. What additional data, if any, should the State Water Board be collecting through the emergency regulation and how should it be used.*

There is no need to add additional data submittal requirements to the regulation, except as necessary to implement adjustments to water suppliers for available local supplies and growth projections (residential and commercial growth).

- 3. How should the State Water Board account for precipitation after January 2016 in its implementation of any extension of the emergency regulation.*

First and foremost, in light of forecasts for significant rainfall in California (and particularly Northern California) in the upcoming winter the State Water Board needs to evaluate the water supplies available to all areas of the State at the end of the winter season (May 2016) and drop the "one size fits all approach" to water conservation targets. With above-average local rainfall and a normal snow-pack, the drought will be effectively over for much of California, particularly for Fairfield. In addition, even though our local supplies had at least a 4-year supply remaining going into this past summer, Fairfield was denied its request for a conservation target reduction because a portion of the City's water supply portfolio comes from the State Water Project (SWP). This provision was unfair and should be eliminated regardless of the type of winter California experiences.

Fairfield is concerned that many State officials are already making the statement that the drought is unlikely to end even if major State reservoirs are largely filled and snowpack levels are substantial, due to the "significant groundwater depletion" that is alleged to have occurred. However, many of the areas being referenced have been chronically over-drafted even during normal and wet years. Ground water basins in other areas are not over drafted. Furthermore, many agencies, such as Fairfield, do not utilize groundwater. So to use groundwater depletion as justification for extending the drought emergency to the entire State is unfounded.

Other general concerns:

In addition to the comments on the specific questions above, Fairfield would like to re-iterate some of the comments made in our May 4, 2015 comment letter to the SWRCB. Fairfield remains very concerned about the State Water Resources Control Board's (SWRCB) current Emergency Conservation Regulations and the SWRCB's reliance on its "waste and unreasonable use" authority to force water suppliers throughout the state to meet arbitrary conservation targets.

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The current emergency regulations ignore the significant steps and financial investments Fairfield has taken in water conservation. Water conservation has been an important aspect of Fairfield's water supply management strategy since the drought of the late 1980's/early 1990's. Fairfield's water conservation program is a model program and is undertaken in conjunction with Solano County Water Agency's regional water conservation program. Prior to this past summer, Fairfield's current water usage was *already* 26% below our baseline used to meet the 2009 20x2020 targets.

For residential water use, Fairfield runs the household water survey program for all of Solano County. As part of that program, Fairfield reviews past water use and makes site visits to check for leaks. Each year, Fairfield representatives visit hundreds of homes, saving hundreds of thousands of gallons of water. Also, and in conjunction with Solano County Water Agency, Fairfield offers rebates for the installation of water saving equipment, like high efficiency toilets and clothes washers, and has a turf replacement and SMART irrigation controller program.

For commercial water users, Fairfield, in conjunction with the Solano County Water Agency, reaches out to meet the unique water conservation challenges that local businesses face. Fairfield monitors irrigation water efficiency at all of the large landscapes in the community, providing review and notification services to assure that large landscapes are not overwatered.

Fairfield has recently gone through a process of upgrading water meters throughout the city. These new state of the art meters provide data logging and automatically analyze use patterns to see if there are leaks. The purpose of using this advanced technology is to find problems and fix them before they become expensive water losses. Along with these meter upgrades, Fairfield aggressively responds to water losses within its service area. Fairfield's most recent water audit showed only 5.6% of unaccounted-for water. This is well below the industry standard of 10% and very close to the 4% level that is generally considered as the lowest level achievable in a utility of any significant size.

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Fairfield's largest industrial water use is Anheuser-Busch. For both economic and sustainability reasons, Anheuser-Busch reduced annual consumption by 56% from 2007 to 2014. Some of this reduction is due to the economic impacts of the recent recession, but the majority is the result of efforts made by Anheuser-Busch to save water. Even prior to the current drought, Anheuser-Busch eliminated almost all of its outdoor landscaping that required the use of potable water. With all of these significant reductions in use, Fairfield still has a contractual obligation to serve Anheuser-Busch through 2019. Anheuser-Busch has recently indicated they would intend to add production their Fairfield Brewery by adding a bottling line within the coming year. **Fairfield has more than an adequate water supply available to meet Anheuser-Busch's needs and a contractual obligation to supply up to three times more than is currently being provided, but should the emergency regulations continue unchanged, Fairfield would likely miss the SWRCB's conservation mandate in doing so.** Of course, part of Fairfield's long-term water strategy and strategic drought planning had these uses in mind and Fairfield has planned and secured stable water supplies to meet customer demands even during prolonged droughts, in order to maintain Fairfield's overall financial health.

The SWRCB's existing arbitrary conservation mandate ignores all of these critical facts, including the nature and extent of water supplies available to Fairfield. It is incomprehensible that the SWRCB and State of California would encourage significant investments in long-term water supply planning and investment and, once a water supplier has undertaken that investment, the SWRCB attempts to make use of those drought water supplies unlawful.

In addition to the specific facts surrounding Fairfield's investments and past conservation, the SWRCB's current emergency regulations violate basic concepts of California water law. The stated authority for imposing mandatory conservation targets contained in the current emergency regulations is the SWRCB's authority to prevent "waste and unreasonable use." The SWRCB has segregated water suppliers into "tiers", which are not based on any particular "unreasonable use" or "waste" of water but are instead simply tied to urban usage from a specific time period in 2013. The "tiers" do not recognize water right priorities, population density, climatic variation, or any other facts particular to water use.

The SWRCB cannot exercise its "reasonable use" authority in the blanket manner as articulated in the current emergency regulations. The SWRCB's "reasonable use" authority is not a panacea. Instead, it is a doctrine by which the SWRCB carefully examines specific diversion and use of water and determines whether, based on facts before it, a particular use is unreasonable. The current emergency regulations do not look at any particular use or type of use and instead simply declare the regulations are necessary to prevent the "waste

and unreasonable use of water.” The tiers altogether ignore, for example, Fairfield’s available supply and particulars of the use of water within Fairfield’s service area.

The current emergency regulations also ignore the rule of priority. Because, in part, the current emergency regulations implemented tiered conservation mandates tied to beneficial use during a portion of 2013, it is likely to result in senior water right holders being forced to cease beneficial use (“conserve”) while junior water right holders are entitled to continue to use water, perhaps at much greater quantities than senior water right holders. Imposing conservation mandates that result in water right holders diverting water without regard to priority “contravene[s] the rule of priority, which is one of the fundamental principles of California water law.” (*El Dorado Irrigation Dist. v. State Water Resources Control Bd.* (2006) 142 Cal. App. 4th 937, 943.) The current emergency regulations also ignore legal preferences for the use of water within the Area of Origin – as there is no consideration whatsoever of the use of water in the Area of Origin as compared to other areas.

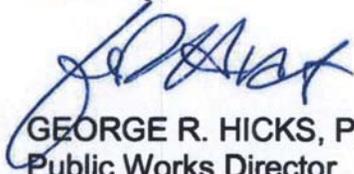
Last, the emergency regulations appear to attempt to impose some sort of “equitable” or “physical” solution to California’s ongoing drought. The California Supreme Court, however, has expressly rejected the imposition of a physical solution that ignores existing rights to water. (*City of Barstow v. Mojave Water Agency* (2000) 23 Cal.4<sup>th</sup> 1224 (*Mojave*)).

As the *Mojave* Court explained, “water right priority has long been the central principle in California water law. The corollary of this rule is that an equitable physical solution must preserve water right priorities to the extent those priorities do not lead to unreasonable use.” (*Mojave*, 1243.) Even where courts impose equitable solutions, those solutions should be based primarily on water right priorities. (*Mojave*, p. 1245-1246.) Where equitable solutions are sought, the primary consideration must be priority, with consideration also given to “physical and climatic conditions, the consumptive use of water in the several sections of the river, the character and rate of return flows, the extent of established uses, the availability of storage water, the practical effect of wasteful uses on downstream areas, the damage to upstream areas as compared to the benefits to downstream areas if a limitation is imposed on the former . . . all relevant factors.” (*Mojave*, p. 1246.) The *Mojave* Court made clear that these factors are “merely illustrative,” not exhaustive and that they underscore the “nature of the problem of apportionment and the delicate adjustment of interests which must be made.” (*Mojave*, p. 1246.) These principles apply to both surface water and groundwater rights. Despite the concern expressed by many water agencies over consideration of these types of factors, the SWRCB’s current emergency regulations fail to address these relevant issues and fail to respect the rule of priority.

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We recognize that California's ongoing drought has reached crisis proportions. However, the existence of a drought does not mean the SWRCB can ignore legal rules governing the allocation of water, and does not provide the SWRCB with the authority to interfere with contracts or mandate water suppliers forego available supplies simply for a need to conserve regardless of drought planning and available water supplies. Conservation cannot be accomplished in a "one size fits all" approach, and cannot punish those that have made investments for these precise circumstances. The SWRCB should not extend the current emergency regulations and should instead consider the specific factual circumstances for each supplier. Moreover, the SWRCB cannot make "reasonable use" determinations based on some hypothetical level of conservation not tied to any particular use of water. Fairfield believes the actions of the SWRCB are illegal, but the City voluntarily continued its water conservation efforts in 2015 and met the State's conservation targets. However, continuing on this unsustainable financial path when local water supplies are adequate to safely meet the needs of the community is not considered an option for 2016, especially if State-wide water resources are largely recovered should there be a wet winter in Northern California, and the City will be forced to explore all legal remedies including fair compensation for the effective "taking" of water rights by the SWRCB.

Sincerely,



GEORGE R. HICKS, P.E.  
Public Works Director