

"Why A Water and Sewer Parcel Tax is Necessary"

CITIZEN PROVIDED WATER AND WASTEWATER REVENUE STUDY

DISCUSSION NEEDS TO TAKE PLACE AT THE SPECIAL MEETING COMING UP AND WORK DONE TO SUPPORT A REVISED PARCEL TAX TO PAY FOR WATER AND WASTEWATER DEBT AND CAPITAL IMPROVMENTS IF IT IS SUPPORTED BY CITY COUNCIL

City Council is currently considering a parcel tax to be put on the ballot for March of 2024 to address an emergency that may occur in 2026 if general fund revenue and expenses are allowed to grow at currently projected rates.

It is very disappointing to have to consider a new tax on citizens of Sebastopol. It would have been preferable to manage expenses and adjust rates three years ago when the flaws in the last rate study became obvious.

Unfortunately, the Water and Wastewater budget is now in an acute and severe emergency. According to the Finance Director and the Budget Committee, the reserve fund is likely to be depleted by year end and the Enterprises will have to borrow cash from other city funds or a bank to remain in operation. This debt will then be added to the burden rate payers will suffer.

One very viable option to lower future rate increases is to implement a parcel tax to pay Water and Wastewater debt and capital expenses.

This needs to be considered now as there is likely to be only ***"one bite at the parcel tax apple"***.

A parcel tax for Water and Wastewater debt and capital investments offers four advantages:

- First, the revenue hike to rebalance the budget is reduced from nearly 100% to closer to 30%. Still very high but perhaps manageable with some reductions in operating cost and a phase in period.
- Second, the operating expenses, after the catchup year, generally increase annually in line with inflation. A rate can be established based on even annual increases (say 4%)
- Third, capital expense is highly variable year to year. Debt payments will vary as debt is retired over the next 10 years. A flat tax funding a reserve would allow budgeting variable size projects over time using the reserve fund.
- Fourth, the parcel tax is a flat tax that provides a predictable stream of revenue that does not decrease in response to lower water use due to a drought emergency. Our pipes and equipment require repairs and replacement over time independent of actual water use.

Following is a more detailed rationale for a parcel tax funding strategy and some considerations for expense adjustments to address the current financial crisis in our Water and Wastewater operations.

SCENARIOS TO ADDRESS THE WATER AND WASTEWATER BUDGET CRISIS

Problem:

Initial proposals from consultants (Raftelis) suggested revenue increase scenarios largely unacceptable to Council or citizens who would have to pay increases of 65 – 175% of current water and sewer rates to address expense increases in the past 3 years.

Model:

An Excel Model was constructed using the operating expense data from the 2023-24 adopted budget along with the capital improvement projects and debt payment information. 23-24 adopted budgets by department were then increased annually based on an inflation assumption.

- Inflation assumptions were taken from the Raftelis consultant document (See Appendix) as the increases built into the Adopted Budget Forecast were unrealistically low.
- Capital investment dollars were taken from the Adopted Budget document for the next 2 years and then estimated from the graphs provided by the consultant for future years. Forecast capital expenses by Raftelis are well above recent historical capital expenses. All these charts are included in the Appendix.

Expenses were projected and totaled.

	2022-23 Estimated Actual	23-24 Adopted Budget	FY 24-25	FY 25-26	FY 26-27	FY 27-28	FY 28-29	FY 29-30	FY 30-31	FY 31-32
WASTEWATER OPERATION										
TOTAL OPERATING EXPENSE (Direct)	2,763,634	3,157,214	3,259,581	3,366,395	3,412,618	3,526,389	3,643,224	3,764,999	3,892,003	4,024,544
TOTAL OTHER SOURCES/USES (G&A Allocation)	1,032,084	1,113,046	1,108,594	1,138,526	1,173,820	1,198,470	1,242,814	1,283,827	1,326,193	1,369,957
TOTAL OPERATING EXPENSE (Direct & ALLOCATED)	3,795,718	4,270,260	4,368,175	4,504,921	4,586,438	4,724,859	4,886,038	5,048,826	5,218,196	5,394,501
Transfers Out (Capital Improvement projects)	91,000	606,000	1,593,000	276,500	700,000	600,000	750,000	780,000	790,000	815,000
Total Expense w debt & Capital	3,886,718	4,876,260	5,961,175	4,781,421	5,286,438	5,324,859	5,636,038	5,828,826	6,008,196	6,209,501
WATER OPERATION										
TOTAL OPERATING EXPENSE (Direct)	1,633,086	1,872,319	1,947,863	2,028,683	2,104,483	2,184,691	2,261,416	2,342,222	2,427,390	2,517,222
TOTAL OTHER SOURCES/USES (G&A Allocation)	-	-	1,357,645	1,394,301	1,437,524	1,467,712	1,522,018	1,572,244	1,624,128	1,677,725
TOTAL OPERATING EXPENSE (Direct & ALLOCATED)	1,633,086	1,872,319	3,305,508	3,422,984	3,542,007	3,652,404	3,783,434	3,914,466	4,051,518	4,194,946
Transfers Out (Capital Improvement projects)	392,000	633,000	810,500	1,642,000	650,000	3,400,000	1,300,000	1,352,000	1,406,080	1,462,323
Total Expense w debt & Capital	2,025,086	2,505,319	4,116,008	5,064,984	4,192,007	7,052,404	5,083,434	5,266,466	5,457,598	5,657,269

New Scenario Proposals:

SCENARIO #1 -All expenses including debt and capital are paid by rate payers in the year they occur.

Revenue is set equal to the total of all direct, allocated and capital expense in the model. This results in an annual budget that is balanced. It will not increase or decrease any reserve fund from year to year. (Full model output in Appendix)

Substantial revenue increases are required in 24-25 to get back to a balanced budget (See arrow 1 on the chart below).

- Wastewater 92%
- Water 70%

(These are similar in magnitude to Raftelis but different for 3 reasons: 1. I don't have the exact data they used. 2. The cost to pay-off ongoing accumulating deficit is not included. 3. No new headcount is assumed as no data or rationale was provided in the budget process.)

	2022-23 Estimated Actual	23-24 Adopted Budget	FY 24-25	FY 25-26	FY 26-27	FY 27-28	FY 28-29	FY 29-30	FY 30-31	FY 31-32	
WASTEWATER OPERATION											
	REVENUE W/DEBT&CAPITAL	3,197,500	3,109,000	5,961,175	4,781,421	5,286,438	5,324,859	5,636,038	5,828,826	6,008,196	6,209,501
2.	Annual Increase w/ Debt& Capital			91.7%	-19.8%	10.6%	0.7%	5.8%	3.4%	3.1%	3.4%
WATER OPERATION											
	REVENUE W/DEBT&CAPITAL	2,465,750	2,414,650	4,116,008	5,064,984	4,192,007	7,052,404	5,083,434	5,266,466	5,457,598	5,657,269
2.	Annual Increase w/ Debt& Capital			70%	23%	-17%	68%	-28%	4%	4%	4%

Future revenue increases in this scenario were quite variable and would be difficult to address with a simple rate structure with even annual increases (Arrow 2).

The variability is driven by the large and variable annual budget requests for capital improvements combined with changes in annual debt payments as debt is retired over time. Debt payments are described in detail in the 23-24 Adopted Budget Document. Decreased debt payments here reflect retirement of debt per that document description.

Below are highlighted the debt and capital improvement costs in the forecast. The combined total is highlighted with year over year changes showing the high year over year variation in costs(Arrow 3).

	2022-23 Estimated Actual	23-24 Adopted Budget	FY 24-25	FY 25-26	FY 26-27	FY 27-28	FY 28-29	FY 29-30	FY 30-31	FY 31-32
WASTEWATER OPERATION										
Debt Payments	199,263	203,434	203,434	203,434	140,494	140,494	140,494	140,494	140,494	140,494
Transfers Out (Capital Improvement projects)	91,000	606,000	1,593,000	276,500	700,000	600,000	750,000	780,000	790,000	815,000
Total Debt plus capital expense	290,263	809,434	1,796,434	479,934	840,494	740,494	890,494	920,494	930,494	955,494
WATER OPERATION										
Debt Payments	321,583	357,298	357,298	357,298	357,298	357,298	357,298	357,298	357,298	357,298
Transfers Out (Capital Improvement projects)	392,000	633,000	810,500	1,642,000	650,000	3,400,000	1,300,000	1,352,000	1,406,080	1,462,323
Total Debt plus capital expense	713,583	990,298	1,167,798	1,999,298	1,007,298	3,757,298	1,657,298	1,709,298	1,763,378	1,819,621
3 → TOTAL DEBT PLUS CAPITAL WATER AND WASTEWATER	1,003,846	1,799,732	2,964,232	2,479,232	1,847,792	4,497,792	2,547,792	2,629,792	2,693,872	2,775,115
Year Over Year Change		79%	65%	-16%	-25%	143%	-43%	3%	2%	3%

Scenario #2 Pay for debt payments and capital improvements from another revenue source than rate payer revenue.

The table below shows the revenue needed to pay direct and allocated operating expenses without debt payments and capital investments described on the table immediately above this section.

	2022-23 Estimated Actual	23-24 Adopted Budget	FY 24-25	FY 25-26	FY 26-27	FY 27-28	FY 28-29	FY 29-30	FY 30-31	FY 31-32
WASTEWATER OPERATION										
5 → REVENUE W/O DEBT&CAPITAL		-	4,164,741	4,301,487	4,445,944	4,584,365	4,745,544	4,908,332	5,077,702	5,254,007
Annual Increase w/0 Debt& Capital			34.0%	3.3%	3.4%	3.1%	3.5%	3.4%	3.5%	3.5%
WATER OPERATION										
5 → REVENUE W/O DEBT&CAPITAL		-	2,948,210	3,065,686	3,184,709	3,295,106	3,426,136	3,557,168	3,694,220	3,837,648
Annual Increase w/0 Debt& Capital			22%	4%	4%	3%	4%	4%	4%	4%
			4 ↑							

Paying for capital improvements and debt payments for Water and Wastewater from another revenue source than rates would lessen the initial increase required to balance the budget (Arrow 4).

- Wastewater 34%
- Water 22%

This scenario provides a more acceptable year over year increase in revenues to adjust to the radical increase in expense over the last three years.

This scenario also smooths the annual change in rates that would be needed to meet growing future costs (Arrow 5).

Scenario 2 also simplifies the budget discussion. Each department’s operating expenses have a rationale and can be compared to history.

Lowering the dramatic first year increase to get back to a balanced budget is critical as there will also be a cost to payback the debt being accumulated as the ongoing deficit depletes the reserve fund and requires borrowing from other funds or the bank to manage cash. Paying back this deficit is not included in this analysis.

Scenario #3 Use a Parcel Tax to pay for Water and Wastewater debt payments and capital investment requirements.

	2022-23 Estimated Actual	23-24 Adopted Budget	FY 24-25	FY 25-26	FY 26-27	FY 27-28	FY 28-29	FY 29-30	FY 30-31	FY 31-32
TOTAL DEBT PLUS CAPITAL WATER AND WASTEWATER	1,003,846	1,799,732	2,964,232	2,479,232	1,847,792	4,497,792	2,547,792	2,629,792	2,693,872	2,775,115
Year Over Year Change		79%	65%	-16%	-25%	143%	-43%	3%	2%	3%

Combined debt and capital investments average around \$2.5MM per year. They are quite variable but don’t have an obvious upward trend. A flat parcel tax estimated at around \$450-500 per parcel could provide this level of annual revenue.

Parcel tax revenue go to a reserve fund dedicated to pay for future debt payments and capital projects for Water and Wastewater Enterprises.

NOTE: THIS DISCUSSION NEEDS TO TAKE PLACE AT THE SPECIAL MEETING COMING UP AND WORK DONE TO SUPPORT A REVISED PARCEL TAX TO PAY FOR WATER AND WASTEWATER DEBT AND CAPITAL IMPROVEMENTS

Expense reduction is another strategy to reduce the rate increases needed to balance the budget. Although these can be discussed at a later meeting, they need to be discussed soon.

Scenario 4: Reduce *Allocated* operating expenses for Water and Wastewater to reduce the hurdle to return to a balanced budget.

There is a substantial question regarding the allocations to Water and Wastewater rate payers. The current allocations are made based on a study and resulting policy established 20+ years ago. There are a couple of big issues.

First the % allocations to overall department budgets result in expenses unrelated to water and sewer being allocated to rate payers which is **likely contrary to the California constitution and case law** that limits charges to rate payers only the cost of delivering water and sewer services.

Examples of city expenses subsidized by Water and Wastewater rate payers that seem inappropriate:

- 75% of Costs to initiate ballot measures to raise sale and property taxes unrelated to the Water or Sewer operation.
- 50% of Police and Fire Generator maintenance, holiday décor, maintenance of city buildings not housing water and sewer operations
- 26% of Community Grants for Peacetown summer concerts, Fireworks, Apple Blossom Parade, Support for World Friends, electric shuttle fare subsidies & homeless outreach
- 18% of non-departmental expenses that cannot be assigned to any department are assigned to Water and Sewer rate payers including the Park Village Management Contract
- 8% of City Legal costs to defend ACLU lawsuit – homeless.
- 8% of Election book, City Arborist, Community outreach tech meeting support costs for Climate action committee, Design review board, public art committee meetings,
- 7% of the Fire Department Operating Expense

Even if we focus only on the allocation of staff time the %'s seem extremely high. For example, those of us who watch every City Council Meeting have not seen anything approaching 25% of their time spent on Sewer and Wastewater.

City Manager (40% of his time allocated) recently explained the rationale that he easily spends this amount of time dealing with employee issues in Public Works. It appears however that only 2 out of 92 city employees are fully tasked to the Water and Sewer. Further if we total public works and finance headcount that only represents about 20% of the overall city staff. 40% seems extreme.

Finance is allocated 75% to Water and Sewer. It seems like the description of their department accomplishments and objectives argues that more than 1FTE is doing all that work for the city while the remaining three spend full time doing bimonthly billings. We see that some of the billing is outsourced as well for Sewer to Santa Rosa. Again, a careful study needs to be done.

Public works allocates nearly all the expense for the storage yard and 50% of the cities building expense to Water and Sewer. The current inventory of buildings includes the Youth Annex, Community Center, Senior Center, History Museum, and park buildings. None seem to be utilized for Water and Sewer Operations.

Fire is also a questionable area. As a city we have learned a great deal about the contributions of our volunteer department. Their role in maintaining our water service has not reached the highlights.

Allocated operating expense makes up 1/3 the expense that rate payers are funding. Reducing this by ½ would cut rate payer funded expenses by 15%. This would be significant factor in lowering the first-year revenue increase needed to balance the budget.

OVERHEAD ALLOCATION					
Department	***** Percentage of Overhead Allocated by Fund *****				
	General Fund	T&U Fund	Water Fund	Sewer Fund	Total
City Council	74.0%		12.0%	14.0%	100.0%
City Manager	60.0%		20.0%	20.0%	100.0%
City Attorney	92.0%		5.0%	3.0%	100.0%
Assistant City Manager/City Clerk	85.0%		8.0%	7.0%	100.0%
Finance	25.0%		38.0%	37.0%	100.0%
Building	74.0%		13.0%	13.0%	100.0%
Planning	92.0%		5.0%	3.0%	100.0%
Engineering	38.0%		34.0%	28.0%	100.0%
Fire Services	93.0%		7.0%		100.0%
Police Services	89.6%	10.4%			100.0%
Public Works					
Corporation Yard		17.0%	48.0%	35.0%	100.0%
Government Building	50.0%		25.0%	25.0%	100.0%
Streets		100.0%			100.0%
Parking Lots	100.0%				100.0%
Parks & Landscaping	58.5%	41.5%			100.0%
Storm Water		100.0%			100.0%
Non Departmental	82.0%		9.0%	9.0%	100.0%

Scenario 5: Examine the Direct Operating Expense for Water and Sewer for possible reductions in cost.

Water and Sewer have experienced double digit increases in costs across many line items at a time when water use is declining due to drought restriction and Wastewater use similarly must be in decline.

While other city departments were carefully reviewed, the Water and Sewer only got a cursory discussion at one of the final Budget Committee Reviews and a brief discussion after 10pm by the full council on the last night of budget discussions.

I don't believe any of the Budget Committee targeted reductions were directed at Water or Wastewater. In fact, in at least one \$97,000 expense (dump truck purchase) was moved to Water and Wastewater. There has been no line-item review and discussion of these expenses that I have been able to find.

Given the current state of emergency for the Water and Wastewater operating budgets such a review seems practical.

Five year budget forecast from 23-24 Adopted Budget Document

**City of Sebastopol, CA
General Fund/Transaction & Use Tax Fund History and Forecast
FY 2016-17 Through 2028-29**

	Estimated Actual FY 22-23	Adopted Budget FY23-24	Forecast FY 24-25	Forecast FY 25-26	Forecast FY 26-27	Forecast FY 27-28	Forecast FY 28-29
Department Expenditures:							
City Council	466,134	170,318	410,579	430,442	451,298	473,196	496,190
City Manager	230,277	302,682	344,881	358,030	371,862	386,248	402,771
City Attorney	432,759	593,621	600,609	601,266	601,948	602,567	603,903
City Clerk	381,643	369,258	365,762	345,829	386,240	366,679	410,050
Administrative Services (Finance)	317,218	397,920	364,695	381,100	398,500	416,790	437,712
Planning	566,848	592,259	606,931	629,937	654,129	679,240	708,487
Building	182,793	185,481	190,681	198,412	206,490	214,790	224,583
Engineering / Storm Water	329,016	288,087	230,955	242,060	253,769	266,121	279,154
Fire	1,222,818	1,452,312	1,253,066	1,295,199	1,308,865	1,353,553	1,404,948
Police	5,227,005	5,477,732	5,085,672	5,270,673	5,432,766	5,602,423	5,802,891
Public Works	1,285,552	1,286,184	1,413,434	1,432,828	1,454,394	1,471,770	1,497,905
Community Center	750,921	667,757	697,937	731,908	767,664	805,309	844,956
Non Departmental	254,159	236,980	266,867	280,210	294,221	308,932	324,379
Debt Service	261,802	265,904	265,500	230,500	230,500	133,000	133,000
Other Sources - Insurance							
Total Department Expenditures	11,908,944	12,286,495	12,097,869	12,428,392	12,812,646	13,080,618	13,570,929
Transfers Out:							
Others - Overage of AD & GT	-	-	-	-	-	-	-
Others - Streets Pavement Reserve	-	-	-	-	-	-	-
Others - Pension & Infrastructure	100,000	100,000	150,000	150,000	-	-	-
Others - SLESF	-	-	-	-	-	-	-
Others - Capital Projects	112,000	151,500	83,500	-	-	-	83,500
Others -Gas Tax	-	-	-	-	-	-	-
Others -PD Grant Funds	-	-	-	-	-	-	-
Total Transfers Out	212,000	251,500	233,500	150,000	-	-	83,500
Total Resources Used: (Departmental, Other Expenditures & Transfers Out)	\$ 12,120,944	\$ 12,537,995	\$ 12,331,369	\$ 12,578,392	\$ 12,812,646	\$ 13,080,618	\$ 13,654,429
Net Results of Operations: (Total Resources Available less Total Resources Used)	\$ 470,381	\$(1,677,535)	\$(1,298,514)	\$(537,302)	\$(543,304)	\$(578,610)	\$(915,254)
Contribution/(Uses) of Reserves:							
Total Annual Surplus/(Deficit): (Net Results of Operations & Contribution to Reserves)	\$ 470,381	\$(1,677,535)	\$(1,298,514)	\$(537,302)	\$(543,304)	\$(578,610)	\$(915,254)
Policy Reserve Level (15% to 20%)	\$ 1,818,142	\$ 1,880,699	\$ 1,849,705	\$ 1,886,759	\$ 1,921,897	\$ 1,962,093	\$ 2,048,164
Unassigned Reserves Balance	\$ 3,527,869	\$ 1,850,334	\$ 551,820	\$ 14,518	\$(528,786)	\$(1,107,396)	\$(2,022,650)
Actual Reserve Level	29.1%	14.8%	4.5%	0.1%	-4.1%	-8.5%	-14.8%

Inflation Assumptions from Raftellis Consultant Document

Assumptions – Inflationary Escalation

Expense Category	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28	FY 2028-29	FY 2029-30	FY 2030-31	FY 2031-32	FY 2032-33
O&M Expenses										
General	Budget	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%
Salary	Budget	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%
Benefits	Budget	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%
Utilities	Budget	10.0%	10.0%	7.0%	7.0%	5.0%	5.0%	5.0%	5.0%	5.0%
Capital Expenses										
Capital		4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%

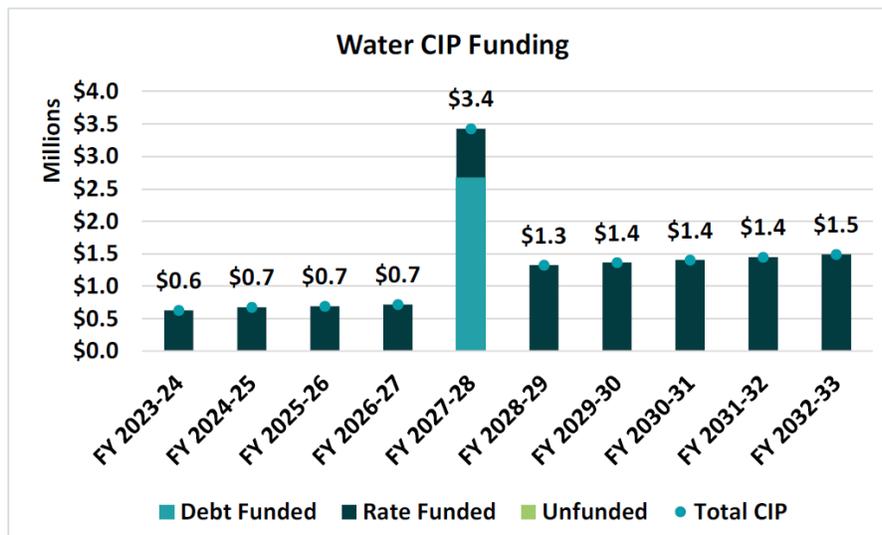
Water Capital Projects from 23-24 Adopted Budget

Category Summary Report City of Sebastopol FY 2023-24 to 2027-28 8 - Water Projects

PROJECT TITLE	FY22-23 Estimated	2023-24	2024-25	2025-26	2026-27	2027-28	TOTALS
0815-83.00 Florence: Water Line Replace South	500	26,000	181,500				207,500
0816-84.00 Florence: Water Line Replace North	500	56,000	402,000				458,000
0818-20.09 1st Street Water Main Replacement-COMPLETED	340,000						
0819-21.01 Parquet Street Water Line Replacement (combined City project #1000-21.01)	51,000	551,000					551,000
0820-23.03 NEW: Pleasant Hill Rd. Water Line: Mitchell Ct. to Lynch Rd.			227,000	1,522,000			1,749,000
0821-23.09 NEW: Water System Master Plan Update				120,000			120,000
	392,000	633,000	810,500	1,642,000			3,085,500
PROJECT FUNDING SOURCES							
001 Grant - Unsecured				1,522,000			1,522,000
501 Water Capital Fund	392,000	633,000	810,500	120,000			1,563,500
	392,000	633,000	810,500	1,642,000			3,085,500

Long-term Water Capital Funding from Raftelis Consultant Document

Capital Improvement Program



Note: The values displayed are inflated by the 4% capital inflator

Wastewater Capital Improvement Projects from 23-24 Adopted Budget

Category Summary Report

City of Sebastopol FY 2023-24 to 2027-28

6 - Sewer/Wastewater Projects

PROJECT TITLE		FY22-23 Estimated	2023-24	2024-25	2025-26	2026-27	2027-28	TOTALS
0604-37.00	Zimpher Creek Sewer Relocation Part 1 - Covert Lane Rerouting	32,000	1,000	222,000				223,000
0610-70.00	Zimpher Creek Sewer Relocation Part 2 - West End	115,200	1,000	604,500				605,500
0611-80.00	Zimpher Creek Sewer Relocation Part 3 - Repairs at East End		31,000	417,000				448,000
0612-81.00	Florence Avenue Sewer Line Improvements - South		1,000	21,000	276,500			298,500
0613-82.00	Florence Avenue Sewer Line Improvements - North		21,000	196,500				217,500
0615-21.01	Parquet Street Sewer Line Replacement (combined City project #1000-19.01)	51,000	551,000					551,000
0615-23.04	NEW: Sewer System Master Plan Update			132,000				132,000
		198,200	606,000	1,593,000	276,500			2,475,500
PROJECT FUNDING SOURCES								
000	Unfunded			1,566,500	275,000			1,841,500
511	Sewer Capital Fund	198,200	606,000	26,500	1,500			634,000
		198,200	606,000	1,593,000	276,500			2,475,500

Long-term Wastewater Capital Funding from Raftelis Consultant Document

Capital Improvement Program

