

City of Garden Grove

INTER-DEPARTMENT MEMORANDUM

To: Matthew J. Fertal
Dept.: City Manager
Subject: YEAR ONE REVIEW OF FINANCIAL PLAN
FOR THE WATER ENTERPRISE

From: Keith G. Jones
Dept.: Public Works
Date: May 13, 2008

OBJECTIVE

For City Council to receive and file information concerning the Water Enterprise's completion of year one of the Financial Plan and projections for the remaining term of the plan.

BACKGROUND

Implementation of a fair and appropriate water service fee structure is a necessary investment in the future of the City's Water Enterprise in order to provide the public with safe, reliable, and pleasant drinking water and to provide fire flow capability throughout its infrastructure. Critical capital improvements and facility replacements had been deferred since 2004, due to the severely negative financial condition of the Water Enterprise Fund. The Water Enterprise Fund was not meeting its core business principles and required a sustainable financial plan to meet its immediate and long-term obligations.

In July 2007, Council adopted a Ten-Year Water Financial Plan (Plan) prepared by Black & Veatch to maintain the financial stability of the Water Enterprise Fund. The Plan identified the overall revenue needs for essential financing of the operations and maintenance expenses, debt obligations, capital improvement requirements and cost increases for imported water, which were projected to rise approximately 5% on an annual basis. To meet the essential financial needs, the first five years of the Plan included incremental annual rate adjustments of 40%, 20%, 7.5%, 5% and 5% to be applied to the service charge and commodity adjustment charges.

DISCUSSION

As a result of plan implementation in Year-1, the Water Enterprise was able to meet its financial obligations for the year. In addition, the initial rate adjustment enabled staff to begin ramping back up its capital improvement project (CIP) program, which had been deferred for the past three years.

During the past year, staff has progressed towards the completion of the following critical capital improvements and replacements that are supported by the Plan:

- Water Master Plan: Scheduled for completion in October 2008, it is a comprehensive plan that will enable staff to identify and prioritize current and future capital improvements in a pro-active and fiscally prudent manner.
- Chlorine Conversion Projects: The Chlorine Conversion Project entails modifications necessary to change disinfection from chlorine gas to a safer liquid form of chlorine for its disinfection, at ten (10) well sites. City staff will have four (4) well sites completed by July 2008, while the remaining gas chlorine sites are scheduled for completion by March 2009.
- Miscellaneous Capital Replacement Projects: By the end of July 2008, staff will have completed: 140 fire hydrant replacements, 500 service line replacements, 870 meter replacements, 82 gate valve replacements.

The Plan schedule for Years 2 through 10 continues to build the CIP program and includes the following projects with estimated amounts completed and costs per year:

- 5,000 to 10,000 linear feet of main replacement/year (\$1M to \$2.5M/year)
- Replace 140 fire hydrants and 20 fire hydrant valves/year (\$0.35M/year)
- Replace 756 service lines/year (\$1.35M/year)
- Replace 3,780 small meters and test and repair or replace 400 large meters/year (\$ 0.98M/year)
- Replace 132 gate valve/year (\$ 0.56M/year)
- Replace 35 air/vacuum valves/year (\$ 0.054M/year)
- Well improvements (varies - \$0 to \$2.78M/year)
- Booster pump replacements at 5 pump stations (varies - \$0.2M to \$0.6M/year)
- Natural gas engine replacements at 4 pump stations (varies \$0 to \$ 2.0M/year)
- Miscellaneous improvements and/or repairs (varies \$0 to \$0.73m/year)

Year-2 of the Plan calls for the issuance of bonds totaling \$32 million to be used over the next several years. Revenue requirements in Year-2 will increase to \$26.7 million, which consist of existing expenses, funding for reserve accounts, inflationary costs, imported water costs and an additional bond repayment. The planned rate adjustment of 20% for Year-2 is designed to meet the Water Enterprise's current and future financial obligations without further drawing on existing capital funds.

FISCAL IMPACT

An assessment of the Plan for Year-1 shows the beginning of the year projections and year end actual (based on ¾ review) for revenues and expenditures will end for the year within a difference of \$100,000, which is very acceptable. It demonstrates that the original assumptions in the financial plan were valid. It is important to note that the continued success of the Plan is heavily dependent on the implementation of the rate adjustments approved in July 2007(20%, 7.5%, 5% and 5%) over these next four years. Furthermore, our original assumption based on discussions over a year ago with Metropolitan Water District (MWD) that costs for imported water would increase by 5% on an annual basis has been supplanted by new information from MWD. Staff was recently told that MWD would enact a rate increase of 14% for this coming fiscal year and have proposed an 11% increase for the following year. It is staff's professional opinion that any reduction in the City's approved rate adjustments would be catastrophic for the Water Enterprise and would result in its insolvency.

COMMUNITY VISION IMPLEMENTATION

The project is consistent with the community vision for maintaining and upgrading the water system to ensure maximum protection for public health and the environment.

RECOMMENDATION

No action is required; this item is submitted for information only.


KEITH G. JONES
Public Works Director

By: David E. Entsminger
Water Services Manager

Recommended for Approval


Matthew Fertal
City Manager