

**BUSINESS OF THE COUNCIL OF THE CITY OF HALF MOON BAY**

**AGENDA REPORT**

For meeting of: **April 7, 2020**

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**TO:** Honorable Mayor and City Council

**VIA:** Bob Nisbet, City Manager

**FROM:** John T. Doughty, Public Works Director  
Lisa Lopez, Administrative Services Director  
Maz Bozorginia, City Engineer

**TITLE: SEWER SERVICE CHARGES REPORT FROM MUNICIPAL FINANCIAL SERVICES, INTENT TO ESTABLISH SANITARY SEWER SERVICE CHARGES EFFECTIVE FISCAL YEARS 2020-21 THROUGH 2024-25, AND SET PUBLIC HEARING FOR JUNE 2, 2020**

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**RECOMMENDATION:**

It is recommended that the City Council: 1) adopt a resolution accepting the report titled “2020 Sewer Service Charges Study”, dated April 1, 2020 prepared by Municipal Financial Services (MFS); stating the City Council’s intent to establish sanitary sewer fees for fiscal years 2020-21 through 2024-25; adopting City Guidelines for Submission and Tabulation of Protests; setting the Public Hearing for June 2, 2020; and directing staff to release notices to property owners in accordance with Proposition 218; and 2) direct staff to return with revisions to Municipal Code Title 13 to codify the rate structure for residential uses and other related changes.

**FISCAL IMPACT:**

The purpose of the rate adjustment is to create a financially sustainable Sewer Enterprise Fund. Over the last five years, fixed sewer system costs have continued to grow with costs exceeding revenues generated by the current rates. Over the last three years, the City has found it necessary to utilize emergency/capital reserve funds for fixed operational costs. In FY 2019-20, \$2,006,000 was transferred to the operating fund from the capital reserve fund.

**STRATEGIC ELEMENT:**

This recommendation supports the Infrastructure and Environment, Healthy Communities and Public Safety, and Inclusive Governance Elements of the Strategic Plan.

**ENVIRONMENTAL REVIEW:**

As set forth in California Code of Regulations Section 15273, the California Environmental Quality Act does not apply to the establishment, modification, structuring, restructuring, or

approval of rates and other charges by a public agency provided the purpose is to maintain and operate services within the existing service area boundary.

### **SEWER SYSTEM OVERVIEW:**

The City's collection system includes approximately 35 miles of gravity sewer lines, three (3) pump stations and three (3) force mains. Wastewater from residences, businesses, schools, restaurants and other buildings and uses is conveyed through sewer mains owned by the City of Half Moon Bay to the sewer treatment plant operated by Sewer Authority Mid-Coastside (SAM). The City collection system serves residences, businesses, and public uses from Frenchman's Creek on the north to Miramontes Point Road on the south. The City primarily serves properties located in the incorporated area; however, the City serves some adjacent areas outside city limits including the Moonridge Housing Development.

The City, Granada Community Services District (Granada), and Montara Water and Sanitary District (Montara) formed the Sewer Authority Mid-Coastside via an exercise of Joint Powers Authority (JPA). SAM facilities include a conventional wastewater treatment plant (located at 1000 N. Cabrillo Highway, Half Moon Bay) and the Intertie Pipeline System (IPS), which conveys flows through pumping facilities, force mains, and interceptor pipelines from Granada and Montara service areas to the wastewater treatment plant. Under the current JPA, the City is responsible for paying a proportional share of the plant flow for operations, maintenance, and capital costs of the wastewater treatment plant. In FY 2019-20, the City's proportional share of operations and maintenance was set at 56 percent. In 2017, the City filed for Declaratory Relief regarding language in the JPA related to member agencies' respective obligations for paying for capital projects (notably the IPS). The parties and City agreed to enter into mediation and have been actively engaged in settlement discussions.

The regional wastewater treatment plant was originally constructed in the late 1970s, following the formation of the JPA. The treatment plant was substantially upgraded in late 1999/2000 and has sufficient capacity to receive and treat anticipated wastewater flows. The treatment plant, due substantially to deferred maintenance, is in need of major maintenance and capital repair which have been estimated between \$30 and \$40 million. This rate study includes funding for capital repair and replacement on either a financed or pay-as-you-go scenario. The rates include approximately \$2.4 million in combined annual contributions from the City, Granada, and Montara.

The IPS was constructed in the late 1970s and is, for the most part, comprised of original system components. In 2017, the Granada Force Main suffered a major break and resulted in a significant sanitary sewer spill (SSO). Two smaller SSO events occurred on other sections of the Granada Force Main. As a result, SAM completed replacement of approximately 5,700 feet of the Granada Force Main at a cost of almost \$2 million. SAM recently commenced work on an additional 1,500 feet of the Granada Force Main. SAM was fined, (and member agencies proportionately paid) approximately \$600,000, by the Regional Water Board for the 2017 SSO events. SAM was subsequently sued by the Ecological Resource Foundation (ERF). In addition to some cash considerations, the settlement of this suit included commitment to a series of

replacements of the IPS over the next five years totaling an estimated almost \$9 million. Total IPS repair and replacement is estimated between \$20 and \$25 million.

#### **SEWER ENTERPRISE FUND OVERVIEW:**

The City's Sewer Fund is a government enterprise fund. An enterprise fund is a self-supporting government fund that provides a specialized service. In this instance, City sewer services represent the specialized service; the Sewer Fund is the City's only enterprise fund. The Sewer Fund is shown in the City's Annual Operations Budget as two separate accounts: Fund 05 (Operating Fund); and 06 (Sewer Capital Fund). The separation exists solely to separately account for operations expenses and capital expenses.

Ninety-nine percent (99%) of sewer system (utility) revenues is derived directly from rates charged to the users of the sewer system. Per state law, sewer service charges are permitted to recover only revenues sufficient to adequately fund sewer utility operations, maintenance, and capital replacement expenditures including maintenance of emergency and capital reserves. As noted, the City's sewer service charges include not only the operation and maintenance of the City collection system, but also the proportional costs of operating and maintaining the Sewer Authority Mid-Coastside (SAM) (including the treatment plant and intertie pipeline system).

Operations and maintenance costs for sewer services have increased significantly over the last three years. Between FY 2015-16 (\$2,299,898) and FY 2019-20 (\$4,131,899), Half Moon Bay's proportion of SAM budgeted costs alone have almost doubled. Additionally, the City's share of the costs has increased by almost 10 percent over the last five years. SAM related increases are attributable to a number of factors including the need to provide sufficient staffing, address deferred maintenance, pay for sewer spill related costs, and account for the rapidly increasing cost of materials and labor for capital construction and maintenance.

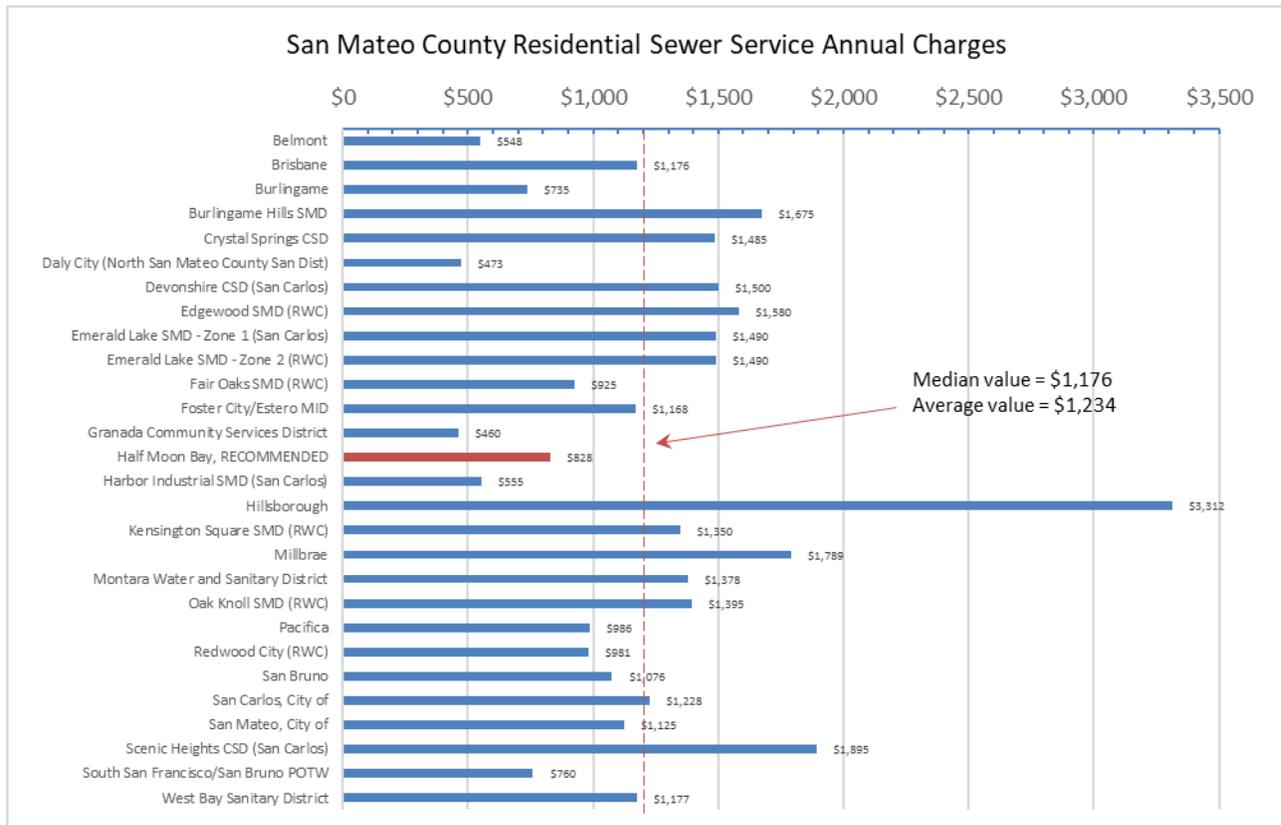
The City's collection system operating costs have also risen in response to statutory oversight obligations, addressing long deferred maintenance, providing oversight of the operations and maintenance, and also to account for the rapidly increasing cost of materials and labor for capital construction and maintenance. The City is currently advertising bids for the Ocean Colony Pump Station and Force Main Project. This project is needed to replace aging infrastructure necessary to protect the environment and limit liability. The engineer's estimate of construction costs is nearly \$3 million. Additional capital maintenance and repair will continue to be needed to protect the environment, limit liability, and meet statutory obligations. While the City is proactively managing and maintaining its sewer assets, portions of the inground pipes are 70-80 years old and approaching normal life expectancy.

The last rate increase for City sewer customers was effective July 1, 2014, based upon a rate study approved by the City Council in 2012. The increases covered rates for FY 2012-13 and FY 2013-14. This adjustment followed a rate increase approved in 2010 which increased rates in FY 2010-11 and FY 2011-12. Granada and Montara are subject to the same fixed costs issues and have each increased rates during this period of time. Montara is considering three years of nine percent annual rate increases which will be effective on July 1, 2020. Many San Mateo

County/Peninsula agencies have or will be considering rate adjustments to address increasing fixed costs and environmental compliance.

**BACKGROUND:**

The City currently serves 4,455 residential units and 307 non-residential customers. City sewer service charges across-the-board are among the lowest in San Mateo County. Today, the average single-family rate (averaged across all customers) is approximately \$830 annually or the equivalent of \$69 per month. Across San Mateo County, the average annual service charge is \$1,234 (\$103 per month) and the median annual sewer service charge is \$1,176 (\$98 per month). The rate comparison table for San Mateo County is below. The City rate (in red) reflects the anticipated rate for an average single-family residence as of July 1, 2020.



**Figure 1—Rate Comparison for Single Family 2020**

City sewer customers have enjoyed six years of rate stability. Unfortunately, revenues are not keeping pace with the increasing cost of operating and maintaining the City’s collection system or SAM operations and facilities. While efforts have and will continue to be made to operate efficiently and cost effectively, the cost of “doing business” has increased and the rates need to be adjusted. Further, neither the City nor SAM can defer infrastructure repairs and replacements as the cost of deferral would be significantly greater in both actual costs and potential liabilities. Over the last several years, the City has been required to use emergency and capital reserve funds to cover the increasing costs of operations.

In light of this, the City commissioned the services of Municipal Financial Services (MFS) to assist the City in evaluating current rates and rate structure, City costs (current and anticipated costs), SAM costs (current and anticipated), and to recommend a revised rate structure in accordance with Proposition 218. The City has been working with MFS since the fall of 2019 to complete the statutorily required cost of service analysis.

The City Council's Finance Subcommittee met in December, February, and March to discuss the study, rate structure, and proposed fees. On March 10, 2020, the Subcommittee authorized staff to present the proposal to the City Council.

On March 17, 2020, the City Council conducted a study session regarding the rate study, proposed rate structure, and implications on the annual sewer service charges over the next five fiscal years. Following questions and discussion, the City Council authorized staff to proceed with the rate adjustment process including returning for acceptance of the report.

**DISCUSSION:**

Pursuant to Section 6 of Article XIID of the California Constitution (a provision of Proposition 218) the City must give notice by mail to each property owner of record as of the last equalized assessment roll of the proposed rate adjustment. As the City utilizes the annual tax assessment process for billing, the account holders and addresses are based upon the last equalized assessment roll. A copy of the sample Notice is provided as Attachment 2. In addition to the mailed Notice, the City has created a web page that includes frequently asked questions (FAQs), related information, and links to assist account holders in understanding the rate adjustment request, the basis for the request, and the protest process.

Property owners have the right to submit written protests against the proposed charge(s) and may do so by mail or in person to the City Clerk before the end of the Public Hearing (scheduled for June 2, 2020). Given the unique Covid-19 situation, accommodation will be made for submittal of protests should the hearing be conducted virtually. Staff is asking the City Council to approve Guidelines for the Submission and Tabulation of Protests, included as Exhibit A to the Resolution.

At the Public Hearing, the City Council will consider all protests against the proposed charge(s). If written protests against the charge(s) are presented by owners of a majority of affected parcels, the City Council may not impose the revised charge(s). The opposite is also true, should the City not receive majority protest, the City Council may impose the new charge(s).

As required by statute, the City will also give notice of the time and place of the Public Hearing by publishing notice for two consecutive weeks not less than 14 days in advance of the Public Hearing. Additionally, a copy of the resolution setting the Public Hearing will be posted on the official bulletin board outside City Hall as well on the City's website.

**CONCLUSION:**

Upon review of financial plans, annual expenditures, and the capital improvement programs for the City and SAM, the Cost of Services Report concluded that the City Sewer Enterprise was fiscally unsustainable with current rates and charges. MFS was asked by the City to evaluate the City’s rate structure and provide recommendations. MFS recommended retention of the non-residential rate structure. Staff and MFS spent considerable time evaluating the residential rate structure. Following this assessment, MFS was directed to develop the Study assuming a transition to a flat rate structure for residential uses. This structure eliminates a Proposition 218 issue of a minimum fee. The structure also provides for rate stability and predictability. Finally, the structure reduces annual administrative costs. These changes were discussed by the Finance Subcommittee and the City Council.

The following Table reflects the recommended service charges by customer/premise classification. The 2020 Sewer Service Charges Study, included as Exhibit A to the Resolution, provides additional details.

**Table 1—Proposed Sewer Service Charges (next page)**

Classes of Premises	2020-21	2021-22	2022-23	2023-24	2024-25
Residential/Mobile Home/Retirement *			<i>Per Account or Unit Per Year</i>		
Residential Single Family	\$828	\$936	\$1,056	\$1,188	\$1,344
Residential Single Family w/ADU	\$960	\$1,104	\$1,236	\$1,392	\$1,572
Residential Multiple Family	\$828	\$936	\$1,056	\$1,188	\$1,344
Mobile Home	\$504	\$576	\$648	\$732	\$828
Senior Apartments (New Class)	\$504	\$576	\$648	\$732	\$828
Nonresidential **			<i>Per Account or Unit Per Year</i>		
Retirement Homes	\$504	\$576	\$648	\$732	\$828
Annual Account Charge			<i>Per Account Per Year</i>		
All classes	\$183	\$208	\$235	\$264	\$298
Flow Rate, \$/HCF			<i>Annual Water Use</i>		
Office	\$8.11	\$9.26	\$10.44	\$11.72	\$13.25
School	\$8.11	\$9.26	\$10.44	\$11.72	\$13.25
Recreational	\$13.03	\$14.88	\$16.77	\$18.83	\$21.28
Commercial	\$9.35	\$10.68	\$12.04	\$13.52	\$15.28
Medical	\$11.12	\$12.70	\$14.32	\$16.08	\$18.17
Motel	\$13.74	\$15.70	\$17.69	\$19.87	\$22.45
Restaurant	\$19.75	\$22.56	\$25.43	\$28.56	\$32.27
Individual					
Annual Account Rate					
All classes	\$183	\$208	\$235	\$264	\$298
Flow Rate, \$/HCF					
Individual premise					
Flow Rate, \$/kgal	\$8.54	\$9.76	\$10.99	\$12.35	\$13.95
BOD Rate, \$/pound	\$1.22	\$1.40	\$1.57	\$1.77	\$2.00
TSS Rate, \$/pound	\$1.15	\$1.31	\$1.48	\$1.66	\$1.88

The City Council is committed to fiscal sustainability and environmental protection. Without a rate adjustment, the City sewer system will not be a financially viable enterprise. Without adequate funding of the sewer system, the City will not be able to operate and maintain the City sewer system in conformance with state and federal regulations, likely resulting in sewer system overflows (SSOs) and legal liability to the City.

**NEXT STEPS:**

June 2, 2020 – Conduct Public Hearing and determine whether there is no majority protest and adopt new sewer charges if so.

**ATTACHMENTS:**

1. Resolution with Exhibits
2. Sample Public Hearing Notice