REPORT TO COUNCIL 32
City of Sacramento

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Staff Report
August 29, 2006

Honorable Mayor and
Members of the City Council

Title: Alternative Funding Sources for Capital Improvement Program (CIP) Costs Funded by the Stormwater (Drainage) Fund 425

Location/Council District: Sacramento Region

Recommendation: Adopt a **Resolution** providing direction to staff relating to the following alternative funding sources for the Stormwater (Drainage) Fund 425.

- Develop the necessary fee study, initiate an outreach program, and prepare a regulatory fee ordinance and fee resolution to be brought to the Law and Legislation Committee by January 2007.
- Complete a study by January 2007 that may be used as the basis for subsequent approval of a drainage impact fee to finance construction of common drainage facilities in infill areas.
- Accomplish the following: (1) develop an estimate of the cost to put a storm drain rate increase measure for voter approval in accordance with Proposition 218, (2) determine whether such a vote could be included on the same ballot as a SAFCA assessment vote, (3) prepare multi-year rate increase proposals and, (4) report back to Council when this is completed.
- Work with the League of California Cities to obtain a consensus on the need to amend Proposition 218's language to exclude local drainage rates from the voter approval requirement, and the City's lobbyist(s) are directed to communicate to the drafters of ACA13 the critical need to keep the local drainage fees as part of the bill.

Contact: Charlene McKoy, Business Services Manager, 808-1462

Presenters: Gary Reents, Director of Utilities, 808-1433, Dave Brent, Engineering Manager, 808-1420, Charlene McKoy, Business Services Manager, 808-1462, Andy Hunt, Supervising Engineer, 808-1408, Bill Busath, Supervising Engineer, 808-1434

Department: Utilities

Division: Engineering Services

Organization No: 3331

Description/Analysis

Issue: The estimated cost for replacement or rehabilitation of life-cycled drainage infrastructure over the next 20 years is estimated to be $40 million. In addition to the rehabilitation and replacement needs, the current estimated cost for all identified improvement projects to meet the Council approved goals for drainage is $1 billion.

At the same time the costs required to operate and maintain the drainage system have steadily increased, due to inflation, increased cost of maintaining an ever-aging system including the replacement of pumps, electrical systems, etc., and salary adjustments. Over the past 5 years, operations and maintenance costs have increased an average of 7.6% annually.

Prior to the passage of Proposition 218, which mandates voter approval to increase the rates charged for storm drain service, the funds allotted for drainage CIPs was about $8M per year. Due to inflation, the use of drainage funds to comply with mandated regulatory requirements, and the absence of rate increases for the past 10 years, the amount available for drainage CIPs has steadily declined and has been reduced from $8 million to less than $2 million per year in FY06/07.

Due to this steady decline in available funding, the Department of Utilities (DOU) has limited the focus of the CIP program the past 2 years to highest priority rehabilitation/ replacement projects except for a few improvement projects that were previously approved by City Council, and no further improvement projects are being recommended by the Department of Utilities. Within the next 3 to 4 years, without changes in the current funding sources or policies, DOU projects that there will be no funds available, even for necessary rehabilitation/ replacement drainage CIP's or to fund the drainage component of combined sewer system CIPs. Soon after, there will begin to be impacts to our ability to operate and maintain the existing infrastructure.

At the January 24, 2006 presentation to Council on drainage infrastructure staff introduced three potential options to help stabilize the drainage fund; (1) a regulatory fee to cover non-drainage related regulatory mandates currently funded out of the drainage fund; (2) a development impact fee to pay for drainage improvements in infill areas; and (3) a Proposition 218 vote to raise drainage rates. Council directed staff to report back with further refinement of those three alternatives and considerations of additional funding alternatives. The additional funding alternatives considered in this report are bond financing, assessment districts, General Fund support and special taxes.

These alternatives are discussed in detail at Attachment 2.

Policy Considerations: This report and the attached resolution are in response to a Council request and are consistent with the Council approved policy to provide adequate flood protection to all areas of the City.

Environmental Considerations: This report seeks direction relating to the implementation of alternative funding sources for costs funded by the Drainage Fund, and is not a project that requires environmental review pursuant to section 15378(b)(4) of the CEQA Guidelines.

Financial Considerations: Attachment 2 discusses the financial considerations relating to implementation of alternative funding sources for CIP costs funded by the Drainage Fund 425.

Emerging Small Business Development (ESBD): None, as no goods or services are being purchased.

Respectfully Submitted by: _____
David L. Brent
Engineering Manager

Approved by: _____
for Gary A. Reents
Director

Recommendation Approved:

_____
Ray Kerridge
City Manager

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Attachment 1

BACKGROUND

Over the past 15 years, since the Department of Utilities (DOU) was formed, there has been a tremendous effort on the part of DOU to identify critical projects and to have them constructed in an ongoing effort to meet the level of service goals approved by City Council as part of the 1995 "Utility Infrastructure Report" (revised and presented to Council January, 2006): "to prevent street flooding higher than the top of the curb during 10-year return storms (storms having a 1-in-10 chance of occurring in any given year) and to prevent flooding of structures during 100-year return storms (storms having a 1-in-100 chance of occurring in any given year) at complete build-out in each drainage basin".

There are 128 drainage basins throughout the City, over 100 drainage pump stations in a variety of conditions, with miles of streams, canals and pipe and thousands of drain inlets. Many of the pump stations, pipes and inlets were designed to outdated standards and are too small to convey the runoff during even moderately intense storms.

To bring all drainage areas of the City up to the level of service adopted by the City Council, DOU has engaged in a multi-year master planning program and has developed master plans and computer models for 43 of the most critical (i.e. underserved) drainage basins. These master plans emphasized the use of detention as a primary solution to flooding instead of digging-up and replacing pipes and enlarging pump stations because this generally tends to be a more cost effective approach.

In addition, the Department of Utilities has applied a power back-up policy for pump stations. The storms of 1995, which included heavy rainfall combined with high winds, resulted in 5 pump stations losing power in the Valley Hi area causing area-wide flooding and property damage. The current policy was developed as a result of that experience and stipulates that all pump stations will have a means of providing backup power supply to operate at design rating. This policy was included in the 1995 "Utility Infrastructure Report."

One aspect of pump stations most vulnerable to age is their electrical systems and switch gear necessary to run the station. These components may have an economic life span of about 25 years and, yet, most of our pump stations are far older than that.

The following rehabilitation/replacement projects and improvement projects, valued at over $61M, have been completed in the last ten years:

Rehabilitation and Replacement Projects:

- Fourteen (14) pump stations have been significantly rehabilitated or entirely reconstructed.

- Thirty-six (36) antiquated pump station electrical systems have been replaced, eighteen (18) pump stations have been provided with onsite backup power facilities, eighteen (18) portable generator units have been added to our fleet and all remaining pump stations have been equipped with quick hook-up capability.

Improvement Projects:

- There were nine detention basins existing prior to 1995. Since then, 34 additional detention basins have been constructed: 18 were funded by developers and 16 by the City. There are two detention basins under construction and 7 more currently being designed.
- Sixty-two smaller improvement projects have been completed most, involving the up-sizing of pipes and replacement and upgrade of drain inlets.

Future Projects

The Utilities Department is engaged in developing an asset management program which includes the assessment of existing assets and their rehabilitation requirements and prioritizing these in conjunction with master plan-identified improvements in accordance with Council approved standards and sound business practices.

As part of the asset management program, all drainage pump stations have been inspected and analyzed by operators and maintenance personnel as to the age and condition of the equipment and structure and have received a "condition assessment." Drainage channels have been likewise inspected and assessed. Furthermore, the adequacy of existing pipes, pump stations and other infrastructure in the most critical drainage basins has been determined by hydraulic/mathematical models and alternative improvements have been identified.

Based on these condition assessments and criticality analysis staff estimates that over the next twenty years about $40 Million in rehabilitation and/or replacement will be required to maintain existing service levels. The greatest need in drainage is to repair and rehabilitate aging pump stations. Simply put, if the pump station fails, the whole drainage basin will flood, no matter how good the rest of the infrastructure is.

Improvements have been divided into the following five categories in descending order of priority:

- The project eliminates an existing public safety hazard caused by the 100 year storm
- The project eliminates existing 100 year property flooding
- The project eliminates existing 10 year street flooding
- The project advances development (eliminates future flood hazard only)
- The project improves storm water quality only

The total of identified future improvement projects throughout the City is valued at approximately $1billion. These prioritized projects will allow the development of a long term capital improvement program with the goal of bringing the entire City up to the City Council approved level of service for drainage.

Funding Decline

Prior to the passage of Proposition 218, which mandates voter approval to increase the rates charged for storm drain service, the funds allotted for drainage CIPs was about $8M per year. Due to inflation, the use of drainage funds to comply with mandated regulatory requirements, and the absence of rate increases for the past 10 years, the amount available for drainage CIPs has steadily declined and has been reduced from $8 million to less than $2 million per year in FY06/07.

Due to this steady decline in available funding, the Department of Utilities has limited the focus of the CIP program the past 2 years to highest priority rehabilitation/replacement projects except for a few improvement projects that were previously approved by City Council, and no further improvement projects are being recommended by the Department of Utilities. Within the next 3 to 4 years, with no changes in the current funding sources or policies, we project that there will be no funds available, even for necessary rehabilitation/replacement drainage CIPs or to fund the drainage component of combined sewer system CIPs. Soon after, there will begin to be impacts to our ability to operate and maintain the existing infrastructure.

Attachment 2

Alternative Funding Sources
At the January 24, 2006 staff presentation to Council on drainage infrastructure, Council requested that DOU investigate and report back on various funding alternatives that could be considered to stabilize the drainage fund and increase spending on drainage system rehabilitation and improvements.

The first three alternatives; a regulatory fee, a drainage impact fee and rate increases in conformance with Proposition 218 have been investigated by staff in some detail and staff is requesting City Council to take action on each.

The remaining alternatives are presented for City Council consideration but no further action is being recommended at this time.

Regulatory Fee
State and Federal government-mandated regulatory costs have been increasing at an accelerated rate over the past ten years. These costs, which have been funded exclusively from the Drainage Fund, include costs incurred by the City to comply with regulatory requirements imposed under the federal Clean Water Act and California's Porter Cologne Water Quality Control Act, the Americans with Disabilities Act, and the National Flood Insurance Program administered by FEMA.

Currently, complying with these regulatory requirements costs the Drainage Fund about $2 million per year. Establishing a separate regulatory fee to pay these regulatory costs would allow this portion of the Drainage Fund to be used for its intended purpose; to fund operation and maintenance of the drainage system and critical drainage CIPs, rather than funding mandated regulatory costs.

More details regarding this proposed regulatory fee approach will be presented by staff in a Power Point presentation at the time this report is presented to Council (copy attached). If Council supports this regulatory fee proposal, staff proposes to develop the necessary fee study, conduct outreach and prepare a regulatory fee ordinance and fee resolution to be brought back to the Law and Legislation Committee and Council later this fiscal year.

Drainage Development Impact Fee
Establishing a drainage development fee would require developers to pay a fee representing their fair share of capital costs incurred for new and/or upgraded drainage facilities that serve their development. Other local agencies in the region such as the County of Sacramento charge a Drainage Development Fee for all new development on a per acre or per lot basis. The agencies use a pro-active approach to identify future requirements, to design and construct common drainage facilities to facilitate development in outlying areas in an organized fashion and for in-fill. The funds collected provide the means for master planning and for design and construction of capital improvement projects to allow development.

The County is divided into three geographical regions for impact fees based on the receiving waters: areas that drain to the American River, areas that drain to Linda Creek, and areas that drain to Laguna/Morrison Creek. Fees also vary by type of development which affects the amount of runoff. County drainage development fees average around $14K per acre.

The City's longtime policy has been to require developers to "pay as they go" in providing common drainage facilities. This generally is accomplished by hiring private consultants to plan and design the common drainage facilities in accordance with City standards. This makes it necessary for groups of developers to combine their efforts and resources to develop in outlying areas and sometimes they use public funding mechanisms such as Mello Roos bonds to finance expensive infrastructure, including common drainage facilities. This "pay as you go" policy has provided an effective means of constructing common drainage facilities to serve new development in outlying areas, such as North Natomas.

In infill areas, where only a few landowners are involved and where common drainage facilities may be more costly, the "pay as you go" policy has not been as effective and sometimes development in these areas has languished.

Our recommendation is not to replace the "pay as you go" policy for new development in outlying areas, but to provide a drainage development fee option as a tool for developing infill areas. The program could include credits for construction of common drainage facilities and could provide for interim drainage solutions to allow development prior to the construction of core infrastructure.

The master planning to identify critical infrastructure, necessary improvements and common drainage facilities for most of the infill areas within the City has already been completed as the first step towards such a policy. As an example, DOU has completed preliminary calculations in Basins 157 and 144 in Council District 3, where there is interest in the development of infill areas and where master plans have been completed to determine the requirement for new infrastructure necessary to allow development. Our preliminary estimate is that the required drainage development fees would be in the range of $16.5K to $20K per acre depending on the type of development in this area.

Rate Increases in Conformance with Proposition 218

Proposition 218 mandates voter approval of an increase in the rate charged for storm drain service, unlike rates for sewer, water and refuse collection services, which Proposition 218 exempts from the voter approval requirement. Since passage of Proposition 218 , due, in part, to the perception that a majority of voters would not be likely to approve an increase in their storm drain service rates no rate increases have been proposed. However, due to increased public awareness of the need for adequate well-maintained drainage facilities occasioned by Hurricane Katrina, the flooding and threat of flooding that occurred in early 2006 and the publicity surrounding the vulnerability of the Central Valley's levee systems, the likelihood of obtaining an affirmative vote to raise rates has probably increased.

Our rough preliminary estimate of the cost to develop a proposed rate increase and

present it for voter consideration is upwards of $ 1 million; this cost would need to be refined and considered as a factor in determining whether to pursue voter approval of a rate increase. If voter approval of a rate increase is pursued, staff believes that the measure presented to voters should include provisions for an automatic annual adjustment of the fee amount that is tied to the rate of inflation. If SAFCA moves forward with a new assessment for flood control projects, linking the City's drainage rate increase as a companion measure should be considered.

Bond Financing

Another option for funding rehabilitation and upgrades to the drainage system is through bond financing. This report does not explore bond financing in great detail because bonds provide only a temporary funding solution that will likely result in future rate increases. If bonds were sold, the drainage fund would be obligated to pay back these funds over time.

Two different types of bonds would likely be considered: revenue bonds and asset bonds. Revenue bonds would be underwritten by the Drainage Fund revenue stream, which, due to Proposition 218, has not had a rate increase for 10-years and is sorely stressed by inflation, increased labor costs, etc. Asset bonds, which were used to finance our water treatment plant expansion projects, are based on the value of the Drainage Fund assets. While their value is substantial and would probably support a significant bond, a healthy revenue stream is also needed to make the required payments. The condition of the Drainage Fund revenue stream makes both of these alternative bonds an unlikely source of funding.

Assessment Districts

Historically, many of the improvements to underserved areas were funded by assessment districts: providing new streets, curbs, gutters and sidewalks, street lighting, water, sewer, and drainage infrastructure, usually in unincorporated areas which had annexed to the City.

These public funding instruments include 1913 or 1915 bonds. Both require that the majority of property owners, based on the area of property owned, must vote in favor of the bond. Bond debt is paid by individual property owners, proportional to the benefit received, over a 15 year period.

In case a drainage assessment district is approved, DOU would design and construct the facilities and Special Districts would administer the funding.

General Fund Support

Another option for funding improvements is to provide support from the General Fund. If drainage rates only support maintaining and repairing the existing drainage system, the General Fund could be considered for funding improvements to the drainage system such as installing larger pipes, building larger pump stations, and detention basins, which will prevent flooding and increase property value.

Tax

A tax could be considered to fund certain drainage improvements, without which streets

may be flooded and property damaged. This alternative would require voter approval.

Supporting State Legislation to Modify Proposition 218

The inability to raise rates for storm drain service without voter approval, even to simply keep up with inflation, has affected many local agencies throughout the State of California. A current Assembly bill, ACA13, introduced by Assembly Members Harman, Jones and Mullin and supported by the League of California Cities, would call for a vote on a constitutional amendment to alter Proposition 218 so that rates for flood control and storm drainage could be raised without voter approval, the same as rates for water, sewer and refuse collection services. Raising storm drainage rates would continue to be subject to Proposition 218's notice and protest provisions that also apply to water, sewer and refuse collection rates.

There is talk, at the state level, about altering the bill so that it only affects rates collected to fund levee repairs. However, this emphasis ignores the essential need to keep internal drainage systems in good repair or improve them to prevent flooding.

In support of ACA 13 or similar legislation we recommend the following: 1) Work with the League of California Cities and survey local agencies throughout the state to obtain a consensus on the need to amend Proposition 218's language to exclude local drainage rates from the voter approval requirement, and thereby provide for state wide efforts to that end; and 2) direct the city's lobbyist(s) to communicate to the drafters of the bill the critical need to keep the local drainage fee aspect as part of the bill. We believe that it is critical to include local drainage rates in any Proposition 218 reform, or it will be tremendously difficult to get another, separate effort to do it later.

RESOLUTION NO.

Adopted by the Sacramento City Council

ALTERNATIVE FUNDING SOURCES FOR CAPITAL IMPROVEMENT PROGRAM (CIP) COSTS FUNDED BY THE STORMWATER (DRAINAGE) FUND 425

BACKGROUND

A. Over $61 Million in rehabilitation and improvements has been expended over the past ten years to attempt to reach the level of service for flood protection approved by City Council in 1995. Additional improvements are required, prioritized using the infrastructure rehabilitation and management program, estimated to cost over $1 Billion.

B. Since the passage of Proposition 218 funds for this purpose have continually declined. Consequently, alternative funding sources are needed.

BASED ON THE FACTS SET FORTH IN THE BACKGROUND, THE CITY COUNCIL RESOLVES AS FOLLOWS:

Section 1. The Department of Utilities is directed to develop the necessary fee study, initiate an outreach program, and prepare a regulatory fee ordinance and fee resolution to be brought to the Law and Legislation Committee by January 2007.

Section 2. The Department of Utilities is directed to complete a study by January 2007 that may be used as the basis for subsequent approval of a drainage impact fee to finance construction of common drainage facilities in infill areas.

Section 3. The Department of Utilities is directed to (1) develop an estimate of the cost to put a storm drain rate increase measure for voter approval in accordance with Proposition 218, (2) determine whether such a vote could be included on the same ballot as a SAFCA assessment vote, (3) prepare multi-year rate increase proposals and, (4) report back to Council when this is completed.

Section 4. The Department of Utilities is directed to work with the League of California Cities to obtain a consensus on the need to amend Proposition 218's language to exclude local drainage rates from the voter approval requirement, and the City's lobbyist(s) are directed to communicate to the drafters of ACA13 the critical need to keep the local drainage fees as part of the bill.

Storm Drainage Funding Alternatives

Presented to City Council
August 29, 2006

Presentation Overview

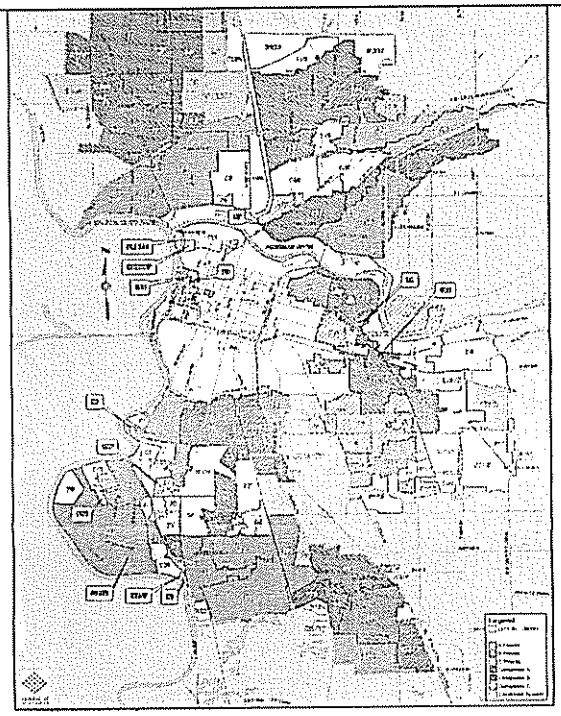
- Levels of Service
- CIP Backlog
- Drainage Fund Trends
- Funding Alternatives

Levels of Service

- Water level below finished floor for 100 year storm
- Water level at top of curb for 10 year storm

Drainage Rates

- Provides funds for:
  - Drainage operating expenses
  - Maintenance of Drainage system and financial reserve
  - Necessary equipment purchase
  - Drainage Capital Improvement Projects (CIPs)

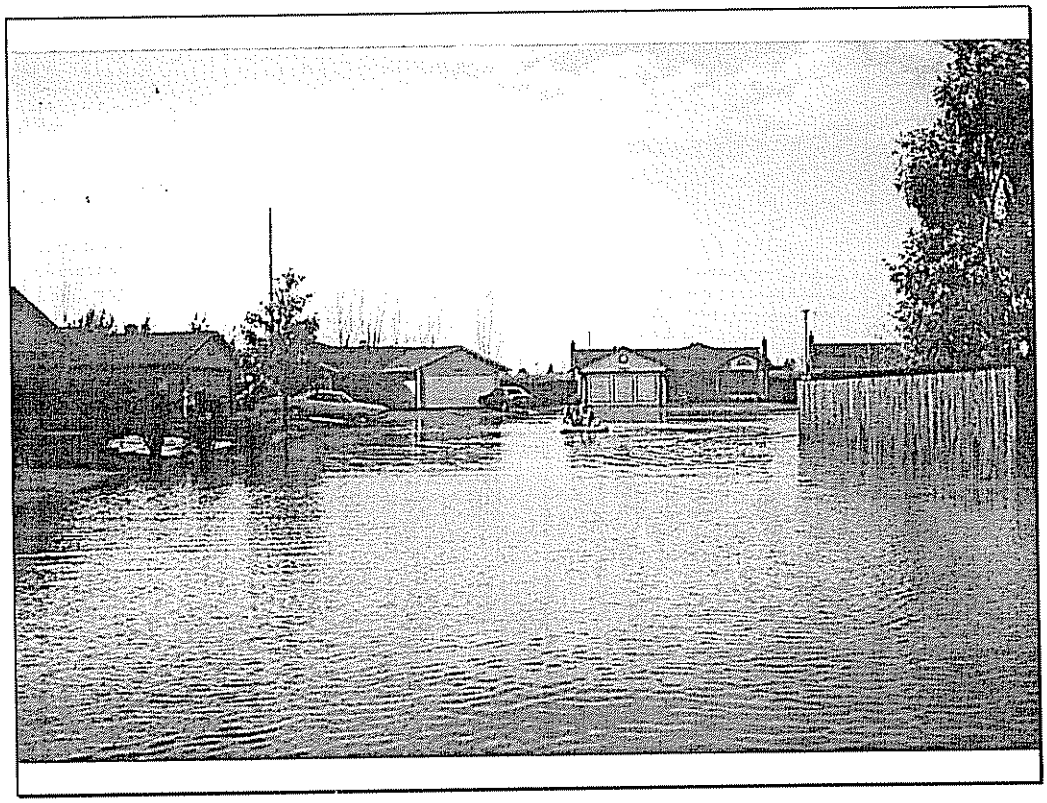


Benefits of Improvement CIPs

- Reduced street flooding
- Reduced property flooding
- Reduced maintenance cost
- Reduced response time
- Protection of critical facilities

Causes of Past Flooding

- Past flooding has occurred because of drainage system limitations
  - Undersized pipes, pumps
  - Lack of back-up power



Presently only limited rehab and replacement is being performed in an effort to maintain the existing level of service, but not improve it.

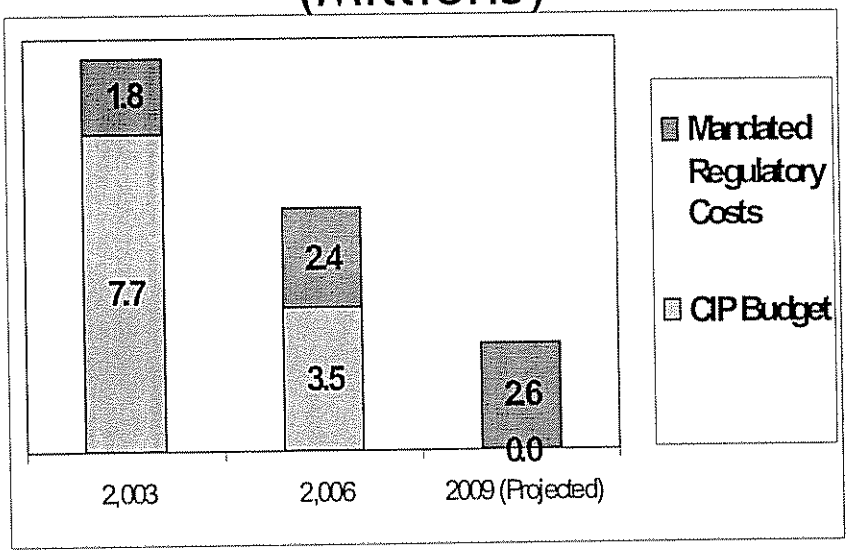
Drainage Improvement CIPs

- One billion dollars in improvements gets you:
  - Water level below finished floor for 100 year storm
  - Water level at top of curb for 10 year storm

425 Drainage Fund Model

Source	2006-07 Budget	2007-08 Estimate	2008-09 Estimate	2009-10 Estimate	2010-11 Estimate
Projected Rate Increase					
BEGINNING BALANCE	**12,517**	**8,060**	**6,324**	**4,610**	**3,569**
REVENUE					
User Fees	31,558	33,189	32,833	33,498	34,159
Interest	631	644	657	670	342
Other	788	794	802	811	818
Development Fees	0	0	0	0	0
Total Revenues	**32,977**	**34,627**	**34,292**	**34,979**	**35,319**
EXPENDITURES					
Operating	28,808	29,985	31,360	32,374	33,304
Debt Service	3,398	3,548	3,592	2,592	3,592
CIP	5,228	2,830	1,054	1,054	1,000
Total Expenditures	**37,434**	**36,363**	**36,006**	**36,020**	**37,896**
ENDING BALANCE	**8,060**	**6,324**	**4,610**	**3,569**	**992**

Utilities Drainage Fund Trends (Millions)



Regulatory Costs (2006)

Stormwater Quality Improvement Program	$1,750,000
National Flood Ins Program	$405,000
Americans with Disabilities Act	$250,000

Recommended Funding Alternatives

- Regulatory Fee
- Drainage Impact Fee
- Prop 218 Election for Multi-year Rate Increase