



## Council Agenda Report

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Item 7a

**Department:** Utilities  
**Cost Center:** Water and Sewer Funds  
**For Agenda of:** 4/29/2025  
**Placement:** Business  
**Estimated Time:** 45 minutes

**FROM:** Aaron Floyd, Utilities Director  
**Prepared By:** Julie Ridgeway, Utilities Business Manager

**SUBJECT:** INTRODUCTION OF THE 2025-27 WATER AND SEWER RATES AND  
AUTHORIZATION TO RELEASE THE ASSOCIATED PROPOSITION 218  
NOTICE

### RECOMMENDATION

1. Direct the publication and mailing of a notice consistent with Article XIII D of the California Constitution and the Proposition 218 Omnibus Implementation Act (Prop 218) as it relates to water and sewer rates; and
2. Set two Public Hearing dates on June 17, 2025, to consider the adoption of updated water and sewer rates if there is no majority protest in accordance with Prop 218.

### REPORT-IN-BRIEF

The City is proposing water and sewer rate increases consistent with the requirements of California Constitution Article XIII C and D, commonly referred to as Proposition 218 ("Prop 218"), the City's Charter and Municipal Code, and City Financial Plan fiscal policies. Rates provide funding to the City's Water Fund and Sewer Fund, for the operation, maintenance, and capital project needs commensurate with the costs to provide adequate water and sewer services to the community. In order to meet projected revenue requirements for operations, maintenance, and capital needs, water rates are proposed to increase 5.5 percent on July 1, 2025, and July 1, 2026, and sewer rates are proposed to increase 6.5 percent on July 1, 2025, and July 1, 2026.

This report is the first of a series of two council items scheduled for April 29, 2025, and June 17, 2025. This item, for the Council meeting scheduled on April 29, 2025, requests Council authorize the release of a public notice (Prop 218 notice) informing property owners and account holders of proposed increases for the City's water and sewer rates and requests that Council authorize staff to set two public hearings for the potential increases on June 17, 2025. This report also provides the constitutional, regulatory, and policy basis for the proposed rates, identifies the rate setting methodology and proposed rates, and summarizes the public outreach that will be conducted to ensure customers are provided timely and comprehensive information regarding the proposed increases and opportunities to engage with staff and submit comments, questions, and written protests.

## POLICY CONTEXT

The City's Water and Sewer Funds utilize rates and fees to fund operating, capital, and debt service expenditures to operate and maintain the City's water and wastewater (sanitary sewer) systems. These funds are treated as enterprise funds, which means they must operate fully on their own and are not subsidized by the City's General Fund. Rates and fees collected from customers make up the primary funding source for both funds and must be developed in compliance with Prop 218.

When proposing increased rates, some of the key Prop 218 requirements include:

1. A noticed public hearing must be held on the proposed rate increases at least 45 days after mailing a written notice to the parcel owner and account holder of record of each parcel subject to the proposed rates.
2. The cost of service shall not exceed the proportional cost of services provided to the corresponding parcel.
3. Revenues generated by the rates must be used solely for the services for which the rates are imposed.
4. Written protests must be submitted by the parcel owner of record or account holder of record that is directly responsible for payment of the utility bill, and must include a signature and identification of the parcel (e.g. service address). Only one protest per parcel is counted and protests must be received before the close of the public hearing to be valid.
5. The proposed rates cannot be adopted if a majority of affected property owners or account holders submit written valid protests opposing the rates before the close of the public hearing.

In addition to Prop 218 requirements, the City aims to set rates that promote the stability and predictability of water and sewer services. No changes to the current *rate structure*, which defines how customers are charged for water and sewer services (i.e. fixed fees and variable charges), are being proposed and the proposed rates are consistent with rate structure prioritization goals previously established by the City Council ([August 15, 2017](#); [January 9, 2018](#)). These prioritized goals include revenue stability and predictability, stability and predictability of the rates, fair allocation of total cost of service among customer classes, and reflection of all present and future costs. The proposed rates are also consistent with policies identified under [Section 3. Enterprise Fund Fees and Rates](#) of the City's Financial Plan, which states that:

*"The City will set fees and rates at levels which fully cover the total direct and indirect costs including operations, capital overlay, and debt service" and "the rate setting process will be in accordance with Proposition 218 and its notification requirements."*

In addition to these policies, the fiscal evaluation includes identification of community needs for essential services (provision of drinking water and treatment of wastewater) and integration of climate risk, climate action, and customer assistance considerations throughout all financial decisions including identification and implementation of resilient

capital projects that equitably provide water and sewer service to the community, consistent with Financial Plan Objectives.

### **AB 2257**

AB 2257 requires ratepayers to raise specific legal objections during the public process before pursuing litigation, establishing a statutory prerequisite to a legal challenge. The process for presenting legal objections and the City's requirement to respond to such comments is similar to the public review process in CEQA. Legal objections are separate from rate protests. If the City complies with the requirements of AB 2257 a potential litigant may only bring litigation if they have submitted a timely written objection. AB 2257 also limits litigation to the administrative records of the proceedings.

Property Owners of record and tenants directly liable to the City for payment of water and/or sewer rates may file legal objections with the City. To be valid, legal objections must be in writing and include the filing parties name, address, signature, and the legal basis for their objection. The legal objection must include sufficient detail to allow the City to substantively respond to the objection. For example, stating that the proposed rates are too high or illegal without further explanation will be deemed insufficient.

Legal objections must be submitted no later than June 16, 2025 to the City Clerk's office. **Failure to submit a valid legal objection bars any right to file a legal challenge to the proposed water and sewage rates.** Legal objections sent electronically will not be accepted.

Any valid legal objections received will be answered in writing. All objections and responses shall be presented to the Council for consideration prior to the hearing. This new legislation formalizes a requirement for potential litigants to exhaust administrative remedies prior to suing the City and establishes the notice and process pre-requisites for both potential litigants and the City.

## **DISCUSSION**

### **Background**

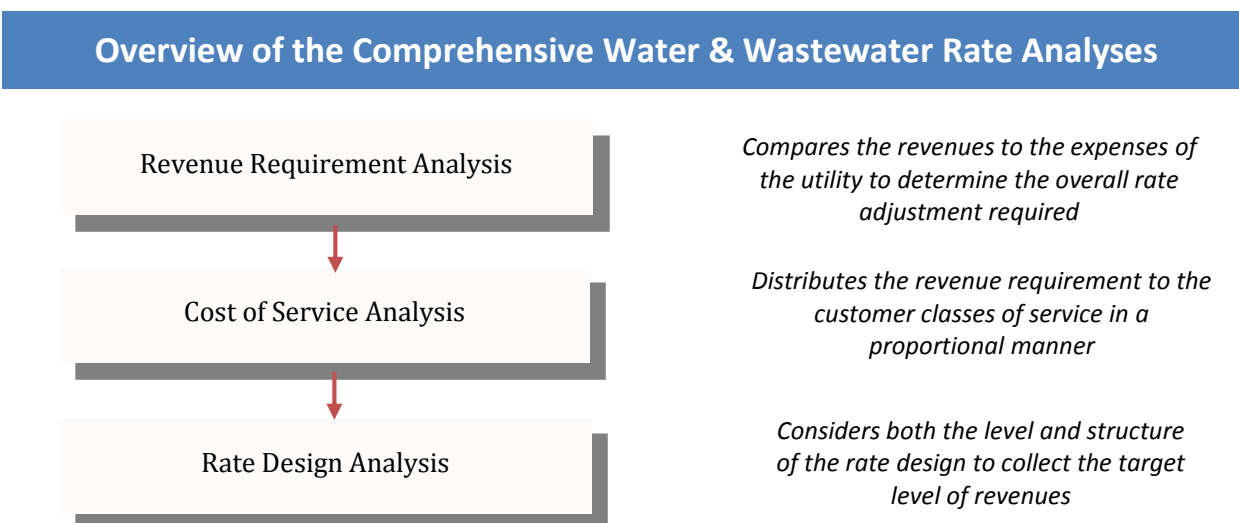
As stated above, the City's Water and Sewer Enterprise Funds are primarily funded through rate revenues paid for by customers of the City's water and wastewater systems. Enterprise funds utilize rates and fees paid for services rendered to fund all operating, capital, and debt service expenditures. Water rates pay for all costs associated with bringing water from surface water reservoirs to the City's water treatment plant and distributing 1.7 billion gallons of drinking water annually to approximately 17,000 service connections. Sewer rates support the activities needed to collect and treat approximately 1.4 billion gallons of wastewater through the City's wastewater collection and treatment facility annually.

### Rate Setting Methodology

The goal of the rate-setting process is to provide suitable funding to the City's Water and Sewer Funds for operation, maintenance, and capital project needs for the City's water and wastewater systems. Rates must be developed that are stable, equitable, and cost-based in compliance with Prop 218.

The City hired HDR Engineering, Inc. (HDR) to assist with reviewing and updating the 2025-27 water and sewer rates and preparing a report of the updated water and wastewater rate study (2025 Rate Study Update; Attachment A). For the *2025 Rate Study Update*, HDR utilized industry-standard methods consistent with the *M1 Manual: Principles of Water Rates, Fees, and Charges* published by the American Water Works Association (AWWA) for setting water rates and the *Manual of Practice No. 27* published by the Water Environment Federation (WEF) for setting sewer rates. The *2025 Rate Study* provides the necessary documentation for the City's proposed water and sewer rates in compliance with Prop 218 Section 6, which regulates property-related fees and charges to which water and sewer rates are bound.

The methodology used for both water and sewer rates includes a revenue requirement analysis, a cost-of-service analysis, and rate design analysis, as outlined in the graphic below (Figure 1). This methodology is consistent with Financial Plan Enterprise Fund Fees and Rates policies for ongoing rate review and cost of service fee assessment. The policies state that the City will review and adjust enterprise fees and rate structures as required to ensure that they remain appropriate and equitable and that the City will treat the water and sewer funds in the same manner as if they were privately owned and operated. This means assessing reasonable cost of service fees while fully recovering service costs.



**Figure 1.** Overview of the three interrelated analyses conducted during a water and/or sewer rate analysis (source: *2025 Rate Study Update*, HDR Engineering, Inc.).

In 2023, the City hired HDR to conduct a comprehensive water and wastewater study, including a full cost of service analysis, to develop a 5-year projection through fiscal year (FY) 2026-27. However, the City's historical practice has been to adopt rates for a 2-year period and conduct an updated analysis with each new financial plan. Given this, the *2025 Rate Study Update* utilized the results of the cost of service analysis from 2023 as the basis for the proposed rates for FY 2025-26 and FY 2026-27. As a part of the 2025 updated analysis, HDR confirmed that the cost of service still reflects the current customer characteristics of the City's customer basis. Therefore, only revenues and expenses, both operating and capital, of the water and wastewater utilities were updated to match the updated customer characteristics and costs of providing water and wastewater services to the City's customers. Rate designs based on a cost-of-service methodology that fairly apportions costs to all customers is in accordance with the provisions of Prop 218. No changes were made to the current rate structure at this time.

This rate setting methodology is consistent with the rate structure goals established by Council, the City Charter, and the San Luis Obispo Municipal Code (SLMC). Specifically, water and sewer rates must be adopted by Council resolution (SLMC [Section 13.04.090](#)), and all revenue generated from these rates is legally restricted to funding the operation, maintenance, improvement, and debt obligations of the respective utility system (SLMC [Section 13.08.410](#); City Charter [Section 806](#)).

### **Study Findings**

As a part of the *2025 Rate Study Update*, and in keeping with the best practices for capital project funding approach, a concerted effort was made to increase the overall level of "pay-as-you-go" (rate) funding and to avoid debt financing to the extent practical. Based on the results of the *2025 Rate Study Update*, HDR concluded that the City will need to adjust the level of water and wastewater rate revenues for the next two financial years (FY 2025-26 and FY 2026-27) in order to meet revenue requirements. These results are summarized below and more detailed information can be found in the full *2025 Rate Study Update* report.

### **Water Rates**

Based on the results of the *2025 Rate Study Update*, water rate revenues are recommended to be adjusted to increase 5.5% in each of the two-year rate setting periods of FY 2025-26 and FY 2026-27. This takes into account updated revenue projections, including projected changes in the number of customer accounts served and water consumption, operation and maintenance costs, including anticipated ongoing costs to operate the City's future groundwater system, and the City's updated capital improvement plan (CIP), including projects that continue to address impacts from the 2023 storms. The rate analysis incorporates anticipated FEMA reimbursement for eligible portions of storm-related projects to avoid overcollection through rates. If reimbursement is not received, adjustments would need to be made to the City's water related CIP and in the next rate analysis to reflect actual funding.

To address nationwide cost increases and to maintain the current CIP, which both drive water rate increases, the Department has been focusing on an approach to supplement ratepayer funds through the utilization of grant funding and by exploring short-term non-potable water sales opportunities. Since 2020, the Utilities Department has received over \$2.1 million in grant funding for the Water Fund, which has been utilized for projects that improve resiliency for the community while also decreasing long-term operating costs. The Water Treatment Plant Tesla Battery Pack Project and the Groundwater Contamination Remediation Project are both grant-funded and provide long-term operational cost decreases by reducing electricity usage and allowing for electricity to be utilized during off-peak periods for treatment operations. The Department has also applied for and are waiting to hear back about grant funding to help supplement the City's transition to Advanced Metering Infrastructure (AMI), which will reduce operational costs and improve customer experiences by allowing for increased consumption monitoring and leak detection. These projects, amongst others, focus on utilizing grant opportunities to stabilize or decrease costs that otherwise would drive additional annual rate increases.

In addition to pursuing grant opportunities and increasing operational efficiencies, the City has also been exploring opportunities to sell surplus water supplies that the City is unable to use each year pursuant to policy 1.13.2 of the Land Use Element of the City's General Plan. Surplus water sales programs include the potential to sell short-term non-potable surplus recycled water and surplus water from Nacimiento Reservoir. These water sales programs could result in additional revenue for the Water Fund, without compromising long-term water supply sustainability. However, because surplus water sales have not been negotiated and significant additional work is required to finalize any such agreements, the rate study analysis did not include any projected revenue from potential sales.

Overall, the Water Fund's projected rates are slightly lower than those that were previously projected in the 2023 rate study for FY 2025-26 and are slightly higher in FY 2026-27 and projected future years, as shown in Table 1 below. Since the 2023 study, updated expense and revenue data have resulted in a refinement of the now proposed and projected rate increases. The increases in the proposed water rate adjustments for FY 26 through FY 33 are due primarily to increased costs for capital improvement projects, the addition of new projects as a result of the 2023 storms, increased regulatory compliance costs, inflation, and increased costs of doing business. While there have been changes to the proposed rates since the 2023 rate study, proposed rate increases are more similar to those projected in the previous study than the Utilities Department has seen when there have been significant factors that need to be incorporated, such as those coming out of the 2019 COVID pandemic and/or drought years. This consistency indicates that the City's long-term financial planning approach is working as intended, providing a stable foundation that can absorb moderate cost fluctuations without requiring sharp or unexpected rate adjustments. It also reflects that, while some factors such as the 2023 storms and cost increases have added new cost pressures, the overall financial outlook for the Water Fund remains aligned with prior expectations, supporting the reliability of the City's water system.

**Table 1.** A comparison of proposed and projected water rate percentage increases identified in the 2023 Comprehensive Rates Study compared to the 2025 Rate Study Update.

Water Rate Increases (%)	Proposed		Projected					
	FY 26	FY 27	FY 28	FY 29	FY 30	FY 31	FY 32	FY 33
<b>Previous Rate Study (2023)</b>	7.5	4.5	4.5	4.0	4.0	4.0	3.5	3.0
<b>Current Rate Study Update (2025)</b>	5.5	5.5	5.0	5.0	5.0	5.0	4.5	4.5
<b>Difference</b>	(2.0)	1.0	0.5	1.0	1.0	1.0	1.0	1.5

If the recommended 5.5% increase is implemented for each of the next two fiscal years, the City's proposed water rates for 2025-27 would be as shown in Table 2, below.

**Table 2.** Current and proposed water rates for FY 2025-26 and 2026-27.

Summary of the Present and Proposed Water Rates			
Present Rates		Proposed Rates	
Effective 7/1/24		Effective 7/1/25	Effective 7/1/26
<b>Proposed Rate Revenue Adjustment</b>		<b>5.5%</b>	<b>5.5%</b>
<b>Fixed Charge - \$/Month</b>			
<b>Residential</b>	\$30.25	\$31.91	\$33.67
<b>MF / Non-Res / Irr</b>			
3/4" & Less	\$30.25	\$31.91	\$33.67
1"	50.50	53.28	56.21
1 1/2"	100.80	106.34	112.19
2"	161.30	170.17	179.53
3"	302.60	319.24	336.80
4"	504.45	532.19	561.46
6"	1,008.60	1,064.07	1,122.59
8"	1,613.85	1,702.61	1,796.25
Water System Access Charge <sup>1</sup>	\$108.50	\$114.47	\$120.76
<b>Usage Charge – \$/Unit<sup>2</sup></b>			
<b>Residential</b>			
0 – 5 CCF	\$8.54	\$9.01	\$9.51
6 – 12 CCF	9.84	10.38	10.95
12 + CCF	16.97	17.90	18.88
<b>Multi-Family</b>	\$9.58	\$10.11	\$10.67
<b>Non-Residential</b>	\$10.14	\$10.70	\$11.29
<b>Irrigation</b>	\$10.35	\$10.92	\$11.52

<sup>1</sup>One unit of water = 100 cubic feet = 748 gallons

<sup>2</sup>Water System Access Charge applies where the City provides only fire protection to accounts that utilize a private well for domestic purposes.

**Sewer Rates**

Based on the results of the *2025 Update*, sewer rate revenues are recommended to be adjusted to increase 6.5% in each of the two-year rate setting period of FY 2025-26 and FY 2026-27. This is moderately higher than what was previously projected for upcoming years as is summarized below (Table 3). Primary changes between the last analysis and this analysis include additional funding for operating the City's new Water Resource Recovery Facility (WRRF), changes of which are primarily regulatory driven, and an expected loss in revenue associated with California Polytechnic State University (Cal Poly) building an on-campus wastewater treatment system.

The loss in revenue from Cal Poly is based on projected flows provided by the University, which drop off significantly starting in FY 2025-26, when the University begins treating a portion of its own wastewater, and then steadily increase as on campus student population projections increase. During FY 2025-26, flows to the City are expected to decrease by approximately 75%, resulting in a projected revenue loss of \$935,268, when compared to what was collected during FY 2023-24. By FY 2026-27 flows, are projected to be 29% of those sent to the City during FY 2023-24, resulting in a projected revenue reduction of \$920,578. The projected reduction in sewer revenue from Cal Poly accounts for approximately 48% of the additional rate revenue that would be generated from the proposed rate increase for FY 2025–26 and 21% of the additional rate revenue that would be generated from the proposed rate increase for FY 2026–27. This relative impact continues to decrease in future years, as the City's overall revenue requirements grow at a faster rate than the revenue loss from Cal Poly. In other words, while the Cal Poly revenue decline is a significant near-term driver of rate adjustments, its proportional influence diminishes over time as other cost drivers, such as capital funding needs and inflation, become more prominent.

As with the Water Fund, staff aim to minimize ongoing expenses and help to offset inflationary increases by pursuing grants, improving operational efficiencies, and exploring infrastructure replacement alternatives within the City's Sewer Fund. Over the past five years, the Sewer Fund has received \$2.6 million in grants to fund capital projects that would have otherwise relied on ratepayer contributions. Capital planning projects, such as the Wastewater Collection System Infrastructure Renewal Strategy, a long-range plan for the City's wastewater collection system, allow staff to be strategic and proactive in infrastructure maintenance and replacement planning. Additionally, staff have applied for Inflation Reduction Act funding associated with work completed during the WRRF upgrade. Although this cannot be factored into the analysis now due to uncertainties in Federal funding, if received, this additional revenue could be used to offset funding that would otherwise be collected by rates or support additional needed projects. Lastly, once the new WRRF facilities stabilize following the completion of construction, staff will be able to evaluate opportunities to further optimize processes to reduce operational expenditures and maximize the utilization of onsite biogas to energy production.



**Table 3.** A comparison of proposed and projected sewer rate percentage increases between the 2023 Comprehensive Rates Study and 2025 Rate Study Update.

Sewer Rate Increases (%)	Proposed		Projected					
	FY 26	FY 27	FY 28	FY 29	FY 30	FY 31	FY 32	FY 33
<b>Previous Rate Study (2023)</b>	4.0	4.0	3.5	2.5	2.5	2.5	2.5	2.5
<b>Current Rate Study Update (2025)</b>	6.5	6.5	6.5	6.5	6.5	3.5	3.5	3.5
<b>Difference</b>	2.5	2.5	3.0	4.0	4.0	1.0	1.0	1.0

If the 6.5% increase is implemented for each of the next two fiscal years, the City's proposed sewer rates for 2025-27 would be as shown below in Table 4.

**Table 4.** Current and proposed sewer rates for FY 2025-26 and FY 2026-27.

Summary of the Present and Proposed Sewer Rates			
Present Rates		Proposed Rates	
Effective 7/1/24		Effective 7/1/25	Effective 7/1/26
<b>Proposed Rate Revenue Adjustment</b>		<b>6.5%</b>	<b>6.5%</b>
<b>Fixed Charge - \$/Month</b>			
<b>Residential</b>	\$24.52	\$26.11	\$27.81
<b>MF / Non-Res</b>			
3/4" & Less	\$24.52	\$26.11	\$27.81
1"	40.95	43.61	46.44
1 1/2"	81.65	86.96	92.61
2"	130.70	139.20	148.25
3"	245.21	261.15	278.12
4"	408.76	435.33	463.63
6"	817.28	870.40	926.98
8"	1,307.70	1,392.70	1,483.23
10"	1,880.02	2,002.22	2,132.36
<b>Usage Charge - \$/Unit<sup>1</sup></b>			
<b>Residential / Multi-Family (up to sewer cap)</b>	\$9.82	\$10.46	\$11.14
<b>Non-Residential (all usage)</b>	\$10.27	\$10.94	\$11.65

<sup>1</sup>One unit of water = 100 cubic feet = 748 gallons

Overall, the proposed adjustments for FY 2025-26 and FY 2026-27 for both water and sewer rates reflect a more stable and predictable financial planning environment, following years of uncertainty caused by droughts and the pandemic. While the updated rate study includes an increase in revenue needs due to increased costs and changes to revenue from Cal Poly, the overall revenue requirements remain relatively consistent with prior rate studies. The recommended rate increases are designed to maintain essential services, fund critical infrastructure projects, and reduce reliance on debt, while staff continue to pursue grants and operational efficiencies to help stabilize long-term costs.

### **Customer Assistance and Conservation**

Prop 218 prohibits water providers from imposing fees that exceed the proportional cost of service to a parcel and revenues generated from fees cannot exceed the cost of doing business nor can they be used for an unrelated purpose. Thus, the City is unable to use rate funds to provide low-income customer assistance programs. Given this constraint, the City uses late fees paid by utilities customers who do not make their payments on time, to fund its Customer Assistance Program (CAP). Of the 17,075 active utility accounts, approximately 180 accounts receive reduced rates. However, budgets have historically been underutilized for this program, so the Department plans to recommend that the City Council increase the discount that is offered through this program from 15 percent to 20 percent at the June 17, 2025 City Council meeting to continue to help low income customers with their utility bills. Customers experiencing challenges paying their utility bills also have the ability to set up payment plans.

In addition to discounted rates through the CAP, the City also offers a variety of water conservation measures that help all customers lower their water usage. The City's water conservation program offers complementary water conservation items, discounts on smart sprinkler controllers, high-efficiency toilets and urinals, water-efficient restaurant dipper wells, and assistance with conducting home and business water audits. As part of its ongoing efforts, the City's Water Resources section also monitors customer usage and alerts them to potential water leaks. Building on these efforts, the City is also now transitioning to AMI, which will allow customers the ability to monitor their own water use in real-time and receive automatic alerts for possible water leaks. According to the Alliance for Water Efficiency's [Smart Practices to Save Water](#) (March 2023), of 16 utilities utilizing AMI, the average reported savings was 7,600 gallons per account, with results varying based on system size, leak thresholds, communication methods, and notification types.

### **Previous Council or Advisory Body Action**

City Council last approved the now current water and sewer rates on [June 6, 2023](#):

- [Item 7a. Consideration of the 2023-25 Water Rates \(staff report and study\)](#)
- [Item 7b. Consideration of the 2023-25 Sewer Rates \(staff report and study\)](#)

### **Public Engagement**

The City is committed to helping the public understand the recommended water and sewer rates and their right to protest. If directed by Council, and in compliance with Prop 218 noticing requirements for the Public Hearing on June 17, 2025, a public notice (in English and available online in Spanish) will be mailed to every parcel owner and account holder (customer) on record currently receiving water and sewer services from the City of San Luis Obispo. These notices will be mailed at least 45-days prior to the Public Hearing date. The Prop 218 notice (Attachment B) includes the proposed rate increases, a summary of the purpose of the increase, a fee schedule, and instructions on how to protest the proposed increase. The notices also includes the recipients' official protest form. In addition to those that are mailed, notices are also posted to the City's website and extra copies will be made available at the City of San Luis Obispo Clerk's Office and at the public hearing on June 17, 2025.

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In addition to the Prop 218 notice, the public will also be notified of the proposed rate adjustments, protest process, and the City's Customer Assistance Program through the following:

- City e-notifications and social media posts;
- At a public informational session scheduled for Wednesday, June 4, 2025, from 5:30 – 7:00 pm at the Ludwick Community Center (864 Santa Rosa Street, San Luis Obispo, CA 93401);
- At the annual Public Works and Utilities Week farmers market event located in downtown San Luis Obispo on Thursday, May 22, 2025 from 6:00 – 9:00 pm;
- Through legal notices of the Public Hearing published in a local newspaper 45 days and 10 days before June 17, 2025, in accordance with Section 1002, Article X of the City's Charter.

Staff also presented to the Chamber of Commerce of April 10, 2025, to inform businesses of the proposed changes and answer questions. Staff have also reached out to the following organizations to see if there is an upcoming meeting staff can come and speak at or share information through their social media platforms:

- Central Coast Commission for Senior Citizens
- CAPSLO
- Latino Outreach Council
- Cal Poly Student Affairs
- Cuesta Student Success and Support Programs

A copy of the full *2025 Rate Study Update* will be made available on the City's website and Frequently Asked Questions (FAQs) and online calculators are available to assist customers' understanding of proposed rate changes are also available on the Department's website ([www.slocity.org/utilityrates](http://www.slocity.org/utilityrates)). Staff also prepared a summary sheet that includes key dates and frequently asked question (FAQs) (Attachment D). Lastly, staff will continue to respond to questions by phone and email on how customer's bills would be affected.

### **CONCURRENCE**

The City Attorney's Office has reviewed and approved the draft Prop 218 notice and the *2025 Rate Study Update*. The City Finance Department concurs with the proposed water and sewer rate increases and the City Clerk's office concurs with associated adherence to Prop 218 required procedures.

### **ENVIRONMENTAL REVIEW**

Modification of rates and charges by public agencies are exempt from the California Environmental Quality Act (CEQA) under Public Resources Code 21083 and 21080(b)(8) and California Code of Regulations Title 14 Section 15273 (Rates, Tolls, Fares, and Charges) because changes in rates and charges is for the purpose of:

- a) Meeting operating expenses;
- b) Purchasing or leasing supplies, equipment, or materials;
- c) Meeting financial reserve needs and requirements;
- d) Obtaining funds for capital projects necessary to maintain service within existing service areas; and
- e) Obtaining funds necessary to maintain such intra-city transfers as authorized by City Charter.

The change in fees is not intended to fund expansion of capital projects not otherwise evaluated under CEQA. Therefore, no environmental review is required for this item.

## FISCAL IMPACT

Budgeted: No

Budget Year: 2025-27

Funding Identified: Yes

## Fiscal Analysis - Water Fund

To meet the rate revenue requirement of the Water Fund detailed in the *2025 Rate Study Update*, the proposed water rates are projected to generate a total of \$1.4 million additional dollars during FY 2025-26. This includes both the 5.5 percent increase in rates as well as projected customer growth (0.8%). Combined with forecasted revenues from current rates and miscellaneous revenues, total revenues for the Water Fund during FY 2025-26 are anticipated to be \$30.3 million. The Water Fund's projected total revenue and revenue requirement for the following fiscal year, FY 2026-27, is \$32.1 million. This is summarized in Table 5. If approved, the proposed rate increase would be implemented on July 1 of each corresponding fiscal year.

**Table 5.** Water Fund forecasted revenues and revenue requirements for FY 2025-2026 and FY 2026-27 (in thousand dollars).

Comprehensive Water Rate Study (in thousands)	FY 2025-26 Forecast	FY 2026-27 Forecast
Rate Revenues Without Proposed Rate Increases	\$25,999	\$26,207
Additional Rate Revenue from Proposed Rate Adjustment (5.5%)	\$1,430	\$2,962
Miscellaneous/Other Revenues <sup>1</sup>	\$2,885	\$2,947
<b>Total Revenues With Proposed Rate Increases</b>	<b>\$30,314</b>	<b>\$32,116</b>
<b>Total Revenue Requirement</b>	<b>\$30,314</b>	<b>\$32,116</b>

<sup>1</sup>Miscellaneous/Other Revenues includes non-rate revenues such as interest earnings, set-up fees, revenue collected from Cal Poly, miscellaneous penalties (including late fees), credit collections, and development review fees.

### Fiscal Analysis - Sewer Fund

To meet the rate revenue requirement of the Sewer Fund detailed in the *2025 Rate Study Update*, the proposed increases in sewer rates are projected to generate an additional \$1.3 million dollars during FY 2025-26. This includes both the 6.5 percent increase in rates as well as projected customer growth (0.8%). The Sewer Fund's projected total revenue and revenue requirement for 2025-26 is \$21.7 million and the total revenue requirement for FY 2026-27 is \$23.3 million. This is further summarized in Table 6. If approved, the proposed rate increase would be implemented on July 1 of the corresponding fiscal year.

**Table 6.** Sewer Fund forecasted revenues and revenue requirements for FY 2025-2026 and FY 2026-27 (in thousand dollars).

<b>Comprehensive Sewer Rate Study (in thousands)</b>	<b>FY 2025-26 Forecast</b>	<b>FY 2026-27 Forecast</b>
Rate Revenues Without Proposed Rate Increases	\$19,294	\$19,448
Additional Rate Revenue from Proposed Rate Adjustment (5.5%)	\$1,254	\$2,610
Miscellaneous/Other Revenues <sup>1</sup>	\$1,216	\$1,256
<b>Total Rate Revenues With Proposed Rate Increases</b>	<b>\$21,764</b>	<b>\$23,314<sup>2</sup></b>
<b>Total Revenue Requirement</b>	<b>\$21,764</b>	<b>\$23,315</b>

<sup>1</sup>Miscellaneous/Other Revenues includes non-rate revenues such as interest earnings, industrial user charges, set-up fees, revenue collected from Cal Poly, miscellaneous penalties (including late fees), credit collections, and development review fees.

<sup>2</sup>Discrepancy between total rate revenue and total revenue requirement in FY 2026-27 is due to rounding. See the *Summary of the Revenue Requirement (Exhibit 1)* in Appendix B for more details.

### NEXT STEPS AND PROTEST PROCEDURES

If directed by City Council, staff will:

1. Set two Public Hearings (one for water and one for sewer) on June 17, 2025, for the proposed water and sewer rates.
2. Release the Prop 218 notice at least 45-days prior to the Public Hearing.

Under Prop 218, property owners and/or customers directly responsible for the payment of the fee subject to proposed rate increase(s) may submit a written protest against the proposed rate increases. If directed by council, the Prop 218 notice, which includes an official ballot form, will be mailed to the mailing address on file for each parcel owner and each utility bill account holder within the City. Protests must be received by the City Clerk at or before the close of the public input portion of the public hearing on June 17, 2025, and must identify whether water and/or sewer is being protested, contain the service address, and include the original signature of the parcel owner or account holder of record. In the event that there is more than one protest submitted for a parcel, only one valid protest will be counted for the parcel.

At the public hearing, Council will consider all objections or protests, and any person shall be permitted to present written or oral testimony. At the conclusion of the public hearing on June 17, 2025, the City Clerk will announce whether a majority protest exists and provide a summary of the protests received. If valid written protests are filed by a majority (50%+1), the proposed water and/or sewer rates may not be imposed. A majority of the City's 17,035 water accounts is 8,518 plus one and a majority of the City's 16,479 sewer accounts is 8,239 plus one. All protests will need to be validated regarding property ownership and duplicate addresses.

The resolutions for adoption of the proposed water and sewer rates and for updating the Customer Assistance Program will be provided at the Public Hearing meeting scheduled for June 17, 2025. If adopted, rates would be implemented July 1 of the corresponding fiscal years.

## ALTERNATIVES

1. ***Council could decide to delay authorization to release the Prop 218 notice and consider water and sewer rate adjustments at a later date.*** If Council directs staff to delay the release of the Prop 218 notice, the required 45-day noticing period would push the rate hearing and adoption beyond the originally planned timeline. This would likely result in any new rates taking effect after the start of the fiscal year (July 1, 2025). Since the proposed rates are based on the assumption that they would be in effect for the full fiscal year, a delay in implementation would reduce projected revenues. To account for the reduced revenue collection period, staff may need to postpone or phase capital projects and work with the consultant to revise the capital improvement plan and proposed rate adjustments accordingly.
2. ***Council could decide not to authorize the release of the Prop 218 notice and direct staff that no rate adjustment be moved forward at this time.*** If Council chooses not to authorize the release of the Prop 218 notice, the City will not proceed with the proposed 2025 water and sewer rate adjustments. As a result, the Prop 218 process will be paused until directed by Council. This would prevent any rate increases from being adopted or implemented for the upcoming two fiscal years. Because the proposed rates were developed with the assumption of a full 12 months of increased revenue starting July 1, 2025, and July 1, 2026, not moving forward with the rate adjustments would create a significant shortfall for the City's water and sewer funds. If this were the case, staff would need to delay or scale back planned capital improvement projects and re-engage the consultant to revise the capital improvement plan based on revenue projection with no rate increases.
3. ***Council could decide not to set the Public Hearing dates for June 17, 2025.*** If Council chooses not to set the public hearing date for June 17, 2025, a new date must still comply with Prop 218 requirements, which mandate that a public hearing occur no sooner than 45 days after the Prop 218 notice is mailed. Council may select an alternate hearing date, but doing so could delay rate adoption and implementation beyond July 1, 2025. As with the alternative to delay the mailing of the Prop 218 notice, a delay would shorten the revenue collection period assumed in the rate analysis and may require staff to adjust the capital improvement plan and revisit the proposed rates with the consultant to ensure financial health of the funds.

4. ***Council could direct modifications to the proposed rates, or to the proposed implementation dates.*** If Council wishes to proceed with modifying the proposed rate adjustments included in the notice, or adjusted the implementation timeline, staff would work with the rate consultant to update the financial analysis and revise the Prop 218 notice accordingly. Modifying the proposed implementation dates, such as phasing in the rate increases or delaying the effective date, would reduce the revenue collected and could impact the timing or scope of planned capital improvement projects. Changes like this would require additional time to prepare updated materials and require staff to delay the mailing of the Prop 218 notice and subsequent public hearings. It is also important to note that the values included in the Prop 218 notice represent the maximum rates that Council may adopt at the public hearing, provided there is no majority protest. However, Council may choose to adopt lower rate increases than those that are included in the Prop 218 notice at the public hearing.

#### **ATTACHMENTS**

- A - Draft City of San Luis Obispo Water and Wastewater Rate Study Update Report (March 2025)
- B - Draft Water and Sewer Prop 218 Notice
- C - 45-Day Legal Notice
- D - Informational and FAQ Sheet