MINUTES

MILWAUKIE CITY COUNCIL WORK SESSION
JULY 14, 2003

Mayor Bernard called the work session to order at 5:30 p.m. in the City Hall conference room.

Councilors present: Barnes, Lancaster, Loomis, and Stone.

Staff present: City Manager Mike Swanson, Community Development/Public Works Director Alice Rouyer, Engineering Director Paul Shirey, and Associate Engineer Jay Ostlund.

Information Sharing

The group discussed the upcoming July 26 Riverfront Event and promotional efforts for the North Main Street Redevelopment Project.

Councilor Lancaster asked for comments on the July 8, 2003 letter from Clackamas County Commissioner Bill Kennemer in response the Mayor Bernard's June 23 letter regarding Milwaukie's MTIP application. The group discussed communications and negotiations related to the JPACT decision not to fund the Lake Road Multi-Modal Plan. Mayor Bernard will respond to Kennemer that the Milwaukie City Council looks forward to partnering in the future.

Open Public Forum

None.

Water Cost of Service Study Recommendation

Ostlund said the last water rate adjustment was in 1994, and rates have gone unchanged since then. The City contracted with Donovan Enterprises last April to conduct a water cost of service study. The consultant presented his findings and alternatives to the Citizens Utility Advisory Board (CUAB) in May and June, and a recommendation was prepared. Ostlund introduced Steve Donovan.

Donovan discussed the study and recommendation. His agenda included an explanation of how rates and charges are built, an analysis of the financial wherewithal of the utility, the existing rate structure and where the money is coming from, key issues affecting Milwaukie, CUAB analysis and the alternatives that were rejected, the recommendation, and finally the proposed rates.

Rates are considered using history, audits, budgets, and a determination of how much the City department as a business enterprise needs to operate. Within that, there is further consideration of fiscal policies, amount of cash to have on hand, depreciation funding, replacement, and similar issues related to operating a water utility. From that, revenue requirements are generated. Also taken into account are the resources required to fund system replacements and improvements. Finally, a financial model is constructed and rates are proposed.

Milwaukie is a residential community. 88% of all customers are residences served by ¾-inch meters. These customers currently pay a flat rate of $5.95 every two months and $1.35 for every 100 ccf of metered water supplied. In 2002 residential customers consumed 63% of the water sold. The balance went to multi-family, commercial, and industrial class customers. The only difference in rates is the fixed portion. All customers pay the same $1.35 per 100 ccf.

Donovan said one key point to remember is that Milwaukie has not adjusted its rates since 1995. The real key is the legal fees associated with the groundwater contamination litigation. Since 2002, the City has spent $330,000, and another $200,000 is budgeted this year. That money is not coming from ratepayers; it is coming out of the capital reserve fund. The outcome of the litigation will drive the future well being of the water utility. He understands from the city attorney that the litigation phase of this will be completed in about a year, and appeals are anticipated. For planning purposes, $50,000 is being budgeted for the next 5 years for the lawsuit.

Further, the City is not currently funding replacement. Money is taken out of rates to fund the depreciation expense, and some portions of the system are over 50 years old. As in any business, replacement needs to be funded out of current income. The surrogate used is the audited depreciation expense. The City is currently not funding anything because rates have not been adjusted since 1995. The department has been careful with its money, and the reserves are in good shape.

Finally, Milwaukie is residential and is at build out, so growth cannot be the engine to fund future requirements. Over the past 10 years, the customer growth in the base is about 0.29% per year. The rule of thumb in the utility industry is about 0.50% per year for infill, so Milwaukie is growing less than the infill and redevelopment rate.

The CUAB wants to fund the legal fees from the reserves, not by raising rates because that action would generate a large spike. The Board also wanted to phase in rate increases over a five-year period. The CUAB wants to find ways to implement level, understandable increases over the forecast horizon. Depreciation phasing starts immediately in 2004 and is fully funded by 2009. This approach fully funds all the operating requirements and has enough cash

generated to fund future capital improvements based on the approved plan. This option meets the CUAB's desire to have level, predictable rates.

He provided graphs of the anticipated rate increases in the preferred alternative. These did not include any outcomes of the groundwater litigation since these are unknown. A 4.17% increase is anticipated this year with legal fees being funded from reserves and phasing in depreciation expenses. Donovan briefly reviewed the alternatives the CUAB did not recommend because they resulted in undesirable rate spikes. Milwaukie is fortunate in that it can fund its legal fees through its reserves.

Donovan showed the Council a bar graph that indicated how Milwaukie's rates compared to those of neighboring providers based on customer use of 10 ccf. Milwaukie customers currently pay $16.48. The preferred alternative results in a $.69 per month rate increase. Relative to other communities in the metropolitan area, Milwaukie would still be quite low.

Councilor Lancaster asked for an example of the volume of 10 ccf.

Donovan said 1 ccf of water is about 7.48 gallons of water.

Councilor Lancaster understands the CUAB is recommending a 5-year phase in, so that by 2009, the department will be funding for its infrastructure based on anticipated replacements. At that level, would the City be able to fund for all future infrastructure on an ongoing basis?

Donovan said that would fund replacement but not necessarily improvements. This depreciation and replacement recommendation simply replaces and maintains the current level of service. It would not cover improvements, expansions, or enhancements.

Councilor Lancaster asked how much was in reserves for unanticipated early failure of the infrastructure.

Donovan said the City has about $2 million in cash for unanticipated failures. Milwaukie is in very good shape for a community its size; it has been prudent and costs have been controlled. However, while the City has not adjusted its rates since 1995, operating costs including energy and labor have gone up.

Councilor Lancaster asked Donovan his opinion of an adequate amount of reserve.

Donovan said typically a reserve should be 1% of the original costs plus depreciation or book value of the assets, and Milwaukie meets that. There was a bond issue for the packed towers, and the City is paying those on time.

Milwaukie is in very good financial shape. He believes the rate on the current bond is 4.5% - 5%.

Councilor Lancaster asked if there would be a refinancing opportunity.

Swanson said the bonds have been refinanced and believes the City has to go to term on these.

Donovan said these are refunded bonds, and typically there are covenants in the bond ordinance that would preclude advanced refunding. Refinancing can usually be done once under certain conditions.

Swanson said this and the public safety building bond have covenants that prohibit another refunding.

Councilor Stone asked the interest rate, and **Donovan** offered to get that information for her.

Swanson said any decision to get into a lawsuit carries a certain amount of risk, and that is the question to ask the lawyers. If there is a recovery in this lawsuit, because the money was generated by the water fund, it will go back to that fund. He asked if the City Council might revisit the rate structure if there is a recovery.

Donovan said there could be a surplus to the water fund that could, based on policy guidance, result in any number of things including lowering rates.

Mayor Bernard said every business owner likes to put money aside for depreciation, but the City does not. If the City does not, does it sell bonds to make major repairs and maintenance or take it out of reserves?

Donovan said that is typically how it is done. The last two rate studies he conducted for other cities took into account bond sales and the incremental interest expense and raising rates. If an entity has the wherewithal to write the check by raising fees, the pipe is much cheaper in the long run.

Bob Hatz, CUAB Chair, said the Board feels it is definitely much better to go on a steady rate of pay rather than getting reserves down and trying to catch up. The group feels most of the Milwaukie ratepayers would agree.

Mayor Bernard supported the CUAB option.

Donovan discussed public involvement, education, and implementation.

Shirey said the intent is to bring the rate adjustment to Council for formal approval on September 16. The plan is to mail customers an insert in their utility bills about the rate adjustment and why it is needed.

Councilor Barnes recommended an article in *The Pilot* regarding the rate adjustment. She believes there are a lot of people who do not remember or who need an update on the lawsuit itself with an explanation of where the funds are coming from to cover it.

Councilor Stone said the result of the lawsuit could be positive for everyone.

Mayor Bernard suggested a recommendation at a City Council meeting.

Councilor Stone asked when the lawsuit was filed.

Swanson said activity on the packed towers has been going on for more than 10 years. The City just filed the lawsuit within the past year or year and one half. There were about eight months of quiet study of groundwater samples, and as those came in, it looked more and more like there was a good case for recovery. Even though there was a period of 10 years, laws allowed the City to proceed. The groundwater analysis consultant and attorneys, even though they are conservative, felt we had a very promising defendant.

Councilor Stone thought it would be a good idea to recap this for the public so they know what is happening with their money.

Councilor Loomis would not object to lowering the sewer charge as staff recommended in order to counterbalance the water rate increase. The consultant recommended lowering the sewer rate, but Council decided not to proceed with that recommendation. He suggested lower the sewer rate if the water rate goes up.

Mayor Bernard said there is still the $1 million surprise treatment bill the City is trying to pay off.

Councilor Lancaster said that is intended to be dedicated to the unanticipated liability, which has a serious impact on the City's viability.

Councilor Loomis said he was just considering the staff recommendation based on the health of the reserve fund.

Mayor Bernard said he was satisfied holding off until September. The water rate increase, although it could be significant to some, is not really that great.

Councilor Lancaster felt the City was on the right track by making the increases incremental and more predictable for personal budgeting.

Mayor Bernard asked how many customers have six-inch meters.

Donovan said these are industrial meters, and one of these customers is Precision Castparts.

Shirey corrected Donovan's comment and explained Precision Castparts uses a four-inch meter.

The group discussed business recruitment calling attention to Milwaukie's competitive water and sewer rates within the metropolitan area.

The group briefly discussed the upcoming teambuilding session.

Advisory Board Interview

The City Council interviewed Rob Gabrish for a position on the Park and Recreation Commission.

The work session ended at 7:05 p.m.

Pat DuVal

Pat DuVal, City Recorder

AGENDA

MILWAUKIE CITY COUNCIL WORK SESSION
JULY 14, 2003

WORK SESSION – 5:30 p.m.
Second Floor Conference Room

MILWAUKIE CITY HALL
10722 SE Main Street

Discussion Items

	Time	Topic	Presenter
1.	5:30 p.m.	Dinner and Information Sharing • Questions/Comments on July 15 Agenda Items – these questions and/or comments can only be on those items that are legislative and not on those that are quasi-judicial, like land use or liquor license hearings	Group
2.	6:00 p.m.	Open Public Forum	
3.	6:30 p.m.	Water Cost of Service Study Recommendation	Paul Shirey/Jay Ostlund/Consultant
4.	7:00 p.m.	Advisory Board Interview	Group
5.	7:15 p.m.	Adjourn	

Public Notice

- The Council may vote in work session on non-legislative issues.
- The time listed for each discussion item is approximate. The actual time at which each item is considered may change due to the length of time devoted to the preceding items.
- Executive Session: The Milwaukie City Council may go into Executive Session. If an Executive Session is called to order, the appropriate ORS citation will be announced identifying the applicable statute. All discussions are confidential and those present may disclose nothing from the Session. Representatives of the news media are allowed to attend Executive Sessions

as provided by ORS 192.660(3) but must not disclose any information discussed. No Executive Session may be held for the purpose of taking any final action or making any final decision. Executive Sessions are closed to the public.

- For assistance/service per the Americans with Disabilities Act (ADA) please dial TDD 786-7555.

- The Council requests that all pagers and cell phones be either set on silent mode or turned off during the meeting.

CITY OF MILWAUKIE

To: **Mayor and City Council**

Through: **Mike Swanson, City Manager** AOR
Alice Rouyer, Director of Community Development & Public Works

From: **Jack R. Ostlund Jr., Associate Engineer** JRO
Paul Shirey, Engineering Director

Subject: **Water Cost of Service Work Session**

Date: **June 30, 2003 for July 14, 2003 Meeting**

Action Requested

Review and discuss material presented

Background

On April 3, 2003, the City of Milwaukie contracted with Donovan Enterprises to perform a Water Cost of Service Study. Water rates have remained unchanged for the past eight years. The purpose of the study is to match rate revenue to the cost of future capital needs (re: water line replacement, storage capacity and well-head costs) and projected operating expenses. The study was also designed to evaluate the cost of services provided by the City of Milwaukie water department

On May 7, 2003, the consultant team presented the Citizens Utility Advisory Board (CUAB) with the City's current revenue requirements and a review of the overall financial health, fiscal policies and operations of the water department. The consultants discovered that the water department had not been funding the cost of capital depreciation for some time, contrary to sound financial practices. The consultants were advised to develop three rate scenarios to fund depreciation and return for the June 4, 2003 CUAB meeting to discuss the implications of each.

On June 4, 2003, the consultant team shared the rate options with the CUAB. The CUAB recommended adopting the rate option that provides a regular, consistent, and affordable increase over a period of seven years. This gradual rate increase will start funding depreciation immediately and fully fund depreciation by the end of the fiscal year 2009. The current five year capital improvement plan would also be fully funded under this scenario.

The proposed rate increase, if adopted, would take effect on January 1, 2004.

WS. 3 2

Preliminary Draft

City of Milwaukie

Water Rate Study
June, 2003

Presented by

DONOVAN enterprises

WS. 3 3

City of Milwaukie
Water Rate Study

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Executive Summary

Revenue Requirements and the Citizens Utility Advisory Board

This study addresses the levels and structure of rates needed to support the operations of the water utility in the City of Milwaukie. A five year planning period, 2005 through 2009, has been used in the analysis with rates based on cost of service principles. Fiscal 2004 data are based on the City's proposed budget for the period July 1, 2003 through June 30, 2004.

Based on the estimated results of the current fiscal year and the data discussed above, three optional analyses were developed and presented to the Citizens Utility Advisory Board (CUAB) at two meetings held in May and June of 2003. The fundamental differences between these three alternatives centered on the funding of legal fees associated with the City's pending ground water contamination litigation, and a strategy to begin funding infrastructure replacement from rates. A detailed discussion of the specifics of each of these cases is contained in the body of this report.

The guiding policy criteria that were used by the CUAB to evaluate the options were:

- Legal fees arising out of the pending groundwater contamination litigation are transient in nature and should be funded from the Water Capital Reserve Fund. It was felt by the Board that the rate spikes that would result from having rate payers fund this expense via current rates was unnecessary. There are sufficient resources in the Reserve Fund to meet the anticipated short term legal fee requirements. The Board realized that by using this money to pay for legal fees, it would be diverting resources that would have been used for system repair, replacement, and enhancement. The City Attorney anticipates bringing the litigation to a close by the end of fiscal 2004. Since fiscal 2002, the City has spent $330,000 prosecuting this case. For the upcoming fiscal year, an additional $200,000 has been budgeted. The forecast assumes an additional $50,000 per year thereafter will be spent to fund anticipated appeals and challenges by the defendants. The Board also felt that any judgments or settlements that arise out of this litigation to the benefit of the City, would in effect be a return on the ratepayers' investment.

- To the greatest extent possible, any future rate increases should be structured to be smooth across the forecast horizon. The Board has historically supported small regular rate adjustments in lieu of one time spikes followed by years of no increases.

- After taking into account the preferred treatment of legal fees, and the Board's overriding preference of having small regular rate adjustments, the City should begin phasing in the funding of infrastructure replacement via rates. Currently, the City is not transferring cash from the Water Operating Fund to the Water Capital Reserve Fund for the replacement of infrastructure(i.e., pumps, pipes, wells, and reservoirs). There simply is not enough revenue being generated from current rates to meet this requirement after all of the utility's other fiscal needs have been met. According to the City's audited

financial statements, the water system incurred $315,636 in depreciation expense in fiscal 2002. Depreciation expense is a surrogate for replacement requirements. This issue is of particular importance in Milwaukie because some parts of the water distribution system have been in service in excess of 50 years. Conversation with the City's operations staff indicate that this infrastructure needs replacement.

After considerable discussion, the Board unanimously agreed to recommend a water system funding option to the City Council that contains the following strategy:

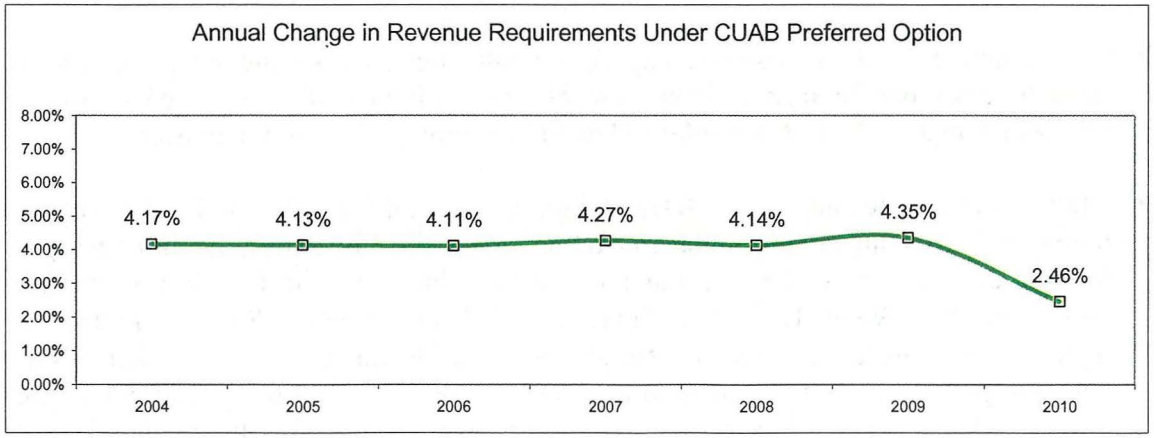
- Fund legal fees from the Water Capital Reserve Fund. Although these fees will be budgeted in and paid from the Water Operating Fund, the resources will come from the capital reserve via transfer. As of April 30, 2003, there was $1,770,462 in the water capital reserve fund.

- Start a five year phase-in program for the funding of infrastructure replacement from rates. The phasing should start in fiscal 2004. By 2009 the City will achieve full funding at a level of the $315,636.

Based on these criteria, the following forecast of changes in revenue requirements ensued:

Table ES-1
City of Milwaukie
Analysis of Annual Percentage Increases in Revenue Requirements
Citizens Utility Advisory Board Preferred Option

Option Number and Description	2004	2005	2006	2007	2008	2009	2010
Preferred Option : Fund legal fees from the Capital Reserve Fund and start depreciation phasing in 2004	4.17%	4.13%	4.11%	4.27%	4.14%	4.35%	2.46%
Key Assumptions:							
Legal fees to be funded from rates	$ 200,000	$ 50,000	$ 50,000	$ 50,000	$ 50,000	$ 50,000	$ 50,000
Depreciation funding from rates	$ 150,000	$ 175,000	$ 190,000	$ 225,000	$ 265,000	$ 315,636	$ 325,105



Rates and Rate Structure

The City has not adjusted water rates since 1995. In 1993, the City moved away from a fixed bi-monthly fee approach for residential water service in favor of the current system that consists of fixed (i.e., base charge) and variable (i.e., use charge) elements. The preponderance of the City's total customer base (88%) is residential. Almost all of these customers are served by 5/8"-3/4" meters. These customers pay the city a fixed bi-monthly base fee of $5.95 in addition to a variable use fee of $1.35 per one hundred cubic feet of water consumed (i.e., metered). In fiscal 2002 these residential customers consumed 63% of all water sold in the City. The balance of the water sales was made up by multifamily, commercial and industrial customers. These customers pay the same use fee of $1.35 per one hundred cubic fee of water consumed (i.e., Ccf). However, the bi-monthly base charge for these customers varies depending on the size of the meter that is installed. These charges start out at a bi-monthly rate of $8.29 for a one inch meter and go up to $129.90 for a six inch meter.

The basic design of the City's rate structure for water is sound. The current rates afford customers the opportunity to avoid and control costs based on their metered potable water consumption patterns. This is sound policy and is effectively the standard in the utilities industry.

It is at this point in the rate study process that alternative rate structures are usually explored. The consultant team has reviewed the process that was used to develop the existing system and find no reason to make changes to that structure. The most compelling argument for staying with this system is contained in Table ES-2

Table ES-2
City of Milwaukie
Analysis of Water Accounts Fiscal 1992 - 2002

Account Description	Average Number of Accounts 1992	2002	10 Year Compounded Annual Change
5/8" X 3/4" Meter	5,655	5,865	0.36%
1" Meter	308	252	-1.99%
1 1/2" Meter	79	86	0.87%
2" Meter	140	150	0.69%
3" Meter	16	16	0.00%
4" Meter	8	7	-1.33%
6" Meter	1	1	0.00%
Clackamas Billing	1	1	0.00%
Low Income Rate	144	159	1.01%
2" Standby	9	8	-1.81%
4" Standby	26	30	1.44%
6" Standby	23	31	3.03%
8" Standby	31	28	-1.01%
10" Standby	10	10	0.00%
12" Standby	3	3	0.00%
Total Accounts	6,454	6,646	0.29%

Generally, the primary reason to change a rate structure is to rectify a looming rate inequity. These inequities are usually the result of changes in consumption patterns over time by unique classes of customers. For example, a growth in peaking demand by one class of customer (say a 4 inch industrial customer) would warrant a shifting of cost recovery to that class. In the case of Milwaukie, the demands that are placed on the system are effectively static and have been static for the last ten years. Milwaukie is now a community at buildout. As the data in Table ES-2 show, the total growth in the customer base has been averaging 0.29% per year since 1992. This is a very small change with respect to planning and accounting for system demand. This is particularly true in the case of the commercial and industrial customers. The relative change in the composition of those customers with meters in the 1 inch to 6 inch range is effectively zero.

In addition to analyzing trends in the number of accounts served by the City, the consultant team also reviewed very recent trends in water sales and peaking requirements to determine if there has been a shift demand, which may call for a review of how costs are recovered from customers. In both cases, the team found no unusual changes or shifts in the amount of water delivered to customers or the way that water was consumed by each class of metered customer.

Based on the analysis discussed above, it is recommended that the City implement a uniform water rate increase of 4.17% for fiscal 2004 and adjust rates in future years with the benefit of annual reviews of revenue requirements and customer demographics and demand. The existing and proposed schedule of water rates for fiscal 2004 are contained in Table ES-3.

Table ES-3
City of Milwaukie
Current and Proposed Water Rates
CUAB Preferred Option

Uniform Rate Adjustment Percent 4.17%

Billing System Code	Description	Current Rates		Proposed Rates	
		Bimonthly Base Rate	Use Charge $ per 100 Cubic Feet	Bimonthly Base Rate	Use Charge $ per 100 Cubic Feet
2	5/8" X 3/4" Meter or Smaller	5.95	1.35	6.20	1.41
3	1" Meter	8.29	1.35	8.64	1.41
4	1 1/2" Meter	13.38	1.35	13.94	1.41
5	2" Meter	20.78	1.35	21.65	1.41
6	3" Meter	51.22	1.35	53.35	1.41
7	4" Meter	72.78	1.35	75.81	1.41
8	6" Meter	129.90	1.35	135.31	1.41
20	Low Income Rate	-	1.35	-	1.41
502	2" Standby	8.85	1.35	9.22	1.41
504	4" Standby	31.88	1.35	33.21	1.41
506	6" Standby	46.41	1.35	48.34	1.41
508	8" Standby	63.02	1.35	65.65	1.41
510	10" Standby	79.61	1.35	82.93	1.41
512	12" Standby	96.21	1.35	100.22	1.41

Impact of Rate Increase on Actual Customers

In order to judge the financial impact on customers as a result of the recommended general rate increase, a sample of actual customer accounts were analyzed. Based on the knowledge of the customer service staff, an attempt has been made to look at the bi-monthly bills of a cross section of the City's customers. Itemized in table ES-4 is a breakdown of the actual bi-monthly bills for selected customers for the period June-July, 2002. Also included, is a calculation of those customers' bills under the proposed increased rates.

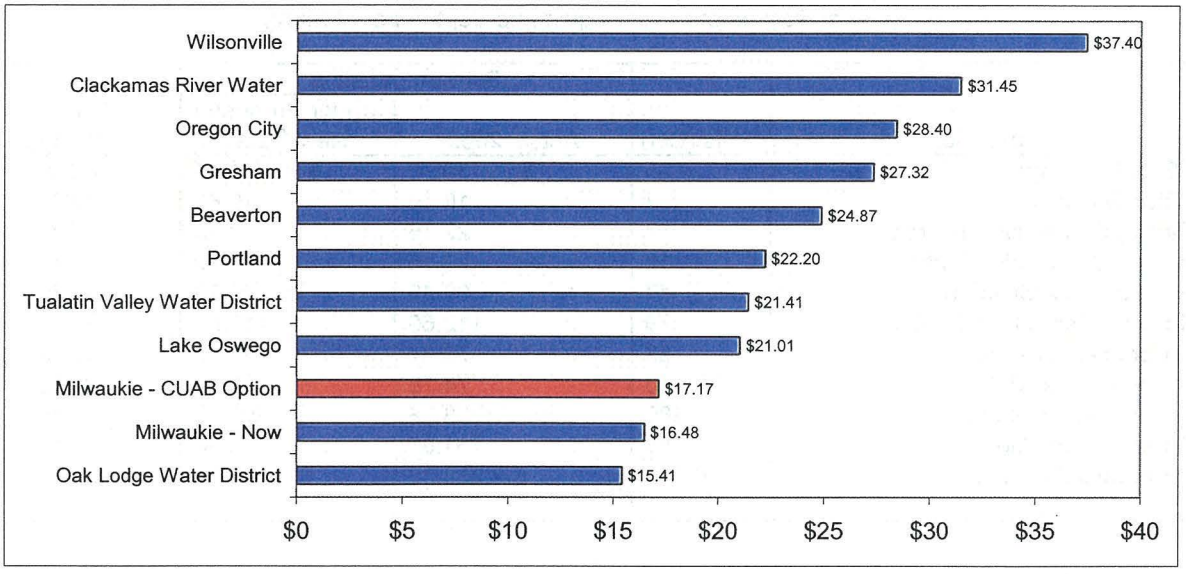
Table ES-4
City of Milwaukie
Comparison of Actual Water Bills to Water Bills Under Proposed Rates
(Actual Consumption for August and September of 2002)

Customer	Units (Ccf)	Bill Comparisons		Percent Change
		Actual 2002	Under Proposed New Rates	
1 Elderly Person	25	$ 39.70	$ 41.40	4.3%
1 Elderly Person	3	10.00	10.60	6.0%
Married Couple No Children	12	22.15	23.20	4.7%
Married Couple No Children	12	22.15	23.20	4.7%
Married with 2 Children	47	69.40	72.20	4.0%
Married w/more than 2 Kids	79	112.60	117.00	3.9%
1" Commercial Meter	53	79.84	83.25	4.3%
2" Commercial Meter	40	74.78	79.79	6.7%
2" Commercial Meter	380	533.78	555.79	4.1%
4" Commercial Meter	58	151.08	168.88	11.8%
4" Commercial Meter	6,878	$ 9,358.08	$ 9,716.88	3.8%

Milwaukie Rates Relative to Neighboring Communities

In addition to evaluating the impact on Milwaukie customers relative to what they are currently paying for domestic water service, a survey was performed to determine how the City's water rates compare to those charged in neighboring communities. In order to make an "apples-to-apples" comparison, a representative monthly bill was calculated for a single family residential customer that consumed 10 Ccf per month. This assumes these customers are served by 5/8"-3/4" meters. Figure ES-1 shows the resulting monthly bills for ten local communities.

Figure ES-1
Milwaukie Water Rates Relative to Neighboring Communities (Monthly) as of July 1, 2003
(Assuming Monthly Consumption of 10 Ccf)



Development Services Fees and Charges

The City routinely provides services and incurs costs for new water customers that are not covered by monthly rates. The most common service is new meter installation. For a one-time and set fee, the City will install a meter for a new customer. Typically, these installations are for new developments. However, there are instances where existing customers request to have a meter changed out to accommodate increased (or decreased) anticipated usage. The City also sells approved meters to customers who, in turn, install them at their own expense and subject to final inspection by the City. There are other miscellaneous development related services that the Water Department provides and bills to customer on a scheduled basis. All of these development related fees are itemized and contained in City Resolution # 23-2002 (adopted 9/17/02). The water fees and charges that are in place have not been adjusted since 1993. Over the last three fiscal years, the City has received an average of $27,673 per year by providing these services. To put this figure in perspective, revenues recognized form water rates will amount to almost $1,800,000 this fiscal year. Clearly, development related service fees are a small part of the Water Department's revenue base.

A suggestion has been made that the City consider moving away from charging for these direct services for development on a **pre-set or scheduled** basis. The alternative is to implement a job cost approach for cost recovery where direct labor, equipment and materials are billed to a specific developer based on the actual costs incurred. The primary advantage of the job cost approach is that the City will recover its exact costs in providing the direct service on a work order basis. Under a pre-set or fee schedule basis of cost recovery, the actual costs incurred do not necessarily match the fee schedule due to timing and the scope of each individual site specific job. While accuracy of billing is a recognized advantage in the job cost approach, it is also the case that the City does see disadvantages to moving away from its pre-set or scheduled fees. These are:

1. Increased Administration for the City. In order to send an accurate bill for services rendered, the City would have to implement a system able to track time, materials, and overhead by work order. The City currently does not have a system in place to accommodate this process. Discussions with public works staff indicate that this type of system could be developed, but it would take time and unbudgeted resources.

2. Adversity for Customers. Under the current process, developers and existing customers know - up front - how much they will be charged for the services they are requesting from the City. Under the suggested time and materials approach, the City could only give the prospective developer or customer an estimate of the costs. The final cost would not be know until the job in question was completed. This "certainty" factor is important, particularly in the case of developers, because this cost data is used to calculate the feasibility of prospective projects.

Recommendation: Milwaukie is at effective buildout. There is limited new development activity at this time. According to Public Works staff, there were only ten or twelve new service meter installations last year. If there was substantial development/redevelopment activity, it might be appropriate to commit the resources necessary to implement a job costing system. However, given the current level of development and the adequacy of development fee revenue to offset current

meter installation costs, no such change is warranted.

Therefore, it is recommended that the City continue its policy of setting a schedule of fees for development related services and periodically adjusting these fees based on available actual cost of service data. An analysis of recent cost data indicates that the schedule of fees that are currently in force are adequate to recover the City's costs. Therefore, no adjustments are recommended to the development support fee schedule at this time. The current fee schedule is as follows:

WATER FEES & CHARGES IN SUPPORT OF DEVELOPMENT AND CUSTOMER SERVICES

Service and Equipment:

Connect Service 5/8" or 3/4" Residential Service	$2,460
Connect Service 1"	$2,547
Connect Service 1 1/2"	$2,923
Connect Service 2"	$3,067

Equipment:

3/4" Meter	$208
1" Meter	$301
1 1/2" Meter	$510
2" Meter	$625
Hydrant Meter Deposit	$579

Miscellaneous:

Delinquent Account – Past Due Notice*	$5
Delinquent Account – Notice of Termination*	$25
After Hours Restoration of Service* (Monday-Friday 5:00 pm to 8:00 pm; Saturday & Sunday 8:00 am to 5:00 pm)	$80
Information Research	$44/hr.
Reimbursement District Fee	To be determined by scope of project

* Accounts remaining delinquent more that three (3) months subject to 10% per year added to the outstanding balance to pay the City's interest and collection costs.

Summary of Consultant Recommendations

- The City should consider adopting a set of uniform financial policies for all of its utilities. **Appendix A** contains an issue paper that lays out recommended guidelines for the financial planning and management of the water system.

- The City should adopt the CUAB's preferred option for the ongoing funding of the water utility. This recommendation calls for a 4.17% increase in the systems revenue requirements for fiscal 2004. It is further recommended that this increase be uniformly implemented across all customers by size of water meter in service.

- The modeling that has been done to develop the water system's revenue requirements is predicated on a five year comprehensive financial plan. It is recommended that the City endeavor to implement this plan through annual reviews of the water systems financial performance. Periodic updates to the plan are expected and prudent as operating and strategic conditions change over time.

- Fees and charges related to water system development services are adequate at this time to recover anticipated costs incurred by the city in the support of development activities. As in the case of water rates, the City should review these fees and charges annually to insure that revenues from this source are sufficient to cover the costs incurred to provide development related services.

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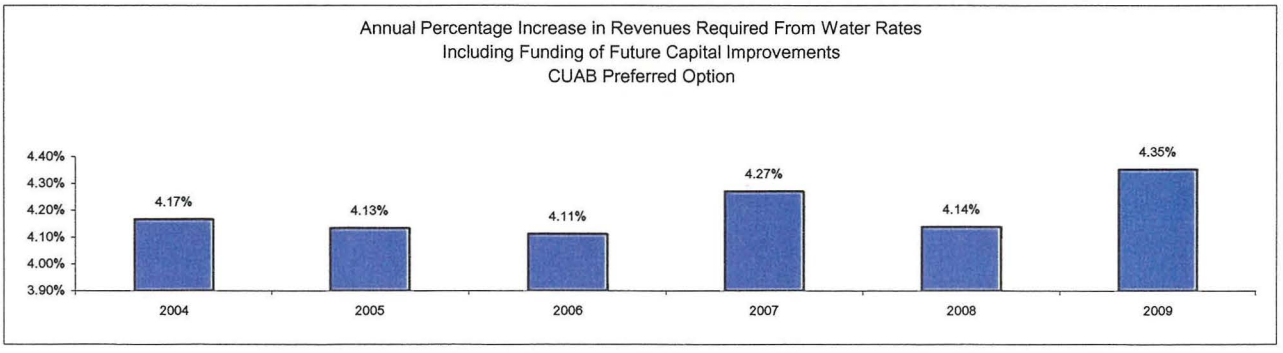
Analysis Section

Detail of the CUAB Preferred Option – Fund legal fees from the Capital reserve Fund and start the phase-in of capital replacement funding from rates in fiscal 2004

Water Operating Fund Revenue Requirements

City of Milwaukie
PRELIMINARY Projection of Water Operating Fund Revenue Requirements
CUAB Preferred Option

Line Item Description	Estimated 2003	Proposed 2004	Forecast 2005	2006	2007	2008	2009
Projection of Cash Flow:							
Transfers IN	258,400	205,000	328,000	328,000	328,000	328,000	328,000
Gross Revenues:							
Miscellaneous Fees & Charges	28,691	20,000	20,000	20,000	20,000	20,000	20,000
Water User Fees	1,835,622	1,835,000	1,920,628	2,009,631	2,102,338	2,202,654	2,304,828
User Penalty Fees	74,835	60,000	60,000	60,000	60,000	60,000	60,000
Intergovernmental Charges	10,804	1,500	1,500	1,500	1,500	1,500	1,500
Interest Earned	4,740	15,751	15,839	13,118	13,094	12,983	14,176
Rental Revenue	25,225	29,000	29,000	29,000	29,000	29,000	29,000
Bad Debt Recovery	1,712	-	-	-	-	-	-
Other Revenues	73	1,000	1,000	1,000	1,000	1,000	1,000
Subtotal Gross Revenues	1,981,702	1,962,251	2,047,967	2,134,249	2,226,932	2,327,137	2,430,504
less: Operations & Maintenance Expense	(1,247,750)	(1,421,254)	(1,472,590)	(1,520,421)	(1,570,044)	(1,616,513)	(1,670,377)
less: Transfers OUT	(251,681)	(437,277)	(470,895)	(494,772)	(538,915)	(588,333)	(648,669)
less: Cash Financing of Capital Improvements	(76,411)	(200,000)	(200,000)	(200,000)	(200,000)	(60,301)	(77,746)
less: Existing Debt Service	(134,085)	(134,765)	(130,110)	(130,360)	(130,260)	(134,800)	(133,475)
less: New Debt Service	-	(45,374)	(52,995)	(67,013)	(71,961)	(71,961)	(71,961)
Net Cash	530,175	(71,418)	49,377	49,684	43,752	183,228	156,275
Net Deficiency/(Surplus)	(530,175)	71,418	(49,377)	(49,684)	(43,752)	(183,228)	(156,275)
Test of Coverage Requirement:							
Operating Expenses as Defined in Ordinance No. 8-1997	1,499,431	1,858,531	1,943,485	2,015,193	2,108,959	2,204,846	2,319,046
Debt Service on Series 1997 Water Refunding Bonds:							
Interest	44,085	39,765	35,110	30,360	25,260	19,800	13,475
Principal	90,000	95,000	95,000	100,000	105,000	115,000	120,000
Total Debt Service on Series 1997 Bonds	134,085	134,765	130,110	130,360	130,260	134,800	133,475
Debt Service on New Serial Revenue Bonds	-	45,374	52,995	67,013	71,961	71,961	71,961
AdditionalCoverage Required: 25%	33,521	45,035	45,776	49,343	50,555	51,690	51,359
Total Revenue Required with Coverage	1,667,037	2,083,704	2,172,366	2,261,909	2,361,736	2,463,298	2,575,842
Gross Revenues Allowable for Coverage Test:							
Gross Revenues Recognized From Fees and Charges	1,981,702	1,962,251	2,047,967	2,134,249	2,226,932	2,327,137	2,430,504
System Development Charges	45,990	45,000	45,000	45,000	45,000	45,000	45,000
Gross Revenues Allowable for Coverage Test	2,027,692	2,007,251	2,092,967	2,179,249	2,271,932	2,372,137	2,475,504
Coverage Recognized	3.94	0.83	0.82	0.83	0.81	0.81	0.76
Coverage Required	1.25	1.25	1.25	1.25	1.25	1.25	1.25
Net Deficiency/(Surplus)	(360,655)	76,453	79,400	82,659	89,804	91,161	100,338
Projection of Revenue Sufficiency:							
Maximum Deficiency	-	76,453	79,400	82,659	89,804	91,161	100,338
Percent Increase Required Over Current Rate Revenues	**0.00%**	**4.17%**	**4.13%**	**4.11%**	**4.27%**	**4.14%**	**4.35%**
Revenue Recovered From Existing Rates and Charges		1,835,000	1,920,628	2,009,631	2,102,338	2,202,654	2,304,828
add: Revenue From Growth in the Customer Base		9,175	9,603	10,048	10,512	11,013	11,524
add: Revenues Recovered From Rate Increase		76,453	79,400	82,659	89,804	91,161	100,338
Total Revenues Recovered From Rates & Charges after Increase		1,920,628	2,009,631	2,102,338	2,202,654	2,304,828	2,416,690



Water Operating Fund Sources and Uses of Funds (Cash Flow)

City of Milwaukie
Statement of Cash Flow and Changes in Fund Balance - Water Operating Fund
CUAB Preferred Option

Line Item Description	Estimated 2003	Proposed 2004	Forecast 2005	2006	2007	2008	2009
Sources of Funds							
Beginning Fund Balance	$ 647,471	$ 927,646	$ 656,227	$ 655,604	$ 653,788	$ 644,494	$ 773,086
Revenues:							
Miscellaneous Fees & Charges	28,691	20,000	20,000	20,000	20,000	20,000	20,000
Water User Fees	1,835,622	1,835,000	1,920,628	2,009,631	2,102,338	2,202,654	2,304,828
User Penalty Fees	74,835	60,000	60,000	60,000	60,000	60,000	60,000
Intergovernmental Charges	10,804	1,500	1,500	1,500	1,500	1,500	1,500
Interest Earned	4,740	15,751	15,839	13,118	13,094	12,983	14,176
Rental Revenue	25,225	29,000	29,000	29,000	29,000	29,000	29,000
Bad Debt Recovery	1,712	-	-	-	-	-	-
Other Revenues	73	1,000	1,000	1,000	1,000	1,000	1,000
Total Revenues	1,981,702	1,962,251	2,047,967	2,134,249	2,226,932	2,327,137	2,430,504
Transfers IN:							
Fund 515 - System Development Charges	8,400	5,000	78,000	78,000	78,000	78,000	78,000
Fund 520 - Capital Reserve Fund	250,000	200,000	250,000	250,000	250,000	250,000	250,000
	258,400	205,000	328,000	328,000	328,000	328,000	328,000
Total Sources of Funds	2,887,573	3,094,897	3,032,194	3,117,853	3,208,720	3,299,631	3,531,590
Uses of Funds							
Personal Services	378,052	430,650	443,570	456,877	470,583	484,700	499,241
Materials and Services (including Existing Debt Service)	1,003,783	1,125,369	1,159,130	1,193,904	1,229,721	1,266,613	1,304,611
Well Field Litigation Legal Fees	250,000	200,000	50,000	51,500	53,045	54,636	56,275
Capital Outlays:							
Minor Capital	-	-	-	-	-	-	-
Water Capital Projects	76,411	200,000	200,000	200,000	200,000	60,301	77,746
Total Capital Outlays	76,411	200,000	200,000	200,000	200,000	60,301	77,746
New Debt Service for Future Capital Projects	-	45,374	52,995	67,013	71,961	71,961	71,961
Contingencies and Reserves:							
Operating Fund Contingency	-	-	-	-	-	-	-
Transfer to Fund 650 - Engineering	158,018	165,984	170,964	176,092	181,375	186,816	192,421
Transfer to Fund 520 - Capital Reserve	-	150,000	175,000	190,000	225,000	265,000	315,636
Transfer to Fund 540 - Sewer Vactor Pmt.	13,378	13,378	13,779	14,193	14,619	15,057	15,509
Transfer to Fund 600 - Comm. Dev. Admin.	80,285	107,915	111,152	114,487	117,922	121,459	125,103
Total Contingencies and Reserves	251,681	437,277	470,895	494,772	538,915	588,333	648,669
Total Uses of Funds	1,959,927	2,438,670	2,376,590	2,464,065	2,564,226	2,526,545	2,658,504
Ending Fund Balance	$ 927,646	$ 656,227	$ 655,604	$ 653,788	$ 644,494	$ 773,086	$ 873,086

Summary of Five Year Water Capital Improvement Plan

City of Milwaukie
Summary of Water CIP Funding Strategies
CUAB Preferred Option

Assumptions:	
Fund Earnings %	2.00%
Issuance Cost:	
Short-Term	2.50%
Long-Term:	
Revenue Bonds	2.50%
G.O. Bonds	2.50%

Interim Financing:	
BANs Used? (1=Y,0=N)	0
BAN Interest Rate:	4.80%
Long-Term Financing:	
Revenue Bonds:	
Life of Debt (Years)	20
Interest Rate	5.15%
Coverage Factor Required	1.10
Fund Reserve from Proceeds? (	1
General Obligation Bonds:	
Life of Debt (Years)	20
Interest Rate	4.85%
Fund Reserve from Proceeds? (	1

Fiscal Year	2004	2005	2006	2007	2008	2009
Type of Long Term Debt Issued (1=Y,0=N):						
Revenue Bonds	1	1	1	1	1	1
General Obligation Bonds	0	0	0	0	0	0

Capital Improvements Financing	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**
Capital Costs to be Funded	$704,000	$611,820	$682,159	$582,423	$388,301	$405,746
less: Grant Funding	-	-	-	-	-	-
less: Contributions Fund 515 Water SDCs	5,000	78,000	78,000	78,000	78,000	78,000
less: Contributions From Utility Rates	200,000	200,000	200,000	200,000	60,301	77,746
less: Contributions Fund 520 Water Reserve	-	250,000	250,000	250,000	250,000	250,000
Amount to be Financed	$499,000	$83,820	$154,159	$54,423	$0	$0
Interim Borrowing:						
BANs Issued:	$0	$0	$0	$0	$0	$0
less: Borrowing Cost	0	0	0	0	0	0
less: Interest Payments	0	0	0	0	0	0
plus: Interest Earnings	0	0	0	0	0	0
Net Available from BANS	$0	$0	$0	$0	$0	$0
Long-term Borrowing:						
Revenue Bonds:						
Amount Borrowed	$558,332	$93,786	$172,488	$60,895	$0	$0
less: Financing Cost	13,958	2,345	4,312	1,522	0	0
less: Reserve Funding	45,374	7,622	14,017	4,949	0	0
less: Refunding of BANs	0	0	0	0	0	0
Net Funds from Revenue Bonds	$499,000	$83,820	$154,159	$54,423	$0	$0
General Obligation Bonds:						
Amount Borrowed	$0	$0	$0	$0	$0	$0
less: Financing Cost	0	0	0	0	0	0
less: Reserve Funding	0	0	0	0	0	0
less: Refunding of BANs	0	0	0	0	0	0
Net Funds from G.O. Bonds	$0	$0	$0	$0	$0	$0
New Annual Debt Service:						
Debt Service	$45,374	$52,995	$67,013	$71,961	$71,961	$71,961
Coverage	$4,537	$5,300	$6,701	$7,196	$7,196	$7,196
Reserve Funding	$0	$0	$0	$0	$0	$0

Water System Rates and Charges

City of Milwaukie
Current and Proposed Water Rates
CUAB Preferred Option

Uniform Rate Adjustment Percent 4.17%

Billing System Code	Description	Current Rates		Proposed Rates	
		Bimonthly Base Rate	Use Charge $ per 100 Cubic Feet	Bimonthly Base Rate	Use Charge $ per 100 Cubic Feet
2	5/8" X 3/4" Meter or Smaller	5.95	1.35	6.20	1.41
3	1" Meter	8.29	1.35	8.64	1.41
4	1 1/2" Meter	13.38	1.35	13.94	1.41
5	2" Meter	20.78	1.35	21.65	1.41
6	3" Meter	51.22	1.35	53.35	1.41
7	4" Meter	72.78	1.35	75.81	1.41
8	6" Meter	129.90	1.35	135.31	1.41
20	Low Income Rate	-	1.35	-	1.41
502	2" Standby	8.85	1.35	9.22	1.41
504	4" Standby	31.88	1.35	33.21	1.41
506	6" Standby	46.41	1.35	48.34	1.41
508	8" Standby	63.02	1.35	65.65	1.41
510	10" Standby	79.61	1.35	82.93	1.41
512	12" Standby	96.21	1.35	100.22	1.41

Billing System Code	Description	Number of Accounts	Consumption Ccf	Estimated Revenue Recovery with Increase		
				Base Charge	Use Charge	Total
0	No Meter	16.83	37,607	-	53,025.87	53,025.87
1	5/8" Meter	16.00	9,205	595.00	12,979.05	13,574.05
2	5/8" X 3/4" Meter	5,864.50	667,344	218,085.49	940,955.04	1,159,040.53
3	1" Meter	252.00	61,989	13,056.71	87,404.49	100,461.20
4	1 1/2" Meter	86.17	67,140	7,205.67	94,667.40	101,873.07
5	2" Meter	150.00	193,082	19,481.20	272,245.62	291,726.82
6	3" Meter	16.00	40,425	5,121.99	56,999.25	62,121.24
7	4" Meter	7.00	49,852	3,184.12	70,291.32	73,475.44
8	6" Meter	1.00	664	811.87	936.24	1,748.11
10	Clackamas Billing	1.00	1,775		2,502.75	2,502.75
20	Low Income Rate	159.17	11,795	-	16,630.95	16,630.95
502	2" Standby	7.50	-	414.84	-	414.84
504	4" Standby	30.00	-	5,977.48	-	5,977.48
506	6" Standby	31.00	-	8,991.91	-	8,991.91
508	8" Standby	28.00	-	11,028.47	-	11,028.47
510	10" Standby	10.00	-	4,975.61	-	4,975.61
512	12" Standby	3.00	-	1,803.93	-	1,803.93
		6,679.17	1,140,878	300,734.29	1,608,637.98	1,909,372.27

Reconciliation of Revenue Requirements to Recovery of Revenues From Unit Rates

Revenue requirements for fiscal 2004 per financial model	$	1,920,628
Estimated revenue recovered from rates after uniform rate increase using fiscal 2002 customer statistics		1,909,372
add: miscellaneous rate revenues collected from unmetered water customers		6,260
Reconciled revenue recovered from rates after uniform rate increase	$	1,915,632
Percent of estimated revcovered revenue from rates after uniform rate increase to forecasted revenue requirements from the financial model		99.74%

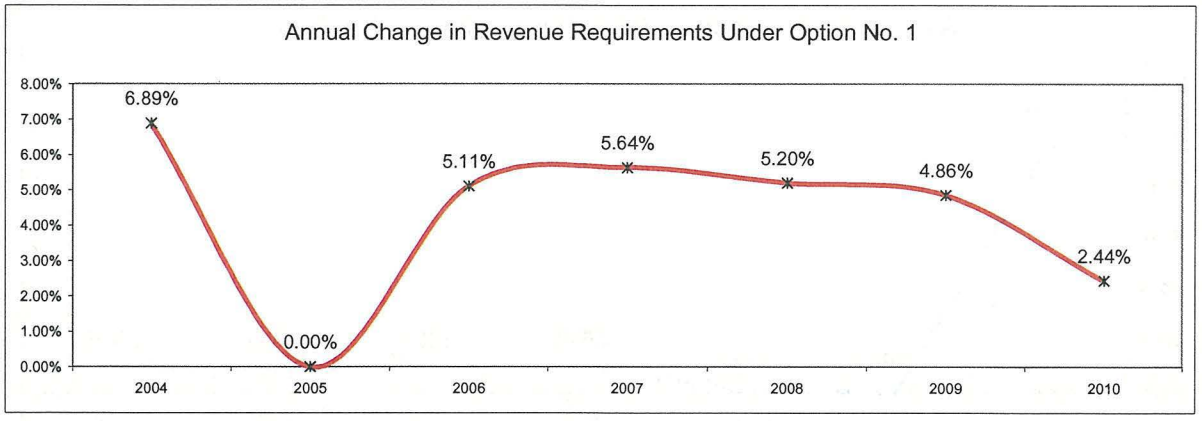
Alternative Options Reviewed by the CUAB

Option 1 – Fund legal fees from rates and start the phase-in of capital replacement funding from rates in fiscal 2005

Under this option, all of the planning and financial modeling assumptions that were used in the CUAB preferred option were held constant with the exception of how legal fees were paid and how capital replacement funding was treated. The following table lays out the numerical treatment of these two issues, and the resulting impact on the future change in revenue requirements.

City of Milwaukie
Analysis of Annual Percentage Increases in Revenue Requirements
CUAB ALTERNATIVE OPTION No. 1

Option Number and Description	2004	2005	2006	2007	2008	2009	2010
Option 1: Fund legal fees from rates and start funding depreciation in 2005 (the case presented to the CUAB on May 7, 2003	6.89%	0.00%	5.11%	5.64%	5.20%	4.86%	2.44%
Key Assumptions:							
Legal fees to be funded from rates	$ 200,000	$ 50,000	$ 50,000	$ 50,000	$ 50,000	$ 50,000	$ 50,000
Depreciation funding from rates	$ -	$ 63,127	$ 126,254	$ 189,382	$ 252,509	$ 315,636	$ 325,105



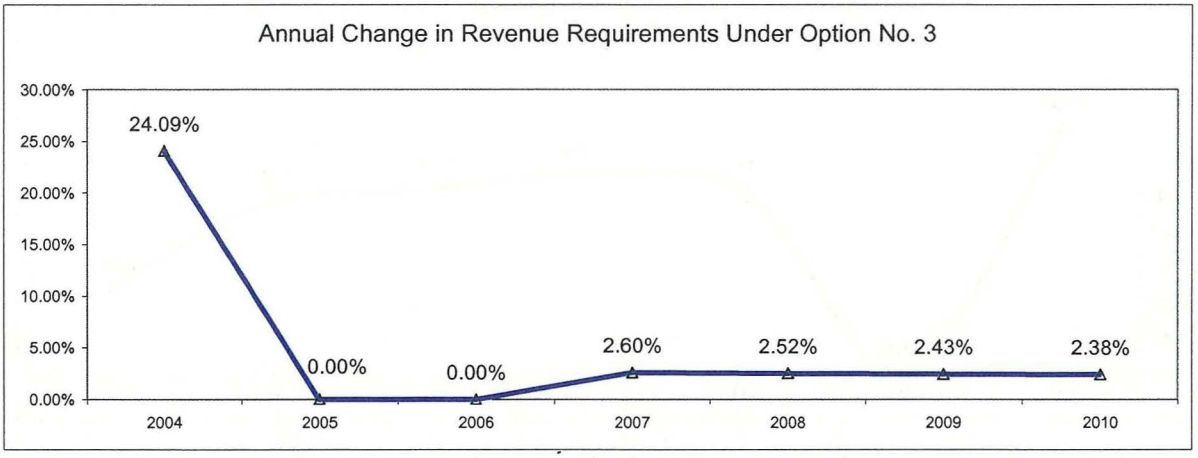
The CUAB members rejected this option for further consideration because they did not think that the rate spike that resulted in fiscal 2004 could be averted by funding anticipated legal fees from the Capital Reserve Fund balance rather than from current rate payers.

Option 2 – Fund legal fees from rates and fully fund capital replacement funding from rates in fiscal 2004

As in the case of Option 1, this option contains all of the underlying planning and financial modeling assumptions contained in the CUAB preferred approach. This option assumes that rate payers would have to immediately shoulder the burden of anticipated legal fees in addition to fund the $316,636 in depreciation expense (i.e., the estimate of current capital replacement costs). The following table lays out the numerical treatment of these two issues, and the resulting impact on the future change in revenue requirements.

City of Milwaukie
Analysis of Annual Percentage Increases in Revenue Requirements
CUAB ALTERNATIVE OPTION No. 2

Option Number and Description	2004	2005	2006	2007	2008	2009	2010
Option 3: Fund legal fees from rates and fund depreciation 100% in fiscal 2004	24.09%	0.00%	0.00%	2.60%	2.52%	2.43%	2.38%
Key Assumptions:							
Legal fees to be funded from rates	$ 200,000	$ 50,000	$ 50,000	$ 50,000	$ 50,000	$ 50,000	$ 50,000
Depreciation funding from rates	$ 315,636	$ 325,105	$ 334,858	$ 344,904	$ 355,251	$ 365,909	$ 376,886



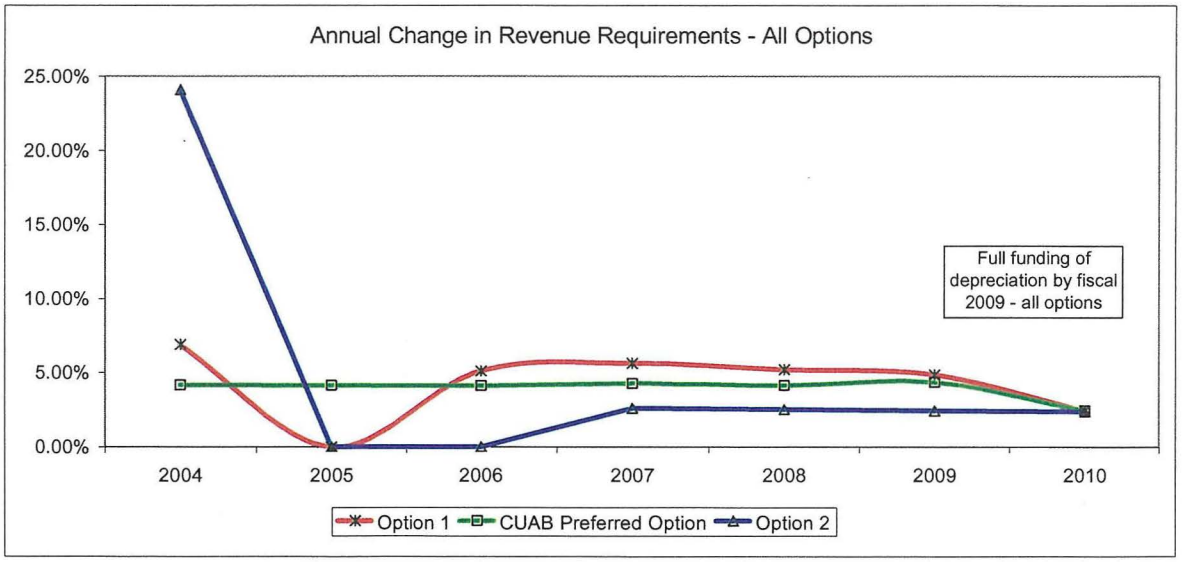
The CUAB rejected this option because of its severe impact on rates in 2004. It was felt by the CUAB members that this severe spike could be mitigated by funding legal fees from the Capital Reserve Fund and by phasing in depreciation funding over five years.

The following graphic lays out the three options on a single chart. As the data shows, the CUAB preferred option results in:

- The elimination of rate spikes in fiscal 2004
- Depreciation phasing starts immediately in 2004, and is fully funded by fiscal 2009
- This option meets the direction of the CUAB to have regular and affordable rate adjustments.

City of Milwaukie
Analysis of Annual Percentage Increases in Revenue Requirements Under Alternative Options

Option Number and Description	2004	2005	2006	2007	2008	2009	2010
Option 1: Fund legal fees from rates and start funding depreciation in 2005 (the case presented to the CUAB on May 7, 2003	6.89%	0.00%	5.11%	5.64%	5.20%	4.86%	2.44%
CUAB Preferred Option1: Fund legal fees from the CIP reserve fund and start funding depreciation in 2004	4.17%	4.13%	4.11%	4.27%	4.14%	4.35%	2.46%
Option 2: Fund legal fees from rates and fund depreciation 100% in fiscal 2004	24.09%	0.00%	0.00%	2.60%	2.52%	2.43%	2.38%



Notes:
1. Option III is not charted; it was included in the table for comparison purposes only.
2. Annual Depreciation Funding:

Year	Option 1	CUAB Option	Option 2
2004	$ -	$ 150,000	$ 315,636
2005	63,127	175,000	325,105
2006	126,254	190,000	334,858
2007	189,382	225,000	344,904
2008	252,509	265,000	355,251
2009	315,636	315,636	365,909

APPENDIX A

Issue Papers Presented to the CUAB

ISSUE PAPER No. 1

TOPIC: Recommended Fiscal Policies for Management of the Water Fund

FOR: City of Milwaukie Water and Sewer Rate Study

BACKGROUND

Our initial modeling of the City's revenue requirements and the corresponding review of its overall financial position confirms that -sound policies exist for the City's fiscal operations. The purpose of this issue paper is to document these policies and outline key additional financial directions that may guide the financial management of the water fund as well as the rate modeling process. For each key policy issue identified, we have listed options/alternatives that we can discuss for possible consideration by the City. We propose to focus discussion on the important fiscal policy issues that the City may wish to incorporate into its future operations and which will impact the modeling.

DISCUSSION OF OPTIONS AND RECOMMENDATIONS

A. Accounting Conventions/Methods The essence of the City's rate structure for water service is founded in the cost accounting system used by Milwaukie. Some municipalities, counties and cities invest substantial amounts of time and money in their "business information systems". The overriding policy guiding any information collection and archiving system should be that the cost of acquiring data not exceed the value of that data to the user. In the case of the City's water funds (Operating, SDC, and CIP reserve), the discussion should be focused on the following three key cost accounting issues:

1. Segregation of costs by type of service delivered to customers;
2. Capital fund restriction – that is, segregating and restricting balances available for funding capital construction; and
3. Methods for allocating common overhead to water, sanitary sewer and stormwater services.

Based on our preliminary analysis of the City's current cost accounting practices, it is evident that these actions are being applied

B. Reserve Policies These policies are established to ensure the financial strength and integrity of the utility enterprises. Reserve policies are generally broken down into four key subcategories which are:

1. **Operating (Working Capital) Reserves** – The user charges must be sufficient to provide cash for the expenses of operating and maintaining the City's services. To ensure the fiscal and physical

integrity of the City, cash needs will be defined to include sufficient reserves to accommodate routine fluctuations in revenues and expenses. The typical method for expressing the appropriate level of working capital reserves is in days of operating expenses. We suggest that the City consider the following target for working capital reserves:

- Water: 75 days of water system operating expenses

The rationale for the higher reserve against water expenses is the greater volatility of water revenues as compared to sewer revenues. Perhaps offsetting this is the fact that higher revenue periods occur at the start of the fiscal year, meaning that the beginning balance is normally augmented before declining revenues cause a seasonal decline in fund balances. Nonetheless, the greater exposure to revenue risk merits a somewhat higher balance, as suggested above.

2. **Equipment Reserves** – It is prudent to establish and maintain a contingency reserve to meet unexpected emergency outlays. The City currently maintains permanent water and sewer reserve funds. This reserve should represent a reasonable percentage of the original cost of total fixed assets, but should be no less than the cost to replace or repair a critical element of system equipment. We suggest that an appropriate contingency reserve level would be:

   - Water: 1% of water system fixed assets (expressed as book value; i.e., original cost less accumulated depreciation)

   Whenever contingency reserves fall below target levels, or when target levels are increased, the reserve level should be established and maintained in no more than three budget cycles. If a replacement reserve is also maintained, the replacement reserve may serve as a source of contingency funds. In such case, the above requirements are reduced to the extent of existing replacement reserves, or simply viewed as a minimum balance for replacement reserves.

3. **Replacement Reserves** – It is prudent to protect the City's investment in long-term fixed assets. A recognized method to achieve this end would be to establish a replacement reserve and funding strategy. The reserve would enable the City to support future replacement needs without extraordinary rate increases, while recognizing the potential burden on existing customers of funding both current improvements and future replacement needs. A common formula for

arriving at an appropriate replacement reserve level for the utility enterprise is as follows:

For water plant-in-service, the annual depreciation expense less scheduled principal repayments and budgeted capital improvements to be paid from rates. Often times, an absolute dollar minimum is also prescribed to be certain that a positive contribution is made for replacement of assets. It should also be highlighted that Oregon State Budget Law inhibits the ability of governmental jurisdictions to fully fund depreciation. This is due to the fact that budget law requires that monies collected under a general depreciation or replacement reserve account be expended within 10 years (while the life of many facilities is 20 to 30 years); depreciation or reserves set aside for specific facility replacement can be held for a maximum of 12 years.

4. **Bond Reserves** – The City has made use of revenue bond debt to fund improvements to the water and sewer systems. A typical covenant in the bond ordinance or loan agreement is the funding of reserves to assure repayment of interest and principal to the lender/investor. We suggest that the City consider adopting a formal policy of fully funding any such reserves with cash or reserve equivalents. Reserve equivalents in this case would be insurance policies issued by private sector municipal bond insurance companies.

C. Capital Financing Policies In order to provide reliable water service, assets must be improved and replaced on a regular basis. Without a set of deliberate capital financing policies in place, the City may not have the financing to implement this orderly improvement and replacement program. We suggest that the City consider the following policies concerning capital financing:

1. **Capital Planning** – Due to the impact of capital costs on rates and charges, and due to the variation in funding levels needed over time, we suggest that the City establish and maintain a capital projects schedule of at least five years in duration. This schedule should include project descriptions, scheduled year of construction, and total estimated costs. Each project should be identified as an improvement project or a replacement project (including repair and rehabilitation). If projects provide both improvement and replacement benefits, then the schedule should include an appropriate allocation of project costs to those two categories and then use the criteria below for the allocated portions.

2. **Improvement Projects** – Improvements to the system should be scheduled and budgeted with consideration of the rate impacts which may result. SDC improvement fees should be dedicated to funding

projects in this category, and SDC reimbursement fees considered as a supplemental source of funding. Beyond these resources, the cost of improvements would fall to utility ratepayers. In general, it should be the City's intent to make such improvements while minimizing or eliminating the need for debt. However, when annual capital outlays meet a threshold level (i.e., a specific dollar threshold for a three year period or longer), the City should evaluate alternatives including phasing, deferral, and debt financing as methods to mitigate rate impacts.

3. **Replacement, Repair, and Rehabilitation Projects** – To the extent that funds are available, replacement projects should be funded first from the replacement reserve, then through any uncommitted SDC reimbursement fees, then through unencumbered surplus fund balances, and then through rates. If the rate-funding of replacement projects results in a total rate-funded capital program exceeding a specific threshold per year, the City should evaluate alternatives including phasing, deferral, and debt financing as methods to mitigate rate impacts.

D. Rate Policies Rate and charge revenues are the lifeblood of the water fund. Without thoughtful policies guiding the construction of rates and charges, the City's financial position can rapidly deteriorate. We suggest that the City document the following policies relating to the construction of rates and charges:

1. **System Development Charges** – The City should maintain SDC's which recover eligible costs from new customers in accordance with the statutory requirements of ORS 223.297 – 223.314. Additional policy considerations would include whether such charges should emphasize equity among generational classes of customers, economic development incentives or disincentives, or maximizing equitable cost recovery from new growth. Any such policies must continue to comply with aforementioned sections of ORS 223. It is further recommended that the city account for and track the receipt of reimbursement and improvement fees separately. ORS 223.307 specifically states that "...improvement fees shall be spent only on capacity increasing capital improvements, including expenditures relating to repayment of debt for such improvements...". Conversely, reimbursement fees are not held to this specific standard, and therefore can be expended "... on capital improvements associated with the systems for which the fees are assessed including expenditures relating to repayment of indebtedness...". This distinction will give the City additional flexibility and resources to fund water and sewer system capital improvements from reimbursement fee proceeds that may not expand capacity but are nonetheless critical to the delivery of services to customers.

2. **Rate Equity** – The City should establish rates and charges which equitably recover the cost of service from its customers. Changes in rate structure should be accompanied by a cost of service analysis justifying the equity of such changes.

3. **Conservation** – The City wishes to promote efficient and conservative use of water. Therefore, water and sewer rates should, to the extent practical, promote water conservation through an emphasis on volume-based charges and allocation of the cost to appropriate variable components of the consumption based rate structure.

4. **Low Income Rates** – The City currently has in place a program that reduces water bills for qualifying low income customers. Under this program a qualifying customer is forgiven the fixed component of the rate structure (i.e., the bimonthly charge of $5.95). Under the current program, the general fund reimburses the water operating fund for this loss of revenue. The Council has indicated its desire to continue the low income subsidy program for the fiscal year beginning July 1, 2003.

City of Milwaukie – Water Rate Study

ISSUE PAPER No. 2

Issue Title: RECOMMENDED COST RECOVERY METHOD FOR DIRECT SERVICES TO DEVELOPMENT

Background Discussion: The City routinely provides services and incurs costs for new water customers that are not covered by monthly rates. The most common service is new meter installation. For a one-time and set fee, the City will install a meter for a new customer. Typically, these installations are for new developments. However, there are instances where existing customers request to have a meter changed out to accommodate increased (or decreased) anticipated usage. The City also sells approved meters to customers who, in turn, install them at their own expense and subject to final inspection by the City. There are other miscellaneous development related services that the Water Department provides and bills to customer on a scheduled basis. All of these development related fees are itemized and contained in City Resolution # 23-2002 (adopted 9/17/02). The water fees and charges that are in place have not been adjusted since 1993. Over the last three fiscal years, the City has received an average of $27,673 per year by providing these services. To put this figure in perspective, revenues recognized form water rates will amount to almost $1,800,000 this fiscal year. Clearly, development related service fees are a small part of the Water Department's revenue base.

A suggestion has been made that the City consider moving away from charging for these direct services for development on a **pre-set or scheduled** basis. The alternative is to implement a job cost approach for cost recovery where direct labor, equipment and materials are billed to a specific developer based on the actual costs incurred.

Evaluation: . The primary advantage of the job cost approach is that the City will recover its exact costs in providing the direct service on a work order basis. Under a pre-set or fee schedule basis of cost recovery, the actual costs incurred do not necessarily match the fee schedule due to timing and the scope of each individual site specific job. While accuracy of billing is a recognized advantage in the job cost approach, it is also the case that the City does see disadvantages to moving away from its pre-set or scheduled fees. These are:

3. Increased Administration for the City. In order to send an accurate bill for services rendered, the City would have to implement a system able to track time, materials, and overhead by work order. The City currently does not have a system in place to accommodate this process. Discussions with public works staff indicate that this type of system could be developed, but it would take time and unbudgeted resources.

4. Adversity for Customers. Under the current process, developers and existing customers know - up front - how much they will be charged for the services they are requesting from the City. Under the suggested time and materials approach, the City could only give the prospective developer or customer an estimate of the costs. The final cost would not be know until the job in question was completed. This "certainty" factor is important,

particularly in the case of developers, because this cost data is used to calculate the feasibility of prospective projects.

Recommendation: Milwaukie is at effective buildout. There is limited new development activity at this time. According to Public Works staff, there were only ten or twelve new service meter installations last year. If there was substantial development/redevelopment activity, it might be appropriate to commit the resources necessary to implement a job costing system. However, given the current level of development and the adequacy of development fee revenue to offset current meter installation costs, no such change is warranted.

Therefore, it is recommended that the City continue its policy of setting a schedule of fees for development related services and periodically adjusting these fees based on available actual cost of service data. An analysis of recent cost data indicates that the schedule of fees that are currently in force are adequate to recover the City's costs. Therefore, no adjustments are recommended to the development support fee schedule at this time. The current fee schedule is as follows:

WATER FEES & CHARGES IN SUPPORT OF DEVELOPMENT AND CUSTOMER SERVICES

Service and Equipment:

Connect Service 5/8" or 3/4" Residential Service	$2,460
Connect Service 1"	$2,547
Connect Service 1 1/2"	$2,923
Connect Service 2"	$3,067

Equipment:

3/4" Meter	$208
1" Meter	$301
1 1/2" Meter	$510
2" Meter	$625
Hydrant Meter Deposit	$579

Miscellaneous:

Delinquent Account – Past Due Notice*	$5
Delinquent Account – Notice of Termination*	$25
After Hours Restoration of Service* (Monday-Friday 5:00 pm to 8:00 pm; Saturday & Sunday 8:00 am to 5:00 pm)	$80
Information Research	$44/hr.
Reimbursement District Fee	To be determined by scope of project

* Accounts remaining delinquent more that three (3) months subject to 10% per year added to the outstanding balance to pay the City's interest and collection costs.

WS. 4 1

CITY OF MILWAUKIE
APPOINTED ADVISORY BOARD APPLICATION

Name: Rob Gabrish Date: 11/8/03

Street address: 12723 SE Vernic Ave 97222

Business Phone: (503) 254-2600 Home Phone: (503) 653-0024

"O"

How long have you been a Milwaukie resident? 4 yrs

Are any members of your household currently serving on a City of Milwaukie Advisory Board or Commission? If so, which one. No

Are you a registered voter in Milwaukie? yes

How did you hear about the position? Public Access Channel

Occupation: Quality Inspector Employer: Copper and Brass Sales

Employer's Address: 12815 NE Airport Wy Phone: (503) 254-2600

Please list any prior civic or professional activities. Past Exalted Ruler - Milwaukie ELKS Lodge.

Why have you applied for this position? To gain a better knowledge and understandg of the Parks/Recreation board through participation.

What special training, skills, or experience have you had that would be pertinent to this application? My past participation with various ELKS committees as well as my experience with facilitating meetings gives me good insight for participation with this/other boards.

Board(s) or Commission(s) in which you are interested. Parks and Recreation Board

Please complete this form fully so City Council can evaluate your application. Thank you for the extra time and effort. Please return to City Recorder's Office, 10722 SE Main, Milwaukie, OR 97222. If you need additional information, please call 786-7502.

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Received at City Hall _____ Information Sent _____

Interviewed _____ Appointed _____

Commission _____ Term Expires _____