



CITY OF SIGNAL HILL

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STAFF REPORT

3/25/2025

AGENDA ITEM

**TO: HONORABLE MAYOR
AND MEMBERS OF THE CITY COUNCIL**

**FROM: CARLO TOMAINO
CITY MANAGER**

**BY: THOMAS BEKELE
PUBLIC WORKS DIRECTOR/CITY ENGINEER**

**SUBJECT: CONFIRMATION OF PROPOSED RATES FOR WATER DELIVERED THROUGH THE
CITY'S DISTRIBUTION SYSTEM AND OUTLINE OF PROPOSITION 218 PROCESS**

Summary:

The 2023-2028 City of Signal Hill Strategic Plan identifies updating the Water Master Plan (WMP) and Water Rate Study (RS) as key initiatives for Fiscal Year 2024-2025. The WMP evaluates the City's water infrastructure, identifies deficiencies, and outlines a plan for necessary improvements. The RS conducts a comprehensive rate analysis, establishing a sustainable and equitable five-year tiered rate structure that integrates public engagement and City Council recommendations. In December 2023, the City entered into a professional services agreement with Dudek to assist in preparing the WMP & RS. City staff collaborated with Dudek and its subconsultant, Raftelis, to evaluate water system operations, assess financial needs, and develop recommendations.

On December 10, 2024, the City Council appointed a Water Rate Subcommittee to review the WMP, assess Capital Improvement Projects, evaluate rate structures, and analyze the reserve policy. During the Subcommittee Meeting on January 27, 2025, members reviewed the Water Division's current and projected costs, considering the financial impact of infrastructure improvements and ongoing operational expenses. After evaluating three rate structure options, the Subcommittee selected the Self-Funded option as the most viable. This option includes a 15 percent rate increase in the first two years, 14 percent in the third and fourth years, and 10 percent in the fifth year, ensuring sufficient funding for capital projects, debt repayment, and financial reserves to address consumption fluctuations and economic uncertainties. The proposed rate adjustment is driven by high-priority Capital Improvement Projects, many of which are required to meet state-mandated regulations. Additionally, revenue losses resulting from water conservation efforts have impacted the Water Division's financial stability, making a structured rate increase necessary.

On February 27, 2025, the Public Works Department presented the findings of the WMP & RS in a public workshop, outlining the three rate adjustment options reviewed by the Subcommittee. After considering the financial implications and public input, the City Council directed staff to proceed with

the Self-Funded option as the preferred rate adjustment plan. The recommended rate adjustment ensures that the Water Division can fully fund its operating expenses, capital projects, reserves, and debt service obligations over the next five years without issuing additional debt.

Following a community workshop on March 10, 2025, staff proposes implementing the recommended rate adjustments beginning in Fiscal Year 2025-2026. The proposed changes require amendments to Signal Hill Municipal Code Section 13.04.130 and confirmation to initiate a Proposition 218 Protest Hearing. Staff recommends that the City Council approve the proposed rate adjustments and authorize the necessary actions for implementation.

Strategic Plan Goal(s):

Goal No. 1 Financial Stability: Ensure the City's long-term financial stability and resilience.

Goal No. 4 Infrastructure: Maintain and improve the City's physical infrastructure, water system, and recreational spaces.

Goal No. 5 High-Functioning Government: Strengthen internal communication, recruitment, retention, systems, and processes to increase the effectiveness and efficiency of City services.

Recommendation:

1. Confirm the recommended water rate adjustments of 15% in FY 2025-26, 15% in FY 2026-27, 14% in FY 2027-28, 14% in FY 2028-29, and 10% in FY 2029-30.
2. Set a Proposition 218 Protest Hearing for May 27, 2025.

Fiscal Impact:

Pursuant to the findings of the Water Rate Subcommittee meeting on January 27, 2025, the City Council Workshop on February 25, 2025, and the Community Workshop on March 10, 2025, the recommended water rate adjustment would allow the Water Division to fully fund its operations, capital projects, reserves, and debt service over a five-year rate adjustment without the need to issue new debt. The proposed water rate adjustments are as follows:

Year	Rate Increase
FY 2025-2026	15%
FY 2026-2027	15%
FY 2027-2028	14%
FY 2028-2029	14%
FY 2029-2030	10%

This option also includes a one-time \$3 million bridge loan from the General Fund to the Water Enterprise Fund to support the Gundry Reserve Roof Replacement and Rehabilitation Project. In addition, this option avoids additional debt, helping to maintain the financial stability of the City's

Water Division, which currently holds \$12.8 million in existing loans and debt, with \$6.8 million still outstanding in subsequent years.

Background:

The City's Water Division is responsible for the operation of the City's water system, guaranteeing the efficient distribution of potable water to more than 3,000 customers. In addition to employing professionals with the required training, certification, and experience to service and maintain the City's complex water system, the Water Division must also implement a capital program that regularly replaces and upgrades aging infrastructure to meet evolving safety standards. Due to continuously updated State water quality standards as well as the needs of the City's aging system, the City conducts a water rate study to assess the operating and capital needs of the Water Division and recommend rate adjustments as necessary. Given the important public health responsibilities associated with maintaining the water system, periodic rate adjustments are necessary to ensure the system remains financially solvent.

The City of Signal Hill's Water System is supplied by a combination of imported water from the Metropolitan Water District (MWD) and groundwater extracted from the Central Basin through three city-owned wells: Well 7 and Well 10, located in Long Beach, and Well 9, located at the City Yard in Signal Hill. The City's water infrastructure includes three storage reservoirs and three booster pump stations at Gundry, Temple, and Hilltop. Groundwater treatment facilities are located at Gundry and Well 9, ensuring that potable water is safely distributed through 50 miles of pipeline, ranging from 4 to 20 inches in diameter. Water collected from Wells 7 and 10 is pumped to Gundry Treatment Plant where the Gundry Reservoir functions as a critical forebay for the broader distribution network. Gundry Reservoir functions as a forebay to the distribution lines. Well 9, in contrast, undergoes an advanced on-site treatment process, utilizing a three-stage nano-filtration system followed by liquid granular activated carbon (LGAC) treatment. Given the City's geography, the City's water system operates within three primary pressure zones (Zones 1 through 3) and a subZone 3A. To enhance supply reliability, the system maintains two emergency connections with the cities of Long Beach and Lakewood.

Water Master Plan and Rate Study

On December 12, 2023, the City Council awarded a contract to Dudek to update the WMP and RS, which were last updated in 2018 and 2019, respectively. The RS assessed the Water Division's five-year capital needs while also considering the community's ability to afford essential water services. The WMP serves as a comprehensive strategy for managing, distributing, and conserving the City's water resources over the next ten years. Key components of the WMP include an assessment of current and future infrastructure needs to support the water system, an evaluation of water supply and demand, and recommendations for necessary improvements. The WMP also outlines maintenance requirements to ensure the system remains in good standing, provides a structured approach to addressing deficiencies, and includes a prioritized list of projects and recommendations for infrastructure improvements necessary to comply with the latest State Water Board regulations.

The objective of the RS is to assess the water system's revenues and expenditures and develop a sustainable, equitable, five-year tiered rate structure that incorporates recommendations from the WMP to ensure adequate funding for operations and capital improvements. The City's water system revenue primarily comes from customer water rates, structured by usage tiers and customer

classifications (residential, commercial, industrial, and irrigation). Additional revenue sources include connection fees and potential state or federal grants. The Water Development Fund also generates revenue by collecting fees from developers to support capacity enhancements required for new developments; however, contributions are inconsistent and cannot be relied upon as a stable funding source. Water system expenses include costs for water supply, maintenance, system upgrades, administrative operations, and debt service payments. The RS establishes a rate structure that aligns revenues with expenditures while incorporating the WMP's recommendations, ensuring the long-term financial stability of the water system.

Factors Impacting WMP & RS Recommendations

The WMP and RS recommendations are shaped by the City's infrastructure needs and financial challenges. A water rate adjustment is essential to address unfunded state and federal mandates, aging infrastructure, declining revenues from conservation efforts, rising water purchase costs from the Water Replenishment District (WRD) and MWD, and increasing operations and maintenance expenses. Without an adjustment, the City risks service disruptions, regulatory non-compliance, and an inability to fund critical infrastructure projects. Some of the most significant factors driving the rate structure recommendations include:

Water Capital Improvement Projects & Regulatory Compliance

The City's Water Capital Improvement Project (CIP) plan, a key driver of the proposed rate increase, addresses deferred maintenance and compliance with unfunded state and federal mandates. These regulations require significant infrastructure upgrades to maintain water quality, adding financial burdens and creating challenges to the City's efforts to reduce dependence on imported water. For instance, while the Water Division completed Well 10 in 2022, it remains offline due to new PFOA/PFOS testing requirements and the need to update several operational manuals and procedures. In order to comply, the Water Division must replace well components with NSF 61-certified materials or demonstrate equivalency. Additionally, the City must update its Operations and Maintenance Standards and revise its disinfection strategy to meet evolving regulations, further limiting efforts to decrease reliance on imported water from MWD.

A recent State Water Board survey confirmed the City's water quality but identified essential capital projects, including:

- Replacing 110,000+ linear feet of AC pipes at \$550-\$900 per foot.
- Clearing vegetation at Temple Reservoir and constructing a new disinfection station at \$400,000, with annual chemical costs of \$50,000-\$70,000.

The proposed water rate adjustment is required to fund these projects, ensuring service reliability, regulatory compliance, and long-term sustainability.

Impact of Conservation on Revenue

The 2019 rate adjustment did not account for a significant drop in water consumption. Following the 2021 statewide drought emergency, the State enacted Level II conservation measures, reducing per

capita water use from 146 gallons/day in 2020 to 119 gallons/day in 2023. This 67-million-gallon reduction resulted in revenue losses of \$600,000-\$900,000 over four years. Despite the Governor lifting drought restrictions in 2024, laws such as AB 1572 continue to enforce conservation efforts, impacting revenues.

Aging Infrastructure & System Failures

The City's aging infrastructure continues to impact system reliability, driving the need for rate adjustments. Many pipelines, reservoirs, and treatment facilities have exceeded their useful life, leading to rising maintenance costs and emergency repairs. A primary concern is the aging cast-iron pipes, which frequently leak, resulting in water loss and costly repairs. Over the past two years, the City repaired more than 20 mainline leaks at a total cost of approximately \$360,000 in emergency repairs. To mitigate further failures, the proposed CIP plan includes replacing 1.5% of asbestos cement and cast-iron pipes annually. Other critical infrastructure concerns include the Gundry Reservoir, built in 1929, which has surpassed its expected lifespan. The treatment facility's tank walls, also constructed in 1929, require structural improvements, while high-pressure valves and pressure-reducing stations from the 1960s and 1980s need replacement. Additionally, Well 7, built in 1978, has significantly deteriorated. Once operating at 1,830 GPM, its output has declined to 900 GPM, reducing capacity by nearly half. The water rate study includes the replacement of Well 7 in years 3 to 5, with an estimated cost of position to Supervisor, overall operations and maintenance costs continue to rise. Increased \$5.5 million.

Rising Operations & Maintenance Costs

The City's Water Division operates at all time to ensure compliance with stringent water quality monitoring requirements. While there have been no major changes to salaries and benefits outside of a single reclassification of a Senior Operator, costs include:

- Higher chemical and insurance expenses, with insurance alone totaling \$500,000 annually, which is more than a \$200,000 annual increase from the last time new rates were adopted in 2019.
- Growing debt service obligations tied to infrastructure projects and regulatory compliance.

Increased Water Replenishment & Imported Water Costs

Between 2020 and 2024, WRD's replenishment assessment fee increased 15% (\$382 to \$437 per acre-foot), while MWD's imported water cost rose 30% (\$1,078 to \$1,395 per acre-foot). With 70% of the City's supply from WRD and 30% from MWD, these increases have added at least \$200,000 in ongoing annual costs.

Well 9 Advanced Water Treatment Project

Completed in 2016, Well 9 was designed to enhance groundwater pumping but now produces only 650 GPM instead of the intended 1,200 GPM due to sediment issues. The City plans to redevelop the well and install a turbine pump as part of the Five-Year CIP plan.

Reserve Policy for Financial Stability

The City's reserve policy ensures long-term financial resilience, with three key components:

1. Capital Reserve - 50% of the five-year CIP average to fund infrastructure projects and unexpected failures.
2. Rate Stabilization Reserve - 15% of commodity revenue to buffer revenue fluctuations and prevent sudden rate spikes.
3. Operating Reserve - 365 days of operating cash to cover expenses during revenue shortfalls or emergencies.

These reserves enhance financial stability while supporting necessary water system improvements.

Water Rate Study Options

Dudek and Raftelis completed the WMP, evaluation of revenues and expenditures, and provided the following three five-year rate adjustment options for the Subcommittee and City Council consideration:

Option 1: Self-Funded CIP

This approach involves a phased rate increase of 15% in the first two years, 14% in the third and fourth years, and 10% in the final year. By relying solely on existing cash reserves and future revenues, this option avoids debt issuance entirely, making it the most fiscally conservative strategy.

A primary advantage is the elimination of interest payments, resulting in significant long-term cost savings. Additionally, the City gains immediate and unrestricted ownership of all completed infrastructure assets, free from long-term financial obligations. However, the key challenge of this approach is the requirement for substantial upfront rate increases to generate the necessary funding.

Option 2: Partially Debt-Financed CIP

This option proposes rate increases of 14% in the first year, 12% in the second, 10% in the third, and 8% in the fourth and fifth years. A \$9 million bond would be issued in the fourth year, allowing the City to distribute the cost of infrastructure improvements over time while mitigating immediate rate increases. By leveraging bond financing, critical projects can be completed without exhausting cash reserves, preserving financial flexibility for operational needs and unexpected expenses. If market conditions are favorable, securing a low-interest rate could reduce the long-term cost of borrowing, making this a strategic financing tool.

However, this approach introduces long-term debt, increasing overall project costs due to interest payments. Additionally, future ratepayers will be responsible for servicing the debt even after projects are completed, potentially necessitating further rate increases. The City will also be subject to debt covenants, which may impose financial restrictions and limit budgetary flexibility. While this option helps moderate initial rate increases, it ultimately increases long-term capital costs due to interest expenses.

Option 3: Partially Debt-Financed CIP

This option implements a consistent annual rate increase of 9% over five years, coupled with the issuance of two bonds: \$6 million in the third year and another \$6 million in the fifth year. This structure reduces the immediate financial burden on ratepayers while ensuring that infrastructure projects are completed in a timely manner. Additionally, by spacing out the bond issuances, the City can preserve cash reserves and maintain greater financial flexibility.

However, this model results in the highest overall debt obligations, leading to increased interest costs and a greater total expenditure on capital improvements. It also exposes the City to market risks, particularly if interest rates rise before the second bond issuance. Managing multiple bonds adds financial complexity, requiring strict compliance with debt covenants and careful credit management. While this option minimizes short-term rate increases, it could necessitate future rate hikes to accommodate rising debt service costs, potentially restricting funding for new projects or emergency needs.

Subcommittee Meeting

On December 10, 2024, the City Council appointed a Water Rate Subcommittee to review the WMP and associated CIP, evaluate various rate structures, and assess the reserve policy. The Water Rate Subcommittee is comprised of the following members:

Robert D. Copeland	Council Member
Charlie Honeycutt	Council Member
Carlo Tomaino	City Manager
Yvette Aguilar	Deputy City Manager
Matthew Richardson	City Attorney
Thomas Bekele, P.E.	Public Works Director/City Engineer
Siamlu Cox	Acting Finance Director
Margarita Beltran	Contracts Manager
Greg Ripperger	Dudek Consultant
Kevin Kostiuik	Raftelis Consultant

The Subcommittee met on January 27, 2025, and received a presentation covering water rate history, water system funds, reserve practices and policies, cost of service analysis, and factors driving the need for a rate adjustment. The Subcommittee Meeting consisted of a presentation on a financial analysis performed by Dudek, Raftelis, and City staff that included water rate history, water system fund accounts, water fund reserve policies, and cost factors driving the need for a rate adjustment. The Subcommittee reviewed three five-year rate adjustment scenarios for consideration and recommended Option 1 as the preferred choice. This option avoids additional debt, helping to maintain the financial stability of the City's water department, which currently holds \$12.8 million in existing loans and debt, with \$6.8 million still outstanding in subsequent years.

City Council Workshop

The City Council Workshop took place on February 25, 2025, during which the City Council received a presentation on the WMP assessment, recommendations, and a rate analysis outlining three

proposed rate options and reviewed the Subcommittee's recommendations. During this meeting, the City Council approved a \$3 million Inter-Fund Loan Agreement between the City's General Fund and Water Enterprise Fund to fund the Gundry Reservoir Roof Replacement and Rehabilitation Project, directed staff to proceed with option 1 rate structure, and instructed staff to proceed with the prop 218 process and schedule a tentative date to conduct a Proposition 218 hearing.

Analysis:

Community Workshop

The City held a second workshop to present the WMP & RS, review state study options, discuss recommendations from the City Council and Subcommittee, and gather community input. On March 10, 2025, the community workshop took place in the City Council Chambers, with five residents in attendance. City staff provided a comprehensive presentation on the water rate analysis and addressed residents' questions. The meeting was interactive, with participants seeking clarification on various aspects of the water system and proposed rate adjustments.

During this workshop, community members raised several questions, including the purpose of the workshop, the maintenance and operation of Well 9's treatment system, the servicing schedule for the City's water valves, and the timeline for Well 10 to become operational. Residents also inquired about the current structure of water consumption tiers, potential cost recovery for Well 9 expenses, meter size change requests, and the impact of deregulation on utility costs.

City staff explained that the workshop aimed to provide transparency and thoroughly addressed all questions raised. Staff also engaged in follow-up conversations, phone calls, reviewed reports provided by some residents, and conducted one-on-one meetings with residents who requested further clarification. Staff understand that residents or rate payers may have additional questions as they review the Master Plan and proposed rate structure and is committed to providing clear responses to all inquiries.

By the end of the workshop, there was a general consensus that a five-year rate adjustment was necessary for the Water Division to maintain the City's water system and infrastructure in optimal condition, fully fund operating costs, and implement required system upgrades to comply with the latest regulations without incurring new debt.

Proposition 218 and Water Rate Adjustments

Proposition 218, known as the "Right to Vote on Taxes Act", regulates the process by which local agencies impose or increase property-related fees, such as water service charges. Proposition 218 requires that water rates maintain a clear and direct relationship between costs incurred and the rates charged, establishing key requirements to guarantee transparency and fairness in rate-setting. Revenues collected from property-related charges imposed by a public agency must not exceed the costs required to provide the corresponding services. Additionally, these revenues must be used exclusively for the purpose for which they were imposed, and fees may only be charged for services that are actively used or immediately available to the property owner.

To ensure public participation, the City is required to mail a written notice of any proposed fee or charge to all record property owners and tenants responsible for paying water service charges at

least 45 days before a public hearing, during which all written protests will be considered. The notice must include the proposed rate structure, the rationale for the rate increase, basis for rate calculations, and details of the public hearing, allowing affected parties ample time to review and respond.

At the public hearing, property owners and customers or rate payers have the opportunity to submit oral comments or written protests. Written protests must include the protestor's name, parcel address, and signature. Each parcel is limited to one protest submission, and electronic or email submissions are not permitted. If more than 50% of affected property owners or customers of record submit written protests, the proposed rate increase cannot be adopted. If a majority protest is not received, the City Council may proceed with adopting the proposed water rates.

By adhering to these procedures, the City ensures transparency, provides the public with meaningful participation opportunities, and safeguards against excessive or unjustified rate increases. These measures reinforce the City's commitment to maintaining equitable and legally compliant water rate structures that align with the principles established under Proposition 218.

Next Steps

In accordance with Proposition 218, the City must notify property owners and ratepayers of any proposed water rate adjustments and hold a public hearing at least 45 days after mailing the notices. Staff recommends public hearing date of May 27, 2025, to provide sufficient time for public notice and input. If a majority protest is not received, the City Council may proceed with adopting the proposed water rates, which include a 15% increase in FY 2025-26, a 15% increase in FY 2026-27, a 14% increase in FY 2027-28, a 14% increase in FY 2028-29, and a 10% increase in FY 2029-30. Staff will bring forth an Ordinance amendment to the existing municipal code in April 2025 as part of the process of updating the current rates.

If approved, staff would proceed with mailing and publishing the Notice of Proposition 218 Public Hearing (Attachment A), tentatively scheduled for March 28, 2025, but no later than 45 days before the Proposition 218 hearing on May 27, 2025. In accordance with Signal Hill Municipal Code Section 13.040.130, the water rates are adopted by resolution if approved. The proposed water rate structure would take effect on July 1, 2025.

Reviewed for Fiscal Impact:

Siamlu Cox

Attachment:

A. Draft Notice