Agenda Report

Fullerton City Council

MEETING DATE:	**NOVEMBER 18, 2025**
TO:	**CITY COUNCIL / SUCCESSOR AGENCY**
SUBMITTED BY:	**STEPHEN BISE, P.E., PUBLIC WORKS DIRECTOR**
PREPARED BY:	**TODD P. LE, P.E., PRINCIPAL WATER ENGINEER** **ANDREW GRAJEDA, WATER SYSTEM MANAGER** **RICHARD ARMENDARIZ, ASSISTANT DIRECTOR OF PUBLIC WORKS** **GAR HUANG, ASSOCIATE WATER ENGINEER**
SUBJECT:	**2025 WATER RATE STUDY REPORT STUDY SESSION**

SUMMARY

Review the draft 2025 Water Rate Study Report, which provides an evaluation of the revenue needs for the City of Fullerton Water Fund and recommendation for a multiyear water rate increase and structure adjustments.

PROPOSED MOTION

Provide direction on the proposed water rate adjustments.

ALTERNATIVE OPTIONS

Other options brought by City Council.

STAFF RECOMMENDATION

Staff recommends the proposed motion.

CITY MANAGER REMARKS

None.

PRIORITY POLICY STATEMENT

This item matches the following Priority Policy Statements:

- Fiscal and Organizational Stability
- Infrastructure and City Assets.

FISCAL IMPACT

The Fullerton Water Division, which includes water operations and water capital improvements, is supported by an enterprise fund, Water Enterprise Fund (Fund 44). Enterprise funds are self-supporting funds that recover the costs of service (capital, operations, and maintenance) through revenue from fees and user charges. The typical mechanism for revenue collection for the Water Fund is through the City's utility bill.

The recommendations from the 2025 Water Rate Study are to ensure the Water Fund continues to be self-supporting and not require supplemental funding from other City revenue sources, such as the General Fund, for the next 10-years. The revenue will provide for operational expenses, needed pipeline replacement, and high priority reservoir, well, and pump replacements/upgrades. The proposed rates are intended to establish fiscal stability for the Water Fund. Without a water rate increase, the Water Fund balance will continue to decrease, resulting in a projected deficit of $65 million by 2031 with scheduled improvements required in the Water Master Plan.

The Water Rate Study projects that the proposed water rate modifications will result in additional revenues of approximately $2.6 million in Year 1 (rates effective April 1, 2026) and reach $30.5 million in Year 5 (rates effective April 1, 2030).

BACKGROUND AND DISCUSSION

The City owns a full-service water system that produces and distributes water to all properties within the City service area which involves operating and maintaining underground piping, storage reservoirs, wells, pumps, and fire hydrants. The City is responsible for the water system and property service up to the water meter.

The system relies on a combination of imported water and local groundwater to meet its water needs. The City works together with two primary agencies, Metropolitan Water District of Southern California (MWD) and Orange County Water District (OCWD) to purchase and provide a safe and reliable drinking water supply.

The Fullerton Water Division provides water to over 32,000 services, including for residential and commercial uses, fire line building protection, required street fire hydrant coverage, and all City facilities (irrigation, public restrooms, community centers, splash pads/spray pools, Laguna Lake, etc.). The system is designed to meet the demands required for adequate fire flow protection, not the actual usage of the services. There is no recycled/reclaimed water system in the City or adjacent areas to offset these needs.

DISCUSSION

A previous Water Rate Study was completed in 2019; City Council approved a phased five-year rate increase ending in Fiscal Year (FY) 2023-24. These current rates were expected to provide sufficient funding for approximately 5 years; however, since 2019, there have been considerable unforeseen global and regional changes that have negatively impacted the Water Fund. The following describes the drivers that initiated the need for this Study, and a general description of the solutions that were used to address those challenges.

Driver: The 2019 Rate Study adopted a rate schedule through the 2023-24 fiscal year.

- **Solution:** Update the Water Fund financial plan and rates to meet the revenue needs over the next five years.

Driver: The Water Fund has experienced revenue shortfalls relative to the projected revenue from the 2019 Study due to a period of high inflation, and increases in wholesale water costs and capital costs, and combined with a gap in rate adjustments since July 2023.

- **Solution:** Adjust water rates to meet revenue sufficiency and establish a sustainable path forward for the Water Fund to meet operating and capital needs.

Driver: The City's water distribution system continues to experience above-average pipe breaks which are expensive to repair and disruptive to the community. Additionally, pumps, wells, tanks and other water assets are approaching or have aged beyond their useful lives and need replacement.

- **Solution:** Include in the financial plan an increase in capital spending to address the system's pipe replacement needs and replacement of other critical infrastructure.

Driver: The legal environment in California (namely Proposition 218) has significantly increased the burden of proof required of public utilities to demonstrate that the rates being charged for utility service are proportionate to the cost of providing the utility services.

- **Solution:** Conduct a full cost-of-service allocation analysis and make rate structure modifications, as appropriate, to support inter- and intra-class equity in rates charged to customers.

In September 2022, City Council awarded a professional services contract to Stantec Consulting Services, Inc. (Stantec) to update the City's Water Master Plan and prepare a Water Rate Study based on the results of the Master Plan. The Water Master Plan, which details the system maintenance and improvement needs, was received and filed at the April 1, 2025 City Council meeting. This Study consisted of the following phases:

1. Revenue Sufficiency Analysis (RSA) – The Study developed a multi-year financial forecasting model for the Water Fund to determine the level of annual rate revenue required to satisfy projected annual operating costs, debt service expenses, and capital cost requirements while maintaining adequate reserves. In the RSA, Stantec evaluated the sufficiency of the Water Fund's rate revenues to meet current and projected financial requirements over a 10-year projection period and determined the level of rate revenue increases necessary over the next five years to provide sufficient revenues to fund cost requirements. Input data and key assumptions were reviewed with City staff, and several alternative capital spending scenarios were evaluated by both staff and the City's Infrastructure and Natural Resources Advisory Committee (INRAC) during the RSA. This process generated a recommended financial plan and corresponding annual rate increases.

Like many utilities around the state and country, the City is currently facing challenges of aging infrastructure. Many of the City's wells, pump stations, and reservoirs have reached the end of their useful service life, and requirements to address per- and polyfluoroalkyl substances (PFAS) in groundwater have added to the Water Fund's capital investment needs. In addition, over 50% of the City's approximate 430 miles of water distribution pipes are over 50 years old. The City has often experienced over 100 water main breaks per year, which is among the highest rate of breaks per 100 miles of pipe in Orange County. These pipe breaks are a nuisance to residents and local business, they are expensive to repair, they damage homeowners' properties in extreme cases, and consequently they are a drain on the City's financial and staffing resources.

City staff evaluated multiple alternative capital improvement program (CIP) project schedules spanning the period from FY 2026 through FY 2035 (fiscal year 2026 spans the period from July 1, 2025 through June 30, 2026). These projects were identified in the City's recently updated 2025 Water Master Plan, also prepared by Stantec, and are necessary for the long-term health of the system. These CIP alternatives were evaluated with the **goal of balancing the need to address critical infrastructure deficiencies while minimizing water rate increases**. The final recommended CIP totaled approximately $269 million (in current dollars) over the period of FY 2026 through FY 2035. This CIP includes a ramp-up in spending on water main replacement, reaching the goal of replacing approximately seven miles per year by FY 2030. A pace of seven miles of pipeline replacement per year would result in replacing the entire distribution system over the course of approximately 60 years.

The 5-year rate revenue adjustment plan is presented in Table 1. It is important to note that, while in Year 1 rate revenues across all customer classes will increase by 5%, the proposed rate structure adjustments (discussed further below) will result in the average single-family residence with a 5/8-inch meter experiencing an increase of less than $3 to their monthly bill. Results will vary among different customers due to the proposed rate structure adjustments. To be clear, some customers' bills will increase by more than the average rate revenue adjustment for Year 1, while other customers' bills will increase by less.

Due to the factors discussed above regarding historical cost increases and future infrastructure investment needs, staff recommends the schedule of water rate revenue increases presented in Table 1.

Table 1: Proposed Plan of Water Rate Revenue Increases

Rate Adjustment Date	Rate Adjustment
April 1, 2026	**5.0%**
April 1, 2027	**12.0%**
April 1, 2028	**12.0%**
April 1, 2029	**12.0%**
April 1, 2030	**7.0%**

2. Cost-of-Service Analysis (COSA) – Using the revenue requirements from the RSA for FY 2026, Stantec performed a detailed COSA based upon principles outlined by AWWA and other generally accepted industry practices to determine the proper distribution of costs and corresponding revenue requirements. The purpose of a COSA is to allocate the cost of providing water service so that the revenue requirements of the utility may be equitably collected through rates. The COSA included the following steps:

- Step 1: Allocate costs to the appropriate activities/functions
- Step 2: Allocate the costs of each function to specific system parameters
- Step 3: Calculate unit costs
- Step 4: Credit non-rate revenue

3. Rate Structure Analysis – The Study developed specific rate schedules to recover the identified level of required rate revenue. The recommended rate schedules were designed to:

- Fairly and equitably recover costs through rates;
- Conform to accepted industry practice and legal requirements; and
- Provide fiscal stability and recovery of fixed costs of the system.

The City's existing water rate design is a two-part structure comprised of a Fixed Service Charge that is assessed based on meter size and a consumption-based rate (as measured in thousands of gallons or "TGAL") that is assessed based on the total amount of water that is used. Additional details that describe the City's current rate structure are included in the full report. This Study proposes to maintain the existing basis for determining rates with adjustments made to maintain consistent underlying allocations of costs to specific components of the rate structure. Specifically, the tier allocations (i.e. the amount of water allowed in each respective tier) are calculated based on the amount of water available from each source of water supply. Based on changes in water consumption patterns, tier allotments required updates to maintain the same alignment with the volume of supply from each source.

Table 2 shows the proposed rates effective April 1, 2026. The complete list of rate schedules through April 1, 2031 are provided in the complete report.

Table 2: Proposed Rates, Effective April 1, 2026

Fixed Charges

Meter Size	Monthly Rate
5/8" & 3/4"	**$36.65**
1"	**$58.35**
1 1/2"	**$112.59**
2"	**$177.68**
3"	**$351.25**
4"	**$546.53**
6"	**$1,088.95**
8"	**$1,739.86**
10"	**$2,607.73**
12"	**$3,665.45**

Tiered Usage Rates (for Residential accounts)

Tier	Rate (per TGAL)	Single Family Monthly Allocation	Multi-Family Monthly Allocation
1	$3.80	11,900 gal.	5,000 gal.
2	$6.99	17,800 gal.	7,800 gal.
3	$7.52	All Add. Usage	

Uniform Usage Rates (for Non-Residential accounts)

Rate ($ per TGAL)
$4.62

<u>Attachments:</u>

- Attachment 1 – PowerPoint Presentation
- Attachment 2 – Water Rate Study Draft Report

cc: Interim City Manager Eddie Manfro