



COUNTY SANITATION DISTRICTS OF LOS ANGELES COUNTY

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GRACE ROBINSON HYDE
Chief Engineer and General Manager

June 5, 2019

Board of Directors
County Sanitation District No. 8
of Los Angeles County

Dear Directors:

Wastewater Budget Matters for Fiscal Year 2019-20

The agenda for the Board meeting on June 12, 2019, contains an item relating to wastewater budget matters for fiscal year (FY) 2019-20. These matters include establishing an appropriations limit on the proceeds of taxes, adopting the sewerage system final budget, requesting the tax levy, and authorizing appropriations per the sewerage system budget.

APPROPRIATIONS LIMIT

The Constitution of the State of California places a limit on the authorization to expend the proceeds of taxes levied by state and local governments in California. In addition, the Government Code requires the governing body for each local jurisdiction to establish, by resolution, an appropriations limit for each fiscal year. The appropriations limit for FY 2019-20 has been determined by adjusting the previous limit for FY 2018-19 based upon population change factors for Los Angeles County and the change in the California Personal Per Capita Income. The appropriations limit has also been adjusted to include the increased operation and maintenance costs of secondary treatment needed to comply with federal requirements. All of this is in accordance with the procedures outlined in Article XIII B of the Constitution and Section 7910 of the Government Code. The proposed appropriations limit and anticipated tax revenue are shown in Exhibit No. 1. This information has been available to the public at the Districts' Joint Administration Office in conformance with the requirement that the documentation used in the determination of the appropriations limit be available fifteen days prior to its establishment by the Board of Directors.

FINAL BUDGET FOR FISCAL YEAR 2019-20

Enclosed for your review is the proposed final budget for FY 2019-20, a list of proposed capital projects, and information on the monies set aside in various funds/reserves. The final budget provides a comparison with the current 2018-19 budget and a breakdown of the items included in the budget. It is divided into three sections: anticipated expenses, projected revenues, and transfers to or from reserves. In preparing the budget, it is projected that the general revenue sources available to the District for meeting

expenses during the coming fiscal year include a pro rata share of the ad valorem (property) taxes, service charges, industrial wastewater surcharges, grants, state low-interest loans, interest income, and contract revenue. In addition, monies will be utilized from both the Joint Outfall and District's Capital Improvement Funds (restricted funds for the accumulation of connection fees paid by new users) to cover the cost of expansion-related capital projects. Finally, previously accumulated monies in the unrestricted and designated reserves will be used to help fund the construction of capital improvements.

The budget has been prepared in accordance with the Joint Administration and Joint Outfall Agreements. These agreements allocate Joint Administration and Joint Outfall costs to each signatory District according to the ratio of the number of sewage units in a District to the total number of sewage units in all the Districts signatory to each agreement. A sewage unit represents the average daily sewage flow and strength (measured in terms of chemical oxygen demand and suspended solids) from a single-family home. This method of allocating costs considers flow as well as the strength of sewage from all types of users and is the most equitable way to distribute Joint Administration costs.

WASTEWATER FINANCIAL RESERVE POLICY

The Board has adopted a wastewater financial reserve policy for the District. Maintaining prudent financial reserves provides the resources to allow the District to continue to fulfill its commitment to deliver reliable and high quality service to its customers.

The policy creates certain reserves (unrestricted, designated, and restricted) and establishes targeted goals for each of those reserves. The goals serve as a guideline to staff in preparing budgets and proposing rates for the Board's consideration. The policy anticipates that there will be fluctuations in the reserves, with periodic draws taking place, and calls for a plan to replenish reserves when they drop below certain levels. At the beginning of fiscal year 2018-19, District No. 8 was at 48% of its targeted goal, significantly below the level requiring the development of a plan to replenish the fund.

The current planned rate increases of \$6 per year under the existing rate ordinance (adopted in 2017 and providing for rate increases through fiscal year 2020-21) are not sufficient to restore reserves to the target level. In fact, reserves are projected to decrease further. This is due to significant sewer rehabilitation work that is necessary to safely convey the District's wastewater. In order to replenish and maintain reserves through fiscal year 2020-21, staff is recommending that the District borrow an estimated \$11.7 million from its Capital Improvement Fund to meet its short-term cash flow needs, as provided for in the reserve policy. The loan will be repaid, with interest, over time. In order to ensure the loan can be repaid and to ensure reserves do not further decline, it is anticipated that rates will need to increase at least 5% per year starting with the next rate cycle beginning in 2021-22. Staff will evaluate and update the reserve levels and brief the board further at that time.

SIGNIFICANT EXPENDITURES

Most of the issues outlined below relate to the Joint Outfall System (JOS). This is the system of trunk sewers and treatment plants jointly owned by the seventeen Districts signatory to the Joint Outfall Agreement. The costs for the JOS projects shown are the combined total for all of the JOS Districts, not the proportionate share for which this District is responsible. Each District in the JOS is required to pay its share of the costs based on the number of equivalent users (sewage units) in that District. The share of each project cost for which this District is responsible is shown on the attached budget pages. In addition, District No. 8 has costs related to local sewers specifically owned by the District. Those costs are solely borne by District No. 8.

Operation and Maintenance (O&M) – In general, O&M expenditures in the JOS increase at the rate of inflation. No significant changes in O&M-related activities are anticipated at this time.

Sewer System Repair and Rehabilitation – One of the naturally occurring processes in sewer systems is the formation of hydrogen sulfide gas. Through a series of complex biological and chemical reactions this gas is transformed into sulfuric acid, which can lead to extensive corrosion of the sewers. In an effort to slow down the corrosion rate and to control odors, iron salts and sodium hydroxide are routinely added to the sewer system and the crowns of the sewer pipes are sprayed with acid-neutralizing magnesium hydroxide. Although the chemical addition has reduced the rate of corrosion, it has not eliminated the problem. Where feasible, the Districts' sewer rehabilitation program utilizes technological advancements for the in-place repair of sewer lines by inserting corrosion-resistant liners into the sewers. These liners restore the structural integrity of damaged lines and represent a permanent solution as they prevent further corrosion from occurring. In some instances, corroded sewers are being replaced with pipelines containing corrosion-resistant material. For fiscal year 2019-20, capital expenses related to the repair and rehabilitation of the Joint Outfall sewer system (i.e. those sewers jointly owned by the 17 Districts signatory to the Joint Outfall Agreement and for which District No. 8 is responsible for a proportionate share of the costs) is estimated to be \$32 million.

In addition to its share of the Joint Outfall sewers, District No. 8 has three local sewers requiring significant rehabilitation, the 216th Street Trunk Sewer (TS), the Main Street TS and the Davidson City TS. The 216th Street TS involves replacement of the damaged pipe. It is scheduled to be completed in fiscal year 2020-21 at a total cost of \$12.5 million, with \$4.8 million being spent this fiscal year. The Main Street TS will be rehabilitated with the insertion of a corrosion-resistant liner. It is scheduled to be completed in fiscal year 2020-21 at a total cost of \$2.4 million, with \$1.1 million being spent this fiscal year. The Davidson City TS will be rehabilitated with the insertion of a corrosion-resistant liner. It is scheduled to be completed in fiscal year 2019-20 at a total cost of \$2.1 million, with \$1.3 million being spent this fiscal year.

Concrete Protection – The concrete at the various treatment plants is subject to corrosion in the same way that the sewers are. Liners were installed a number of years ago to protect concrete structures at the plants that were subject to significant corrosion. These liners have reached the end of their useful life. In order to preserve the structural integrity of the plants, it is necessary to remove the old liners, repair any existing damage, and then add new protective liners to prevent future corrosion. This work has been ongoing for a number of years and is projected to be completed by fiscal year 2022-23, with a total estimated cost of \$66 million, of which \$7 million is budgeted for fiscal year 2019-20.

Clearwater — Effluent from the Joint Water Pollution Control Plant (JWPCP) in Carson is conveyed to the ocean through two tunnels, one completed in 1937 and the other in 1958. Both tunnels have had continual flow in them and cannot be taken out of service under any condition. As has been discussed extensively with the Boards, construction of a third tunnel (the Clearwater Project) has been proposed. District No. 2, acting in its capacity as the administrative agent for the JOS, awarded the construction project to Dragados USA, Inc., for \$630 million on January 23, 2019.

The Clearwater Project will be funded with a combination of monies accumulated in the Capital Improvement Fund (fees paid by new users of the system and dedicated to capital projects) and debt financing. The Districts previously sold bonds in 1993 (which have subsequently been refinanced), with debt service that expires between 2021 and 2023. It is proposed to use the Capital Improvement Fund monies first and wait until the existing debt is retired before issuing the new debt. Because the new debt will be fairly equivalent in size to the debt being retired, the annual repayments will be similar and the

impact on the rates will be minimized. Several options exist for issuing new debt, including Districts-issued bonds, State Revolving Fund (SRF) loans, and Federal Water Infrastructure Finance and Innovation Act (WIFIA) loans. In March 2018, \$127 million was designated for this project through the SRF program. Additionally, in November 2018, the Districts' application for funds for monies from the WIFIA was accepted for a loan amount of \$426 million. Staff will continue to actively monitor the financial markets before making a final recommendation as to the most cost-effective borrowing mechanism. This project is scheduled to be completed in fiscal year 2025-26, with \$110 million to be spent in this next fiscal year.

Flow Equalization at the San Jose Creek Water Reclamation Plant (WRP) — Influent flows at the treatment plants are not static; they vary over the course of the day with maximums and minimums occurring at different times. Unfortunately, flows are highest during the day when the demand for recycled water is lowest, meaning that water may be discharged to the San Gabriel River and go unused. Conversely, flows are lowest at night when the demand for recycled water is highest, meaning that some of the need may go unmet. An 8 million gallon storage tank is being constructed at the San Jose Creek WRP that will store the peak flows during the day and then feed them back into the plant during the low-flow periods. This will make more recycled water available and also improve the operational efficiency of the WRP. This project, which is already under construction, is scheduled to be complete in fiscal year 2020-21 at a total cost of \$56 million, with estimated expenses in fiscal year 2019-20 of \$17 million.

Power Distribution System – This project involves the modernization of the power distribution systems at the various treatment plants to include redundant power feeds to improve the maintainability and reliability of those systems. These projects began in fiscal year 2015-16, and the total project cost is estimated at \$53 million. Work is projected to be completed by fiscal year 2023-24, with the majority of costs for these projects (\$20 million) budgeted for this work next fiscal year.

Process Air Compressors – All of the upstream treatment plants bubble ambient air through the secondary treatment system to enhance the biological treatment process. This air is first compressed and then injected into the aeration tanks through a series of diffusers. As the equipment ages or as technology improves, the process air compressors (PACs) must be replaced to ensure maximum efficiency in the transfer of oxygen, which leads to lower overall operating costs. Scheduled replacement of the PACs will occur through fiscal year 2024-25 at a total estimated cost of \$24 million, including replacements and work completed in prior years. Approximately \$6 million will be spent on this work next fiscal year.

SUMMARY OF REQUIRED ACTIONS

At the June 12, 2019 Board meeting, it will be recommended that the Board of Directors adopt a resolution establishing the appropriations limit on the proceeds of taxes, adopt the budget for FY 2019-20, adopt a resolution requesting the tax levy, and authorize appropriations in the sewerage system budget, all as shown on the agenda.

Very truly yours,



Grace Robinson Hyde

GRH:gc

Enclosures