

RESOLUTION 23-07

A RESOLUTION TO SELECET RAFTELIS FOR UTILITY COST OF SERVICE AND RATE STUDY PROFESSIONAL SERVICES

WHEREAS, the City of Spring Hill's most recent independent review of its utility cost of service was completed in 2019 that recommended adjustments in utility rates; and

WHEREAS, the City of Spring Hill has experienced significant expansion of its utility services including water, sewer, sanitation, stormwater, and corresponding growth demands upon city services resulting from the continued expansion throughout the City; and

WHEREAS, a detailed utility cost of service study will provide justifiable and equitable methodologies for appropriate rates for utility services that are sufficient to fully fund the expense associated with the utility systems, equipment repair and replacement, and necessary future capital investments in the utility to meet current and future growth and development needs; and

WHEREAS, the City of Spring Hill advertised and received proposals from qualified consultants based upon qualifications, experience, approach, work plan and schedule to perform a utility cost of service and rate study for the City of Spring Hill; and

WHEREAS, the City of Spring Hill utilized a qualifications-based selection approach has selected Raftelis as a qualified consultant based upon qualifications, experience, approach, work plan and schedule to perform a utility cost of service and rate study for the City of Spring Hill; and

WHEREAS, the City of Spring Hill utilized a selection committee composed of the Assistant City Administrator of Utilities, Finance Director, Public Works Director, Public Works Administrative Assistant, City Engineer, and Utility Director have reviewed all responses and unanimously recommends Raftelis; and

WHEREAS, City staff has prepared a Professional Services Agreement ("Agreement") to be utilized between the City and Raftelis to perform the Water and Sewer utility cost of service and rate study that includes Exhibit A referencing the cost proposal and schedule to be made a part therein of the Agreement.

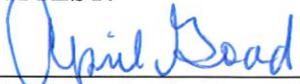
NOW THEREFORE BE IT RESOLVED, by the Board of Mayor and Aldermen of the City of Spring Hill, Tennessee, that Raftelis be selected to provide Utilities Cost of Service and rate study professional services.

1. Approve to execute the Professional Services Agreement between the City and Raftelis to perform a Water and Sewer Utility Cost of Service and Rate Study for the City of Spring Hill at a not to exceed cost of \$92,530.00.
2. Authorize the Mayor to sign the Professional Services Agreement between the City and Raftelis.

Passed and adopted by the Spring Hill Board of Mayor and Aldermen this 3rd day of January, 2023.



Jim Hagaman, Mayor

ATTEST:


April Goad, City Recorder

LEGAL FORM APPROVED:


Patrick Carter, City Attorney



REQUEST: *Approval of Resolution 23-07*
SUBMITTED BY: Jessica Weaver, Utility Director
DATE: January 3, 2023
RE: Authorize the Mayor to Execute a Professional Services Agreement with Raffelis for Water and Sewer Utility Cost of Service and Rate Study
ATTACHMENTS: Resolution 23-07, Agreement

PURPOSE:

To authorize the mayor to execute a professional services agreement with Raffelis for the Water and Sewer utility cost of services and rate study.

BACKGROUND:

The City of Spring Hill has experienced significant expansion of its infrastructure within the urban growth boundaries of the city in the past ten years. The current inflation and other potential future cost increases facing the Utility has brought upon the need to complete a detailed utility cost of service study which will provide justifiable and equitable methodologies for appropriate rates for utility services that are sufficient to fully fund the expense associated with the water and sewer utility needs. The last rate study that was completed in 2019 focused on modification of the base rate structures but made no changes to the cost per thousand for water or sewer. Prior to the 2019 study, the previous study was completed in 2011. In the 2011, the water rates increased from \$3.21 per thousand to the current rate of \$3.69 per thousand. The sewer rates were reviewed by MTAS and Staff with a multi-year phased approach being determined to be the best method of implementation with projections presented in 2010 increasing rates from \$3.16 per thousand in July 2010 to \$4.11 per thousand in July 2011 and then increasing in July 2012 to our current rate of \$4.52 per thousand.

FINANCIAL IMPACT:

The cost of the Raffelis professional services agreement is \$92,530.00 to be funded from budgeted funds (410-52317-254).

STAFF RECOMMENDATION:

Staff recommends approval of Resolution 23-07.



December 2, 2022

Mr. Dan Allen
City of Spring Hill
Assistant City Administrator - Utilities
199 Town Center Parkway,
P.O. Box 789
Spring Hill, TN 37174

Subject: Proposal for Water and Sewer Cost of Service and Rate Study and System Development Fee Analysis

Dear Mr. Allen:

Raftelis is pleased to submit this proposal to assist the City of Spring Hill (City) with a Water and Sewer Cost of Service and Rate Study which will include a system development fee analysis. We appreciate the opportunity to submit this proposal which details our project approach and associated work plan to meet the City's objectives. If you have any questions or need additional information, please don't hesitate to contact me.

Sincerely,
RAFTELIS FINANCIAL CONSULTANTS, INC.

A handwritten signature in black ink that reads 'Melissa Levin'.

Melissa Levin
Vice President

Project Approach and Understanding

As enterprise funds, water and sewer utilities should operate like self-supporting businesses. The scale of operations, infrastructure and investment requires thoughtful planning for future needs. System reliability, sustainability and financial integrity must be balanced with customer costs and impacts. Having a financial roadmap for financial decision making in the future is key to the financial success of the utility(s). A financial planning and rate study will provide the financial roadmap for the City while providing equitable and cost justified rates for customers. Additionally, a system development fee analysis will provide one-time fees to be assessed to customers connecting to the City's water and sewer systems in effort to have growth help pay for growth. Our project approach for this study is provided below.

Task 1: Initiation and Management

The project management task is designed to ensure the study progresses in an efficient and deliberate manner. This task will include administrative components related to project management and quality assurance and control processes.

Task 2: Kick-Off Workshop and Data Request

Raftelis believes the execution of a successful kick-off workshop is instrumental in conducting an efficient and useful study. The goals of this meeting include providing a forum to finalize the work plan and schedule of the study and ensuring Raftelis has a clear understanding of the City's objectives. This meeting also provides an opportunity to review and prioritize the City's most important pricing objectives (e.g., revenue stability, affordability, etc.) for providing water and sewer services. The pricing objectives ultimately influence the "conceptual designs" for rate structure options. Raftelis will prepare a kick-off workshop package that contains the meeting agenda, our initial assessment of the system's current financial state, a list of questions related to the City's water and sewer system, and presentation materials to guide the discussion and describe the project approach and deliverables.

Raftelis will prepare a detailed data request list so that readily available data can be forwarded prior to the workshop. The data required will include, but will not be limited to, operating and capital budgets, billing data, financial reports, Master Bond Resolution (or related document), fixed assets and capital improvement plans for calculating system development fees, population forecasts, ordinances, and/or contractual agreements. Using the information provided, Raftelis will conduct a preliminary review to assess the financial health of the water and sewer funds.

PLANNED MEETINGS:

- Kick-off meeting (web-based or in-person)

DELIVERABLES:

- Data request list
- Agenda for kick-off meeting
- Documentation summarizing the kick-off meeting

Task 3: Development of Financial Plans

With a firm understanding of the utility's overall financial condition, pricing objectives, and policy goals, Raftelis will develop a financial plan that will become the roadmap for financial decision making in the future. Developing the financial plan will include three key tasks:

1. Establishing and projecting system revenue requirements
2. Developing a forecast of billable units and revenues at existing rates
3. Evaluating the sufficiency of existing revenues to meet the projection of revenue requirements

Project System Revenue Requirements

The revenue requirements will include all operating and maintenance (O&M) costs, capital costs, reserve requirements, and bond covenants. In addition, the projection of revenue requirements will also recognize the City's current and future capital program and provide an estimate for future debt service requirements and revenue financed capital.

The City's FY 2023 budget will serve as the baseline for the forecast of future operating costs. Raftelis will review the City's actual O&M costs for the past three to five years to identify trends that should be recognized in the forecast of future costs. We will review the current budget and discuss with staff any known and measurable changes to current cost levels, such as wages and benefits, utility costs, and other significant cost categories. Also, we will discuss with City staff any contractual commitments for future wage and benefit increases and any expected changes in operations and staff that will impact future O&M costs, including the effects of the capital program. In order to project costs over the planning period, we will develop escalators based on historical trends and anticipated impacts of inflation on the various categories of costs. These escalation factors will be reviewed with City staff to obtain their perspectives and input.

A critical component when projecting revenue requirements will be working with the City's capital improvement plan (CIP). We will work with City staff to ensure the projection of revenue requirements incorporates the cost of regulatory requirements, repair and replacement needs of the system, and costs related to system expansion. Depending on the City's level of future capital needs and policies on capital financing, it may be appropriate to consider the issuance of future debt in combination with revenue generated from rates to deliver the capital program while managing the impacts on customers.

As a Registered Municipal Advisor, Raftelis will be available to work with the City to develop a capital financing plan for the study period. This is now a requirement under the Dodd-Frank Wall Street Reform and Consumer Protection Act. As noted previously, the financing sources for the CIP may include a combination of debt and current revenues and will be influenced by the financial policies developed during this task. We will review the proposed CIP financing plan with staff and make appropriate recommendations reflecting their perspectives and comments. As part of this task, Raftelis will incorporate debt service on existing debt and calculate projected debt service payments related to future borrowings to finance the capital program. If necessary, Raftelis will also review bond resolutions and ordinances (or related documents) securing outstanding bonds and loans to ensure we have a comprehensive understanding of the flow of funds and all debt covenants that should be monitored.

Finally, the forecast of revenue requirements will consider all of the City's financial and debt policies (reserve fund balances, and debt service coverage targets). Policies and metrics, both existing and proposed, will be identified, tracked, and incorporated into the forecast of revenue requirements. Raftelis will hold a web meeting with City staff to review all components of the forecast of revenue requirements. We will solicit staff input to ensure the forecast is consistent with the expressed financial objectives.

Establish and Forecast Billable Units of Service and Revenues Under Existing Rates

Raftelis will examine historical utility billing records to determine customer demands for water and sewer service. This analysis includes examining usage patterns as they relate to customer demands, population growth, and usage peaks during different periods of the year. Based on this historical analysis and planning data, Raftelis will develop projections of customer accounts and consumption.

The next step in the financial planning process is to forecast revenue over the planning period at the existing rates. Raftelis will incorporate the results of the customer demand analysis to develop a forecast that projects billable units of service while accounting for any anticipated decline in per capita consumption and any estimates for the impact of price elasticity on customer demand. The forecast of billable units is paired with the existing rates to calculate user charge revenues. In addition to revenue generated from user charges, we will also forecast revenues from various ancillary fees, miscellaneous revenue, and interest income for the planning period.

Evaluate Revenue Sufficiency and Establish Financial Plan

Combining the results from the previous work elements will result in a financial plan over both five- and 10-year forecast periods. Projections beyond 10 years will also be included for planning purposes. The financial plan will summarize the projected revenues and revenue requirements and incorporate annual debt service coverage requirements and reserve fund balance targets. The financial plan will project any future revenue shortfalls under the City's existing rates and provide an indication of the additional revenues necessary to support the projected revenue requirements and financial health of the water and sewer utilities.

PLANNED MEETINGS:

- Web-based meeting to review multi-year financial plans

DELIVERABLES:

- Multi-year financial plans for water and sewer utilities
- Recommendations for reserve fund, debt coverage, and other key financial policies

Task 4: Cost Allocation, Rate Design, and Fee Calculation

We will work with staff to develop conceptual designs, or approaches, for alternative rate and fee structures based on the City's pricing objectives and financial goals. The process will consider the current user charge structure and the financial impact on the various ratepayers based on alternative structures. Although we take care to tailor a utility's cost-of-service analysis to meet the needs of the individual utility, we always make sure to follow the basic premise of cost-of-service allocations set forth by state and local laws, the American Water Works Association's *Manual M1, Principles of Water Rates, Fees and Charges (Manual M1)*, the Water Environment Federation's *Manual of Practice No.27, Financing and Charges*

for *Wastewater Systems (MOP 27)*, and other authoritative bodies. Depending on the results of the conceptual designs, we will determine the most appropriate methodology for allocating costs, which may include detailed cost allocations to functional components of the utility systems, categories of service, and customer classes based on usage characteristics. However, it may be determined that costs need to be allocated more simply between fixed and variable components, for the purpose of calculating fixed and variable charges that are not assessed by customer class. In either case, we will develop an approach to allocating costs that is consistent with AWWA and WEF standards.

Following the cost allocation, Raftelis will calculate preliminary rates and charges based on the conceptual designs for alternative rate and fee structures. Rates under the proposed alternatives will be calculated for each year in the forecast period and adjusted, where possible, to provide for a smooth forecast of rate adjustments. Customer impact analyses will be performed to understand the impact of proposed changes to different types of customers. Raftelis will also compare the proposed rates to those of comparable communities and peers throughout Tennessee. This survey will be incorporated into the report and presentation identified in Task 6.

At the end of this task, we will conduct a web meeting with City staff. At this meeting, Raftelis will review the entire rate and fee development process and present preliminary rates and fees. Prior to the meeting, staff will be provided with the draft rate model so that they may review our methodology and suggest changes. We will discuss all suggested changes and then work with the City to develop our final recommendations.

PLANNED MEETINGS:

- Web-based meeting with City staff to review rate alternatives

DELIVERABLES:

Preliminary and final rate and fee recommendations

Task 5: Rate Model Development

At the heart of any successful rate study is the rate model used to develop revenue requirements, perform operational and capital financial planning, review customer information, and calculate revenue and rates. The rate model will incorporate the results of each of the other tasks in the engagement and be sophisticated enough to perform the complex calculations involved in a comprehensive rate analysis with the ability to analyze various rate structures.

The rate model created for this engagement will be developed using Excel and will be based on a model framework that incorporates industry-standard, rate-setting methodologies in a user-friendly manner. City staff will be provided with working copies of the rate model that they will be able to provide input into its development, if desired. The rate model will be built around our innovative modeling approach and will include a customized and interactive dashboard that will provide the City with an intuitive system to measure, track, and manage the performance of the water and sewer utilities. The rate model will be non-proprietary and will become the property of the City at the conclusion of the study. Raftelis will also provide virtual training for City staff on the construction and use of the rate model.



Raftelis will develop a customized financial model that incorporates a dashboard to allow you to easily run scenarios and see the impacts in real time. Shown here is a sample dashboard that we developed for another project.

Task 6: System Development Fee Analysis

System development fees are one-time charges assessed to new water and/or sewer customers for their use of system capacity. They serve as an equitable method of recovering system capacity costs from those using the capacity. Raftelis will use Microsoft Excel to develop a model to calculate the system development fees, which will incorporate the data requested in Task 2. Once initial data has been entered into the model Raftelis will hold a webinar with City staff to go over the information and give the project team a forum to review the data and to ask a series of questions. Raftelis will discuss the methodologies, concepts, and key assumptions for calculating system development fees using industry guidelines, as described briefly below.

- **Buy-In Approach**

The Buy-In Methodology is most appropriate in cases where the existing system assets provide adequate capacity to provide service to new customers. This approach calculates a fee based upon the proportional cost of each user's share of existing plant capacity. The cost of the facilities is based on fixed assets records and usually includes escalation of the depreciated value of those assets to current dollars.

- **Incremental Cost Approach**

The second method used to calculate water system development fees is the Incremental Cost (or Marginal Cost) Methodology. This method focuses on the cost of adding additional facilities to serve new customers. It is most appropriate when existing facilities do not have adequate capacity to provide service to new customers, and the cost for new capacity can be tied to an approved capital improvement plan (CIP).

- *Combined Approach*

A combined (or hybrid) approach, which is a combination of the Buy-In and Incremental Cost approaches, can be used when the existing assets provide some capacity to accommodate new customers, but where the capital improvement plan also identifies significant capital investment to add additional infrastructure to address future growth and capacity needs.

During this meeting, Raftelis and the City will agree upon the methodology and key assumptions. Raftelis will then apply the methodology and key assumptions and calculate preliminary system development fees. The preliminary results will be discussed with City staff and legal counsel via a webinar to provide the City with the opportunity to review the key assumptions and provide any changes. Specifically, City staff will have an opportunity to provide any changes or modifications based on their knowledge of the water/sewer systems. Raftelis will then model any suggested changes and provide the final results to staff and legal counsel.

Task 7: Report, Recommendations, and Presentations

The final task includes the development of draft and final deliverables and presentations to conclude the study.

Draft Report

Raftelis will provide a draft report that describes the study process along with financial planning, rate, and fee recommendations. The draft report will be submitted to City administration for review and comment. Comments and revisions will be incorporated before finalizing the report.

Final Report

Raftelis will incorporate City staff's comments on the draft report into a final report. Upon finalization of the report, Raftelis will deliver an electronic copy on a flash drive and any requested hard copies of the final report. The final rate model will also be delivered to the City, and Raftelis staff are available to train City staff on the model's continued use.

Presentations

Raftelis will be able to assist the City as necessary in presenting the results of the study and supporting study recommendations.

PLANNED MEETINGS:

- In-person meeting with staff to review draft report and presentation
- In-person public meeting with leadership to present final study report
- Web-based meeting with staff to provide training on the final rate model

DELIVERABLES:

- Draft report
- Final report incorporating staff and stakeholder comments
- PowerPoint presentation
- Final rate model

We accept the terms of this Engagement Letter: (please sign and return one original).

Approved: 	Date: <u>January 3, 2023</u>
Title: <u>Mayor</u>	Name of Signatory: <u>Jim Hagaman</u>

Raftelis is registered with the U.S. Securities Exchange Commission (SEC) and the Municipal Securities Rulemaking Board (MSRB) as a Municipal Advisor. Registration as a Municipal Advisor is a requirement under the Dodd-Frank Wall Street Reform and Consumer Protection Act. All firms that provide financial forecasts that include assumptions about the size, timing, and terms for possible future debt issues, as well as debt issuance support services for specific proposed bond issues, including bond feasibility studies and coverage forecasts, must be registered with the SEC and MSRB to legally provide financial opinions and advice. Raftelis' registration as a Municipal Advisor means our clients can be confident that Raftelis is fully qualified and capable of providing financial advice related to all aspects of utility financial planning in compliance with the applicable regulations of the SEC and the MSRB.

Cost

The following table provides a breakdown of our proposed fee for this project. This table includes the estimated level of effort required for completing each task and the hourly billing rates for our project team members. Expenses include costs associated with travel and a \$10 per hour technology charge covering computers, networks, telephones, postage, etc.

Tasks	Web Meetings	In-person Meetings	Hours					Total Fees & Expenses
			ML	MC	FM	Corp	Total	
1. Project Initiation and Management			8	0	0	8	16	\$3,280
2. Kick-off Workshop and Data Request	1		8	12	16	0	36	\$8,740
Initial Project Meeting								
Data Collection and Initial Review								
3. Financial Plan Development (10-Year Financial Forecast)	1		12	16	40	0	68	\$15,720
Determine Revenue Requirements								
Analyze Billing Data and Project Revenues Under Existing Rates								
Establish Escalation Factors (Cost, Growth, other)								
Establish Financing for Capital Plan								
4. Cost Allocation and Rate Design (Test Year)	1		24	28	40	0	92	\$22,620
Allocate Revenue Requirements to Functional Parameters								
Determine Peaking Factors for System and Customer Classes								
Determine Cost for Rate Structure Components / Customer Classes								
Evaluate Rate Structure Alternatives Using COS Results								
Examine Customer Impacts for Rate Structure Alternatives								
Evaluate Success in Meeting Pricing / Rate Structure Objectives								
Integrate New Rate Structure / Rates into Financial Plan								
5. Rate Model Development	1		4	8	40	0	52	\$11,120
Create Rate Model using Microsoft Excel								
Provide Virtual Training for Staff								
6. System Development Fee Calculation	1		24	32	16	0	72	\$18,960
Determine Appropriate Approach (Buy-In, Marginal, or Combined)								
Perform Calculations, Determine ERU								
Document Results for Adoption								
7. Report, Recommendations, and Presentation	1		12	14	24	0	50	\$12,090
Total Meetings / Hours	4	0	92	110	176	8	386	
Hourly Billing Rate			\$310	\$245	\$185	\$80		
Total Professional Fees			\$28,520	\$26,950	\$32,560	\$640	\$88,670	
							Total Fees	\$88,670
							Total Expenses	\$3,860
							Total Fees & Expenses	\$92,530

ML - Melissa Levin
MC - Mhaela Coopersmith
FM - Ford Moriarty
Corp - Corporate Functions