



445 S. Figueroa Street
Suite 1925
Los Angeles, CA 90071

Phone 213.262.9300
Fax 213.262.9303

www.raftelis.com

September 15, 2023

Nicholas Turner
General Manager
Montecito Water District
583 San Ysidro Road
Montecito, CA 93108

Subject: 2024 Water Rate Study

Dear Mr. Turner,

Raftelis Financial Consultants (Raftelis) appreciates this opportunity to support the Montecito Water District (District) with its Rate Study. We have developed a scope of tasks and work plan within this proposal based on our discussions with staff and our understanding of the Board of Directors' objectives. Our work will build upon prior work performed for the District. Relying on recent tools and work products developed for the District since the last rate study will allow us to move more quickly and minimize costs where possible.

Melissa Elliott, APR will serve as Project Director and will be responsible for the project's success to your satisfaction. Melissa has over 25 years of experience helping utilities tell their stories to customers. Melissa is also a past president of the American Water Works Association. I, Kevin Kostiuk, will serve as Project Manager, managing the day-to-day tasks of the project and ensuring that it stays on schedule and within budget. I will lead our analyst in developing analyses and work products and deliver results to District staff and the Board. I have ten years of California rate-setting experience, focused on water rates, drought impacts, groundwater management, and unique rate structures. I developed the District's prior financial plan and rate model and have a keen understanding of the District's cost structure, operating environment, and service area. Lindsay Roth will be the dedicated analyst on the project. Lindsay is familiar with the District and is responsible for the Long Range Financial Plan tool which was created for the District. With over 45 years of experience, Sudhir Pardiwala, PE will serve as the technical reviewer and a subject matter expert. The technical team will be supported by Matt Wittern and Gina DePinto in Raftelis' Communications and Outreach practice.

We estimate our fee to complete the scoped tasks at \$89,210 excluding the optional tasks identified herein. Raftelis will invoice the project monthly for time and materials. Raftelis aims to begin the project in October 2023 and complete our work effort around April 2024, in time for new rates to be implemented July 1, 2024.

I am authorized to negotiate on behalf of, and to contractually bind, Raftelis. Should you have any questions, please do not hesitate to contact me.

We thank you for the opportunity to assist you and Montecito Water District.

Sincerely,

A handwritten signature in black ink, appearing to be 'K Kostiuk', written in a cursive style.

Kevin Kostiuk, Senior Manager

Office: 323 213 9209 / Mobile: 760 519 8520 / Email: kkostiuk@raftelis.com

SCOPE OF SERVICE

The following sections outline the tasks Raftelis believes will be involved in completing a study that accomplishes the District's objectives. Specifically, Raftelis will perform the following tasks:

-) Develop an updated long range financial plan
-) Perform a cost of service analysis of the water system
-) Evaluate modifications to the District's existing rate structure
-) Organize and present at a series of public meetings including working sessions with the District's Finance Committee and Board of Directors
-) Develop a strategic communications framework and assist in the preparation of outreach materials
-) Document the rate study in accordance with the requirements of Proposition 218:
 - o Write an administrative report that explains the allocation of costs and development of fair and equitable rates
 - o Review the public notice and present rates for approval at a Public Hearing
 - o Coordination with the District's legal counsel

TASK 1: PROJECT INITIATION AND PROJECT MANAGEMENT

Our project management approach stresses communication, teamwork, objectivity, and accountability to meet project objectives. We believe in a no-surprises approach and communicate regularly with clients through in-person meetings and webinars so that the District is aware of the project status at all times. Raftelis' quality assurance/quality control (QA/QC) process fosters high-quality and accurate work.

We believe that a productive kick-off meeting is the most effective way to begin a rate study. Raftelis uses the kick-off meeting to perform our due diligence and ensure that project stakeholders agree to the goals, approach, work plan, schedule, and study priorities.

We propose holding a traditional kickoff meeting with District staff and a separate workshop with the Board of Directors. Raftelis will conduct the project kick-off meeting with staff in advance of the Board Workshop. In our meeting with the Board, we will discuss our process for the cost of service development and the necessary considerations under Proposition 218. The session with the Board will include a preliminary discussion on the existing rates and potential rate structure modifications for the District's consideration, including Budget-based rates. Additional discussion items will likely include reserves policies, use of debt financing, fixed and variable rate revenue recovery, and fire protection charges, among others. Raftelis envisions this meeting will develop the framework for the Study with Board members and staff agreeing to a set of "guiding principles" with which Raftelis will develop financial plan scenarios and constrain the rate model to a handful of alternatives for considerations.

A detailed data request will be submitted prior to the kickoff meeting so that the District can assemble and deliver appropriate data. We will also provide staff with an agenda in advance of the

meetings and detailed notes of the decisions and outcomes of both the kickoff and the Board Workshop.

Meetings: *One kick-off meeting with District staff; one Workshop with the Board of Directors*

Deliverables: *Data Request List; Kick-off Meeting agenda, presentation materials, and meeting minutes*

TASK 2: LONG RANGE FINANCIAL PLAN DEVELOPMENT

Raftelis will update and modify the Financial Plan Model tool developed for the District in 2022 and updating in 2023. We will develop a minimum ten-year cash flow analysis to determine the revenue adjustments needed to meet projected costs for the planning period while minimizing sharp rate fluctuations. The cash flow worksheet incorporates revenues generated from different sources, expenses required to maintain the utility systems, and debt service coverage needed to meet current and proposed financing requirements. We will also review the reserve policies to recommend appropriate reserve balances consistent with industry standards and the District's desire to appropriately address the risk of revenue loss from factors such as conservation, cyclical drought, and natural disasters.

Expense projections will be based on current operating and capital budgets, reserve funding needs, and debt service as applicable. Revenue projections will be based on estimated water consumption and rates. District staff will be able to adjust expenses and revenue to see the effect on financial health. The model has the functionality to view multiple CIP scenarios including changes in timing to planned capital and alternative projects that the District may consider.

Our models include a dashboard and incorporate the below:

-) Allow financing options for CIP (Debt, pay-go, other),
-) Flexibility to change assumptions such as water sales, CIP levels, and revenue adjustments,
-) Error flagging of results such as: failure to meet debt coverage, unmet reserve targets, etc.,
-) Financial metric displays (operating reserve, debt service coverage, reserve levels),
-) Sensitivity analyses that can be viewed immediately

Meetings: *Two webinars to review the financial plan inputs and assumptions*

Deliverables: *Long Range Financial Plan model in Microsoft Excel*

TASK 3: COST OF SERVICE ANALYSIS

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 cost-of-service allocation framework set forth by the American Water Works Association's (AWWA) *Manual M1, Principles of Water Rates*,

Fees, and Charges. This helps to ensure that cost allocations and resulting rates align with Proposition 218. Cost allocations among customer classes will be based on the AWWA-approved Base-Extra Capacity approach, which focuses on the different demand patterns and peaking characteristics demonstrated by each customer class. At this stage, Raftelis will also identify any new customer classes, if warranted.

The first step of a cost-of-service analysis is to complete a cost functionalization to allocate costs to the various functions within the utility. These categories may include source of supply, treatment, transmission, storage, distribution, meter servicing, and customer costs, among others. The next step is the classification of costs based on cost-causative parameters. In water, these parameters typically include supply, average day demand, maximum day demand, maximum hour demand, meters, fire protection, and customer service. Finally, the cost of serving each customer class is determined based on each class's (and tier's) usage characteristics and units of service. This process is the standard approach to cost of service for utilities in California and throughout North America.

The goal of this task is to distribute the cost components to customer classes based on the cost responsibility of each. This is the total cost to serve each customer class and is used as the basis to develop rates. Throughout the water cost allocation process, Raftelis will incorporate the District's policy considerations, as well as current federal, state, and local rules and regulations, such as Proposition 218.

Comparison of Costs by Customer Class

Based on the rate structures identified in this task, we will develop a comparison of the cost of service to rate recovery under the new rates as well as existing rates. This will allow the District to understand any inequities in the existing rate structure as well as how any proposed changes to the rate structure address those inequities.

Meetings: Two webinars with District staff

Deliverables: Draft Cost of Service Analysis in Microsoft Excel

TASK 4: RATE DESIGN & CUSTOMER IMPACT ANALYSIS

At the heart of any successful cost-of-service and rate study is the computer model that is used to develop revenue requirements; perform cost functionalization, classification, and allocation; and calculate rates. The model must be sophisticated enough to perform the complex calculations involved in a comprehensive cost-of-service and rate analysis and yet still be simple enough to allow for future updates.

The model will incorporate any rate structure alternatives for evaluation and changes to rate calculation methodologies identified. During the project, District staff will be provided with working copies of rate model drafts in Microsoft Excel so that they will be able to provide input

into the development of the model. Once the project is complete, the District will be provided with fully functioning copies of the model and Raftelis personnel will train members of the District staff in its use.

Rate Calculation

After the District's costs have been functionalized, classified, and allocated in the cost of service analysis, we will use our water demand analyses and revenue requirements to calculate user rates reflecting the District's specific rate goals and objectives. Raftelis will evaluate the District's current rate structures and discuss how they compare to industry standards. We will discuss and evaluate the need for any rate structure modifications, keeping the desire for easy to understand rates in mind. This evaluation will be based on existing data and the needs of the District.

Rates will be calculated for the five-year adoption period. At the end of this task, we will conduct a meeting with District staff. Raftelis will review preliminary and final rates with staff in multiple meetings. We will discuss any suggested changes and then work with District staff, the Finance Committee, and the Board of Directors, to finalize a rate recommendation.

Customer Impact Analysis

Raftelis will determine the potential financial impact on customers that result from the proposed rates calculated in the rate design task. In our impact analysis graphics, we generate bills at varying levels of usage assuming the new, proposed rates were already in place. The customer impact analysis will include a series of tables and figures that show projected rate impacts by customer class at various levels of usage.

Evaluation of water budget-based rates is described in our Optional Task 9.

Meetings: *Three webinars with District staff*

Deliverables: *Draft and Final Rate Models in Microsoft Excel*

TASK 5: BOARD AND COMMITTEE WORKSHOPS

After developing the framework for the rate study with Board members at the initial Kick-off Workshop, Raftelis will conduct additional, dedicated workshops each with the District's Finance Committee and the Board of Directors. The first series of workshops will be a discussion of the preliminary financial plan results and options. The second series of workshops will discuss preliminary rates based on the alternatives modeled. Raftelis will request feedback and incorporate Committee and Board comments and direction into the final rate proposal. After reaching consensus on a rate proposal, Raftelis will develop the draft rate study report and return to present the final proposal to the Board of Directors. This meeting will serve as authorization to direct District staff to begin the public noticing process and set a date for the public hearing on rate adoption. The draft study report, detailing the rationale for the proposed rates, will be included in the meeting packet at the time the Board of Directors authorizes the notice to customers.

Meetings: Five meetings with the District Finance Committee and Board of Directors
Deliverables: Presentation materials and meeting minutes

TASK 6: RATE STUDY REPORT

Raftelis will prepare a report documenting the Rate Study to serve as the District's administrative record. The draft report will document the rate development process, describe any recommended changes to the existing rate structures and the reason for such changes, and present the results of the cost-of-service and rate study. The report will include an executive summary highlighting the major issues addressed, decisions reached, and recommended rates developed during the Study. The main body of the report will include a brief physical description of the water system and District characteristics, detail of the financial plan and reserve policies, cost of service analysis, rate design details, and the proposed rates. It will also contain a discussion on rate structure selection and rate design assumptions. The methodology describing the cost of service and rate calculations will be described in detail so that the nexus between costs and rates is clearly defined and understandable.

This first draft version will be submitted to staff and the District's legal counsel for review and comment. Raftelis will incorporate changes and commentary into the final report. The report will be developed prior to the noticing period so that customers can review the Rate Study during the noticing period and prior to the Public Hearing for rate adoption.

Meetings: One webinar with District staff to review comments
Deliverables: Draft and Final Reports

TASK 7: PROPOSITION 218 NOTICING AND PUBLIC HEARING

Raftelis will present the results and proposed multi-year rates to the Board of Directors and ratepayers at a public hearing. The presentation will review the rationale behind the rates including the overall revenue needs, any rate structure changes, and estimated customer impacts. We will be available to address any questions from the Board or the public. Presentation materials will be provided to District staff well before the Public Hearing for review.

Proposition 218 mandates specific procedural requirements to be followed for the adoption of new rates and charges for parcel-related services, water included. Raftelis will review and provide suggestions on the notice. The notice should outline the proposed water rate changes, discuss the drivers of the rate changes, explain the payer's right to challenge the proposed rates, and that the District will meet and comply with all procedural requirements of Proposition 218. Once the notices have been printed and mailed to the District's customers, a Public Hearing to adopt or reject the rates may be scheduled as early as 45 days after postmark.

Meetings: Raftelis attendance and participation at the Public Hearing
Deliverables: Reviewed Proposition 218 notice content; presentation materials

TASK 8: PUBLIC OUTREACH & COMMUNICATIONS

Proactive communication increases community acceptance of rate changes, enhances credibility with stakeholders and policymakers, and builds awareness of the value of the service and the need for utility investments on behalf of the community. The District has a strong communications foundation to work from, and it is anticipated that the implementation of a communications and outreach strategy will be done by District staff. Planning for potential rate change is a communication challenge that benefits from experience in developing communication strategies and tactics that will explain this change.

8.1: Develop a Strategic Communications Framework

The communications framework will include:

1. **Situation analysis** that analyzes current issues that may impact customer rate change acceptance (for example, how to thoughtfully communicate about potential rate changes to customers and stakeholders when other communications about smart meters and GSA funding needs are occurring).
2. **Stakeholder identification and mapping** to ensure key influencers are connected to the communication process and identifies special population communication needs.
3. **Messaging platform** to provide messages about why rates may change, how rate study recommendations will be implemented, and potential impacts on customers.
4. **Community outreach tactics** include developing a presentation for use with civic clubs, homeowners' associations, highly impacted customer groups, etc.
5. **Written communication development** for use in such materials as FAQs, infographics, website updates, bill inserts, etc.
6. **Tactics and timeline** to specifically identify when each element in the plan is implemented and who is doing what.

Meeting(s): *One in-person meeting (kick-off meeting) with District communications and finance staff to understand communication needs, current environment and develop communications*

Deliverables: *Strategic Communications Framework*

Note: Pricing includes the development of a draft and incorporating a single round of client changes to arrive at a final document. We propose billing subsequent rounds of revisions using a time and materials method.

8.2: Communication Materials – Development and Design

Visual representation of proposed changes in an easy-to-understand and accessible format can often improve customer understanding of rate structure changes that may impact customer bills. Raftelis' professional graphic design team is experienced in developing infographics, fact sheets, brochures, presentations, event displays, etc., to assist with communicating rate changes in print,

online, or in person. All materials will align with the District's brand guidelines so that materials are integrated into the District's communications program. Although we anticipate collaborating with District staff on communication material needs, we suggest the following materials be developed:

1. Infographic/fact sheet that explains the rate structure change and revenue needs for the utility
2. FAQs that can be used on the website and with District staff
3. General overview presentation that can be provided to community groups and stakeholders by District staff
4. Design for the Proposition 218 notice
5. Bill insert that explains the rate changes after Board approval

Meeting(s): *Conference calls as necessary*

Deliverables: *Bill insert, fact sheet with infographics, FAQ document, PowerPoint presentation, and Proposition 218 notice – draft for review and final ready for printing*

Note: Pricing includes developing draft communications tool content in MSWord and incorporating a single round of client changes to arrive at a final document for use in graphic design. Pricing includes a single round of revisions during the graphic design phase. For both phases, we propose billing subsequent rounds of revisions using a time and materials method.

OPTIONAL TASK 9: WATER BUDGET-BASED RATE DESIGN

(\$14,375)

Raftelis has assisted many agencies in evaluating and adopting water budget rate structures. These agencies include East Valley Water District, El Toro Water District, Rancho California Water District, Crescenta Valley Water District, Placer County Water Agency, Irvine Ranch Water District, Elsinore Valley Water District, City of Tustin, City of San Juan Capistrano, City of Corona, and City of Redlands, among others. As mentioned earlier, a water budget-based rate structure would require additional effort to calculate the water budget for each single-family customer.

To calculate outdoor water budgets, Raftelis requires irrigable, or landscape area, for each account. For this task we assume that the District will provide individual parcel budgets which will identify indoor budgets and outdoor budgets separately; as well as to identify all assumptions relied upon for generating budgets (i.e. monthly evapotranspiration estimates, assumed household occupancies, etc.). Raftelis will rely on the District's calculated water budgets to merge into the District's customer billing data detail. After merging water budget information with customer water use data, Raftelis can perform additional analyses to use in the water budget rate design.

As part of this task we will review the various policy issues and considerations associated with development of water budgets including but not limited to the following:

- Household density for single and multi-family residential parcels

- Per capita water use and efficiency standards
- Landscape area definition using assessor data or aerial photography data
- Any limits/maximums for irrigated area
- Historical or actual evapotranspiration (ET) data
- ET adjustment factors – plant factors and irrigation efficiency
- Tier definitions – indoor, outdoor, etc.
- Variances for special needs – medical, large animals, pools, etc.
- Billing system capabilities

Raftelis will rely upon the water budget model to develop an alternative rate structure and associated rates. The result of this task is the duplication of a rate model very similar in nature to that in Task 4 but with a unique set of rates and customer bill impacts.

Meeting(s): *Two webinars with District Staff to discuss/confirm water budget assumptions and policies; participation at one Committee or Board meeting to discuss water budget policies, if necessary*

Deliverables: *Draft and Final Water Budget Rate Model in Microsoft Excel*

OPTIONAL TASK 10: COMMUNICATIONS AND OUTRACH EXPLAINER VIDEO (\$2,500 - \$5,000)

Key messages developed as part of the strategic communications framework come to life when woven together into powerful communications pieces by Raftelis' strategic communicators and professional graphic designers. Visual representation of proposed changes in an easy-to-understand and accessible format significantly improves customer understanding of rate structure changes that may impact customer bills. Topics include explaining rate structure changes, new rates, investments for a secure water future, the rate study process, etc. The cost of production depends on the length and complexity of the video as well as any translation into languages other than English.

Meeting(s): *Two conference calls with District Staff*

Deliverables: *Explainer Video*

Fee Proposal

Raftelis proposes to complete the scope of work outlined above on a time-and-materials basis with a not-to-exceed cost of \$89,210. The not-to-exceed cost excludes the optional tasks. The following work plan provides a breakdown of the estimated level of effort required for completing each task described and the hourly billing rates for the personnel scheduled to complete the project.

Tasks	Web Meetings	In-person Meetings	Hours								Total Fees & Expenses	
			ME	KK	SP	LR	MW	CS	Admin	Total		
Project Initiation and Project Management	1	1	12	10		12				4	38	\$10,005
Long Range Financial Plan Development	2			12	2	16					30	\$7,240
Cost of Service Analysis	2			8	2	16					26	\$6,100
Rate Design and Customer Impact Analysis	3			16	4	28					48	\$11,420
Board and Committee Workshops		5	12	24		10					46	\$14,265
Rate Study Report	1			8	4	36				2	50	\$10,880
Proposition 218 Noticing And Public Hearing		1		8	1	2					11	\$3,275
Public Outreach Scope											0	\$0
<i>Develop a Strategic Communications Framework</i>	2	1	8	4				36			48	\$13,195
<i>Communications Materials - Development and Design</i>	4		4	2				30	24		60	\$12,830
Optional Tasks											0	\$0
<i>Water Budget-Based Rate Design</i>	2	1		20	4	36					60	\$14,375
<i>Communications and Outreach Explainer Video</i>	2		1					12	10		23	\$4,750
Total Meetings / Hours	19	9	36	92	13	120	66	24	6	440		
	Hourly Billing Rate		\$350	\$285	\$350	\$195	\$250	\$140	\$90			
	Total Professional Fees		\$12,600	\$26,220	\$4,550	\$23,400	\$16,500	\$3,360	\$540	\$87,170		
<i>ME - Melissa Elliott, Project Director</i> <i>KK - Kevin Kostiuik, Project Manager</i> <i>SP - Sudhir Pardiwala, Technical Reviewer</i> <i>LR - Lindsay Roth, Lead Analyst</i> <i>MW -Matt Wittern, Communications Lead</i> <i>CS - Raftelis Creative Services</i> <i>Admin - Raftelis Administration</i>												
Total Fees (Excluding Optional Tasks)											\$87,170	
Total Expenses											\$2,040	
Total Fees & Expenses (Excluding Optional Tasks)											\$89,210	
Total Fees and Expenses - Water Rate Study											\$63,185	
Total Fees and Expenses - Public Outreach											\$26,025	
Total Fees and Expenses - Optional Tasks											\$19,125	
Total Fees and Expenses - Inclusive of All Tasks											\$108,335	