Budget Assumptions for
FY 2016/17 and the 10-Year Forecast

Staff has begun the process for preparation of the FY 2016/17 operating and capital budget, as well as year-end projections for the current fiscal year. While no definite projections have been made at this time, some general guidance has been developed for budget preparation:

Service Levels

Assumption: **Increased recycled water delivery starting in 2016; additional support in Collections; solar and stationary battery storage on line; increased sewer rehabilitation starting in FY 19/20; no other service level changes**

Discussion: With the plant improvements to expand recycled water treatment capacity and the recycled water pipelines to MST and LCWD completed, the 2016 recycled water irrigation season should see a significant increase in the amount of recycled water sold. There will be additional service in sewer repair and system maintenance as two new employees are hired, as recommended in the Employee Master Plan, and increased emphasis placed on sewer rehabilitation and replacement starting in FY 19/20. FY 2016/17 will be the first year with the new photovoltaic array and stationary storage battery systems operational.

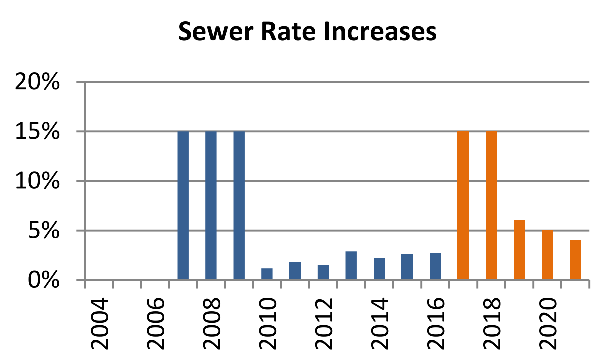
Plant Operations, Reclamation, Administration, Engineering, Pollution Prevention: No change in service levels is included in the 10-year forecast.

Revenues

Sewer Service Charges

Assumption: **Sewer Service Charges/CPI Changes – increase according to the Sewer Service Charge Rate Study**

Discussion: The sewer service charge rate study recommends a rate increase of 15% next fiscal year, and increase of 15%, 6%, 5% and 4% thereafter. For years six through ten of the forecast, an annual rate increase of 2.5% is assumed. These recommendations are based on analysis of the revenue needs of the District, including the current 10-year capital plan and an increase in funding for sewer rehabilitation and replacement starting in FY 2019/20.

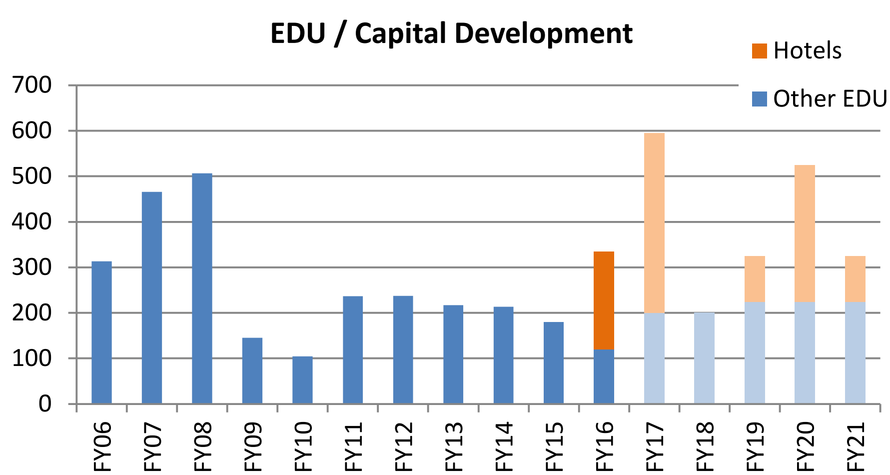


Development / Growth in EDU

Assumption:	**Growth in EDU – based on projected growth of 200 EDU per year for next two years, and 225 EDU thereafter, PLUS openings of new hotel developments.**
Discussion:	EDU has remained fairly flat since FY 2008/09. Activity in plan review and building permits indicate that local development is starting to improve. As part of CIP revision discussions with the Board in Fall 2013, the Board approved a forecast for EDU based on 290 EDU per year for regular business development, plus one-time EDU sales corresponding with planned hotel developments within the District's service area. It appears from recent data that the estimate of 290 EDU were higher than is reasonable. Staff recommends assuming a base of 200 EDU for the next two years, and 225 EDU thereafter, with specific hotels or other developments added in years of most probable development. Development projections include the following:

FY16	Archer Hotel	215 EDU
FY17	Stanly Ranch and Meritage	395 EDU
FY18		0 EDU
FY19	Gasser Housing Development	100 EDU
FY20	Somky/Montelcino and Soscol (Altamura)	300 EDU
FY21	Gasser Housing Development	100 EDU

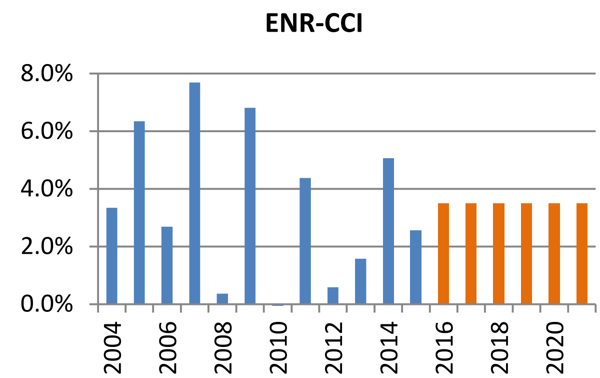
This forecast does not consider the impacts of Napa Pipe development, as additional CIP projects will also be necessary when that property is developed (neither the revenue nor capital expenses relate to Napa Pipe are currently included in the 10-year CIP).



Construction Inflation

Assumption: **Construction CPI – 3.5% per year in future years.**

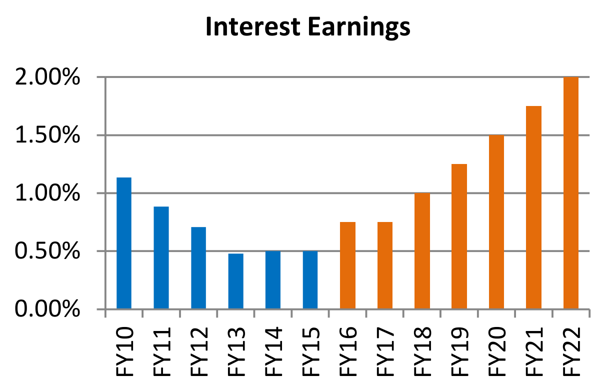
Discussion: The Engineering News Record's Construction Cost Index (ENR-CCI) is used by the District for future increases to the capacity charge rate, as it represents the inflation of construction costs. Starting in FY 2014/15, the rate increased by the annual change in the ENR-CCI index (February-to-February), rather than a set amount. The annual ENR-CCI in July 2015 (latest data) was 2.6%, higher than July the previous year, while the average annual increase for the past 10 years is 3.2%. The recommendation is to assume in the 10-year plan that the construction CPI will increase by 3.5% annually.



Interest Earnings

Assumption: **Interest Earnings – 0.75% for FY15/16 and FY16/17, then increasing to 2.0% by the end of the FY21/22.**

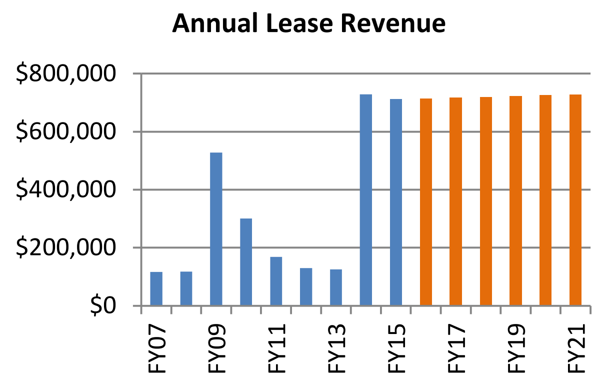
Discussion: The Federal Reserve recently increased the Federal Funds rate by 0.25%, the first increase in over 10 years, and indicated that the Fed intended to continue to raise rates slowly. This assumption is conservative, based on a slowly increasing rate over the next several years.



Lease Revenue

Assumption: **Lease Revenue – Payment of Somky lease from Napa LH1 and new entity, LLC; contractual increases for Eagle Vines. No other lease revenue.**

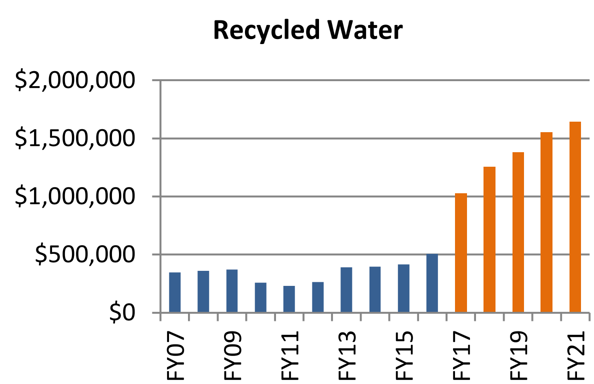
Discussion: The lease rate for Eagle Vines are set by contract and increases with local CPI. The forecast assumes this continues for the next decade. Deferred lease payments from Napa LH1 were received when they refinanced a loan at the very end of 2015, but the associated resort property is in contract to be sold in March 2016. There is no reason to believe that new owners would not pay the lease, but if the sale of the property does not proceed, there may be some difficultly in collecting lease revenues from Napa LH1. The forecast currently includes lease revenue. No lease revenue has been assumed for the Real Energy / Napa Biogas project, nor any other sources. Lease revenues are the source of funding for the Sewer Service Charge Low Income Assistance Program.



Recycled Water

Assumption: **Recycled Water Revenue – increase just over 100% in FY2016/17, with increases in FY 2017/18 and thereafter based on approved fee changes and planned increases in recycled water usage.**

Discussion: FY 2015/16 revenues are expected to increase about 22% because of increased users and the new rate structure that went into effect January 2016. FY16/17 is the first full fiscal year that will take advantage of the new rates and the significant increase in sales due to the MST and LCWD pipelines. For FY17/18 and beyond, it is assumed that rates will increase by CPI and that more users will come on line as infill along existing RW lines continues.

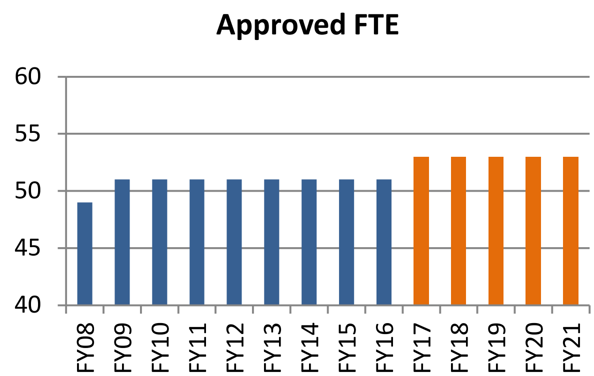


Expenditures

Staffing Levels

Assumption: **Staffing Levels – two FTE increases in the Collections System department.**

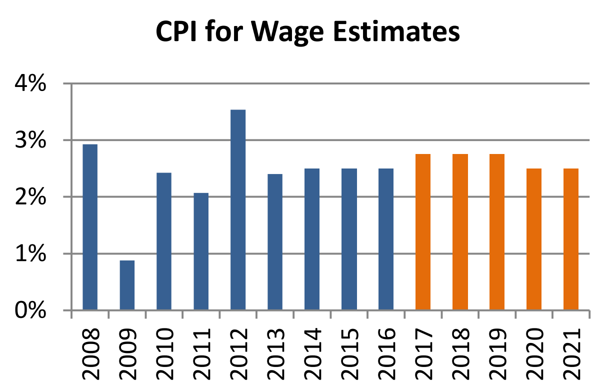
Discussion: The Employee Master Plan approved by the Board in early 2015 included a recommendation to move or change several positions in the District, and to increase the staffing level of the Collection System by two FTE. This is the first increase in staff since FY08/09. There are no planned changes in staffing level for future years beyond this recommendation.



Salary Expenses

Assumption: **Salary Expenses – 2.5% CPI increase in FY16/17, and 2.75% for the three following years, then 2.5%.**

Discussion: A new MOU was approved effective July 2014. The new contract sets the salary increases for 6 years through 2020. For the remaining years of the 10-year forecast, a salary increase of 2.5% per year will be assumed.

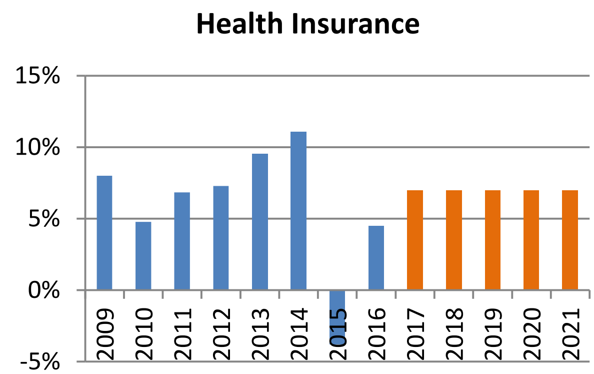


Health Insurance

Assumption: **Insurance Expenses –** 7% per year increases for health insurance, other insurance expenses at known costs.

Discussion: A significant majority of employees have Kaiser for health insurance, and the District uses the Kaiser rate to establish the maximums for employer contributions. The history of Kaiser insurance rates has shown growth in excess of CPI in recent years, with the exception of 2015 where the rates decreased 3.8%. It is believed that this decrease was a one-time adjustment to prior year increases and is not expected to continue.

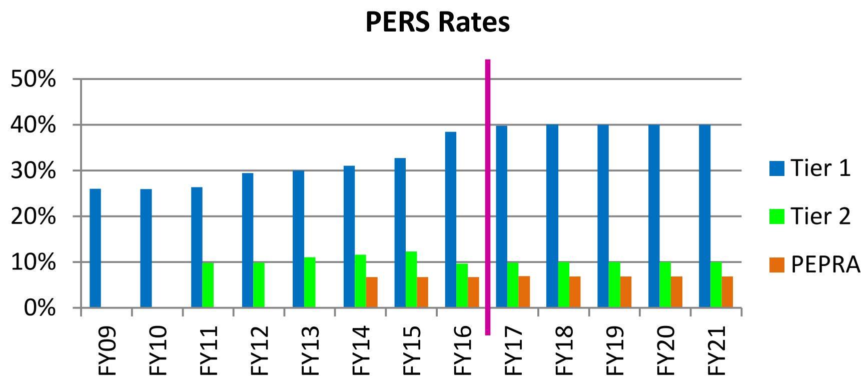
Health care benefit costs are known for calendar year 2016. For budget development purposes, staff recommends planning for a 7% increase in costs in calendar year 2017 and beyond. This is a reduction from estimates made in prior years of 8%.



Retirement Expenses

Assumption: **Tier 1 – 39.8% for FY 2016/17 and 40% thereafter.**
Tier 2 – 9.8% for FY 2016/17 and 10% thereafter.
PEPRA – 6.9% for FY 2016/17 and 7% thereafter.

Discussion: PERS has provided the employer rate for FY 2016/17 (39.8%) and has provided an estimate of 40% for FY 2017/18 through FY 2021/22 for Tier 1 employees. Tier 2 employees decrease 2% for FY 2016/17, while the PEPRA rate has increased by 0.3%. The District currently has 38 Tier 1 employees, 8 Tier 2 employees, 3 PEPRA employee and 2 vacancies.



Services & Supplies

Assumption: **Services & Supplies, Generally – For FY 16/17, as justified, but no more than CPI, expect for contracted and known increases. A 2.3% assumed increase annually thereafter in the forecast for inflation.**
Electricity –Increase in electricity based on increased recycled water pumping to MST and LCWD starting in Spring 2016, offset by impacts of stationary storage and PV solar PPA.
Chemicals –Increase in hypochlorite and decrease in sodium bicarbonate based on increased recycled water production and reduced river discharge.

Discussion: Staff built a budget with no increases to general services and supplies for 4 years, with the base operating budget in FY15/16 increasing only 1.2% (excluding one-time only projects). This practice of limiting the base operating budget to zero or near zero percent increases was justified to encourage staff to find areas in the budget to conserve and become more efficient. However, a long-term practice of no increases is not sustainable. Staff will assume a 2.3% increase for general services and supplies, as long as spending patterns justify an increase and there are no other methods for determining an appropriate increase. One-time only expenditures from prior year budget will be removed, and any new one-time expenditures will be identified separately, following the practices from prior year budgets.

Changes to the electricity and chemical budgets are anticipated in FY 16/17 and beyond, now that the new DAF clarifier has come into production (higher electricity/lower chemical), with the expansion of recycled water to MST and LCWD (higher electricity/higher chemical), and bringing the PV Solar PPA and stationary storage systems online (lower electricity costs).

Capital Projects

Assumption: **Capital Projects – Continuation of the existing 10-year capital plan.**

Discussion: Capital projects identified in prior year 10-year plan will be continued as scheduled. Additional sewer replacements starting in FY19/20 as built into SSC rate forecast.

The discussions with the Board as part of the rate study have provided direction regarding the CIP and sewer replacements. The recommended rates will provide sufficient revenue to finance the existing capital plan.