Budget Assumptions for
FY 2021/22 and the 10-Year Forecast

Staff has begun the process for preparation of the FY 2021/22 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 as more customers come on line in the MST and Carneros areas; continue sewer rehabilitation per Board directive; 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 2021 recycled water irrigation season should continue to see increases in the amount of recycled water sold as more properties convert to recycled water. The CIP will continue to show a continuing, sustained effort at sewer rehabilitation and replacement in the next decade, with a long-term average of 2% of the system replaced annually.

Revenues

Sewer Service Charges

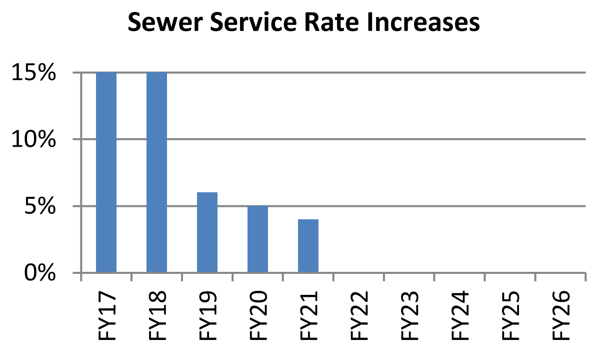
Assumption: **Sewer Service Charges/CPI Changes – increase according to the Sewer Service Charge Rates that will be adopted by Board**

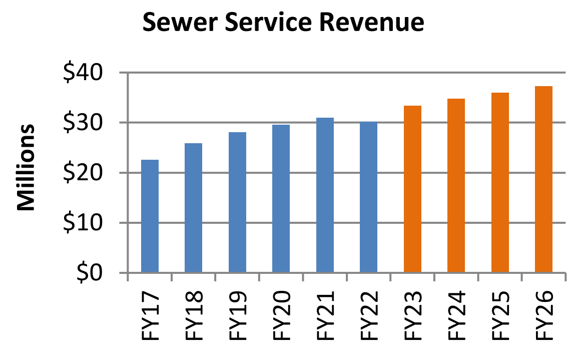
Discussion: The Board of Directors will be establishing a rate modification for sewer service for the next five (5) years during the rate hearing and rate setting process that is scheduled for March 2021. The rate modification will keep the sewer service charge rate the same (0% increase), however the calculation of the rate will generate an increase in overall revenues by 3%. The revenues generated from sewer service charges will increase about 3% - 4% over the next five (5) years which includes projected growth. For years five through ten of the forecast, an annual rate increase of 3.0% is assumed. These recommendations are based on analysis of the revenue needs of the District, including the current 10-year capital plan and the increased efforts toward sewer rehabilitation and replacement.

The sewer service charge revenues in FY 2021/22 have been adjusted to reflect a loss in revenues due to anticipated reduced water usage by the commercial customers. When preparing the 10-year financial forecast last year, the loss was expected to be about 43% or $3.2m. After reviewing actual water usage that will be used to calculate the FY 21/22 sewer service charge, the reduction in water usage was a little under 20%. Instead of a loss of $3.2m, the loss is closer to $1.5m.

The schools’ sewer service charges are calculated using average daily attendance. Schools have been closed for part of this fiscal year and is expected to be closed for part of next fiscal year as well. This will affect the attendance rate and will lower their sewer service bill. This was not taken into consideration last year. The projection includes a 50% reduction in the schools’ sewer service charge which is about $193k.

To stay on the conservative side, the sewer service charges have been reduced by $2m to account for these anticipated losses.





Development / Growth in EDU / Capacity Charge Revenue

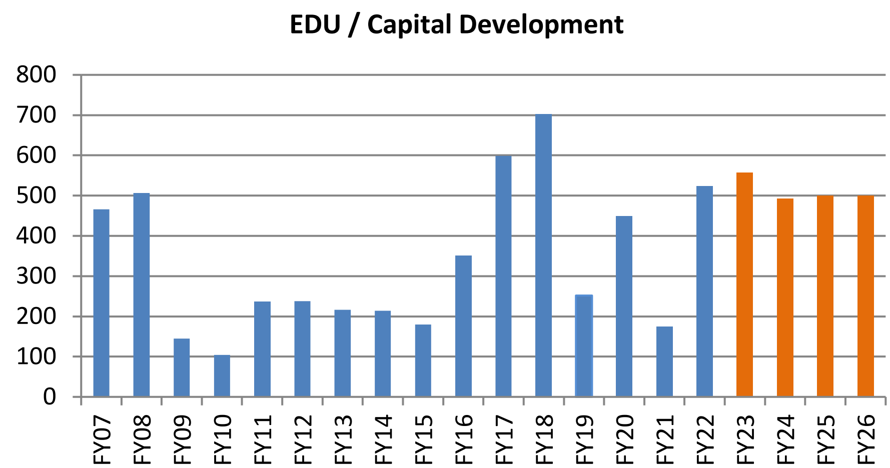
Assumption: **Growth in EDU – for the next four years, projected growth based on estimates of commercial and development projects known to NapaSan staff, plus an assumed baseline of activity for smaller projects. Thereafter, based on assumed growth of 275 EDU annually, consistent with General Plan.**

Discussion: Some development projects that were scheduled to begin in the near future have been delayed or dropped all together. The projections for the next three years are based on Planning Department referrals and development plans reviewed by NapaSan. Staff estimated the potential dates that large developments would proceed to construction and used those estimates in the forecast. The next five years assume a growth level consistent with the General Plan.

Fiscal Year	Commercial	Residential	Total	Capacity Charges
Current-est.	70	105	175	$1,742,800
FY 21/22	224	300	524	$5,296,600
FY 22/23	261	296	557	$5,782,200
FY 23/24	225	268	493	$5,255,900
FY 24/25	250	250	500	$5,474,500
FY 25/26	15	485	500	$5,622,500

FY 20/21 (current year) includes payment for increased capacity for several tenant improvements, Foster Road Townhomes, Saratoga Vineyards Subdivision, and Pear Tree townhomes. Payment for phase 2 of the Stanly Ranch project is expected to be received. **FY 21/22** includes the continuation of phase 2 of the Stanly Ranch project, Embassy Suites, Costco, the Westin and Senza Hotel expansion, SoCo Apartments, Napa Creek Condos, the 1st Street Apartments, and Vista Grove. The beginning of the Napa Pipe project and the Ritz are expected to start. **FY 22/23** anticipates the continuation of the Napa Pipe project and the Ritz, the Zinfandel Subdivision, Borrette Lane and the development of the Brayden Phase 2. Development of Franklin Station is also projected. **FY 23/24 – FY 25/26** includes the continuation of Napa Pipe and the Ritz.

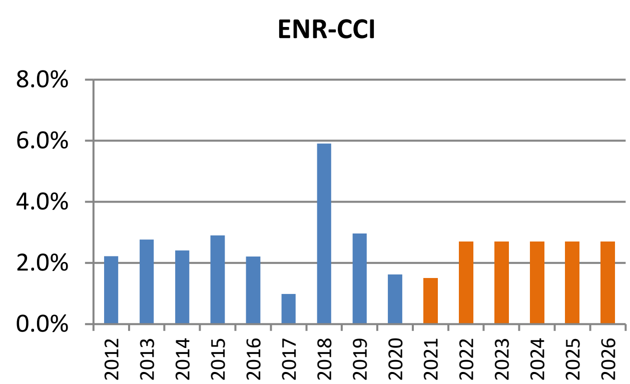
Some developments have not been included in the forecast for the next few years because of their uncertain nature. These include Emmanual Eco Village, Westwood Park Estates, Montalcino, Black Elk, Foxbow, Oxbow South Lot, Bounty Hunter, the Wine Train Hotel, Creekside East Apartments, and future expansion of Napa Pipe development.



Construction Inflation / Capacity Charge Fee

Assumption: **Construction CPI – 1.5% for FY 2021/22, then 2.7% per year thereafter.**

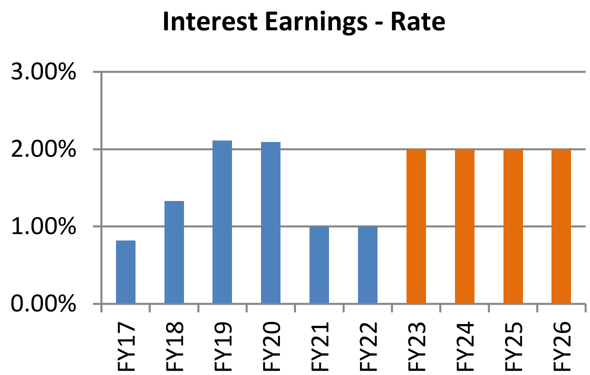
Discussion: The Engineering News Record's Construction Cost Index (ENR-CCI) is used by NapaSan for future increases to the capacity charge rate, as it represents the inflation of construction costs. With recent changes to District Code, the capacity charge rate may increase annually up to the ENR-CCI's 20-city average index (February-to-February). The annual ENR-CCI index in December 2020 (latest data) was 2.2% higher than December the previous year, and the average annual increase for the past 10 years is 2.7%. The economy took a devastating hit due to the COVID-19 pandemic. The economy is still struggling but with the availability of the COVID-19 vaccines, it is anticipated that it will start to show some recovery next year. The recommendation is to assume in the 10-year plan that the construction CPI will increase by 1.5% next fiscal year, and 2.7% annually thereafter. This would increase the rate from $9,959 this year to $10,108 per EDU in FY 21/22.

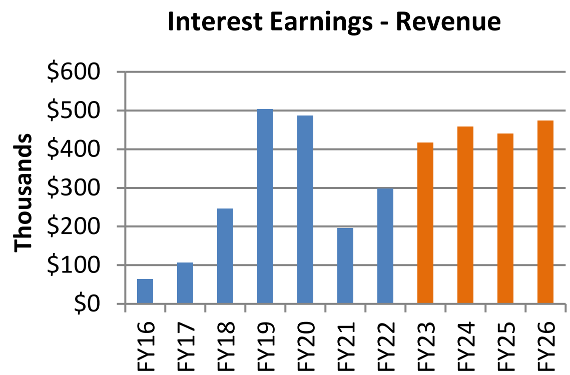


Interest Earnings

Assumption: **Interest Earnings – 1.0% for FY 21/22 and 2.00% in future years.**

Discussion: The Federal Reserve has been maintaining interest rates between 0.00% and 0.25% for the last two years. The market remains depressed due to the economic impact of COVID-19 and the rates are likely to remain low. The interest rate earned for the Napa County Investment Pool in November 2020 (most recently reported month) was 1.67%, with the LAIF rate at 0.576%. The recommended long-term assumption is for the interest earnings rate to be just slightly lower than the assumed long-term inflation rate, at 2.00%.



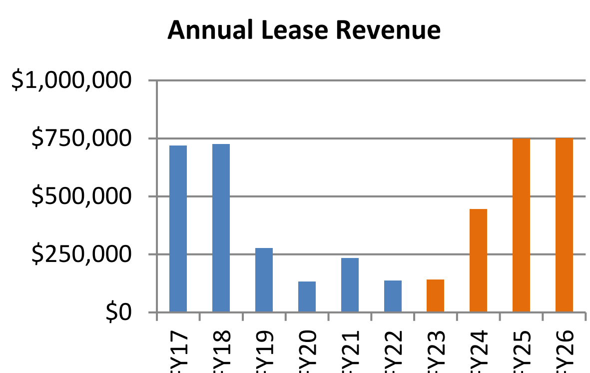


Lease Revenue

Assumption: **Lease Revenue – Contractual increases for Eagle Vines. Lease revenue from Somky or Jameson beginning in FY 2023/24. No other lease revenue.**

Discussion: The lease rates for Eagle Vines are set by contract and increases with local CPI. The forecast assumes this continues for the next decade. Lease payments for the Somky property have been assumed at $0 until a new lease for Somky or a lease for Jameson is developed. It is assumed that lease activities for those properties will begin in FY 2023/24. No lease revenue has been assumed from any other sources. Lease revenues are the source of funding for the Sewer Service Charge Low Income Assistance Program.

An Option to Lease agreement was signed and approved in June 2018 for Ciel et Terre USA to lease the surface of Pond 4 and a portion of Pond 3 for the purpose of installing a floating solar array. Although not included in the budget assumptions at this time, lease payments of $80k per year could potentially start in FY 2023/24.

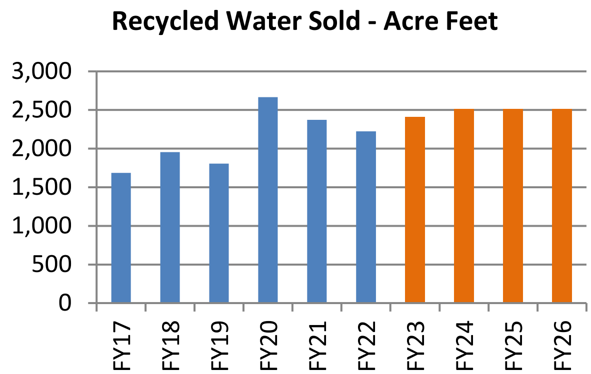


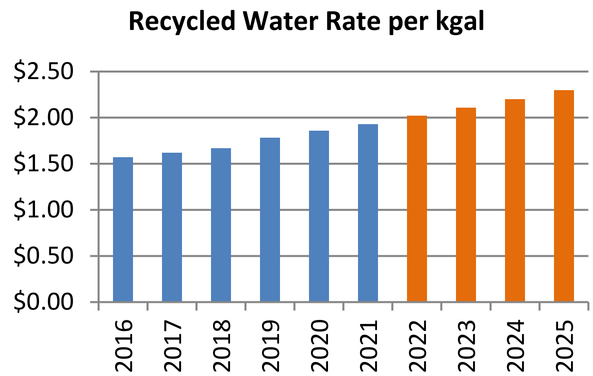
Recycled Water

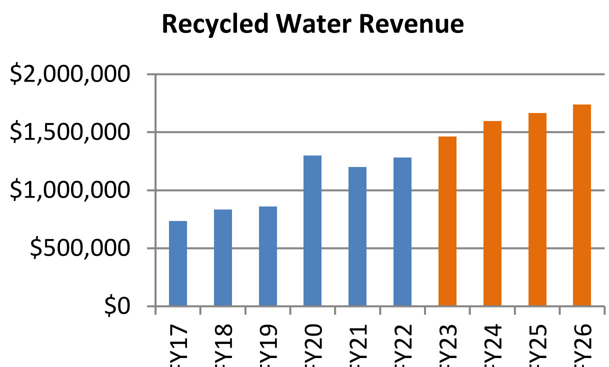
Assumption: **Recycled Water Rates – increase for CPI, estimated at 2.0% in 2021 and 2.5% thereafter; additional 2% for Renewal & Replacement reserve (third year). Gallons sold increases based on estimates for expansion of service.**

Discussion: FY 2020/21 revenues are expected to increase slightly because of increased users and the annual rate increase. The rate per thousand gallons for 2021 is not yet known, but is expected to be about 2.0% based on October 2020 CPI numbers. CPI is estimated at 2.5% for each year thereafter in the forecast. Water delivery is also expected to increase over time as more properties in the MST and LCWD areas connect to the system and begin to use water.

Estimated CPI	2021 Rate (Including 2% for R&R)
1.0%-1.4%	$1.92/kgal
1.5%-2.0%	**$1.93/kgal**
2.1%-2.5%	$1.94/kgal
2.6%-3.1%	$1.95/kgal
3.2%-3.6%	$1.96/kgal
3.7%-4.1%	$1.97/kgal
4.2%-4.7%	$1.98/kgal
4.8%-5.0%	$1.99/kgal







Salary & Benefit Expenditures

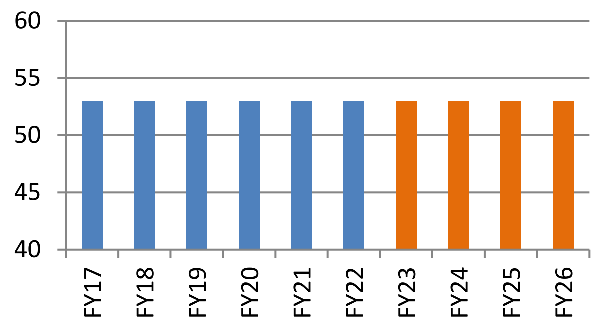
Staffing Levels

Assumption: **Staffing Levels – no change**

Discussion: FY 2016/17 saw the implementation of changes recommended in 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. There are no planned changes in staffing level for future years.

In anticipation of reduced revenues from commercial customers as a result of the economic slowdown/shutdown, two currently vacant FTE positions will not be filled in FY 2021/22 – Plant Attendant and Collection System Worker IT/I/II/III. The savings will be about $222,000.

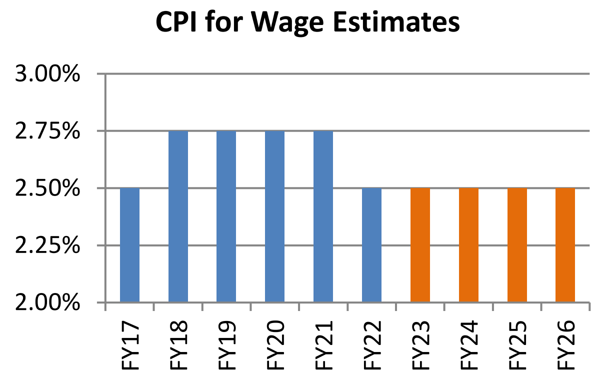
Approved FTE



Salary Expenses

Assumption: **Salary Expenses – 2.50% CPI increase in FY 21/22 per the approved labor MOUs, then an assumed 2.50% increase annually.**

Discussion: A new MOU with a four year term was approved effective July 2020. The new contract sets the salary CPI increases for two (2) years through FY 2022 with a reopener in FY 23 and FY 24 to negotiate the appropriate salary increases in those years. For years two through nine of the 10-year forecast, a salary increase of 2.5% per year will be assumed. This assumption is not an indication of intent regarding future labor negotiations. Note that the salary increases under the current labor agreement (FY21 to FY24) have included an annually increased contribution by employees to PERS. That contribution currently, in this first year of the agreement, is 7.25% (the full employee's share of 7% for employees in Tier 2). The second year will increase to the full 8% for employees in Tier 1.



In addition to the annual CPI increases, certain employee classifications were approved for a market adjustment during the term of this labor contract. The adjustments range from increases of 2.6% to 24.2%. These increases will be phased in and happen over the four year term of the contract. The phase-in approach will be as follows:

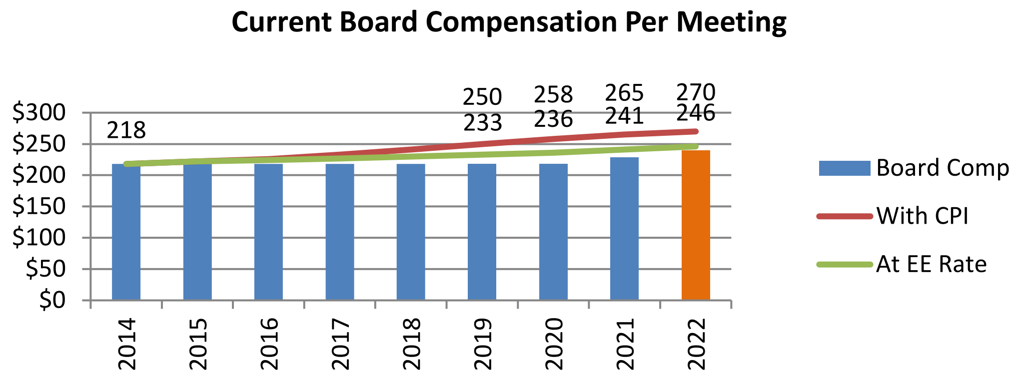
- Year 1 will be adjusted by 35% of the total percentage increase
- Year 2 will be adjusted by 25% of the total percentage increase
- Year 3 will be adjusted by 20% of the total percentage increase
- Year 4 will be adjusted by 20% of the total percentage increase

The cost escalation in salaries with the market adjustments are 13.3%, 7.7%, 7.9%, 6.4%.

Board Compensation

Assumption: **Board Compensation – Increase to earnings of $240 per meeting.**

Discussion: Board compensation is established in District Code as $218 per meeting. For Board Compensation to increase, the Board must pass an amendment to the Code. The last increase was in December 2013. Compensation may increase annually by no more than 5% per year. If Board compensation had increased with CPI, the current rate would be $265 per meeting. If Board compensation had increased at the same rate as employee earnings, the 2021 rate would be $241 and the projected 2022 rate would be $246 per meeting. The Board approved FY 2020/21’s budget to include increased compensation by the 5% maximum, $229 per meeting. However, the increase has not been implemented. The increase can be implemented before the end of the year with an amendment to the Code. If compensation is increased by the maximum 5% for next year as well, the rate for FY 2022 would be $240 per meeting.



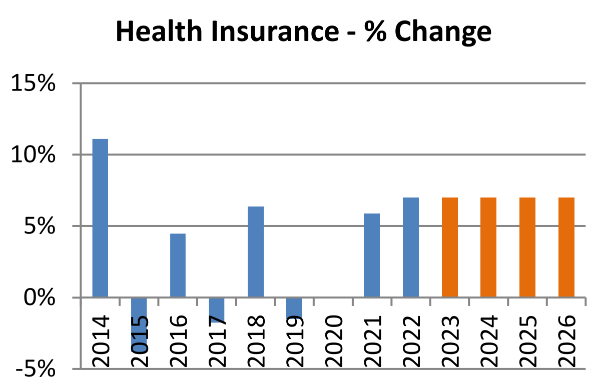
Health Insurance

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

Discussion: A significant majority of employees have Kaiser Permanente for health insurance, and NapaSan 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 the past; however, more recent annual adjustments have been either negative or smaller increases.

CalPERS restructured their rates, reducing the number of regions from five to three. The result was to lower the average rates for Bay Area agencies. The adjustment had a one-time impact to the 2020 rates and only increased by less than 0.5%. The rates for 2021 is a 5.9% increase. Future rates are expected to continue to increase higher than what was seen in 2020.

Health care benefit costs are known for calendar year 2020. For budget development purposes, staff recommends planning for a 7% increase in costs in calendar year 2022 and beyond.

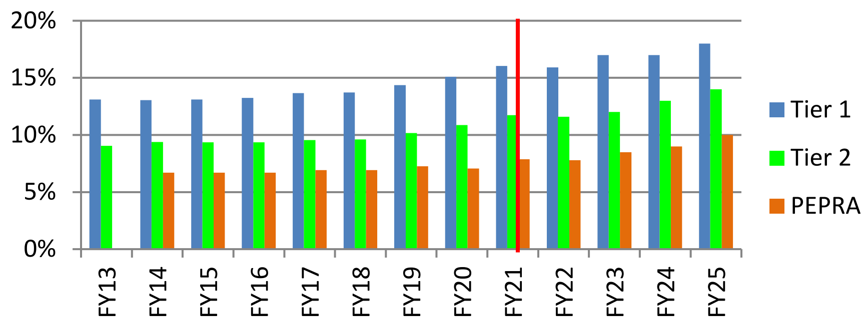


CalPERS Retirement Expenses - Normal Cost

Assumption:		Tier 1	Tier 2	PEPRA
	FY 21/22	**15.9%**	**11.6%**	**7.7%**
	FY 22/23	**16.0%**	**12.0%**	**8.5%**
	FY 23/24	**17.0%**	**13.0%**	**9.0%**
	Thereafter	**18.0%**	**14.0%**	**10.0%**

Discussion: PERS has provided the employer rate for FY 2021/22 and an estimate for FY 2022/23. In the last five years, the rates have increased slightly less than 1% per year. It is anticipated that Miscellaneous Plans will increase from 1-3% of payroll over the next several years due to changes in investment/discount rate assumptions, amortization methods and mortality assumptions. The recommended assumptions are proposed based on the historical pattern. The investment market was impacted by COVID-19. The investment rate came in lower than the targeted 7% return for FY 2019/20. The projected impact has been amortized over 20 years and is included in the 10-year forecast.

PERS Rates for Normal Cost



CalPERS Retirement Expenses - Unfunded Liability

Assumption: **Freeze the Tier 1 liability payment at FY19/20 levels starting in FY 22/23.**

Discussion: NapaSan Financial Policy is to contribute additional payments toward the pension unfunded liability. In FY 18/19 and 19/20, an additional $135,000 payment was made, the amount matching the annual savings from refinancing debt in FY17/18.

FY 19/20 was the last year NapaSan paid on the Tier 1 "side fund" to PERS which resulted in an annual reduction in minimum contribution to CalPERS of approximately $500,000. Current NapaSan policy encourages the use of freed up budgetary capacity from this reduction, and the reduction from debt refinancing, towards additional CalPERS payments. However, it is anticipated that NapaSan will see reduced revenues due to the impact of the COVID-19 pandemic. Therefore, the Board made a decision to postpone making additional contributions until FY 22/23.

The recommended assumption is for NapaSan to make the minimum required payment of $1,126,095 in FY 2021/22. In FY 2022/23, NapaSan will make a payment of $1,529,035 and then retain this same payment for the following seven years. This will attain the stated policy goals.

Fiscal Year	Tier 1 CalPERS minimum payment	Recommended Liability Payment	Additional paid toward liability
2021/22	1,023,695	1,023,695	-
2022/23	1,126,095	1,126,095	402,940
2023/24	1,192,781	1,529,035	336,254
2024/25	1,262.924	1,529,035	266,111
2025/26	1,300,765	1,529,035	228,270
2026/27	1,335,455	1,529,035	193,580
2027/28	1,371,095	1,529,035	157,940
2028/29	1,407,714	1,529,035	121,321
2029/30	1,445,345	1,529,035	83,690
2030/31	1,484,009	1,529,035	45,026

OPEB Payments

Assumption: **Set OPEB contribution at 15.0% of payroll.**

Discussion: NapaSan Financial Policy is to contribute toward OPEBs through direct payment of retiree insurance premiums and a contribution to the OPEB Trust (CERBT), to equal the Actuarially Determined Contribution (ADC). Current projections show that the unfunded liability will be paid off in FY 2034/35, using current assumptions regarding return on investment and health care cost inflation. Non-attainment of actuarial assumptions can result in unplanned increases in the ADC, negatively impacting future operating budgets.

If NapaSan were to maintain its OPEB contribution at a set percentage of payroll over time (15.0%), and not make any reductions, NapaSan is projected to be on target to reduce the unfunded portion of the liability by 2035.

Estimated Impact of Assumptions:
7.7% increase in Salary & Benefit Expenses

Services & Supplies

Assumption: **Services & Supplies, Generally – For FY 21/22, as justified, but no more than CPI, expect for contracted and known increases. A 2.5% assumed increase annually thereafter in the forecast for inflation.**
Electricity –Increase in electricity based on increased recycled water pumping to MST and LCWD.
Chemicals –Increase in hypochlorite based on increased recycled water production and known chemical unit costs.

Discussion: The Service & Supplies budget adopted for FY 20/21 was $6,186,300, compared to the final budget of $5,474,638 in FY 12/13. This represents a total increase of 13.0% over 8 years, or an annual average increase of 1.62%, even while increasing the production and distribution of recycled water. Staff has been able to maintain this extremely low level of growth through efficiencies, particularly in chemistry and electricity, the two highest non-payroll operating expenses for NapaSan. This level of continued efficiency is unlikely to be sustainable in the long term. Staff recommends that the Service & Supplies budget assumptions increase at the rate of 2.5% per year.

Electricity and chemical consumption is expected to increase over time as more recycled water is delivered to the MST and LCWD areas.

Services & Supplies – Significant One-Time Only Expenses

Discussion:

FY 2022/23 and FY 2023/24

Outfall Abandonment – There is an anticipated project to abandon a decommissioned river outfall near the Influent Pump Station. This $180,000 expenses is not capital in nature, as it does not result in an asset to the District, so needs to be planned for as a Services & Supplies expense.

FY 2023/24

Climate Impact Mitigation Study – Study to evaluate adaptation needs and mitigation strategies related to climate change. There is $250,000 set aside for this study.

FY 2025/26

North Napa Pump Station Force Main Abandonment - When the siphon was installed to cross the Napa River and decommission the North Napa Pump Station, the force main was maintained as a backup in case the siphon did not operate as designed and intended. The siphon has proven to be reliable. To avoid I&I and the possibility of a collapse of the force main, the line should be abandoned. This $218,000 project does not result in a new asset or the extension of an asset's useful life, so it is not a capital project. It is expected that this project will be completed in FY 20/21.

Capital Projects

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

Discussion: Capital projects identified in prior year 10-year plan will continue as scheduled. Adjustments will be made to prior plans based on changes approved by the Board.

The Board has provided specific direction regarding sewer replacement schedules and I&I efforts during the rate discussions and hearings in Spring 2016. The forecast will continue with the direction provided by the Board at that time, to reach and sustain the goal of 2% system rehabilitation or replacement annually.

Staff will continue to prioritize I&I and sewer replacement projects that are likely to result in reduced recycled water chloride levels.

Future Debt

Assumptions: **FY 20/21 – Rehabilitation of Main Sewer Trunk**

Anticipate bond financing of 66" Sewer Trunk Rehabilitation. Project is in the Capital Improvement Plan to cost approximately $15 million. Debt issuance in FY 2020/21, with debt service payments beginning in FY 2021/22.

FY 21/22 – Refinance Series 2012A Certificates of Participation

Plan for potential refinancing of Series 2012A COPs in 2022, if appropriate.

FY 24/25 – Second Digester and Third Aeration Basin

Anticipate bond financing of completion of the second digester and construction of the third aeration basis. Project is in the Capital Improvement Plan to cost approximately $26 million. Debt issuance in FY 2024/25, with debt service payments beginning in FY 2025/26. This issuance could be in conjunction with the refinancing of the 2012A COPs, with the rehabilitation of the main sewer trunk and/or could be issued in multiple tranches.

FY 27/28 – Rehabilitation of 66-inch Trunk Sewer Phase 2

Anticipate bond financing of 66" Sewer Trunk Rehabilitation. Project is in the Capital Improvement Plan to cost approximately $18 million. Debt issuance in FY 2027/28 with debt service payments beginning in FY 2028/29.

FY 29/30 – NBWRA Projects

Recycled water expansion projects to meet future recycled water demands. Project components are anticipated to include additional treatment capacity and additional treated water storage capacity.

Not Included in Forecast

Revenue: **Sale of Land and Additional Lease Revenue**

The 10-Year forecast does include an assumption of additional lease revenue starting in 2024 to replace the revenue lost from the Somky property lease, but is not specific about which property is leased, nor does it include the sale of any property.