

# WORK SESSION AGENDA ITEM SUMMARY

City Council



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## STAFF

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## SUBJECT FOR DISCUSSION

**Water Supply Requirements, Excess Water Use Surcharges, and Pre-1984 Non-Residential Allotments.**

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## EXECUTIVE SUMMARY

The purpose of this item is to provide an update to the proposed Fort Collins Utilities Water Supply Requirement (WSR) methodology that was presented at the April 9 Council work session, as well as adjusted impacts to both the WSR fee and the assignment of non-residential water allotments. Staff will also address some follow-up questions from the work session.

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## GENERAL DIRECTION SOUGHT AND SPECIFIC QUESTIONS TO BE ANSWERED

1. What questions do Councilmembers have on the updated proposed WSR fee and related impacts?
2. What questions do Councilmembers have on assigning water allotments to non-residential accounts without allotments under the hybrid method?

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## BACKGROUND / DISCUSSION

At the April 9 Council work session, staff presented options and a recommendation for the methodology for determining a WSR fee. Council expressed general support for the hybrid, cost-based methodology recommended by staff.

### **WSR Fee Update**

A hybrid approach has been used to calculate WSR fees since 2018. The current hybrid approach determines the value of Utilities' water supply by summing the market value of existing water rights and infrastructure (buy-in component) and the market value of future water rights and infrastructure yet to be purchased (incremental component). While full buy-in or incremental approaches are used by some water providers, those approaches do not appropriately reflect Utilities' water supply circumstances where future customers will utilize both the existing and future water supply system. Therefore, neither have been used in the past.

Staff are now proposing to apply a cost-based value to the buy-in component for all existing water rights. Cost-based value is what Utilities originally paid for the water, then increased by the consumer price index (CPI) as opposed to a market-based cost. A cost-based approach for the buy-in component is less expensive and more appropriately reflects the cost for water rights that were purchased early on when the cost of water was lower.

The recommended approach also includes a 30% contingency factor which is meant to cover uncertainties in the cost of future water rights and infrastructure. This contingency is only applied to the incremental portion of the WSR fee. A 20% safety factor is also included. This is intended to cover uncertainties in future water supply and demand such as climate impacts and rate and type of development/redevelopment that may or may not occur. A 20% safety factor is not standard among other water providers; however, most water providers apply some sort of risk factor or methodology to account for potentially lower water supplies. Some of these include building a buffer into dedication requirements, relying on drought response plans to adjust in low water years, or other contingency factors. Staff do not consider the 30% contingency factor or 20% safety factor to be redundant because they serve different purposes and have included both in the WSR fee.

Since the April 9 Council work session, staff worked with a consultant to determine the best approach to adjust the cost of existing water rights under the hybrid, buy-in, cost-based portion of the fee. The decision was to escalate by the CPI. The result is a fee of \$63,800 per acre-foot, which is \$4,400 per acre-foot less than the current fee of \$68,200 per acre-foot.

The other option that was presented on April 9 was to continue with the current hybrid, market-based method for the buy-in and incremental approach. After updating the market values of water rights, the fee is \$110,700 per acre-foot. This is a decrease from the \$116,500 per acre-foot that was presented in April, due to a decrease in Colorado-Big Thompson water rights values over the past nine months.

### **Relationship Between Rates and Fees**

Because Utilities is a municipal-owned, cost-of-service utility provider, there is an inverse relationship between rates and fees. In general, the lower the WSR fee, the more it will impact customer rates. The higher the fee, the less it will impact rates. The WSR fee also impacts the source of funding for projects like the Halligan Water Supply Project (Halligan). The impact to customer rates strongly correlates to the amount of development that occurs. The City's Planning Department has two projections for the type of development and associated growth we can expect, which results in an additional water dedication of either 1,024 or 2,000 acre-feet over the next 40 years. If the recommended WSR fee of \$63,800 is implemented, it is projected that Utilities will collect roughly \$4.5 million less in development fee revenue by 2065 compared to requiring the current fee of \$68,200 per acre-foot. This is a decrease of 6.5% in development fees, which would require roughly a half-percent increase in customer rates to recoup the difference. On average, staff expect development to pay Utilities for roughly 25 acre-feet of water in cash for development each year over the long term. In recent years, though, this amount has been much less, which also drives higher short-term needs to increase rates to stabilize revenue and increase debt capacity for a project such as Halligan. Currently, Utilities estimates a 7-10% increase in water rates each year over the next 10 years based on the current fee and average revenue from WSR and surcharges over the past five years.

### **Dedication Amounts**

The total WSR fee is based on the water supply needed by a development. It was noted at the April 9 Council work session that regional dedication requirements vary by water provider and within the City's Growth Management Area. Other providers use different calculation methods such as tap credit or peak water use, different time periods of historical use, or inclusion of a safety factor. Of note, Utilities serves approximately 80% of the City's population and 60% of the area within City limits. The Utilities WSR is based on a development's business type and characteristics such as square footage of building and

landscape, number of rooms, etc. In general, the fee varies such that lower water-use developments pay less, while higher water-use developments pay more. Utilities water dedications were determined using analysis of existing accounts' actual consumption. Using this method, it was determined that restaurants generally use more water than other businesses. Based on the actual consumption analysis, staff are confident in the dedication requirements for each business category.

### **Assignment of Pre-1984 Non-residential Allotments**

On April 9, staff also provided a history of assigning allotments. Approximately 1,000 pre-1984 non-residential (commercial) accounts do not have an allotment. Staff recommended assigning allotments to these customers for consistency, fairness, and more conservation opportunities. There were four methodologies presented for calculating an allotment with staff recommending a hybrid methodology.

The hybrid methodology assigns an allotment using either the 1989 tap credit or the account's five-year historical average use, whichever is greater. Utilizing a five-year average helps to reflect the most recent history and ownership should businesses have changed owners or uses over time.

By assigning the higher allotment value using tap credit or average use, the goal is to minimize overages and the incurrence of an excess water use surcharge (surcharge). Staff estimated potential surcharge impacts by comparing the account's proposed allotment to the annual consumption for that account in the last five years. Had all accounts been assigned an allotment during that time, between 50-75 accounts – approximately 5-7% of the pre-1984 accounts – would have incurred surcharges each year. For comparison, 8-15% of accounts with existing allotments incurred surcharges in each of the last five years.

Analysis of pre-1984 accounts with identified use types shows the most likely to be impacted by surcharges are irrigation-only accounts, including several City-owned properties, mixed-use strip malls, and restaurants. The potential impact may be attributed to highly variable factors affecting these use types such as weather, patronage, and revolving tenants.

Additionally, staff anticipate some additional, highly variable account uses, including large water users and large tap accounts, some City-owned facilities, and some homeowner's associations that may experience more negative impacts and require more in-depth analysis, customer outreach, and support.

It is likely that many accounts potentially subject to surcharges would benefit from conservation programs, which would decrease anticipated impact. Office hours throughout the next several months will allow customers and staff to discuss specific water needs and any conservation opportunities that may be a good fit for a particular account, property or use type.

Between 2019-2023, 25 of 157 City-owned accounts with allotments have exceeded their allotments. Eleven accounts exceeded more than once in the last five years. Since 2019, City accounts have paid an estimated \$176,000 in surcharges. Of the 138 City-owned accounts without allotments, 10 would have exceeded at least once in the last five years. Five would have exceeded more than once.

### **Customer Outreach**

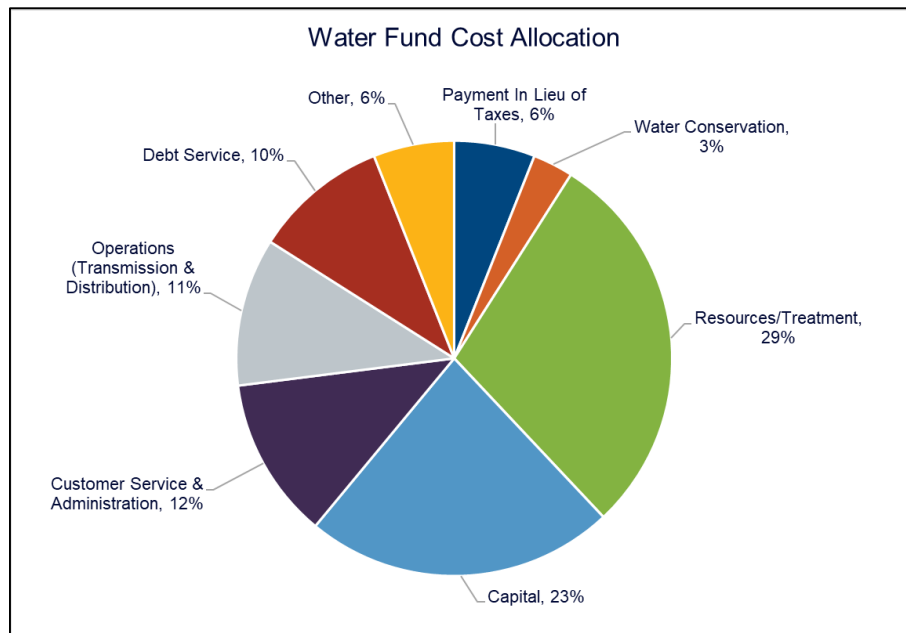
Utilities reached out to customers and community members who will potentially be impacted by these decisions, including developers, community groups, Boards and Commissions, existing customers, and non-residential customers who would be assigned an allotment. In general, the feedback received has been positive or neutral, with most groups interested in better understanding their specific situation. Tactics for outreach included: Our City page, direct email and mail, webinar for potential new allotment customers, lunch and learn for internal staff, and dedicated office hours appointments by request.

## Additional Follow-up

Remaining Councilmember questions with staff responses:

1. What is the breakdown of fees on a customer's bill?

The graph below illustrates the breakdown of a customer's bill. Capital improvement projects (Capital) can vary year to year, and for the next 10-year timeframe, will likely range between 25-35%. This graph is also [available online](#).



2. What WSR fee was used in the base rate setting?

The current fee of \$68,200 per acre-foot.

3. Are we disincentivizing residents to remodel or redevelop?

The residential WSR for indoor water use is based only on the number of bedrooms and is not applicable to general home remodels. Any remodel or redevelopment that adds bedrooms, such as an addition to the home or building a separate accessory dwelling unit, requires the property owner to pay a WSR fee for the increase in water service. However, at a proposed fee of \$63,800, Utilities would still have one of the lower fees for most types of residential developments compared to surrounding providers.

## NEXT STEPS

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1. Bring forth an ordinance for the WSR methodology and fee and assigning allotments for first reading in October 2024.

## ATTACHMENTS

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1. Presentation