CHAPTER 8 CAPACITY FEE EVALUATION

The purpose of the capacity fee is to recoup the capital costs of facilities needed to serve new customers connecting to the wastewater system. This Master Plan outlines two options evaluated for calculating the wastewater capacity fee. Option 1 included the Buy-in to Existing Facilities and includes the depreciated value of existing City pipelines and the value of the City's existing capacity rights at Metro. Option 2 included the Incremental Capacity Expansion and including the cost of expanding City pipelines and building a City-owned recycled water treatment plant. As discussed in Chapter 3 of this report, future flow projections indicate the City must either purchase additional capacity in the Point Loma Wastewater Treatment Plant (PLWWTP) and/or construct City-owned treatment facilities in about 10 years.

The PLWWTP has been issued a waiver from the Environmental Protection Agency (EPA) which allows the plant to operate at an advanced primary treatment level. The waiver expires in 2015 at which time the PLWWTP may be required to upgrade and operate at a secondary treatment level. The City of San Diego's 2012 Recycled Water Study recommends upgrading the PLWWTP to accommodate a secondary treatment level capacity of 143 mgd and offloading 100 mgd of flow away from the PLWWTP to expanded recycled water facilities. As a member agency of Metro, the City of Chula Vista will share in the cost of any upgrades proportional to the city's share of the overall capacity of the PLWWTP.

8.1 ECONOMIC AND LEGAL BASIS FOR CAPACITY FEES

The following section provides a general review of basic economic and legal foundations for capacity fees. Some agencies refer to connection fees as capacity fees, system development charges, impact fees, or other similar names. The City refers to these fees as capacity charges.

Expansion of service to new customers carries with it costs to provide that service. As the number of customers grows, system capacity typically needs to be expanded to provide service to the new customers. Even in those utilities that have available capacity in place that can be used to service new customers, new facilities or capacity will ultimately be required to accommodate growth. Where capacity to accommodate new customers is available in the existing system, there are still costs to be recognized. The costs for making this excess capacity available to serve new customers have, however, been absorbed by present and past customers of the system. The manner in which costs are recovered, whether for existing or expanded capacity, depends on a number of technical, policy, and legal issues. These could include equity in distributing the costs among customers, the ease or cost of implementation and administration, and legal requirements or constraints.

8.1.1 ECONOMIC BASIS FOR CAPACITY FEES

The basic economic philosophy behind imposition of capacity fees is that the costs of providing service should be paid for by those customers receiving the benefits of that service so that no one customer or group of customers subsidizes any other customers. In establishing any fee or charge, achieving equity is one of the primary goals. In the case of capacity fees, this goal has been expressed in the form of "growth should pay for growth."

8.1.2 LEGAL FRAMEWORK GOVERNING CAPACITY FEES

Bartle Wells Associates does not practice law, but is aware of certain provisions of the statutes and regulations that are applicable to the development of capacity fees. In California, the basic statutory standards governing water and sewer capacity fees are embodied in Government Code Section 66013, 66016, and 66022. Government Code 66013 provides the fundamental provisions:

> (a) Notwithstanding any other provisions of law, when a local agency imposes fees for water connections or sewer connections, or imposes capacity charges, those fees or charges shall not exceed the estimated reasonable cost of providing the service for which the fee or charge is imposed, unless a question regarding the amount the fee or charge imposed in excess of the



estimated reasonable cost of providing the services or materials is submitted to, and approved by, a popular vote of two-thirds of those electors voting on the issue.

(b) As used in this section

(1) "Sewer connection" means the connection of a building to a public sewer system.

(2) "Water connection" means the connection of a building to a public water system, as defined in subdivision (e) of Section 4010.1 of the Health and Safety Code.

(3) "Capacity charges" means charges for facilities in existence at the time the charge is imposed or charges for new facilities to be constructed in the future which are of benefit to the person or property being charged.

(4) "Local agency" means a local agency as defined in Section 66000.

(c) Any judicial action or proceeding to attack, review, set aside, void, or annul the ordinance, resolution, or motion imposing a fee or capacity charge subject to this section shall be brought pursuant to Section 66022. Section 66013 indicates that any connection fee must be based on an estimate of the reasonable cost of providing service. The legislative history of this provision indicates that the legislature did not intend to limit the types of costs that would be included.

The underlying basis for the legal framework is that any capacity fees imposed should reflect the estimated reasonable cost of providing service to new customers, unless voters have specifically approved a higher level for the fees.

8.2 STANDARD CAPACITY FEE METHODOLOGIES

BWA reviewed the legal framework for establishing capacity fees and various methodologies for calculating the fees. The capacity fee methodologies are summarized below.

8.2.1 System Buy-in Method

The buy-in concept is based on the premise that new customers are entitled to service at the same price as existing customers. Existing customers, however, have already provided the facilities that will serve the new customers, including any costs of financing those facilities. Under this method, new customers pay an amount equal to the investment already made by existing customers in the facilities. This equity investment is divided by the number of customers (or customer equivalents) to determine the amount of payment required from the new customer to buy in to the utility at parity with existing customers.

Once new customers have paid their fee, they become equivalent to existing customers and share the responsibility for existing facilities. When additional costs are incurred for system improvements, replacement, or expansion, all customers share the costs of such improvements.

8.2.2 Incremental Cost Method

When new customers connect to the wastewater system, they use either reserve capacity available in existing facilities, or they require new capacity that must be added to the system to accommodate their needs. Under this method, each new customer would pay for the marginal cost of their use of the reserve capacity and for new facilities necessary to provide service to them. The goal of this method is to minimize or eliminate the need to raise rates in order to provide for system expansion.

Consequently, new customers pay fully for the additional facilities without imposing a burden on existing customers. Since it is likely that the timing of payments received from the capacity fees will not exactly match the timing of expenditures to provide facilities, the fee should be adjusted to reflect the time value of money. The intent is that the charge be equal to the required investment as if the construction were to occur at the time of contribution.

8.3 EXISTING AND FUTURE CAPACITY

The City's existing capacity and build-out capacity are summarized in Table 8-1. As mentioned, treatment is provided via a capacity purchase agreement with Metro. The City is entitled to 20.864 million gallons per day (mgd) of daily treatment rights at Metro. Currently, the average day flow of the City is 15.73 mgd or about 75% of the City's capacity rights (See Appendix A for the METRO Agreement). At build-out, IEC estimated an average daily flow of 29.89 mgd, which is about 9.026 mgd greater than the City's daily treatment rights.

Table 8-1: Current and Future Capacity

Description	MGD
Current Average Daily Treatment	15.730
Available Daily Treatment Rights at Metro	5.134
Daily Treatment Rights at Metro	20.864
Build-out capacity exceeding daily treatment rights at Metro	9.026
2050 Build-out Capacity	29.890
Incremental Capacity to Build-out	14.160
(2050 Build-out Capacity less Current Average Daily Treatment)	

Source: City of Chula Vista and IEC

8.4 BUY-IN TO EXISTING FACILITIES

To develop a buy-in capacity fee for the collection system, BWA was tasked with determining the value of the system. The City provided BWA with a fixed asset list showing the original value of the collection system at the year constructed.

8.4.1 VALUATION METHODS

To value the collection system, BWA reviewed the Replacement Cost New Less Depreciation, Historic Cost at Present Value, and Estimated Replacement Cost approaches to utility valuation.

8.4.1.1 REPLACEMENT COST NEW LESS DEPRECIATION (RCNLD)

This method is based on the depreciated accounting book value of each asset escalated into current dollars based on the change in the Engineering News-Record (ENR) Construction Cost Index from each asset's original date. The ENR index is a widely-used index for determining construction cost inflation.

This method has a couple of shortfalls consisting of: a) it is based on a conservative estimate of depreciation used for accounting purposes, which often does not correlate with the actual life of assets (i.e. assets may be fully depreciated but still in good working condition), and b) discounts the amount collected from future connections and thereby does not fully recover the cost of the asset in current dollar terms. For example, if the City funds a lift station to meet the needs of growth, but no growth occurs for many years, then the future connections would get the benefit of only buying in for a reduced, depreciated value brought into current dollars as opposed to having to pay for their share of total costs (adjusted for construction cost inflation) regardless of when the connection is made.

BWA used the RCNLD approach to value the City's collection system infrastructure. Each method has advantages and disadvantages, but BWA believes that the RCNLD method is the most equitable as it values facilities at their current, depreciated value.

8.4.1.2 HISTORIC COST AT PRESENT VALUE

This method escalates the original purchase price of each asset into current dollars using the ENR Construction Cost Index to account for construction cost inflation. This approach ensures that new connections buy-in for the full inflation-adjusted cost of existing facilities.

This approach does not consider depreciation. The City made major capital investments in the collection system in the 1970s and 1980s. A number of facilities are past their expected useful lives and are fully depreciated (i.e. have no value based on an accounting perspective). It may not be equitable for new customers to buy into facilities at full cost that have a high degree of "wear and tear" and have no book value.

8.4.1.3 ESTIMATED REPLACEMENT COST

Under this approach, the current (or replacement) value of existing facilities is estimated based on an inventory of existing assets (e.g. pipelines by linear footage) and the current costs of construction. BWA was not able to use this approach because up to date construction costs are not available.

8.4.2 ADJUSTMENTS

BWA made adjustments to the RCNLD value of the collection system to account for developer contributions and City capital reserves.

8.4.2.1 CAPITAL RESERVES

The City has a number of funds to account for fees paid by new customers connecting to the sewer system, see Table 8-2. These funds are restricted by City ordinance and may only be used for improving and expanding the system. These capital reserves have already been paid by new connections and are subtracted from the sewer collection system value. The City expects to fund $5 million in capital improvements from the available reserves.

8.4.2.2 DEVELOPER CONTRIBUTIONS

Since 2003, developers have contributed about $102,501,000 of wastewater facilities to the City of Chula Vista. These facilities were not paid for by existing customers and thus should not be paid for by new customers. BWA determined the RCNLD value of the developer contributions and subtracted it from the calculated buy-in value.

8.4.2.3 TOTAL VALUE LESS CAPITAL RESERVES AND DEVELOPER CONTRIBUTIONS

The total adjusted value of City pipeline (collection system) assets is shown in Table 8-3. The value varies from $39.5 million to $395.0 million based on the approach used. BWA believes that the adjusted RCNLD value (valuation C) of $39.5 million is a fair and reasonable value of City assets. The other valuation methods do not account for the present value of facilities at their current age and condition. The historical cost at year built (valuation A) is the cost that the City paid for facilities at the year of construction and ignores the opportunity cost of the City's investment in its infrastructure. The historical cost at present value (valuation B) brings the City's initial investment into current year dollars but does not reflect the system's age or condition. BWA opines that the historical cost at present value method should not be used for the calculation of capacity fees because it represents the cost of brand new facilities and does not account for system deterioration. It is unfair to charge customers a "like new" price for facilities that are not in "like new" condition. The RCNLD value is the depreciated value of facilities in current year dollars.

Table 8-2: Available Capital Reserves

Fund Name	Revenue Source	Authorized Uses	Included	Estimated Balance End of FY2013
411 - Sewer Income Fund	Revenues collected to recover the City's costs incurred constructing the public wastewater system. The funds are collected from new properties receiving a permit to connect to the City wastewater collection system.	Acquisition, construction, reconstruction, maintenance and operation of sanitation or sewerage facilities, or to reimburse a subdividor or any person who has constructed sewer facilities benefiting other properties.	Not included.	
412 - Special Sewer Fund	Unknown	Fund is used to account for sale of the City's excess Met sewerage capacity.	Included.	$449,972
413 - Trunk Sewer Capital Reserve Fund	Sewerage facility participation fees received from the owner or person applying for a permit to develop or modify the use of any residential, commercial, industrial or other property, which is projected to increase the volume or flow in the City's sewer system, as determined by the City Engineer.	Repair, replace, or enlarge the trunk sewer facilities. Plan or evaluate sewage treatment or water reclamation facilities. City Council can appropriate funds for another purpose provided such purpose shall be for the planning, design, construction, maintenance or operations of sewage collection or treatment or water reclamation purposes.	Included.	$56,342,080
414 - Sewer Service Revenue Fund	Revenues collected for the monthly sewer service charge.	Revenues may be used for any and all sewer related activities.	Not included.	
431, 432, 433 - Sewer Development Impact Fee Funds	Fees that are levied against new development in specific areas of the City, based upon the sewer facility their project will impact.	Construction of public improvements designed to increase the capacity of subject facilities, allowing the City to maintain service levels with increased demand.	Not included.	
Subtotal Fund Balance				$56,792,052
Sewer System Repairs and Replacements				(5,000,000)
Total Fund Balance				$51,792,052

Table 8-3: Valuation of Existing City Pipeline Assets Collection System Capacity Fee

Valuation Method	Asset Value	Less Developer Contributions	Less Capital Reserves	Total
Historic Cost at Year Built	$224,522,152	($102,500,717)	($51,792,052)	$70,229,383
Historic Cost at Present Value (2013 Dollars)	$573,839,104	($127,015,538)	($51,792,052)	$395,031,515
Replacement Cost New Less Depreciation (2013 Dollars)[1]	$192,346,068	($101,025,341)	($51,792,052)	$39,528,676

1 - Used in capacity fee calculation

There are two cost components of the collection system that could be included in wastewater capacity fee calculations: a buy-in to existing facilities and the incremental cost of expanding the collection system to serve new connections.

Table 8-4 shows the buy-in cost for the existing collection system assets. The value of existing collection system assets are divided by the build-out capacity of 29.89 mgd to yield a cost of $1.32 per gallon per day (gpd) of sewer capacity. The gpd cost is multiplied by the estimated average daily capacity used by the connection to calculate the final capacity fee. IEC recently reviewed the City's infrastructure and flow rates for the City of Chula Vista's Wastewater Master Plan Update. As discussed in Chapter 3 above, the average daily flow of a single family residence or equivalent dwelling unit (EDU) for the City is 230 gpd. When compared to other local agencies in the area, this value is lower; however, this is reflective of the downturn in the economy as well as water saving methods implemented throughout the City. As Table 8-4 shows, the buy-in capacity fee for the existing collection system is $303.60 per EDU ($1.32 gpd multiplied by 230 gallons per day).

Table 8-4: Buy-in to Existing Collection System

Net Valuation of Existing City Pipeline Assets	$39,528,676
Build-out Capacity (gpd)	29,890,000
Cost of capacity (gpd)	$1.32
Flow per EDU (gpd)	230
City Pipeline Buy-in Cost per EDU	**$303.60**

Applicable to Buy-in to Existing Facilities

As part of the master planning process, IEC developed a capital needs list for collecting and conveying the wastewater flows of the City through build-out. To serve new customers connecting to the system, IEC projects that the City will need to complete $10,762,400 of pipeline, manhole expansion, and flow meter vault improvements.[1] The incremental cost of expanding the collection system is divided by 14.16 mgd, the capacity used by future customers. The current collection system cannot accommodate any new customers. All new connections between now and build-out should share in the cost of expanding the collection system from 15.73 mgd (current) to 29.89 mgd (build-out). The incremental cost is $0.76 per gpd or $174.80 per EDU, see Table 8-5.

1 - For a description of capital improvements see Wastewater Master Plan Update Draft Report, TM4 – Capital Improvement Costs; Developer Imposed Fee (DIF) projects are not included in the capacity fee calculation

Table 8-5: Collection System Expansion

Incremental Fee of Collection System Expansion	
Pipeline/Manholes/Flow Meter Vault	$10,762,400
Total Capital Improvements	$10,762,400
Expansion Capacity (gpd)	14,160,000
Cost of capacity (gpd)	$0.76
Flow per EDU (gpd)	230
City Pipeline Expansion Cost per EDU	**$174.80**

Applicable to Incremental Facilities Expansion

8.5 COST OF CAPACITY FROM METRO

The value of capacity in the existing Metro system has been evaluated by various consultants over the past eight years. Raftelis Financial Consultants (RFC) was engaged by Metro and the City of San Diego in 2008 to calculate the value of capacity rights. RFC relied upon a Metro fixed asset list from 2005 escalated to 2007 dollars. RFC explored various valuation methodologies and recommended the Buyer's Avoided Cost and the Alternative Investment Values to estimate the cost of Metro capacity.

The Alternate Investment Value methodology calculates the value of Metro's investment in infrastructure based on the 2005 fixed asset list and Metro's weighted cost of capital. Atkins Global, Metro's financial consultant, evaluated RFC's valuations in 2011 and updated the cost of capacity. As shown in Table 8-6, BWA further updated the Alternative Investment Value to reflect 2013 dollars. The cost of capacity for the existing Metro facilities is $3,788.10 per EDU.

Table 8-6: Values of Metro Existing Facility Capacity

Value Approach/Pricing Perspective	Total Value (2007)	Divisor	Total Value (2011)	Total Value (2013)	Value per gpd (2013)	Cost per EDU (230 gpd)
	(billion)	(mgd)	(billion)	(billion)		
Alternative Investment Value[1]	$3.7	255	$4.10	$4.20	$16.47	$3,788.10

Table adapted from DRAFT Evaluation Study of Capacity Valuation conducted by the City of San Diego's financial consultant Atkins Global.
1 - Alternative Investment Value based on July 2011 cost escalated to July 2013 using the ENR CCI for Los Angeles.

Applicable to Buy-in to Existing Facilities

8.6 COST OF CAPACITY FOR A CITY-OWNED RECYCLED WATER TREATMENT PLANT

RMC conducted a study "Acquisition of Additional Wastewater Capacity Project Final Report" in April of 2012. RMC determined that a City-owned recycled water treatment plant with 6 mgd capacity would cost $116 million. The City's wastewater flows would be routed to the plant for treatment producing recycled water that would be sold to customers. Solids from the City-owned plant would be transported to the PLWWTP for disposal. The City's capacity rights in the Metro system are based on flow and would not be impacted by additional solids.

IEC updated the construction cost of the City-owned recycled water treatment plant to reflect an increased build-out flow estimate and to bring the construction cost estimate into current dollars. IEC estimates that by 2050 the City will exceed its daily treatment rights at Metro by 9.026 mgd (see Table 8-1), 3.026 mgd greater than the recycled water treatment plant capacity described by RMC. IEC's estimated construction cost is $180.4 million for a 9.026 mgd recycled water treatment plant. It is assumed that the City will utilize its 5.134 mgd in available treatment rights at Metro and then potentially pursue new capacity with a recycled water treatment plant. The capacity cost for a City-owned treatment plant is $14.24 per gpd or $3,275.20 per EDU, see Table 8-7. The recycled water treatment plant cost shown in Table 8-7 represents the full

construction cost of the plant absent grant funding. The construction cost and capacity fee would be reduced if the City obtained grant funding.

Table 8-7: Incremental Cost of Chula Vista Recycled Water Treatment Plant

City Recycled Water Treatment Plant capital cost	$180,354,807
Less Available Capital Reserves	(51,792,052)
Total Recycled Water Treatment Plant expenditure	$128,562,755
City Recycled Water Treatment Plant capacity (gpd)	9,026,000
Cost of capacity (gpd)	$14.24
Flow per EDU (gpd)	230
City Recycled Water Treatment Plant Cost per EDU	**$3,275.20**

Applicable to Incremental Facilities Expansion

8.7 COMPARISON OF CAPACITY FEE CALCULATIONS

The following sections summarize the capacity fee calculations for the Buy-in to Existing Facilities and for Incremental Capacity Expansion. The figures 8-1 and 8-2 illustrating each option are repeated below for convenience. The Buy-in to Existing Facilities results in a capacity fee of $4,091.70 per EDU and the Incremental Capacity Expansion results in a capacity fee of $3,450.00 per EDU.

8.7.1 Option 1: Buy-in to Existing Facilities

Figure 8-1: Buy-in to Existing Facilities

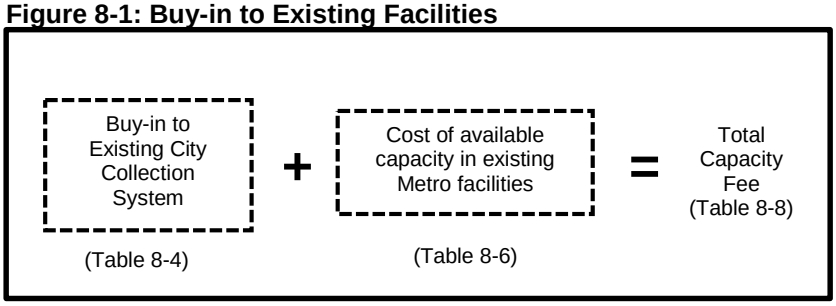


Table 8-8: Summary of Wastewater Capacity Fee Buy-in to Existing Facilities

Capacity Fee Components	Cost per gpd	% of Total Cost	Cost per EDU (230 gpd)	Source
City Pipeline Buy-in	$1.32	7.4%	$303.60	Table 8-4
Available Metro Capacity	$16.47	92.6%	$3,788.10	Table 8-6
Total	**$17.79**	**100.0%**	**$4,091.70**	

8.7.2 Option 2: Incremental Capacity Expansion

Figure 8-2: Incremental Capacity Expansion

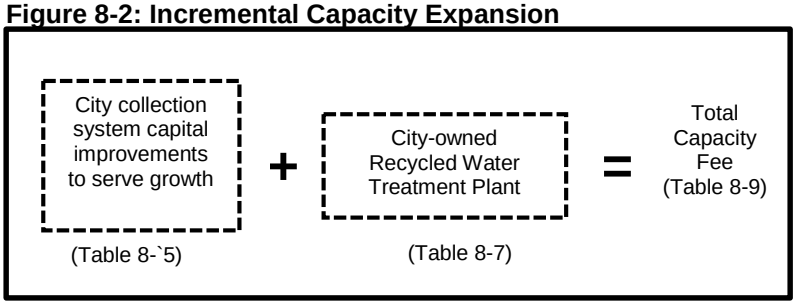


Table 8-9: Summary of Wastewater Capacity Fee Incremental Capacity Expansion

Capacity Fee Components	Cost per gpd	% of Total Cost	Cost per EDU (230 gpd)	Source
City Pipeline Expansion	$0.76	5.1%	$174.80	Table 8-5
City-owned Recycled Water Treatment Plant	$14.24	94.9%	$3,275.20	Table 8-7
Total	$15.00	100.0%	$3,450.00	

8.7.3 PLWWTP SECONDARY EXPANSION

The City currently has 9.026 MGD of capacity available in the Metro system. As development occurs, the available capacity will be allocated to new connections until the City has no capacity available. At that point (estimated between 2022 and 2025), the City could purchase additional capacity in the Metro system. It is envisioned that by the time the City requires additional capacity, the Point Loma Wastewater Treatment Plant will be upgraded to secondary treatment. The City would purchase secondary treatment capacity at a higher cost than the current primary treatment capacity shown in Table 8-8. Tables 8-10 and 8-11 show the estimated capacity fee if the City purchases secondary treatment capacity from Metro.

Table 8-10: PLWWTP Secondary Expansion Capacity Cost

PLWWTP Secondary Expansion capital cost	$288,567,700
Less Available Capital Reserves	(51,792,052)
Total PLWWTP Secondary Expansion expenditure	$236,775,648
Incremental capacity (gpd)	9,026,000
Cost of capacity (gpd)	$26.23
Flow per EDU (gpd)	230
PLWWTP Secondary Expansion Cost per EDU	**$6,032.90**

Table 8-11: Summary of Wastewater Capacity Fee PLWWTP Secondary Expansion

Capacity Fee Components	Cost per gpd	% of Total Cost	Cost per EDU (230 gpd)	Source
City Pipeline Expansion	$0.76	2.8%	$174.80	Table 8-5
PLWWTP Secondary Expansion	$26.23	97.2%	$6,032.90	Table 8-10
Total	$26.99	100.0%	$6,207.70	

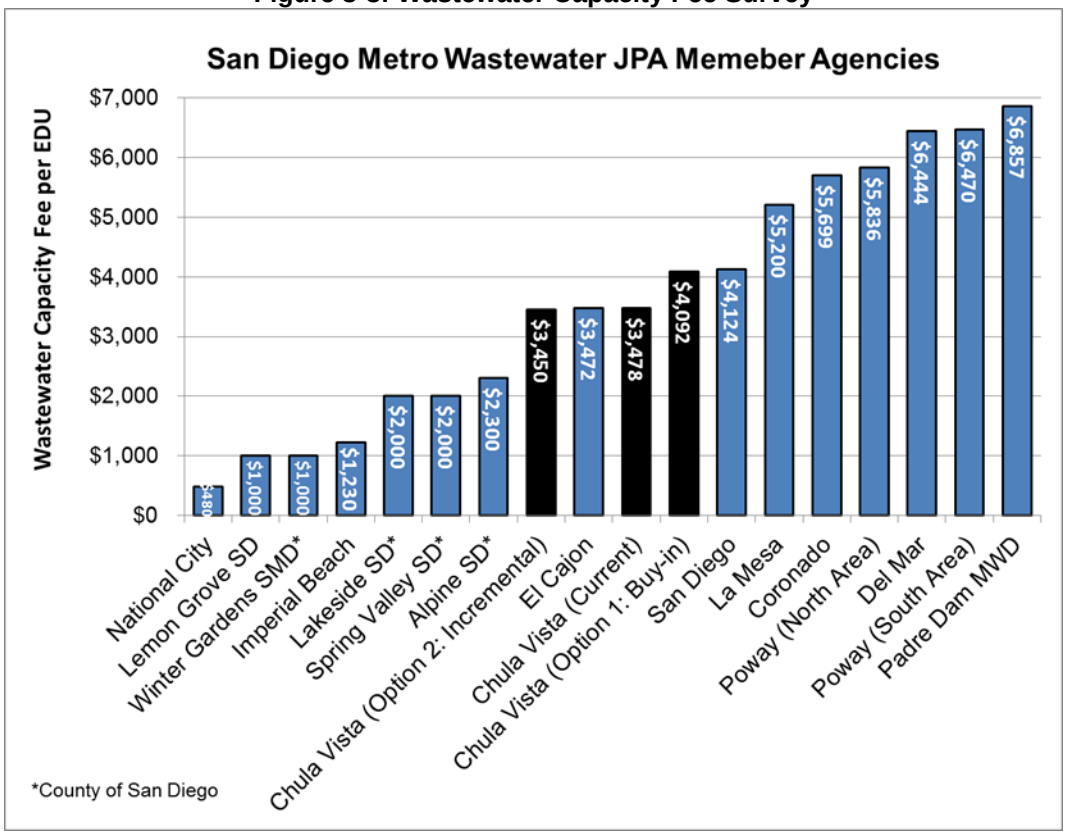
8.7.4 SUMMARY OF CAPACITY FEE OPTIONS

Table 8-12 summarizes the capacity fee options in comparison to the existing capacity fee of $3,478.00 (implemented in 2005), the current capacity fee adjusted to current dollars, and the PLWWTP secondary expansion capacity fee. Option 1: Incremental Capacity Expansion is the lowest capacity fee at $3,450.00 and the PLWWTP Secondary Expansion represents the highest capacity fee at $6,207.70.

Table 8-12: Comparison of Capacity Fee Calculations

Option	Description	Cost of Capacity	Capacity Fee (230 gpd)
Option 1: Buy-in to Existing Facilities	Existing collection system and available capacity at Metro	$17.79	$4,091.70
Option 2: Incremental Capacity Expansion	Collection system expansion and City-owned Recycled WTP	$15.00	$3,450.00
For Comparison	**Description**	**Cost of Capacity**	**Capacity Fee (230 gpd)**
Current Capacity Fee	Wastewater Master Plan, May 2005	$15.12	$3,478.00
Current Capacity Fee escalated to 2013	May 2005 cost escalated to July 2013 using the ENR CCI for Los Angeles	$18.85	$4,336.12
PLWWTP Secondary Expansion	Collection system expansion and PLWWTP Secondary Expansion	$26.99	$6,207.70

Figure 8-3: Wastewater Capacity Fee Survey



8.8 RECOMMENDATIONS

BWA's recommended method for calculating and updating the capacity fee is provided below.

8.8.1 *Recommended Method*

Both the Buy-in to Existing Facilities and the Incremental Capacity Expansion method are fair to customers and reflect the capital costs of providing capacity in the wastewater system. Ultimately, BWA recommends the Incremental Capacity Expansion method to calculate the capacity fee as it is a lower cost option that conservatively recovers expansion related costs from new development. The Incremental Capacity Expansion calculation is based on the best available information regarding the City's preferred treatment expansion alternative. BWA acknowledges a number of unknowns including the status of the PLWWTP secondary treatment waiver and the City's cost to construct its own recycled water treatment plant. If actual construction costs are higher than estimated or if the City pursues an additional capacity purchase at the PLWWTP, this method may result in under collection of revenues for system expansion.

8.8.2 *Adjusting Capacity Fees*

Capacity fees should be adjusted regularly to prevent them from falling behind the costs of constructing new facilities. Several methods can be used to adjust the capacity fees, including:

- ENR Construction Cost Index: ENR (Engineering News-Record) magazine publishes construction cost indices monthly for Los Angeles. This index can be used to estimate the change in the construction cost of facilities. If the ENR Index has increased by three percent since the last capacity fee adjustment, the capacity fee should be increased by three percent.
- U.S., California, or regional consumer price index.
- Interest rate and borrowing costs: The interest and borrowing costs for debt issued to finance sewer capital projects can be added to the capacity fee annually.

We recommend that the City adjust its capacity fee annually by the change in the ENR Construction Cost Index for Los Angeles. This is the most appropriate index because it directly reflects construction costs. Suggested language for implementing this policy is:

> Each year, commencing on ____(m/d/y)____ and continuing thereafter on each ____(m/d)__, the capacity fee shall be adjusted by an increment based on the change in the Engineering News-Record Construction Cost Index for Los Angeles over the prior year.
>
> However, the City Council may at its option determine, by resolution adopted prior thereto, that such adjustment shall not be effective for the next succeeding year, or may determine other amounts as appropriate.

Capacity fees should also be reviewed in detail when updated information, such as a revised master plan or capital improvement program, is obtained, but not less than every five years.