



STAFF REPORT

City Council
Meeting Date: 2/24/2026
Staff Report Number: 26-025-CC

Informational Item: Update on the Menlo Park Municipal Water Rate Study

Recommendation

This is an informational item that does not require City Council action. Staff recommend that the City Council receive a preview of the Menlo Park Municipal Water (MPMW) July 1, 2026 – June 30, 2031, Water Rate Study (Study) in preparation for rate adjustments for an upcoming meeting March 10. The proposed rates would be in effect starting July 1.

Policy Issues

MPMW is a city-owned water service provider for a portion of the City of Menlo Park. The City Council acts as the governing body for MPMW and is responsible for establishing rates that recover the full cost of providing service, consistent with the requirements of Proposition 218 (Prop. 218).

Background

MPMW supplies water to approximately 4,400 customers, including residential, non-residential (commercial, industrial, institutional, irrigation), and fire services (Attachment A). MPMW's sole water supply is purchased from the San Francisco Public Utilities Commission (SFPUC) and delivered to properties within the service area. MPMW operates as a self-supporting enterprise fund. As such, it must develop a financial plan that provides sufficient revenue to meet all operation and maintenance expenses, capital improvement projects (CIP), and other revenue requirements independent of the City.

As a municipal water provider, the City is required to adhere to the requirements of Article XIII(D) of the California State Constitution, known as Prop. 218 in the development of water rates. To comply with Prop. 218, rates studies are developed to ensure that proposed rates meet the following requirements:

- Revenue derived from rates must not exceed funds required to provide the service;
- Revenue derived from rates must not be used for any purpose other than for which it is imposed;
- The rates imposed must not exceed the proportional cost of the service provided;
- A Prop. 218 notice must be mailed to every property owner served by MPMW to provide information about the proposed rates and allow an opportunity to submit written protests at least 45 days before a City Council public hearing to adopt new rates; and
- Rates cannot be adopted if more than 50% of property owners submit written protests.

Historically, water rates have been adopted through periodic rate studies. The City Council adopted five-year rates in 2015 through fiscal year 2019-20 and opted for no increase in fiscal year (FY) 2020-21 in light of the COVID-19 pandemic. During that time, City Council also directed staff to explore a rate for qualifying low-income customers. On Dec. 8, 2020, City Council approved a rate assistance pilot program to assist those suffering financial hardship. Qualified households may receive a 20% monthly discount on solid waste

service from Recology San Mateo County and a monthly discount on the fixed meter charge on water service from Menlo Park Municipal Water. This program is funded by the General Fund and the City Council renews the program annually. For households who live in the California Water (Cal Water) service area, Cal Water provides their own financial assistance program for qualified households. On May 11, 2021, the City Council adopted Resolution No. 6625 approving five-year water rates through FY 2025-26 (Attachment B).

MPMW’s monthly rates include multiple components described in Table 1. To encourage conservation, City Council opted to implement a three-tier rate structure in 2021, reducing the consumption charge for customers using less water. Tier 1 is set with a lower rate for the first 6 centum cubic feet (ccf) of water consumed. Tier 2 has a higher rate for 7 to 12 ccf of water consumed and represents both indoor and outdoor use (the 12 ccf represented the average household monthly use in 2021). Tier 3 is the highest rate for water measured above 12 ccf. The changes in the tiered structure and rates resulted in a \$9.51 decrease in the monthly bill for a typical single-family home customer using 12 ccf in FY 2021-22.

Table 1: Current water rate monthly charges	
Item	Description
Meter charge	This charge is based on meter size. For fire service connections, a separate monthly service charge is applied based on the size of the service connection.
Consumption charge	This charge is based on the amount of water consumption measured in ccf (one ccf = 100 cubic feet = 748 gallons). The charges are based on the following tiers: <ul style="list-style-type: none"> • Tier 1 (lower rate) applies to every customer for up to the first 6 ccf • Tier 2 (medium rate) applies to water consumption between 7 ccf and 12 ccf • Tier 3 (higher rate) applies to water consumption above 12 ccf
Capital facility surcharge	This surcharge is based on water consumption and is used to partially fund capital projects.
Drought surcharge	There are five stages of drought as established by the State Water Resources Control Board (SWRCB) which require varying levels of conservation when declared by City Council. Each stage represents a specific drought scenario and requires that customers conserve 10%, 20%, 30%, or 50%, depending on the stage declared. MPMW is currently at stage 1 (no drought). A drought surcharge is charged when a drought stage requiring conservation is declared.
SFPUC wholesale pass-through rate	MPMW purchases all its water from the San Francisco Public Utilities Commission (SFPUC). The adopted rates include estimated SFPUC wholesale rates that become effective July 1 of each year. Pursuant to California Government Code 53756, any additional increases in SFPUC wholesale water rates may be passed through to water users when the actual SFPUC rates exceed estimates. This pass-through provision applies to wholesale rates, water management charges and other regulatory or environmental charges required by SFPUC.
Capacity charges	This one-time permit connection charge is imposed for new and upgraded connections to the MPMW system. This charge is based on the size of the service connection and recovers the value of system capacity provided for the new/upgraded service. This charge is not included in monthly bills.

In 2025, the City entered into an agreement with Black & Veatch Corporation (Black & Veatch) to develop the Study.

Analysis

The Study includes a 10-year financial plan beginning July 1, 2026, that projects the level of future revenue generated based on historical data and future system growth in terms of the number of water connections and consumption. It also projects the expenses necessary to operate and maintain the system, invest in capital improvements, and cover other water system expenses.

Study principles

The following principles were applied in developing the Study:

- Rates should recover the full cost of providing service and must not exceed the proportional cost of the service provided;
- Revenue derived from rates must not be used for any purpose other than for which it is imposed;
- The allocation of projected revenue requirements to the customer classes of service should be in accordance with the respective service requirements;
- The financial plan should be sound and cover both ongoing operations and planned capital projects;
- Rates should be designed whereby revenues adequately meet financial needs while recognizing customer costs of service and regulatory requirements such as Prop. 218.

The Study uses the following terminology and approach:

- Revenues – MPMW derives revenue from various sources, including water rates, capacity fees, capital facility surcharges, interest earned from the investment of available funds, and other operating charges. The revenues must cover the expenses.
- Revenue increase adjustments – As the cost of providing water services increases, so do the revenue needs. To meet the increase in costs, the Study evaluates options to adjust the future revenue needs.
- Rates and charges – As mandated in California, rates charged must generate the revenue specified in the financial plans to sustain operational and maintenance (O&M) and capital needs. The Study includes a cost-of-service analysis and evaluates increases to water rates, capacity fees, and capital facility surcharges to meet the future revenue needs. The Study recommends a uniform consumption charge for all customers rather than a tiered structure.

Primary drivers for future cost increases and rates

The Study evaluates the following primary cost components:

- Estimated SFPUC wholesale rates – The highest O&M cost is for wholesale water purchases. Wholesale water purchase costs, including the Bay Area Water Supply & Conservation Agency (BAWSCA) surcharge, account for an average 63% of the total annual O&M expenses. SFPUC increased its wholesale water rates from \$1.30 per ccf in FY 2008 to \$5.67 per CCF in FY 2025. The Study incorporates estimated SFPUC increases following this trend.
- Recycled water – The West Bay Sanitary District is in the process of constructing the Bayfront Recycled Water Project, a treatment facility that will serve recycled water in the Bayfront as part of the first phase. The Study accounts for a loss in potable water demand and revenue as recycled water is introduced in the City and used by buildings that are dual plumbed (used for toilet flushing), irrigation, and industrial purposes beginning in mid-2027.
- Capital infrastructure needs – The 2018 water system master plan (WSMP, Attachment C) identifies significant capital improvements over the next 20 years to address infrastructure needs. Debt financing is evaluated as part of the Study to fund the infrastructure improvements.

Capital Improvement Plan projects (CIPs)

MPMW funds annual CIPs from a combination of revenues including water user rates, capacity fees, capital facility surcharge and available water fund balance. The 2018 WSPM identifies \$90 million is needed over the next 20 years to address infrastructure needs. Investing in the water infrastructure is important to limit main failures, water outages and potential future liability. Therefore, water rates need to be reviewed regularly and adjusted as necessary to fund future projects. On June 24, 2025 staff presented the five-year capital improvement plan which included \$50.1 million in water CIPs to be funded by the water fund (Attachment D). As part of this Study, the capital projects were reviewed and revised for the analysis, considering both conservative and aggressive implementation timelines (Table 2). The primary difference being increased spending in water main replacement.

Projects	Conservative CIP (\$ millions)	Aggressive CIP (\$ millions)
Water Storage/Supply	\$9.0	\$9.0
Water Main Replacement	\$7.6	\$23.1
Water Storage Reservoir and Pump Station	\$28.5	\$28.5
Water System Improvements	\$1.0	\$2.0
Total	\$46.1	\$62.6

Debt financing

MPMW currently operates as a cash “pay as you go” basis and does not have existing debt. This approach results in a prolonged timeline for the implementation of capital projects. It is common practice for utilities to utilize debt to finance multi-year capital projects and set feasible timelines for their implementation. Debt payments are spread over a specified time frame, thus smoothing out rate increases for customers over time. The Government Finance Officers Association, a professional organization which regularly publishes best practices, recommends consideration of intergenerational equity in analyses of financing options. In addition to smoothing rate increases, debt financing promotes alignment between payment for and consumption of capital assets.

Debt financing options include revenue bonds, general obligation bonds, and state and federal loans. The City has a history of issuing general obligation bonds for capital improvements, with the latest issuance in 2022. In April 2022, City Council voted to issue \$14.3 million in remaining Measure T bonds, which voters had approved in 2001 for improvements to the City’s parks and recreation facilities. General obligation bonds are backed by ad valorem taxes and require 2/3 voter approval. Revenue bonds for water infrastructure would be backed by revenues generated by rates. While revenue bonds do not require voter approval, they do require approval from the City Council. Other financing options include State Revolving Fund Loans and Water Infrastructure Finance and Innovation Act of 2014 loans.

Recommended rate structure

In conducting a cost-of-service analysis, as mandated in California, rates charged must generate the revenue specified in the financial plans to sustain O&M and capital needs. The Study identified two recommended changes to the rate structure:

1. Elimination of the three-tier consumption rate structure and transition to a uniform charge for all customers. The existing consumption rate was based on an inclining three-tier structure that was designed based on industry guidelines at the time and to encourage water conservation.

2. Adjustments to the consumption and fixed meter charges based on the cost-of-service analysis.

Revenue increase adjustment options

1. For rates to recover the full cost of providing service, the revenue collected must cover the expenses and provide for an appropriate level of reserve. Reserves are designed to ensure financial stability. MPMW maintains 120 days of operating expenses and \$1 million for unforeseen capital needs. The Study recommends increasing the capital reserve target to \$3 million by FY 2031.
2. The Study evaluates four annual revenue adjustment options which consider varying CIP implementation timelines and financing approaches (Table 3). Under all the options, the fixed meter charge, consumption charge based on a uniform rate, capital facility surcharge and drought surcharge increase.

Options 1 through 4 consist of the following:

- Debt financing - Options 1 and 2 include debt financing to help fund capital projects.
- No debt - Options 3 and 4 do not include debt and assume revenues will fully fund capital projects.

Over the last three years, the average MPMW single family home water consumption decreased from 12 to 10 ccf. The average single family residential bill of 10 ccf would see an increase ranging from \$27.56 to \$70.14 between Options 1 to 4 per month, respectively. Option 1 requires the lowest revenue increase and results in lower rates.

CIP implementation timeline	Consumption rate structure	Revenue Increase	Fiscal Year	Result/Impact (refer to Table 2)
1. A conservative CIP	Uniform rates for all customers	4.25%	2026-27 & 2027-28	<ul style="list-style-type: none"> • Debt financing of \$16M by 2029 • Meets cost obligations
		4.5%	2028-29	
		5.0%	2029-30 & 2030-31	
2. An aggressive CIP	Uniform rates for all customers	8.0%	2026-27 & 2027-28	<ul style="list-style-type: none"> • Debt financing of \$24M by 2029 • Meets cost obligations
		8.25%	2028-29 to 2030-31	
3. A conservative CIP	Uniform rates for all customers	20%	2026-27	<ul style="list-style-type: none"> • No debt financing • Meets cost obligations
		6.5%	2027-28 & 2028-29	
		0%	2029-30 & 2030-31	
4. An aggressive CIP	Uniform rates for all customers	35%	2026-27	<ul style="list-style-type: none"> • No debt financing • Meets costs obligations.
		10.0%	2027-28 & 2028-29	
		0%	2029-30 & 2030-31	

Key policy findings

Implementation of any of the options generates sufficient revenues to meet obligations while satisfying reserve targets and attempting to minimize rate impacts to customers. Over the past water rate cycles, City Council has approved five-year rates. In reviewing revenue projections, City Council may consider a three-year plan instead of a five-year plan due to projected recycled water supply becoming available and impacting the revenue generated by MPMW. A three-year option would allow staff to reassess the revenue

projections and increases presented in Table 3 and return to City Council in 2029 with future rate increases.

Next steps

Table 4 provides the timeline to complete the water rate study for the new rates to begin on July 1, 2026.

Table 4: Water rate study timeline	
Date	Description
March 10	City Council meeting to present the water rate study, approve Proposition 218 notice to MPMW property owners and adopt Resolution for the implementation of AB 2257 ¹
May 19	Conduct rate protest hearing and adopt a Resolution to increase water rates at a public hearing
July 1	New rates become effective, and then are adjusted annually on July 1

¹Assembly Bill 2257 is an optional, formalized process for local water and sewer agencies strengthening agency defensibility by requiring ratepayers to raise objections *before* new fees are adopted. Agencies must provide a clear, written basis for proposed fees at least 45 days in advance and must respond in writing to objections before concluding public hearings.

Impact on City Resources

There is no direct impact on City resources associated with this staff report. Implementing the rate adjustments would allow MPWM to remain self-supporting, avoid General Fund subsidies, maintain healthy reserves, and continue to meet all operation and maintenance expenses and CIP. Without rate adjustments, however, the City would be required to identify alternative funding sources to cover annual operating deficits, both of which would place pressure on City financial resources.

Environmental Review

This action is not a project within the meaning of the California Environmental Quality Act (CEQA) Guidelines §§15378 and 15061(b)(3) as it will not result in any direct or indirect physical change in the environment.

Public Notice

Public notification was achieved by posting the agenda, with the agenda items being listed, at least 72 hours prior to the meeting.

Attachments

- A. Map – MPMW service area
- B. Hyperlink – Five-year water rate schedule, adopted May 11, 2021:
www.menlopark.gov/files/sharedassets/public/v/1/public-works/documents/water/adopted-5-year-water-rates-2022-2026_06232025.pdf
- C. Hyperlink <https://www.menlopark.gov/files/sharedassets/public/v/2/public-works/documents/water/menlo-park-municipal-water-2018-water-system-master-plan.pdf> Water System Master Plan (WSMP):
- D. Hyperlink – Five Year Capital Improvement Plan (CIP) [stories.opengov.com/menlopark/ade5a8ed-80f6-42dd-bae7-98d85d32530e/published/BEyK_o5C4?currentPagelD=67c7d7d91d94f5a7089fb068](https://www.stories.opengov.com/menlopark/ade5a8ed-80f6-42dd-bae7-98d85d32530e/published/BEyK_o5C4?currentPagelD=67c7d7d91d94f5a7089fb068)

Staff Report #: 26-025-CC

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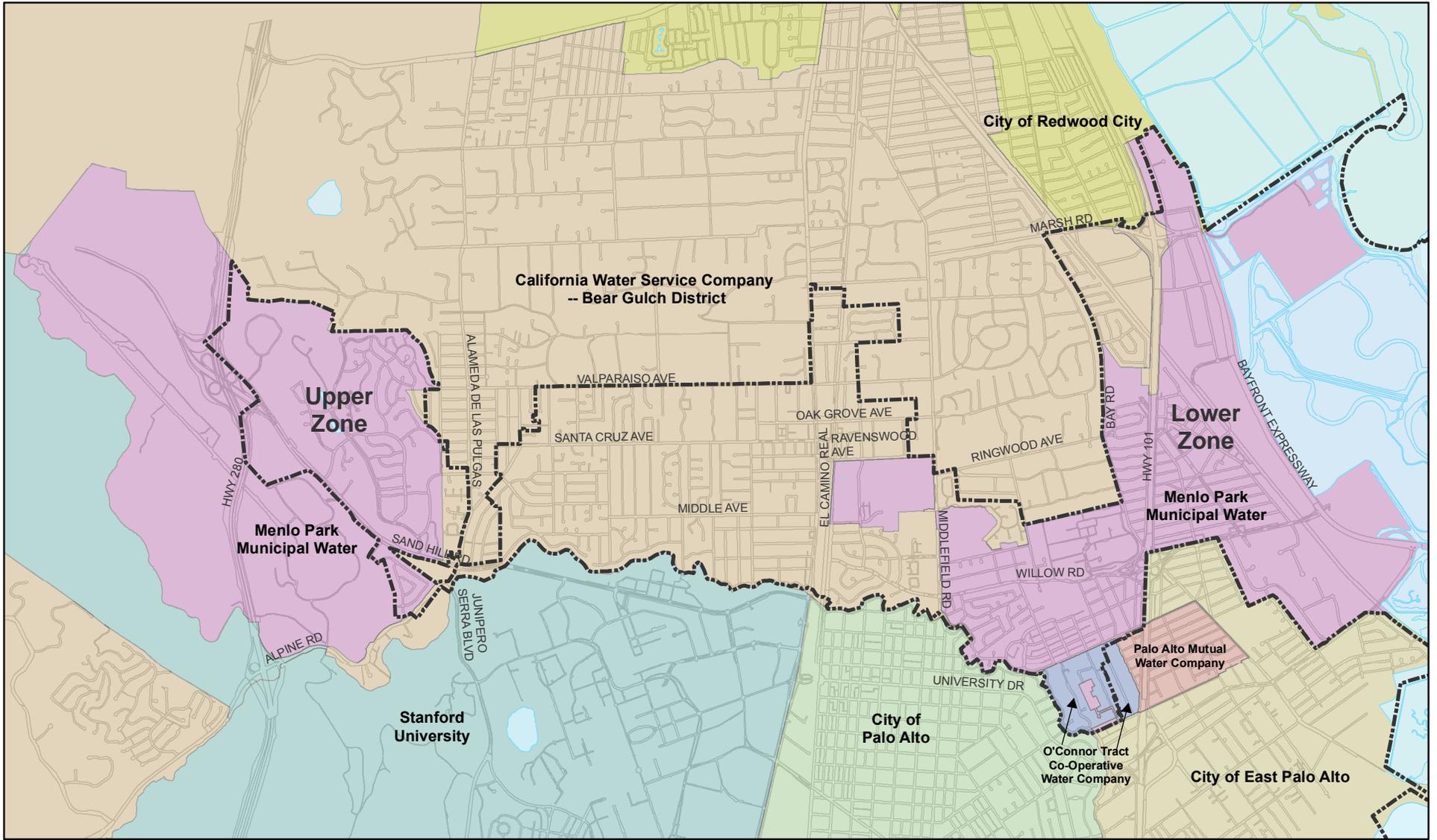
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City Limits	Water Provider
Travel Ways	California Water Service Company – Bear Gulch District
Water	City of East Palo Alto
	City of Palo Alto
	City of Redwood City
	Menlo Park Municipal Water
	Stanford University
	Palo Alto Mutual Water Company
	O'Connor Tract Co-Operative Water Company



Water Agencies Within and Surrounding Menlo Park

