

# ***Lompoc City Council Agenda Item***



**City Council Meeting Date:** March 5, 2013

**TO:** Laurel M. Barcelona, City Administrator

**FROM:** Melinda Wall, Financial Services Manager

**SUBJECT:** Water and Wastewater Rate Study Presentation and Request to Start the Proposition 218 Process for Rate Adjustments

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## **Recommendation:**

Staff recommends the City Council receive rate information from Willdan Financial Services (Consultant) on water and wastewater funds, direct staff to start the process on the next City Council agenda to follow Proposition 218 guidelines and adjust rates by the amounts recommended by Consultant for the water and wastewater services, or provide other direction to staff.

## **Background:**

On March 14, 2012, the City entered into an agreement for consultant services with Consultant. The purpose of that agreement was for Consultant to conduct a rate study for water and wastewater utilities.

Habib Issac and Greg Tobler of Consultant, after working with City staff, met twice with the Utility Commission to present the cost of service for water and wastewater funds and to develop a rate strategy for each customer class to collect appropriate levels of revenues, encourage water conservation, and account for the discharge strength of wastewater loads. The Utility Commission, on a 4-0 vote, made a motion to support the recommended rate adjustments under a five-year implementation plan proposed by Consultant, to continue to meet the City's obligations under the various revenue bond covenants, while minimizing the effect of the rate adjustments on the two utilities' consumers.

At a Special Meeting of the City Council on January 8, 2013, Management Services Director Brad Wilkie provided information comparing the projected results from the most recent rate study performed in 2006, with the actual results for the period from 2006 through June 2012. Immediately following the staff presentation, Consultant presented a PowerPoint presentation to the City Council to review the results of the cost of services component of the utility rate study.

Following this staff report, Habib Issac and Greg Tobler will present the rate structure as recommended by Consultant, staff and the Utility Commission, based on the results of

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the cost of service component of the review. That presentation will utilize the dashboard feature, developed as part of the review. The use of the dashboard during the presentation will allow Consultant to model and present alternative scenarios during the meeting. That will allow comparisons to be made based on input from the Council and others. The dashboard will be available to staff following the conclusion of the rate study, to track actual results during the period rates are implemented.

**Discussion:**

The City is obligated under the bond documents from the 1998, 2005 and 2007 bond issues to set rates and charges each year to produce certain minimum net and gross revenue amounts, based on the combined water and wastewater utilities. Because of that, rate covenants of all the bond issues must be one of the items to be taken into consideration when designing rates. It is also prudent for each fund individually to meet those annual rate covenant tests as well, since the rating agencies and bond insurers also evaluate the credit worthiness of each utility on a stand-alone basis. The three annual rate covenant requirements are:

- 1) Net revenue (operating and certain non-operating revenues less operating expenses) in each fiscal year must be at least one times the annual debt service (both principal and interest) due in that fiscal year;
- 2) Net revenues supplemented by any transfers from a rate stabilization fund must be at least 1.25 times debt service; and
- 3) Gross revenues must be at least 1.0 times all obligations of the two utility funds for the fiscal year.

The State Revolving Fund loan, funded by the State Water Resources Control Board, related solely to the wastewater utility, requires similar covenants. Additional considerations for operating costs, capital repair and replacement costs for the City's infrastructure were also taken into consideration for the rate study.

Proposition 218, passed by voters in 1996, requires compliance with the noticing process in order for the rates to be set by the City Council to be in full-force and effective. Major components of the noticing process include:

- The requirement to notify all affected parties at least 45 days prior to holding a hearing, at which the Council could act on the proposed rates identified in the notice.
- At the public hearing, the Council would be required to reject the fee if a majority of the affected owners file written protests.
- Utility rates must be set so that revenues do not exceed the funds required to provide the service, and the fee or charge imposed on any ratepayer must not exceed the proportional cost of the service.

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- Rates cannot be implemented until 30 days after the adoption of the rates and rate adjustments cannot extend beyond five years.

As part of the 2013-2015 budget preparation process, Management Services staff is reviewing efficiencies that can be implemented to take advantage of the installation of radio read meters for water and electric services. Those efficiencies include:

- Separation of billing routes by class of customer, such that all commercial accounts are billed separately from residential accounts. By making billing cycles more uniform in character, billing staff can utilize additional resources from the meter reading software to improve accuracy and timeliness of delivery of utility bills.
- The City's utility collection resolution has not been revised since 1988 and can be updated to provide additional resources to the City's Collection Division to collect delinquent billings and to reduce the overall collection efforts on chronically delinquent accounts.
- A recent case regarding MasterCard and Visa merchant account charges will allow the City to assess a charge for use of credit cards by utility customers to pay their bills. By passing this charge along to the customer, the two utilities will benefit in the overall reduction of the cost of collections on utility bill payments.

### **Fiscal Impact:**

The operating and maintenance reserve has been depleted in the water and wastewater funds and there will be the need to have an internal advance of funds to sustain the two utilities, until such time that revenues from rates can return the operating reserves to a positive level. Those utilities are enterprise funds and are required to be self-supporting. A component of self-sufficiency is having adequate reserves for capital replacements and repairs. The goals for the adjustment of rates are to meet the bond covenants, replenish operating reserves to a level equal to a 90-day reserve, and to establish a reserve fund to be used to repair and replace infrastructure of each utility.

### **Conclusion:**

The rate study presented for review takes into account the necessary requirements to comply with operational needs, capital costs and the requirements related to the water and wastewater bond covenants. The City Council must balance the needs of the City's utilities with the ability of the citizens to pay for the services.

At this time, we are asking the City Council to give staff direction concerning the rate design, have staff return at the next City Council meeting on March 19, 2013, with the rates resulting from that design and start the Proposition 218 requirements for public notifications and public hearings. The public hearing will be set at the March 19, 2013

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City Council meeting and will be no less than 45 days following the mailing of the hearing notices, or roughly May 21, 2013.

Respectfully submitted,

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Melinda Wall, Financial Services Manager

**APPROVED FOR SUBMITTAL TO THE CITY ADMINISTRATOR:**

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Brad Wilkie, Management Services Director

**APPROVED FOR SUBMITTAL TO THE CITY COUNCIL:**

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Laurel M. Barcelona, City Administrator