

CITY OF MILPITAS
MINUTES of: CITY COUNCIL (FINANCE) SUBCOMMITTEE
Date/Time: Monday, September 14, 2015 – 4:30 p.m.

I. CALL TO ORDER: Vice Mayor Carmen Montano called the meeting to order at 4:36 p.m.

Attendance:

City Council: Jose Esteves, Mayor
Carmen Montano, Vice Mayor

Staff: Steven Machida, Director of Engineering
Nina Hawk, Public Works Director
Marilyn Nickel, Associate Civil Engineer
Eric Hansen, Principal Civil Engineer
Thomas C. Williams, City Manager (came in @ 5:12 pm from Oversight Board meeting)
Emma Karlen, Assistant City Manager/Finance Director (came in @ 5:10 pm from Oversight Board meeting)
Rachelle Currie, Recording Secretary

II. PUBLIC FORUM: None

III. APPROVAL of MINUTES: The April 15, 2015 minutes were approved.

IV. ITEM FOR DISCUSSION

A. WATER RATES

- Steven Machida, Director of Engineering – Made a brief introduction stating that this is a follow-up from the August 4th Council meeting discussion to give analysis on the San Juan Capistrano Proposition 218 decision on tiered rates upheld in the Court of Appeals and turned it over to Bartle Wells Associates representatives Douglas Dove and Michael DeGroot for the presentation on water rates. BWA is the City’s consultant tasked to analyze the financial utility master plan update. Mr. Dove briefly informed the Council Subcommittee that he will be discussing Proposition 218, which is the water rate law in California; water rates background, factors; proposed rate structure; proposed rates and how they affect different customers; and finally overall schedule.

Mr. Dove reported that on April 20, 2015 a decision was reached in the Court of Appeals about the San Juan Capistrano’s litigation on tiered rates. Then in June 2015, Governor Brown requested the State Attorney to recommend the Supreme Court to invalidate the San Juan Capistrano’s appellate decision because of the drought and to allow communities to have this very effective tool pricing of water to encourage water conservation. However, on July 22, 2015, Supreme Court’s final decision is to not change the Appellate Court’s decision and reject the State Attorney’s request because tiers need be cost-justified and tiers cannot be used simply to encourage and promote conservation. Mr. Dove added that it is very common in a lot of communities to have a rate structure to have low rates for the very low users and

then they would increase significantly for the high users. So there really was a strong conservation message on having tiered rates and they really worked because the monthly rates are very low in this area. At the August 4th public hearing for water and sewer rates, City Council approved the sewer rates and tabled water rates so staff can re-evaluate the rates and do a study using uniform water rate instead of the proposed tiered water rates prior to the July 22, 2015 Supreme Court ruling. And because the water rates were not approved at the August 4th meeting, City loses revenue every month until new rates are adopted. In summary, Proposition 218 requires: a) tiered rates must be cost justified (not conservation driven); b) fees must be proportionate to the cost of service; c) no rate subsidies or discounts unless funded separately either from general fund, late fees, etc. and he stressed that water rates cannot be used for discounts; d) everyone pays the same unit water rate which means we cannot have discount on low-rate users and have penalties on high-rate users; and e) higher rate for larger meter because of the extra capacity to pull water out of the system.

- Next, Mr. Dove stated that rates are extremely important especially in drought situation because users reduce water use which equates to lost revenue, if we don't reduce water use City might face possible State fines, etc., the wholesale costs have escalated to 28% for SFPUC. During the drought situation, City's operating costs go up because of conservation programs and other related costs in public outreach. Mayor Esteves inquired if projected maintenance, expansions, and/or replacements of infrastructure could be included in the capital costs, Mr. Dove concurred. Mr. Dove continued the presentation with a pie chart of FY 2016 water enterprise operating costs showing that 61% of operation costs come from wholesale water purchases (provided by Santa Clara Valley Water District, San Francisco Public Utilities Commission, and South Bay Water Recycle); 33% come from other operating expenses; and 6% was estimated for drought program (education and enforcement), Bartle Well's Rate Study, staffing, equipment and software annual costs, emergency repairs, and others. Vice Mayor Montano asked why bring up the monthly billing information (\$500,000) that staff is not recommending if it costs more. Mr. Dove, said that it was included in the cost analysis to be conservative. She asked what the 61% breakdown is for the three vendors the City has as wholesalers. Director of Engineering Machida replied that Hetch-Hetchy has 65-70% of the cost and the remaining 1% or 2% goes to SBWR.

Part of the Capital Plan is to address old infrastructure to prevent the Technology Drive water main accident where we lost a lot of water and have to do emergency repairs. The proposed Capital Costs is \$42 million which includes an additional 5-year CIP cost of \$22 million to the already approved 5-year CIP of \$20 million. The additional 5-year CIP plan is to be used mostly for water supply augmentation where we use recycled water on parks to save potable water and some projects such as Lower Berryessa Creek Crossing – Director Machida briefly explained that Santa Clara Valley Water District is protecting the Berryessa Creek by erecting flood wall and only giving City staff a 9-ft clearance to do underground work and staff is still in negotiations with the Water District about this project; Valve replacements – important to avoid the San Bruno PG&E tragedy; seismic reliability; and water system replacement. Mr. Dove added that a bond is being proposed to fund a little more than half of the additional CIP proposed costs so it does not have to go all to the ratepayers this year and have it spread out in the future because these projects are going to last a long time. Mayor Esteves asked if we the projects can be started as early as possible to which Vice Mayor Montano agreed. Director Machida replied that staff will look into the projects timeline.

- Mr. Dove explained the proposed rate structure changes to the subcommittee and it is being recommended to: 1) assign 25% of total costs to be recovered from fixed revenues – this is the fixed monthly or bi-monthly charge based on meter size and is adjusted to be aligned with

the industry’s standard rates; 2) assign 75% of total costs to be recovered from variable revenues – this is the volumetric charge this is what the people have control of; 3) finance capital program and capital surcharge on the rates so people can see how much money is invested in the water system to approve the reliability; and lastly 4) adopt a 2-year water rate program – this is a 2-step increase. He further explained recommendations 1 and 2 meet the best management practice put forward by the California Water Conservation Council. The 2-step increase recommendation starts on January 2016 then another increase on July 2016 then review the rates after that.

Consultant and staff are proposing uniform tier consumption rate for the 2-step increase recommendation. Table below shows the proposal:

	FY 2015/2016	FY 2016-2017
Potable Rate (per HCF*)	\$ 4.75	\$ 5.13
Capital Surcharge (per HCF)	-	\$ 1.32
Recycled Water (per HCF)	\$ 2.42	\$ 2.61
5/8” Fixed Meter Charge	\$ 18.01	\$ 19.45

* Hundred Cubic Feet

Vice Mayor asked if a customer doesn’t use recycled water are they still going to be charged? Mr. Dove responded they will not. Mayor Esteves inquired why we’re not charging capital surcharge this year if the project are starting next year. Mr. Dove explained further that on the first year no surcharge, then we’re starting with \$1.32 for the first 2 years, and on the 4th year, City is funding about \$3.8 million directly from capital surcharge. Consumers will see capital investment as a line item on their bills so they know that City sets aside funding on the water systems’ reliability. Mayor asked why we can’t start charging for surcharge this year if projects are starting next year. Mr. Dove responded that even though we’re starting the projects in this fiscal year and decided not to start charging for surcharge until next year because that’s when the debt service starts for the bonds to pay back and recover all the costs.

- With the proposed rate structures, Mr. Dove showed the difference between the current residential bill and the FY 2016 bill. The summation is that there will be an increase of roughly \$21 per bimonthly bill for average users (meaning 17 HCF bimonthly use) for the first year. The second step, everyone will see a very significant increase whereby there’s roughly \$30 increase per bimonthly bill for average users. Mayor Esteves commented about the chart comparisons between other Cities; he wanted to be clear that the rates for the cities of Santa Clara, Sunnyvale, San Jose (Zone 1), Foster City/EMID, Mountain View, Redwood City, and Palo Alto along with West Valley Water District, San Jose Water Company are comparable to the City of Milpitas’ current rate of \$77.92 and inform the public that the assumption of Milpitas having the highest water rate is incorrect and that currently City of Milpitas is one of the cities with lower rates and suggested to take the projections for City of Milpitas out of the chart comparison. Mr. Dove concurred with the Mayor’s suggested and added that they could do a research and find out which of the cities listed on the chart have adopted rates and use those new rates for comparison with City of Milpitas’ projected rates.
- Mr. Dove moved on informing the subcommittee about the schedule for water rates adoption. It is set for October 6th public hearing to introduce ordinance and authorize Proposition 218 mailing. On October 30, mail Proposition 218 public notice followed by December 15 public hearing to hear protest, ordinance approval, and authorize bond issuance. January 15, 2016 is the effective date for bills issued on or after January 18, 2016. July 1, 2016 is the 2nd year rates effective date. Vice Mayor commented that since there’s a new mandate, there’s no other

way but to implement the proposed rate structures as opposed to the old rate structure. Mayor Esteves agreed with Vice Mayor but asked if the consultant to identify reasons or factors why other cities can offer lower rates to their consumers so the City of Milpitas could also provide the best possible water rates for our consumers. Mr. Dove interjected that the cities with lower rate have their own wells so they don't have to purchase water from wholesalers. The Mayor would like to see information like this to be out there so consumers are well-informed why the rates are different from cities to cities.

- Robert Marini, from the audience, asked how meter charges where the cost associated to determine how to calculate rates. Mr. Dove replied that capacity ratios are used to take fixed costs and allocating those costs based on theoretical capacity. He then asked if Bartle Wells did analysis on sewer rates because Proposition 218 also applies to sewer rates. Mr. Dove said no. City Manager Tom Williams replied that City does not have tiered rates structure in our sewer rates so we are probably more compliant with our sewer rates today than we were prior to the San Capistrano decision on tiered water rates. Today, we are even more legally defensible on our sewer rates.

With that, Mayor Esteves motioned seconded by Vice Mayor Montano since we are legally defensible to take the extensive study of the proposed water rates and recommend to the entire City Council. The motion passed.

V. OTHER BUSINESS - NONE

VI. NEXT MEETING – TBD

VII. ADJOURNMENT – 5:27 PM