DATE: January 19, 2016

TO: City Council

THROUGH: Greg Nyhoff, City Manager
Office of the City Manager

FROM: Daniel Rydberg, P.E., Public Works Director
Public Works Department

SUBJECT: Utility Enterprise Financial Policy, Utility Rate Assistance Program and Public Hearing on Ordinances to Continue and Establish Water, Wastewater and Solid Waste User Fees and Charges

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RECOMMENDATION

That City Council:

1. Hold a public hearing to receive public testimony and consider all protests concerning the adoption of ordinances continuing and establishing certain water, wastewater and solid waste user fees and charges.

2. Adopt a resolution setting financial policy for the Environmental Resources (Solid Waste), Water, and Wastewater Utility Enterprises.

3. Receive a report on the options for a potential program to provide financial assistance on City utility bills and provide direction to staff on which option to pursue.

4. Approve the first reading by title only and subsequent adoption of an ordinance continuing and establishing water user fees and charges.

5. Approve the first reading by title only and subsequent adoption of an ordinance continuing and establishing wastewater user fees and charges.

6. Approve the first reading by title only and subsequent adoption of an ordinance continuing and establishing solid waste user fees and charges.
BACKGROUND

Utility Enterprise Financial Policy

Following sound financial policy is essential to effective utility operations. A policy provides guidelines for financial management with an overall long-range perspective, provides a basis for coping with fiscal emergencies, helps maintain financial solvency, and enhances financial transparency. The goals of a financial policy are to mitigate risk, stabilize rates, maintain a desirable credit rating in order to reduce interest expense, determine the optimum ratio of cash and debt funding of capital projects, and to determine the opportune time to issue debt. The City currently has a limited utility rate policy and is developing a new comprehensive policy in order to provide greater stability to the utility funds.

On October 13, 2015 staff presented broad recommendations for a utility rate policy to the City Council and on December 15, 2015 staff presented recommended debt service coverage and reserve policies to the City Council and discussed their impact on credit ratings. The proposed updated Utility Enterprise Financial Policy is included as attachment #1.

Utility Rates Assistance Program

The California Public Utilities Commission (CPUC) has approved several programs that provide financial benefit to ratepayers of utilities that it regulates, including the California Alternative Rates for Energy (CARE) Program for electricity and natural gas customers, the LifeLine Program for telephone service, and various smaller programs for private water companies. Locally, the Cities of Camarillo and Port Hueneme also have programs. The CARE Program provides up to a 20% discount off energy bills for low income households, and is funded by CPUC-approved rate cases with Southern California Edison Company and Southern California Gas Company in Oxnard. The LifeLine Program provides an approximately $6 per month discount off basic land line telephone service, and is funded by CPUC-approved rate cases with Verizon in Oxnard. The Water Utility Low Income Assistance Program provides a flat per-month discount for private water company customers, and is funded by CPUC—approved rate cases with Golden State Water, in Ventura County. Golden State Water’s Ojai-area eligible customers receive a $12 per month discount, and its Simi Valley-area eligible customers receive an $8 per month discount.

Unlike utilities regulated by the CPUC, cities, such as Oxnard, are prohibited by state law (Propositions 218 & 26) from funding their financial relief programs with charges to their customers. Cities must fund their programs with discretionary funds, voter-approved special taxes, or donations from citizens and businesses. Some cities are also funding programs using interest revenue from Operations and Maintenance Fund balance. The City of Camarillo provides qualifying low income senior customers with a discount off its wastewater charges and waives the variable portion of the water charges, as long as water usage does not exceed 10 hundred cubic feet (HCF) per month. This program is funded by a voter-approved special tax. The City of Port Hueneme provides qualifying low income customers with a 15% discount on its water, wastewater & solid waste charges.
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An ad hoc committee, with representation from the City Manager’s Office, the City Treasurer’s Office, City Attorney’s Office, Development Services Department, and Public Works Department, researched programs available in California and across the nation, as well as applicable laws and regulations, and presented its findings to the City Council at its February 12, 2013 meeting. The program qualifications included extremely low income seniors with below average water use. At the meeting, City Council requested that staff look at broadening the criteria beyond seniors. The potential cost of the senior program was approximately $200,000 per year for a $25 per month discount. Broadening the eligibility to all extremely low income ratepayers could cost up to $2 million for the same discount. The City has collected approximately $13,000 since 2014 for the program. Using 10% of the interest revenue from utility fund Operations and Maintenance Fund balances would generate approximately $85,000 in the first year, increasing to approximately $200,000 in the fifth year. Based on these cost and revenue estimates, staff recommends a discount of $10 per month in 2016 increasing each year by $2.50 per month up to $20.00 per month in 2020. The discount would be available to extremely low income seniors and disabled ratepayers and to other extremely low income ratepayers as funds are available. The criteria for eligibility would be:

- Ratepayer-occupied residential unit (typically Single Family Residential); and
- Extremely low income (USHUD definition); and
- Using no more than 9 HCF of water per month; and
- Head of Household over 65 years old or older, or disabled; and
- Other extremely low income residents (as funding is available).

Utility Rate Process

On October 13, 2015, City Council approved beginning the rate setting process for water, wastewater, and solid waste rates. The rate setting process includes a Proposition 218 protest procedure including a notice, a 45 day waiting period, and a public hearing to consider protests. On November 17, 2015, Council directed that a protest form be included in the rate notice, and on December 3, 2015, the Proposed Utility Rate Increases Notices were mailed to parcel owners and utility customers.

Need for Utility Rate Increases
The City's primary financial goal for its utility enterprises is to ensure that revenues from rates and fees are adequate to fund daily operations and maintenance, capital improvement, debt service and reserves. The funds generated by utility rates are used to provide safe drinking water, treat wastewater and collect and process trash and recyclables for our residents and businesses. This money funds operations, maintenance, repairs, debt payments, infrastructure costs, and capital projects within each utility. The current revenues from water and wastewater are less than the overall costs to provide the services. Rate increases are needed to improve and support the fiscal health of these vital services.

Current rates are also inadequate to properly maintain or replace vital aging infrastructure including facilities, equipment and pipelines. Some essential facilities have either failed or are reaching the end of their useful life. Much of the City’s wastewater treatment plant was built in the 1950s and upgraded in the 1970s. These facilities are significantly deteriorated and in some cases are at or near
failure. Failing to maintain aging infrastructure poses a public health risk and subjects the City to potential regulatory violations.

To maintain adequate water supply and reliability, the City must comply with strict environmental regulations and State water conservation mandates. These compliance efforts have increased the cost of water supplies and reduced water revenues below the cost of providing those supplies. Because the majority of expenses are fixed costs when water consumption goes down revenues decrease more than expenses.

Recommended Rates
Utility rates and fees are set following specific legal requirements and industry best practices. Utility revenue can only be used for the utility for which it is collected, though indirect charges for General Fund services and Infrastructure Use Fees for public safety and streets are allowable. Utility charges must also not exceed the estimated reasonable cost of service usually based on a Cost of Services Study. In addition, rates must be charged only to the users benefiting from the service.

A court ruling recently changed the way water rates can be structured. Previously, cities were encouraged to have tiered rate structures to encourage conservation. Now tiers are still allowed, however, rates must be tied to costs of service not just conservation goals. This has impacted water rate structures for many California cities including Oxnard. The proposed rates follow the new interpretation of Proposition 218.

In 2015, a consultant completed a Cost of Services Study which details the City’s obligation to address significant infrastructure needs and provides a detailed rate and cost of service analysis. Based on operational requirements, recommended rate policy, and capital improvement requirements, the recommended combined average revenue increase over current rates is 19% for Fiscal Year 2015-16, 9% Fiscal Year 2016-17, and 7% for each of the Fiscal Years 2017-18 through 2019-20 as shown in the table below. The actual increase for individual customers would vary depending on several factors including customer class, account characteristics, and actual level of use.

<table>
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<th>Year</th>
<th>Water</th>
<th>Wastewater</th>
<th>Environmental Resources</th>
<th>Combined Weighted Average</th>
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<td>35%</td>
<td>3%</td>
<td>19%</td>
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<td>12%</td>
<td>10%</td>
<td>3%</td>
<td>9%</td>
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<td>2019-20</td>
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<td>8%</td>
<td>3%</td>
<td>7%</td>
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<td>Net 5 yr</td>
<td>62%</td>
<td>87%</td>
<td>16%</td>
<td>59%</td>
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</tbody>
</table>

Consequences of Not Raising Rates
If Wastewater rates are not increased, the Wastewater Enterprise will not receive enough revenue to cover expenses beginning this year. The fund will not be able to meet bond coverage requirements which could result in a credit downgrade to junk bond status. This would make funding of required
facility replacement projects more difficult and expensive. The Wastewater Fund would run out of money in FY 2016-17 or FY 2017-18 and urgently needed maintenance projects would be delayed. This could result in the failure of primary treatment, bio-tower processes and manholes in the Central Trunk Wastewater Collection pipeline. The repair of tree root damage to sewer pipelines and resident laterals citywide as well as installation of odor control systems for sewer collection pipelines would be delayed. Staffing levels and maintenance would not meet regulatory requirements which could result in National Pollutant Discharge Elimination System (NPDES) violations and potential fines.

If Water rates are not raised, the Water Enterprise Fund will not receive enough revenue to cover expenses beginning this year. The fund will not be able to meet bond coverage requirements which could result in a credit downgrade and increased cost for funding required maintenance projects. The Water fund would run out of money in FY 2020-21 or earlier. Replacement of failed water meters could be delayed which could further reduce revenues. Maintenance of pipeline corrosion protection systems, flushing of pipelines, and exercising of valves would be delayed. Street resurfacing projects would be delayed or streets would be resurfaced without replacing cast iron and asbestos cement water lines. This could result in premature failures and damage to new streets.

If Solid Waste rates are not increased the Environmental Resources Enterprise would begin running deficits in two years and would run out of money in FY 2019-20. Replacement of collection vehicles and sorting equipment would be delayed and State requirements for organics landfill diversion would not be met.

**FINANCIAL IMPACT**

If approved, the rate increase will provide the following revenue in FY 2015-16:

- $2.4 Million for water services in Fund 601 Water operating budget
- $2.8 Million for wastewater services in Fund 621 Wastewater Treatment operating budget and Fund 611 Wastewater Collection operating budget
- $0.36 Million for solid waste services in Fund 631 solid waste operating budget

**ATTACHMENTS**

# 1 - Resolution Updating Utility Enterprise Financial Policy
# 2 - Ordinance Continuing and Establishing Water User Fees and Charges
# 3 - Ordinance Continuing and Establishing Wastewater User Fees and Charges
# 4 - Ordinance Continuing and Establishing Solid Waste User Fees and Charges