

DATE ISSUED: June 2, 2004 **REPORT NO.** 04-120
ATTENTION: Honorable Mayor and City Council, Docket of June 8, 2004
SUBJECT: Reaffirmation of Water Fees and Charges
REFERENCES: City Manager's Report 02-081

SUMMARY

Issues - Should the City Council adopt the following resolutions which:

1. Reaffirm water rate increases previously adopted at its April 30, 2002 meeting to comply with state law; and,
2. Reaffirm previous increases in the water commodity charges and base fees due to increases in the wholesale cost of water purchased by the City and direct the City Manager to pass through future increases in the cost of purchased water, at such time as they occur?

Manager's Recommendation- Adopt the resolutions.

Other Recommendations– None.

Fiscal Impact – Any increases in water fees and charges resulting from increases in the cost of purchased water would be revenue neutral.

Adoption of the Manager's recommendation regarding the pass through of future increases in the cost of purchased water will save approximately \$100,000 annually in Proposition 218 noticing costs over the next three years.

BACKGROUND

Water-Related Proposition 218 Issues

In November 1996, California voters adopted Proposition 218, the Right to Vote on Taxes Act, which added articles XIII C and XIII D to the California Constitution. Article XIII D of the state Constitution specifies various restrictions and requirements for assessments, fees, and charges that local governments impose on real property or on persons as an incident of property ownership. This initiative changed the way the public is notified of proposed fee increases. Specifically, it requires that notices be mailed to all property owners of record at least 45 days in advance of the date on which a proposed property related fee increase may be adopted.

From time to time the assumed applicability of Proposition 218 to water fees and charges has changed. A recent decision of the California Supreme Court held that water rates are subject to the requirements of Proposition 218. Since a series of water rate increases adopted in April 2002 were not noticed in compliance with the provisions of Proposition 218, pursuant to then-current case law, the City Attorney has advised that the appropriate course of action going forward is to comply with the property-related fee provisions of Proposition 218, including noticing the property owners of record of proposed water rate increases and the reaffirmation by the council of rate increases adopted in April 2002. In addition, on January 1, 2004, per San Diego Municipal Code Section 67.0508, water rates were automatically adjusted as necessary to proportionately compensate for increases in the wholesale cost of water purchased by the City. Also consistent with Proposition 218 case law at the time, these increases were not noticed and should therefore be reaffirmed.

Consistent with current Proposition 218 case law, the Water Department mailed approximately 345,400 notices of today's hearing to every affected property owner of record during the week of April 19, 2004.

DISCUSSION

Reaffirmation Of Previously Approved Increases In Water Fees And Charges In Compliance With State Law

On April 30, 2002, the Mayor and Council authorized the City Manager to increase water sales revenue by 6% per year each year beginning July 1, 2002, for a period of five years through July 1, 2006. This was to be accomplished by adjusting the water base fees and commodity charges such that 50% of the additional revenue would be generated from the base fee, and the remaining 50% from the commodity charge. Due to prevailing case law at the time of their adoption, these rate increases were not adopted in compliance with the noticing provisions of Proposition 218. A recent California Supreme Court ruling determined that water fees are property related fees and charges subject to the provisions of Proposition 218. Consequently, it was determined that the

appropriate course of action is to comply with the property-related fee provisions of Proposition 218, including noticing the property owners of record to reaffirm the prior council vote.

Listed in Table 1 below are the previously approved and implemented base fees and commodity charges which became effective on July 1, 2002, and July 1, 2003, respectively, which require reaffirmation as described above. The previously approved but as yet unimplemented revenue increases of July 1, 2004 through July 1, 2006 should also be reaffirmed.

Table 1: MONTHLY WATER FEES AND CHARGES				
<u>Base Fees</u>				
<u>Meter Size</u>		<u>July 1, 2002</u>		<u>July 1, 2003</u>
Less than 1 inch	\$	10.68	\$	11.78
1 Inch		11.35		12.51
1 ½ Inch		51.33		56.59
2 Inch		78.94		87.03
3 Inch		284.57		313.74
4 Inch		474.70		523.36
6 Inch		1,060.41		1,169.11
8 Inch		1,427.21		1,573.50
10 Inch		1,912.57		2,108.60
12 Inch		2,657.24		2,929.61
16 Inch		4,425.83		4,879.48
<u>Commodity Charges</u>				
<u>Customer Class</u>		<u>July 1, 2002</u>		<u>July 1, 2003</u>
<u>Single Family Domestic</u>				
0-7 HCF	\$	1.338	\$	1.395
8-14 HCF		1.703		1.775
Over 14 HCF		1.880		1.959
All Other		1.567		1.634

Affirmation Of Previous And Approval of Future Pass-Through Increases In The Wholesale Cost Of Water Purchased By The City

San Diego Municipal Code Section 67.0508 requires that water rates be adjusted as necessary to proportionately compensate for any increase in the wholesale cost of water purchased by the City. As is the case with respect to prior water rate increases, certain previously imposed adjustments need to be affirmed by the Council.

There were two adjustments to water fees and charges on January 1, 2004 as the result of increases in the wholesale cost of water. At its March 11, 2003 meeting, the Board of Directors of the Metropolitan Water District of Southern California (MWD) set its water rates effective January 1, 2004. The weighted average cost of MWD's portion of wholesale water purchased

increased from \$367.36 per acre foot (AF) to \$378.89 per AF – an increase of 2.74 per hundred cubic feet (HCF), which equals 748 gallons. At its June 26, 2003 meeting, the Board of Directors of the San Diego County Water Authority (CWA) voted to raise wholesale raw water rates beginning January 1, 2004. This increased the average cost of CWA’s portion of wholesale water purchased from \$112.84 to \$114.33 per acre-foot - an increase of .34 per HCF. The Board of Directors of the CWA also voted to increase its meter-based Infrastructure Access Charge. The increase to each San Diego water customer’s monthly base fee was: under 1-inch: \$.15; 1-inch: \$.24; 1.5-inch: \$.45; 2-inch: \$.78; 3-inch: \$1.44; 4-inch: \$2.46; 6-inch: \$4.50; 8-inch: \$7.80; 10-inch: \$11.70; 12-inch: \$19.80; 16-inch: \$42.90.

Based on information provided by MWD and CWA staff, it is anticipated that annual cost-based adjustments will be imposed over the next several years. A range of pre-approved incremental water commodity charges due to increases in the wholesale cost of water purchased by the City is being proposed to maintain the City’s ability to adjust water rates under the Municipal Code while avoiding the substantial expense of annual noticing and public hearings. The resolution would limit the increases in the cost of purchased water to not more than \$.30 per HCF through June 30, 2007. The resolution will also establish an approved range of incremental base fee increases for the same purpose that would not exceed the following: under 1-inch: \$.25; 1-inch: \$.40; 1.5-inch: \$.75; 2-inch: \$1.30; 3-inch: \$2.40; 4-inch: \$4.10; 6-inch: \$7.50; 8-inch: \$13.00; 10-inch: \$19.50; 12-inch: \$33.00; 16-inch: \$71.50.

CONCLUSION

The reaffirmation of the water rate increases previously adopted in April, 2002, and affirmation of increases in the water commodity charges and base fees resulting from increases in the wholesale cost of water purchased by the City in January, 2004 will bring the City into compliance with newly established state law.

Adoption of the Manager’s recommendation regarding future pass-throughs of increased water costs will allow the Water Department to periodically adjust water fees and charges in an efficient and cost effective manner while complying with the legal noticing requirements of Proposition 218.

ALTERNATIVE

Do not approve the requested actions. This is not recommended since failure to reaffirm the City Council’s 2002 action to raise water rates would expose the City to litigation and financial market disclosure risk, and could adversely affect the revenue stream pledged to support debt

service payments on \$287 million in outstanding water revenue bonds which were issued that same year.

Respectfully submitted,

RICHARD MENDES
Deputy City Manager

KAHLIE/CR