



# CITY OF SANTA BARBARA

## COUNCIL AGENDA REPORT

**AGENDA DATE:** March 17, 2015

**TO:** Mayor and Councilmembers

**FROM:** Water Resources Division, Public Works Department

**SUBJECT:** Adoption Of Water Rate Increases For Fiscal Year 2016

### **RECOMMENDATION:**

That Council adopt, by reading of title only, a Resolution of the Council of the City of Santa Barbara Establishing Certain City Fees Effective for Fiscal Year 2016, Beginning July 1, 2015; and Rescinding Resolution 14-048 and Portions of Resolution No. 14-045.

### **DISCUSSION:**

On May 20, 2014, Council declared a Stage Two Drought Condition (Stage Two) in response to the ongoing drought and upon conclusion of the driest three-year period in local records. Stage Two is the second of three stages in the City's Water Shortage Contingency Plan. Among other things, Stage Two response measures include the development and adoption of a drought water rate structure that reflects increased costs associated with responding to the drought, and it targets a 20 percent reduction in customer water demand.

The drought water rates went into effect on July 1, 2014. At the time, there were significant available reserves; therefore, approximately \$7.2 million of reserves were allocated to be used for drought-related expenses, including supplemental water purchases, groundwater well projects, and the Cachuma Emergency Pump Project.

Since adoption of Stage Two, staff has continued planning for sustained drought conditions. Without sufficient rainfall by spring 2015, the next step in drought planning includes Council's decision to reactivate the City's Charles Meyer Desalination Plant (Desalination Plant), which was originally constructed in 1991-1992, during the previous severe drought.

Proposed water rates have been developed with the assumption that the Desalination Plant will produce 3,125 acre-feet per year (AFY) of water, beginning in fall 2016. Once we are out of the drought condition, the Desalination Plant could be placed into standby mode, producing a minimal amount of water sufficient to keep it in a ready state.

Annual operating costs are estimated at approximately \$5 million per year for production at 3,125 AFY, and approximately \$2.5 million per year for standby mode.

Capital costs for reactivating the Desalination Plant are estimated at approximately \$32 million; however, there are significant unknown potential costs. Final project costs will be unknown until a few weeks prior to the award of the contract to design, build, and operate the Desalination Plant, scheduled for June 2015. Staff recommends that the water rates provide the flexibility to generate sufficient revenues to cover up to \$40 million in capital costs for the Desalination Plant, should proposals to design and build the Desalination Plant come in at that range. These substantial added costs require an update to the Water Fund Financial Plan and increased Fiscal Year 2016 water rates that are sufficient to generate the revenues needed to cover capital and debt service for these costs.

Fiscal Year 2016 water rates, as well as the water rates for Fiscal Year 2015, were developed by Raftelis Financial Consultants, Inc., in compliance with California's Proposition 218. Any adjustment to water rates must be made in compliance with Proposition 218 requirements, which is known as the *Right to Vote on Taxes Act* and includes the requirement that rates may not exceed the estimated cost of providing service, and must be reasonable, fair, equitable, and proportional.

Proposed water rates have been designed to incentivize extraordinary conservation, while also providing sufficient revenues to meet operating and debt service requirements in order to maintain compliance with obligations to holders of City bonds. There are no substantial reserves available above Council policy for use in Fiscal Year 2016 (in contrast to Fiscal Year 2015). Therefore, water rates need to be increased to cover the full cost of service, which includes funding of the Water Main Replacement Program (based on Council policy to replace one percent of the pipe system annually), as well as the added costs that are attributable to the reactivation of the Desalination Plant.

Adoption of Fiscal Year 2016 water rates is recommended in March 2015, in order to qualify for loan requirements for the Desalination Project. Before taking effect on July 1, 2015, water rates will be re-assessed based on available information on the actual cost of desalination, the projected Fiscal Year 2016 budget, and the Fiscal Year 2015 ending reserve balance. If, at that time, it is determined that water rates can be lowered, the Fiscal Year 2016 water rates will be resubmitted for adoption prior to taking effect on July 1, 2015. Adopted water rates can be adjusted down from the proposed water rates noticed in January 2015, but they cannot be increased without new noticing per requirements of Prop 218.

The proposed Resolution is comprised of recommended Fiscal Year 2016 water rates, which would take effect July 1, 2015, thereby rescinding Resolution 14-058 and portions of Resolution 14-045 in the Water Rates and Fees Section, Parts 1.A, 1.B, and 1.C. The current 14-058 and 14-045 water rates will remain in effect until July 1, 2015. At that time, the final adopted Fiscal Year 2016 rate increases would take effect.

Water Commission Review

On January 12, 2015, the Water Commission received a presentation from staff and provided policy input on the proposed Fiscal Year 2016 water rates. The Water Commission also discussed policy input on the proposed rates at its meetings on August 11, 2014 and October 13, 2014.

Council Review

On January 13, 2015, Council received a presentation from staff and provided policy input on the proposed Fiscal Year 2016 water rates. Council also provided policy input on the design of the proposed rates at its meetings on September 23, 2014 and December 9, 2014.

Public Meetings

Staff hosted public information meetings on drought, desalination, and water rates on February 18, 2015 and February 26, 2015.

Public Hearing

Per the requirements of Prop 218, a public hearing was held on March 10, 2015.

**PREPARED BY:** Joshua Haggmark, Water Resources Manager/KD/mh

**SUBMITTED BY:** Rebecca J. Bjork, Public Works Director

**APPROVED BY:** City Administrator's Office