



# CITY OF SANTA BARBARA

## COUNCIL AGENDA REPORT

**AGENDA DATE:** November 24, 2015

**TO:** Mayor and Councilmembers

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

**SUBJECT:** Contract For Fiscal Year 2017 Water Rate Modeling Services

### RECOMMENDATION:

That Council authorize the Public Works Director to execute a City Professional Services contract with Raftelis Financial Consultants, Inc., in the amount of \$50,221 for development of proposed water rates for Fiscal Year 2017, and authorize the Public Works Director to approve expenditures of up to \$12,555 for extra services that may result from necessary changes in the scope of work, for a total not-to-exceed amount of \$62,776.

### DISCUSSION:

Staff has received a proposal from Raftelis Financial Consultants, Inc., (Raftelis) to complete the modeling and analysis necessary to develop proposed Fiscal Year 2017 water rates. Due to the uncertainty of continued drought conditions, several scenarios of water rates will be developed that account for various water supply and demand conditions. The actual water rate scenario to be recommended for implementation will be determined in the February-March 2016 time frame, when more information will be known about the impacts of this winter's rainfall on our water supplies.

The City of Santa Barbara (City) is currently in a Stage Three Drought Emergency Condition, requiring a 25 percent reduction in overall water demands. Current water rates, which went into effect on July 2015, account for increased costs associated with responding to the drought, as well as a 25 percent demand reduction. Since June 2015, the community has cumulatively reduced water usage by 35 percent, exceeding the 25 percent conservation goal. While this extraordinary conservation has a beneficial effect on water supply planning, it will result in a loss of revenue beyond what can be recovered under the current rate structure. The City's water fund reserves can temporarily absorb some of the losses but ultimately rates will need to be adjusted to stabilize the financial situation.

The City is a champion in water conservation and, in compliance with California Urban Water Conservation Council policies, has designed its water rates to incentivize

conservation, with 70 percent or more of revenue coming from volumetric rates that vary based on water use. This can be challenging to manage, given that the majority of the water system costs are fixed and are independent of water use. If water demands continue to be low and negatively impact revenues from volumetric rates, the City will be at risk of not meeting fixed financial obligations (e.g., debt service, required maintenance, etc.).

Given the uncertainty of whether the current level of water demands will continue, and the possibility of an increased conservation target for next year, the proposed water rate scenarios for Fiscal Year 2017 will consider a conservation range of 25 to 50 percent. A temporary fee will be considered in the water rate design that stabilizes revenue under various levels of demand reduction. This temporary fee is intended to address revenue loss that occurs when community conservation exceeds the conservation target and would be removed once water usage stabilized and the annually adopted rates were sufficient to cover the cost of service.

While the prospects of rain have improved this year, it is prudent to plan for a range of weather conditions. Therefore, the water rate scenarios will evaluate both 1) the size of the Charles E. Meyer Desalination Plant (Plant) as currently approved and under construction, and 2) a potential expansion, should drought conditions persist. A decision on a potential expansion of the Plant is not expected until spring 2016, after the majority of the rainy season is over. The water rate model will also anticipate potential revenue from the Montecito Water District (MWD), should the City and the MWD enter into a cost-sharing agreement in which the City would provide water to MWD. Negotiations for such an agreement between the City and the MWD are underway and anticipated to be complete in January 2016.

Any adjustment to the water rates must be made in compliance with Proposition 218 requirements, known as the *Right to Vote on Taxes Act*. It includes the requirement that the rates may not exceed the estimated cost of providing the service, and it must be reasonable, fair, equitable, and proportional. Raftelis is a well-known financial expert for water rate consulting services. Raftelis has developed the City's water rate model in support of the 2013 Water Rates Study, as well as our water rates in response to the drought for Fiscal Years 2015 and 2016, in compliance with the requirements of California's Proposition 218, approved by voters in 1996.

Staff has received a proposal from Raftelis to complete the modeling and analysis necessary to develop recommended rate structure scenarios for various water supply and demand conditions. This will build on the water rate model developed by Raftelis under previous contracts. The scope of services includes a revised Water Fund Financial Plan, with particular attention to water rates for Fiscal Years 2017 and 2018.

Two scenarios will be evaluated for Desalination Plant costs: 1) the current Plant capacity under construction, and 2) possible expansion of the Plant up to 7500 acre feet per year. For each cost scenario, various levels of water usage demand reductions will be evaluated to determine necessary fees for stabilizing the Water Fund reserves at

policy levels. The final work will be documented in a report that explains the approach and methodology behind the rates.

Initial work to develop proposed rates will be completed in time to allow rate noticing under Proposition 218 should the Council deem it necessary to move forward with financing an expansion of the Desalination Plant and to meet the timeline for the rates to become effective for Fiscal Year 2017. An extra services authorization equal to 25 percent of base costs is recommended in this case, due to the evolving nature of the water supply and demand conditions, and the need to promptly address unanticipated issues that may arise.

**BUDGET/FINANCIAL INFORMATION:**

There are sufficient appropriated funds in the Fiscal Year 2016 Water Fund budget for the proposed financing and rate model study services. The Water Commissioners heard this item at its November 9, 2015 meeting and the Board voted 5-0-0 to approve these services.

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

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

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