



AGENDA REPORT

Meeting Date: January 5, 2016

Item Number: F-1A

To: Honorable Mayor & City Council

From: Trish Rhay, Assistant Director of Public Works Services, Infrastructure & Field Operations
Caitlin Sims, Senior Management Analyst

Subject: A. AN ORDINANCE OF THE CITY OF BEVERLY HILLS TO MODIFY RATES AND CHARGES FOR WATER SERVICES AND FACILITIES FURNISHED BY THE CITY.

Attachments:

1. Ordinance
2. City of Beverly Hills – Water Rate Study
3. Public Hearing Notices
4. Resolution 15-R-13037
5. Protest Letters Received

RECOMMENDATION

It is recommended that the City Council move that the full reading of the ordinance be waived and that the ordinance entitled "An Ordinance of the City of Beverly Hills to Modify the Rates and Charges for Water Services and Facilities Furnished by the City" be introduced for first reading.

INTRODUCTION

Since July 2015, City staff and the Public Works Commission's Conservation Subcommittee have been working with HF&H Consultants, LLC, ("HF&H") to analyze the City's existing rate structure. The City and consultants conducted a comprehensive analysis and re-evaluation of the tiered rate structure itself, considering the San Juan Capistrano Court Case, the City's mandatory water use reductions, and the implementation of the City's Water Enterprise Plan. This rate structure takes into account long term reductions in consumption as result of ongoing conservation measures and increased operating expenses.

At its November 17, 2015, Study Session, the City Council directed staff to proceed with the notice of public hearing regarding the proposed water rate modifications. California law requires the City to mail notice to all owners of the property subject to the proposed water rate increase and all Beverly Hills water customers. On November 20, 2015, the City mailed a notice of a public hearing scheduled for January 5, 2016, regarding the proposed water rate increases to all customers within the City's water service area. Notice regarding the public hearing was posted in the *Beverly Hills Courier* on December 25, 2015, and will be posted in the *Beverly Hills Weekly* on Thursday, December 31, 2015, again in the *Beverly Hills Courier* on January 1, 2016, and in the *West Hollywood Independent* on December 31, 2015.

DISCUSSION

The City's current water rates structure includes three customer classes: Single Family Residential, Multi-Family Residential, and Commercial. There are four tiers in the Single-Family Residential and Multi-Family Residential Classes and only one tier in the Commercial Class. The City charges the sum of a quantity charge and service charge. The quantity charge varies depending on the amount of metered water use in each two-month billing period. The service charge is fixed based on the size of the service connection. This rate structure has been in effect for a number of years. Service (meter) charges were last increased in September 2014, and quantity charges were last increased in November 2015 by 5%.

The current water rates structure is no longer revenue-neutral as a result of increasing operating costs and decreasing revenues as a result of water conservation during the drought. These decreasing revenues from the sale of water are anticipated to continue in the short-term, as the City works to meet its 32% reduction mandate from the State Water Resources Control Board ("SWRCB"), and in the long-term, as the City works to meet the State's long-term mandate that each water agency reduce its water usage 20% by 2020. The funds collected from the penalty surcharge, which was adopted by the City Council at its June 30, 2015, can only be used to cover the specific short-term costs that are attributed to not meeting the City's reduction mandates. These costs include implementing additional water conservation programs, fines imposed by the SWRCB, and the increased cost of purchasing water from the Metropolitan Water District of Southern California ("MWD") if the City does not reduce its water purchases by at least 12%. The revenues collected from the penalty surcharge cannot be used to cover any budget shortfall that results from decreasing revenues as a result of conservation.

The proposed rate structure, which was presented to the City Council at its November 17, 2015, Study Session, was identified as the best proposed rate structure to address three primary factors:

- (1) Identifies and defines customer classes and tier "breakpoints" in a manner that is consistent with Proposition 218:
 - a. Proposition 218 requires that rates be set in accordance with service costs across a range of consumption. In its decision in *Capistrano Taxpayers Association, Inc. v. City of San Juan Capistrano*, the California Fourth Court of Appeals further clarified that cities must be able to show how rates at different tier levels are based on the actual cost of providing service. In its evaluation, HF&H, staff and the Conservation Subcommittee fully assessed the costs of providing water to the different customer classes and the different tier levels.
- (2) Is revenue neutral:
 - a. The proposed rate structure allows the City to recover its fixed and variable operating costs even with the City's decreasing water consumption revenues, as

the City strives for its long-term water supply and conservation goals. It is also sufficient revenue to cover the cost of implementing the Water Enterprise Plan and capital operating costs.

(3) Accounts for the City's long-term water conservation goals:

- a. State law requires the City to reduce its water usage by 20% by 2020. This is separate from the short-term target of 32% that was set by the SWRCB in response to the Governor's drought declaration. The City's target 2020 usage was identified in the City's Urban Water Management Plan and is based on the City's average daily consumption over a ten-year period (from 1996 to 2005). As the City moves towards this long-term conservation goal and customers use less water, the City's revenues from water consumption will decrease. Many of the City's costs for operating and maintaining the water system are fixed, so rates should be set at a level that allows the City to cover its operating and capital costs even as water consumption revenues are decreasing.

The following sections discuss the rate evaluation process and the resulting rates.

Revenue Requirements

The first step in the rate analysis was to evaluate the City's anticipated expenses and revenues over the next five years. These expenses include the cost of purchasing water from Metropolitan Water District ("MWD") and the fixed costs of operating the water system, including distribution lines, staff needed to operate and maintain the water system, materials and supplies (which may decrease as water purchases decrease but only minimally) and debt service payments. Additional expenses include budgeted capital projects such as water main and hydrant replacements, water meter replacements, water treatment plant maintenance, and reservoir replacement.

The City also recently adopted a ten-year Water Enterprise Plan (WEP), which includes projects and programs that will increase the City's water system reliability. Many of the capital projects identified in the WEP will be debt-financed. The costs included in the City's rate revenue requirements include the debt-service payment requirements for the issuance of bonds for these WEP projects in order to maintain the required bonding agencies' minimum debt service ratio. Other costs identified in the WEP, including additional personnel to implement the WEP, are also incorporated into the revenue requirement.

The City's revenues come primarily from water consumption charges, service charges based on meter size, and fire service charges. The Governor's drought declaration requiring the City to reduce its water consumption by 32% and the City's increased focus on conservation have resulted in a significant decrease to water consumption revenues in FY15/16. In FY 2015-16, it is projected that water consumption will decrease 19.4% compared to FY 2014-15. At the same time, the City has fixed costs that are necessary to operate and maintain its system, including personnel, water distribution lines, materials, supplies, debt service payments, along with the aforementioned capital expenses. Even as water revenues decrease as consumption decreases, the majority of these fixed costs remain the same, while the variable cost of purchased water decreases. With the increased conservation, the City will need to increase its revenues in order to meet the total costs of operating the system and remain revenue neutral.

For the purposes of the analysis, HF&H and staff assumed that there would be a system-wide reduction of 19.4% compared to FY 2014-15 recorded revenues. This assumption is supported by water conservation trends since Stage D Water Conservation Measures were adopted by the

City Council in May 2015. Since May 2015, the City has cut back its usage by 20% compared to the same period in 2013.

Cost of Service Analysis

The next step in the rate evaluation was to determine the cost of providing water service to each customer class. The cost of service analysis allocates the cost of providing service equitably across all the classes (i.e. residential, multi-family, commercial), recognizing that different customer classes have different water use patterns and different peak demands and, as a result, different level of service requirements. Single-Family Residential Class customers typically have larger areas of landscaping and, therefore, more outdoor irrigation during the summer months, so there is more peaking in that class between the summer months and the lowest usage months. The Multi-Family Residential Class has the least amount of peaking because there is typically less irrigation and more consistent usage throughout the year, regardless of the season. The Commercial Class has peaking tendencies between the two other classes. An equitable rate structure must recognize these differences. HF&H and staff used the base-extra capacity methodology, a rate-making methodology approved by the American Water Works Association (AWWA) that allocates the cost of providing service to the different classes based on their usage of the water system. This methodology correlates the cost of service to meet peak demands with the customer class's levels of demand.

In the base/extra capacity methodology, costs are classified by function (e.g., treatment, pumping, storage, distribution, metering) and allocated among the customer classes in proportion to their use of these functions. To account for the peak levels in service, the water systems were designed and constructed to accommodate these peak demands. Some costs, including sources of supply like groundwater and purchased water from Metropolitan Water District, are considered non-peaking, base demands because they are unaffected by levels of demand. Other services and facilities – like those related to water quality and treatment and transmission (i.e. pipelines, pump stations, and storage reservoirs) – are impacted by higher levels of demand because meeting the City's peak demands requires larger, more expensive infrastructure and higher attendant operating costs. Higher levels of demand cost more to supply because of the increased cost of larger infrastructure and the attendant operating costs.

Costs that are related to meeting base and extra capacity demands are allocated among the City's customer classes – Single-Family Residential, Multi-Family Residential, and Commercial – based on their use of these services at the non-seasonal average day (i.e., base day), average day, maximum day, and maximum hour. Non-seasonal average demands correspond to customer billings in the lowest billing period in FY 2014-15. Average day demands are based on the average daily demand according to FY 2014-15 customer billing data. Maximum day demands for each class were estimated based on the maximum day demand for the system in FY 2014-15; an estimate for each class was required because the City does not bill customers on a daily basis. The maximum hour demand was estimated at two times the maximum day demand.

In addition to using the base/extra capacity methodology to determine each class' share of the total costs, the methodology was also used to determine each class's tiered rate structure, which is consistent with Proposition 218 and the San Juan Capistrano decision's requirement that the rates in tiered structures correlate with the cost associated with each tier. The methodology correlates the costs for each tier and the size of each tier for each class to ensure that the rate per tier is proportionate to the cost of service.

Proposed Rates & Bill Impacts

The cost of service analysis provided the proposed rates and tier breakpoints for each class, which can be found for each class below. The analysis also sets the West Hollywood rate at 1.25 times the Beverly Hills rate in recognition that Beverly Hills has extended service out of the city limits to customers that had not contributed to the City's General Fund which funded the initial construction of the City's water system.

Single Family Residential

Currently, there are four tiers in the Single-Family Residential Class. Based on the analysis of revenues from the single-family revenues, the cost of service needed to serve that class, and the water usage and peaking trends, it was determined that the Single-Family Residential Class should consist of four tiers. HF&H and staff analyzed FY 2014-15 customer billing data in the Single-Family Residential Class and proposed new breakpoints based on the average usage in the lowest FY 2014-15 billing period, annual average day usage in FY 2014-15, and peak daily usage in FY 2014-15. The analysis indicated that current demand has decreased since the last time the breakpoints were set.

Table 1 (below) shows the proposed rates and rate structure for single-family residential customers in the City of Beverly Hills. Each bill is issued bi-monthly, and a billing unit is equal to 1 hundred cubic foot (HCF). Table 1 shows the tiers in HCF and the equivalent gallons. Note that one HCF is equal to 748 gallons.

Table 1 – Proposed Single-Family Residential Rates for City of Beverly Hills

	Current				Proposed			
	HCF per Account	Gallons/Day	Rate	Cost per Gallon	HCF per Account	Gallons/Day	Rate	Cost per Gallon
Tier 1	0-10	1 - 136	\$3.71	\$0.005	0-42	1 – 535	\$4.32	\$0.006
Tier 2	11-55	137 – 697	\$4.90	\$0.007	43-61	536 – 772	\$5.17	\$0.007
Tier 3	56-120	698 – 1,507	\$7.73	\$0.010	62-92	773 – 1,158	\$9.27	\$0.012
Tier 4	121+	1,508+	\$14.93	\$0.020	93+	1,159+	\$18.59	\$0.025

The overall rate increase for the single-family residential customer class is approximately 17.7%. Each customer's water bill includes the quantity charge and a service charge, which is a fixed rate based on the size of the service meter.

Table 2 (below) shows several bill impacts for customers at different water use levels. These bills include 1" meter service charges and quantity charges.

Table 2 – Single-Family Residential Bill Impacts (Quantity Charge and Service Charge)

Water Use	Current Bill	Proposed Bill	\$ Change	% Change
Low (6 HCF bi-monthly or 75 gallons/day)	\$65.52	\$69.28	\$3.66	+5.6%
Medium (60 HCF bi-monthly or 748 gallons/day)	\$339.61	\$317.83	\$ -21.78	-6.4%
High (130 HCF bi-monthly or 1,621 gallons/day)	\$952.71	\$1,316.75	\$364.04	+38.2%
Very High (300 HCF bi-monthly or 3740 gallons/day)	\$3,490.81	\$4,477.17	\$986.36	+28.3%

Due to the peaking methodology being used, customers that use the most water, and therefore place the greatest demands on the system, will see the largest bill impacts.

Multi-Family Residential

In the current rate structure, there are four tiers in the Multi-Family Residential Class. While the current breakpoints are different from those in the Single-Family Residential Class, the rates for each of the four tiers are currently the same. The rates for the Multi-Family Residential Class are based on usage per dwelling unit and therefore account for the different building sizes in the City's multi-family housing stock.

An analysis of FY 2014-15 Multi-Family Residential customer billing data indicated that there was very little variation between the average demand in the lowest billing period, the average daily demand, and the peak daily demand. This is because Multi-Family Residential customers typically do not have significant landscape irrigation; most of the water demand is for indoor use only. As such, it is appropriate to replace the current four-tier structure with a two-tier structure.

Table 3 (below) shows the proposed rates and rate structure for Multi-Family Residential Customers in the City of Beverly Hills. The rates are billed per dwelling unit.

Table 3 – Proposed Multi-Family Residential Rates for City of Beverly Hills

	Current				Proposed			
	HCF per Account	Gallons/Day	Rate	Cost per Gallon	HCF per Account	Gallons/Day	Rate	Cost per Gallon
Tier 1	0-4	1 – 61	\$3.71	\$0.005	0-9	1 – 124	\$4.72	\$0.006
Tier 2	5-9	62 – 124	\$4.90	\$0.007	10+	125+	\$17.50	\$0.023
Tier 3	10-16	125-211	\$7.73	\$0.010				
Tier 4	17+	212+	\$14.93	\$0.020				

The overall rate increase for the Multi-Family Residential customer class is 41.6%. Table 4 (below) shows several bill impacts for different customers, based on the number of units and level of usage. These bills include 1" meter service charges and quantity charges.

Table 4 – Multi-Family Residential Bill Impacts (Quantity and Service Charge)

Water Use	Current Bill	Proposed Bill	\$ Change	% Change
Low (6 HCF bi-monthly or 75 gallons/day)	\$28.98	\$32.64	\$3.67	+12.7%
Medium (12 HCF bi-monthly or 150 gallons/day)	\$66.87	\$99.30	\$32.44	+48.5%
High (24 HCF bi-monthly or 299 gallons/day)	\$217.23	\$309.33	\$92.10	+42.4%

Multi-Family residential customers will see the greatest impact to their water bills. This is largely because, in the current rate structure, the Multi-Family Residential Class as a whole is currently recovering 34% less than its overall cost of service. In addition, water usage across all seasons is more concentrated around the average (i.e. there is less peaking) because there is relatively consistent water usage at all times. When demand exceeds average in the Multi-Family Residential Class, the cost of peaking is comparable to the cost of Single-Family Residential

peaking in the highest tier. For both Single-Family Residential and Multi-Family Residential classes, there is a considerable cost increase for maximum day and maximum hour peak service.

Beverly Hills Municipal Code (“BHMC”) Section 4-5-306 allows the landlord to pass through a “utility expense surcharge” for the cost of a basic and essential utility service (i.e. water) to those tenants that are covered by Chapter 5 of the BHMC. Chapter 5 tenants have lived in their current rental unit since at least 1978 and had a rent of less than six hundred dollars (\$600.00) per month at that time. The utility expense surcharge can be passed through to Chapter 5 tenants if the utility costs for the year beginning March 1 and ending February 28 for the current year have increased by a percentage that is greater than the allowed annual rent increase. The allowed annual rent increase for Chapter 5 tenants is 8% or the consumer price index (CPI), whichever is less. The utility increase (comparing March 1 of the current year to February 28 of the previous year) is prorated among all of the units and payable one-twelfth per month over the course of the next year. The utility expense surcharge could not be recalculated again until February 28 of the following year. The utility expense surcharge cannot be levied on BHMC Chapter 6 tenants.

Commercial

Currently, the Commercial Class currently has one uniform rate, regardless of consumption. An analysis of FY 2014-15 Commercial customer billing data revealed that, like in the Single-Family Residential class, there was a wider variation between the average usage in the lowest billing period in FY 2014-15, the average daily usage in FY 2014-15, and the maximum day and maximum hour usage in FY 2014-15. As such, it is appropriate for the Commercial Class to have 4 tiers. The proposed four-tiered structure will more accurately reflect the cost of providing service across a range of consumption.

Table 5 (below) shows the proposed rates and rate structure for Commercial Customers in the City of Beverly Hills.

Table 5 – Proposed Commercial Rates for City of Beverly Hills

	Current				Proposed			
	HCF per Account	Gallons/ Day	Rate	Cost per Gallon	HCF per Account	Gallons/ Day	Rate	Cost per Gallon
Tier 1	n/a	n/a	\$6.34	\$0.008	0-119	1 – 1,495	\$4.40	\$0.006
Tier 2					120-144	1,496 – 1,807	\$4.90	\$0.007
Tier 3					145-177	1,808 – 2,218	\$6.90	\$0.009
Tier 4					178+	2,219+	\$9.99	\$0.013

The overall rate increase for the commercial customer class is 19.7%. Table 6 (below) shows what the bill impacts would be for customers at different water use levels. These bills include meter service charges ranging from 1” to 4” and quantity charges.

Table 6 – Commercial Bill Impacts – 4 Tiers

Water Use	Current Bill	Proposed Bill	\$ Change	% Change
Low (20 HCF bi-monthly or 249 gallons/day)	\$170.16	\$131.42	\$ -38.74	-22.8%
Med (150 HCF bi-monthly or 1,870 gallons/day)	\$1,026.16	\$762.96	\$ -263.20	-25.6%
High (300 HCF bi-monthly or 3,740)	\$2,231.55	\$2,432.36	\$200.81	+9.0%

gallons/day)				
Very High (5000 HCF bi-monthly or 62,333 gallons per day)	\$32,029.55	\$49,385.51	\$17,355.96	+54.2%

Commercial customers with low to average demand will experience decreased bills because the number of tiers is expanding from 1 to 4 and the subsequent Tier 1 and Tier 2 rates are lower than the current uniform rate. Commercial customers with high demand, who place the greatest burden on the water system of all the customers, will experience increased bills, as the proposed Tier 3 and Tier 4 rates are higher than the current uniform rate.

Water Rate Implementation

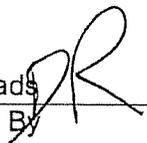
Should the City Council decide to move forward with the proposed rate increases, the implementation schedule would be as follows:

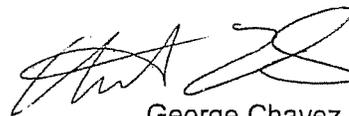
Date	Action
January 5, 2016	Hold Public Hearing on Proposed Water Rates Increases/Introduction of Ordinance
January 26, 2016	Second Reading
February 26, 2016	Effective Date of Ordinance (30 days after Second Reading and upon completion and testing of billing system structure changes.)

The new tiered water rate structure does not address the potential costs that have resulted from non-compliance with the Governor's drought declaration. These costs will be recovered as a part of the penalty surcharge, for which the framework was approved by the City Council at its June 30, 2015 meeting. The additional revenues realized as a result of the penalty surcharge are intended to cover the cost of conservation efforts and penalties imposed by the State Water Resources Control Board ("SWRCB") and MWD. The penalty rate will remain in effect as long as the City continues to maintain stage D water conservation declaration; however, the factors being applied will need to decrease in light of the overall rate increase. The new proposed penalty surcharge multipliers will be discussed separately at the January 5, 2016, City Council meeting.

FISCAL IMPACT

In FY 2015-16, Water Enterprise revenues are estimated to be approximately \$32.6 million, while the projected costs are approximately \$35.9 million; this is a revenue shortfall of approximately \$3.3 million. This projection is based on anticipated reductions of 19.4%, which is similar to actual usage reductions observed during the last several months. The proposed tiered water rates structure would ensure that the City's water system operations are revenue neutral even with increased conservation.

Don Rhoads
 Approved By 


 George Chavez
 Approved By 