



THE CITY OF SAN DIEGO

August 26, 2010

Alex Ruiz
Interim Director of Public Utilities
City of San Diego

Subject: **Agreed-Upon Procedures Review of the Public Utilities Department's
Increase in City of San Diego Water Rates**

We performed the agreed-upon procedures review requested by the Public Utilities Department related to the proposed increase in water rates for City of San Diego rate payers, pursuant to San Diego County Water Authority rate increases effective January 1, 2011, except for the Readiness-to-Serve Charge which is effective July 1, 2010. In summary, we agreed to perform a review of the mathematical accuracy of the Public Utilities Department's calculations of projected increases in water purchase costs and the revenues required to offset the purchases for calendar year 2011.

We conducted our work in accordance with Generally Accepted Government Auditing Standards. These standards provide guidance on performing and reporting on the results of agreed-upon procedures. By specifying the procedures we agreed to perform, the Public Utilities Department is responsible for ensuring that the procedures are sufficient to meet their purposes, and we make no representation in that respect. Our review is intended solely for the information and use of the management of the City and is not intended to be and should not be used by anyone other than these specified parties.

We were not requested to, and did not conduct an audit verifying the reasonableness of the assumptions related to estimates and projections which would have required additional procedures. Such additional procedures may have identified other matters, if they existed, that would have been reported to you. We initiated our agreed-upon procedures on August 5, 2010, and completed our work on August 25, 2010.

Alex Ruiz
Page 2 of 2
August 26, 2010

The agreed-upon procedures and the results of our work in the report attached were provided in draft to the Public Utilities Department for review and comments and they concurred with its contents. The audit staff responsible for this audit report is Judy Zellers, Kyle Elser, and Chris Constantin. Please contact me if you have any questions.

Sincerely,

A handwritten signature in cursive script that reads "Eduardo Luna".

Eduardo Luna
City Auditor

cc: Honorable Mayor Jerry Sanders
Honorable City Council Members
Honorable Audit Committee Members
Jay M. Goldstone, Chief Operating Officer
Jeanne Cole, Interim Program Manager, Public Utilities Department
Chris Ojeda, Supervising Economist, Public Utilities Department
Mary Lewis, Chief Financial Officer
Jan Goldsmith, City Attorney
Ken Whitfield, City Comptroller
Andrea Tevlin, Independent Budget Analyst

Public Utilities Department Agreed-Upon Procedures Review Report CY2011 Pass-Through Charges

Background

The City of San Diego purchases water from the San Diego County Water Authority (SDCWA). As a result of increases in the Metropolitan Water District's (MWD) water supply rates, the SDCWA Board of Directors authorized an increase in the cost of water purchased from the Water Authority, effective January 1, 2011, except for the Readiness-to-Serve Charge which is effective July 1, 2010. The City of San Diego Public Utilities Department has proposed a January 1, 2011 increase to the rates paid by City of San Diego customers to offset these increasing costs. The Public Utilities Department asked the Office of the City Auditor to perform an agreed-upon procedures review to verify the accuracy of those calculations.

Public Utilities Department calculations included the following:

- Increase in base rates per meter, based on water meter sizes
- Increase in costs to purchase water from SDCWA, based on SDCWA rate changes and estimated water purchases
- Increased revenue from San Diego ratepayers necessary to offset the purchase costs based on estimated water sales
- Allocation of the increased revenues to customers, based on water usage

While a Proposition 218 public notice is required prior to increasing rates, a draft of this notice was not provided and was therefore not part of this review. Additionally, we did not trace the City's water purchase costs to the invoices issued by SDCWA, and we make no statement as to the accuracy of the purchase costs provided by the Public Utilities Department.

In summary, we found that the Public Utilities Department calculations were mathematically accurate.

The following table provides the results of our agreed-upon procedures review.

Agreed-Upon Procedure	Result	Review Procedures
<p><i>1) Trace the January 1, 2011 water purchase costs to the SDCWA ordinance.</i></p>	<p>The rates established by the SDCWA agreed to the rates used in the Public Utilities Department's calculations. The rates are effective January 1, 2011 except for the Readiness-to-Serve Charge which is increased on a fiscal year basis at July 1.</p> <p>The Readiness-to-Serve Charges are incurred by the City on a fiscal year (FY) basis; however, the offsetting revenues are collected on a calendar year (CY) basis. Approximately \$700,000 of costs incurred in FY 2010 will be collected from ratepayers in FY 2011. We notified Public Utilities of the timing difference in cost recovery pertaining to the Readiness-to-Serve Charge and discussed this with the City's independent auditor who concluded this is immaterial to the fund.</p>	<p>Traced rates effective as of January 1, 2011 from the SDCWA ordinance to the rates used by the Water Division in their calculations. Payments to the SDCWA for in-lieu taxes are based on budgeted estimates and are the responsibility of the Public Utilities Department; we did not confirm the calculation of these estimates.</p>
<p><i>2) Verify the prior year purchase costs used to calculate the change in costs between calendar year 2010 and calendar year 2011 rates.</i></p>	<p>The prior year SDCWA rates agreed to the rates used in the Public Utilities Department's calculations.</p>	<p>We verified the SDCWA rates, effective January 1, 2010 based on the prior year SDCWA ordinance. Payments to the SDCWA for in-lieu taxes were traced to the prior year estimate.</p>
<p><i>3) Verify the mathematical accuracy of the Public Utilities Department's calculations of projected increases in water purchase costs and the revenues required to offset the purchases for calendar year 2011.</i></p>	<p>Projected increases in water purchase costs and the revenues required to offset the purchases for calendar year 2011 were mathematically accurate.</p>	<p>The projected total increases in water purchase costs and the revenues required to offset the purchases for calendar year 2011 are based on estimates of acre feet of water purchased and sold, which may vary</p>

Agreed-Upon Procedure	Result	Review Procedures
	SDCWA has maintained FY 2010 target allocations through June 2011.	<p>depending on usage. We used the following procedures to verify mathematical accuracy:</p> <ul style="list-style-type: none"> • Traced FY2010 water sales figures to Customer Information System Report U0-400-30. • Verified the projected water sales for CY 2011 do not exceed CWA Target Allocation for FY2010. • Verified mathematical accuracy of revenue estimates for FY2011 and FY2012. • Verified additional revenue required based on projected water sales.
4) <i>Verify the allocation of rate increases to rate payers.</i>	The allocation of rate increases to rate payers is mathematically accurate.	<ul style="list-style-type: none"> • Recalculated July 1, 2010 rates based on 6.5% annual increase approved by Council Res. 302380 for FY2008-2011. • Recalculated projected January 1, 2011 rates prior to the SDCWA increases and verified rate reversals in calendar year 2010. Two rate reversals will occur in CY 2010. On September 1, 2010, the temporary charge to fund the Indirect Potable Reuse Project (IPR) will be reversed. Also, a partial reversal of the City's

Agreed-Upon Procedure	Result	Review Procedures
		<p>January 1, 2010 pass-through rate increase will be reversed. There was a four month timing difference in the prior year between the date the SDCWA increased costs to the City and the date the City passed these increased costs to the rate payers. The CY 2010 rate was calculated to recover sixteen months of costs over a twelve month period. The portion of the rate pertaining to the timing difference will be reversed prior to the January 1, 2011 pass-through increase.</p> <ul style="list-style-type: none"> • Verified the percentage increase in commodity charges based on additional revenue required to offset costs.