



THE CITY OF SAN DIEGO

M E M O R A N D U M

DATE: March 27, 2017
TO: Independent Rates Oversight Committee
FROM: Halla Razak, Director, Public Utilities Department
SUBJECT: Department Response to the Fiscal Year 2016 IROC Annual Report

On December 19, 2016, the Independent Rates Oversight Committee (IROC) and its subcommittees issued their Fiscal Year 2016 Annual Report with 18 recommendations.

The Public Utilities Department (Department) has reviewed and provided responses to IROC's recommendations (see attachment). In summary, the Department agrees with 11 of the recommendations, partially agrees with four of the recommendations, and disagrees with three of its subcommittees' recommendations. We will update IROC periodically to keep you informed of our progress towards implementation.

I would like to express my gratitude on behalf of the Department for your insightful and wide ranging recommendations. Staff will continue to evaluate and consider all of IROC's recommendations. If you have any questions or require additional information, please contact IROC Coordinator, Wilson Kennedy at (858) 614-4070.

A handwritten signature in blue ink, appearing to read "Halla Razak".

Halla Razak

WK/sh

Attachment: Department Response to the Fiscal Year 2016 IROC Annual Report

cc: Honorable Mayor Kevin L. Faulconer and Members of the City Council
Scott Chadwick, Chief Operating Officer
Paz Gomez, Deputy Chief Operating Officer, Infrastructure/Public Works
Andrea Tevlin, Independent Budget Analyst
Thomas Zeleny, Chief Deputy City Attorney, Office of the City Attorney

**Public Utilities Department
Response to the Fiscal Year 2016 IROC Annual Report
Issued: December 19, 2016**

IROC's Key Recommendations

1. That Department staff regularly report to IROC with information regarding water sales, revenues, local supply availability and other factors that influence revenues and expenditures and how these track with cost of service assumptions. IROC also recommends that Department staff present to IROC and seek input to the consultant's independent analysis. Further, IROC recommends that the department proceed with the evaluation of alternative rate structures as soon as possible and involve IROC and stakeholder groups in a thorough evaluation of alternatives given the new tools the Department will have (AMI), water supply conditions and the cost of developing new supplies so that costs and water rates are allocated and distributed in the most fair and equitable manner practicable in accordance with Proposition 218. – Finance Subcommittee

Department Response: The Department partially agrees with this recommendation.

The Department agrees to continue providing IROC with quarterly financial reports for the Water and Wastewater Funds.

The Department, City, and other agencies use a variety of criteria for validating the need for future rate increases. The criteria include debt coverage ratios, cash on hand, and the CIP Program to name a few. The Department also works with other City departments to review the financials including Debt Management, Financial Management, and the Office of the City Comptroller.

As part of the Water Fund's FY 2016 Cost of Service Study, the Department agreed to a Review of Funds to analyze anticipated revenues, expenditures, and capital improvement program expenditures against actual results for FY 2016 & FY 2017 and make any prospective prudent recommendation on adjusting future rate increases. This process will begin in July 2017 with the final report and associated potential recommendations anticipated in the second half of FY 2018. Additionally, the Department will be working on identifying possible alternative rate structures for the Water Fund in FY 2018. This process will involve input solicited from both IROC and varied stakeholders, with the proposal for alternative rate structures from this process anticipated at the end of FY 2018.

2. That the City staff, as part of its ongoing efforts to review alternative rates and rate structures, include reclaimed water pricing. Staff should consider having a separate supply rate and separate transportation rate for reclaimed water so that a unitary cost for each of these reclaimed water cost elements could still be used. – Finance Subcommittee

Department Response: The Department disagrees with this recommendation.

The Department, City, and other agencies use a variety of criteria for validating the need for future rate increases.

In the FY 2016 COSS, the Department reviewed past expenditures for recycled water. Following legal compliance, the Department provided two rate options to the Environment Committee on August 5, 2015 and to the City Council on November 17, 2015. City Council approved the recycled water unitary rate on November 17, 2015.

3. The Department's budget execution, particularly CIP award and completion rates are greatly improving. IROC recommends that the Department report back to IROC a five-year summary of budget completion and capital improvement completion in order for IROC to ascertain how much the trends are improving over past years. The ability to complete CIP activities in a timely manner affects the Department's budget needs and ultimately water and waste water rates and charges. IROC notes that the metric used for water main replacement is miles of pipeline awarded for construction while the goal for sewer main replacement is miles of pipeline replaced or rehabbed. IROC understand that the difference is due to legal reporting issues, however using the actual miles replaced is a better measurement of success than miles awarded and recommends that this metric be added to the water main reporting documents. – Finance Subcommittee

Department Response: The Department agrees with this recommendation.

The Department in conjunction with Public Works Engineering agrees to continue providing IROC with CIP reports for the Water and Wastewater Funds. These reports have been modified to show actual miles replaced for both the Water and Wastewater Funds in addition to all previously provided metrics.

4. That IROC continue to monitor budget expenditures throughout the year. As recommended last year, the Subcommittee reiterated its request that the Department provide IROC a copy of future proposed budgets as soon as possible after release by the Mayor's office, in addition to budget summaries normally prepared for the Subcommittee. IROC also recommends that future departmental budgets include key assumptions of drivers of revenues and costs, such as projected water sales and purchase volumes and availability of local supplies.

Further, IROC recommends that the City's budget document, as it pertains to the Department, include baseline assumptions (detailed above) so that year-to-year comparisons can be made of these assumptions as they relate to previous budget documents and the COSS. It also recommends that the budget document expand descriptions of the Department's goal and objectives, and include all relevant performance indicators to measure departmental success.

Finally, IROC recommends that key issues such as the budget continue to be discussed in detail at the Subcommittee level, but Department staff also present the budget to the full IROC. This will allow all IROC members to have a greater understanding of the Department revenues and expenditures. Also, IROC recommends that key budget drivers, such as overall water sales, local supply availability be reported at each IROC meeting so as IROC can understand the ongoing trends, rather than once a year reporting after the fact. – Finance Subcommittee

Department Response: The Department agrees with this recommendation.

The Department will continue to provide IROC with financial information as soon as possible. In addition, the Department will continue to present key drivers of revenues and costs at IROC meetings.

5. That Department staff reevaluate its method for assigning AMI cost to the wastewater (sewer) system to reflect cost of service and actual benefits received by sewer customers and make the appropriate budget adjustments to both Water and Wastewater funds so that sewer customers are not charged for AMI costs that provide only nominal benefits to them. – Finance Subcommittee

Department Response: The Department disagrees with this recommendation.

The data needed for the wastewater (Sewer) system requires the information from the AMI System. Though the billing data is evaluated for the winter monitoring period, the data will also be collected and used to monitor climate and conservation impacts on the sewer collection and treatment processes. This data is crucial for the operational monitoring.

6. That the Department continue to pursue all options available to get regulatory certainty that the Pure Water San Diego Program will suffice to offset the requirement to move up to secondary treatment. – Infrastructure & Operations Subcommittee

Department Response: The Department partially agrees with this statement.

The City is not currently under a requirement to convert the Point Loma Wastewater Treatment Plant to secondary treatment. The City continues to exercise the authority within the Clean Water Act to apply for modified National Pollution Discharge Elimination System (NPDES) permits to operate the facility at Advanced Primary. We expect to complete the current modified permit hearing process in Fiscal Year 2017 which will authorize a renewal for an additional five years.

The Department continues to pursue viable options for legislative or regulatory certainty as it relates to future permitting for the Point Loma Wastewater Treatment Plant.

Finance Subcommittee:

1. That the Department continue to implement and report progress to IROC on recommendations made by the Water Policy Implementation Committee and accepted by the City Council.

Department Response: The Department agrees with this recommendation.

The Department will continue to implement and report progress to IROC on recommendations made by the Water Policy Implementation Committee that have been accepted by the City Council.

2. That as the State Water Resources Control Board revises its conservation mandates, the Department continue to provide a leadership role in shaping California's drought policy, so that the City receives credits for its actions and efforts in water conservation, reclamation, and Pure Water San Diego Programs.

Department Response: The Department agrees with this recommendation.

The Department will continue to play a leadership role at the State level with the goal of receiving credit for the Department and regional actions in water conservation, reclamation, and Pure Water San Diego Programs.

Infrastructure & Operations Subcommittee:

1. That the Department continue to perform condition assessments in order to help guide the CIP for replacement or repair of major components of the system. However, IROC also recommends that routine replacement programs continue for system components whose service life is predictable.

Department Response: The Department agrees with this recommendation.

The Department has implemented a robust condition assessment program for water and wastewater infrastructure, which includes pipelines. The results of these assessments, along with forecasted demands and operational data, are used to determine future capital improvements and needs. The Department has a 10-year CIP model in place to identify and prioritize capital assets and financial tools to successfully carry out the Department's mission to provide a reliable service at the lowest cost possible, and in an environmentally responsible manner. Furthermore, the Department is in the process of implementing a user friendly SAP Enterprise Asset Management System.

2. That the Department continue to implement the improvements to the CIP process and provide appropriate management-level information in a way that will facilitate project visibility and enable appropriate IROC oversight.

Department Response: The Department agrees with this recommendation.

The Department agrees to continue to provide the Infrastructure & Operations Subcommittee with quarterly CIP progress reports and the end of the year CIP accomplishment report to full IROC. These reports will provide IROC with dashboard information on program performance, which includes fiscal year expenditures and mileage goals.

3. That the City and the region continue their investment in developing secure sources of water and water storage as well as encouraging a sustained culture of water efficiency and conservation. IROC also encourages the City to develop a clear policy and regulations to guide the City Council and Mayor in making decisions to implement voluntary water use reductions, mandatory reductions, and enforcement for use reductions when they are needed.

Department Response: The Department partially agrees with this recommendation.

The Department regularly assesses long-term water supply needs, taking into account its conservation initiatives and the state imposed water conservation mandate. These assessments are conducted in consultation with regional partners to ensure consistency and validity. The Department is also actively working to develop an adaptive strategy with decision criteria to guide the City Council and Mayor in making decisions to implement voluntary water use reductions or mandatory reductions, if needed, quickly and decisively.

4. That the Department review its Long Range Water Demand Forecast and update, as appropriate, to reflect the lower future demand projects contained in the 2015 UWMP.

Department Response: The Department agrees with this recommendation.

The Department updates its Long-Range Water Demand Forecast to reflect the best available and validated projections that are used to develop its Urban Water Management Plan (UWMP). As the Department updates the 2015 UWMP (submitted to in 2016 in accordance with DWR requirements), the Department will review the Long-Range Water Demand Forecasts accordingly.

5. IROC has no recommendations at this time, but could after hearing the latest results of the optimization studies at an upcoming Subcommittee meeting. IROC requests periodic updates from the Department until the project is completed.

Department Response: The Department agrees to this recommendation.

The Department will continue to provide the Subcommittee with periodic updates on the operation optimization studies until the project is complete. The anticipated project completion date is May 2017; at that time the department will report the final results of the optimization study to the subcommittee.

Outreach & Communications Subcommittee:

1. Near the end of the fiscal year, the Department announced changes to the program and schedule, accelerating implementation and favoring delivery of Pure Water to Miramar reservoir rather than San Vicente Reservoir. The Department needs to better explain these changes, reasons for the changes and cash flows and overall cost impacts to the public, community leaders and IROC. Also, the Department should enhance public understanding of the costs and benefits of the water and wastewater system, through consistent information and messaging, under a clear, compelling, value statement (e.g., “San Diego Water: Pure Value”).

Department Response: The Department agrees with this recommendation.

Following a thorough alternative analysis that extended over a 12-month period, the Miramar Reservoir Alternative was determined to be superior to the San Vicente Reservoir Alternative for the following reasons:

- Program Environmental Impact Report (PEIR) concluded Miramar Reservoir to be environmentally superior, resulting in less impacts to sensitive habitats and wetlands, and less energy requirements and associated greenhouse gas (GHG) emissions;
- Includes two additional treatment processes that result in enhanced treatment reliability and water quality;
- Provides greater long-term operational flexibility of the City of San Diego water system, with a greater ability to optimize the use of water stored in local reservoirs;
- Involves less schedule and delivery risks, including land acquisition and permitting requirements;
- Minimizes impacts on the surrounding communities; and
- Provides the required protection of public health and ocean environment, and is estimated to be about \$50M less costly over the life of the infrastructure.

Additionally, the Department is developing a comprehensive outreach campaign specifically designed to provide the general public, customers, stakeholders and elected officials with relevant messaging for all service lines of the Public Utilities Department. The purpose of this new campaign is to increase public awareness of water and wastewater activities and better align their perception of value to the services we provide. We expect the new campaign to kick off in Fiscal Year 2017.

2. The Pure Water San Diego Program represents one of the largest investments ever made by the Department. As such, it needs greater visibility at IROC. IROC recommends that reporting of the Pure Water budget, schedule, progress and other key elements of the program be separated out from reporting of other departmental programs to IROC so that better tracking of the program can be done. IROC understands that reports on the program are regularly made to the Pure Water Technical Advisory Committee; these reports should also be provided to IROC and could serve as a beginning template for improved reporting to the full IROC.

Department Response: The Department agrees with this recommendation.

The Department will provide an annual report by December 31 of each year. The report will describe Pure Water progress and accomplishments for the preceding year and will be distributed to IROC as well as the Metro JPA and environmental stakeholders who are party to the 2014 Cooperative Agreement.

3. That the Department continue to strengthen the “Water Conservation” campaign program messaging in order to sustain its effectiveness (despite improved water conditions) and report back to IROC the results of all water conservation efforts and programs.

Department Response: The Department partially agrees with this recommendation.

The Department continues to promote water conservation as an important way of life for its customers through a proactive and robust public outreach effort. The Department has developed a scalable campaign that is adaptive to changes in both the hydrology and the regulatory arenas and serves the customers well. Artificially elevating the calls for conservation can result in customer apathy or worse, antithesis. Striking the correct balance in our message is of paramount importance to retain credibility with our customers, stakeholders and the public at large. Updates on water conservation will continue and will be aligned to the updates we provide to the Environment Committee.

4. That the Department continue to monitor and report back to IROC CCS system wait and response times and continuing efforts for improvement. In many cases the CCS is the only contact that residents have with the department. Resolving issues promptly and fairly will help create a favorable impression of both the City and the Department.

Department Response: The Department agrees with this recommendation.

The Department continues to monitor the CCS system to ensure excellence in customer service.

5. That the Department evaluate methods to incentivize existing owners of multifamily buildings to encourage sub-metering of individual units. Along with this, as part of its ongoing examination of the water rate structure, new tiered water rates for multifamily units with sub-meters should also be examined in order for residents in these units to take advantage of the lower tier water rates available to single family units when conservation measures are taken.

Department Response: The Department disagrees with this recommendation.

Both the City’s Municipal Code and now State law have established requirements for the installation and administration of water sub-meters for new or significantly remodeled multifamily dwellings. Additionally, these laws also provide authority for existing multifamily dwellings to convert and administer a sub-meter program. In doing so, an incentive is inherent in that property owners can establish a way for their tenants to pay for the water instead of the utility being assumed in the rent and reducing the net benefit for the property owner. With limited funding available for water saving incentives, the Department does not believe subsidies or financial incentives for property owners to install sub-meters is the best and highest use of scarce resources.