
Timing of Rate Changes

April 1, 2009
Board Meeting

Two Potential CWA Rate Changes

- CWA Annual Increase - Sept. 1st
 - Typically January 1st
 - Regardless of when Otay would implement a rate increase, a full 218 process would be required
 - There is sufficient time to implement on Sept. 1st

- CWA Drought Penalty Pricing - July 1st
 - 218 process completed – prepared to implement
 - Staff is evaluating a recommended implementation date
 - There is time to notify customers and implement on July 1st

Timing of Increases

- Annual Rate Increases:

It is important for the District to match the timing of CWA rate increases in order to maintain the debt coverage ratio without causing dramatic fluctuations in rates.

- Drought Rates Implementation:

The recommended timing of the drought rates is being evaluated. The analysis must consider the following:

1. Administrative factors
 2. Customer education
 3. Over allotment penalties with the declaration of Drought Stage II
 4. Financial risk assessment
 - Impact on cash flow and budget fluctuations
 - Impact on debt coverage ratios
 5. Greater uncertainty of projected water sales
 - Economic pressures
 - Effectiveness of drought messages
 - Impact of significant rate increases on purchases
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1. Administrative Factors

Early Implementation – Two separate increases

- Consistent timing with the underlying events
- Early information on customer reaction to rate changes
- Added implementation cost and effort
- Two rate increases in a short period of time creates:
 - Training difficulties
 - Difficult historical analysis due to 3 sets of rates in a short period of time
- Adds cost to the customer notification process

Delayed Implementation – One combined rate increase

- Complicated 218 notice

2. Customer Education

Early implementation – Two separate increases

- Keeps increases distinct yet may generate questions
- More consistent with media coverage
- Earlier price signal motivates greater conservation
- Questions will be asked why there are back to back increases

Delayed Implementation – One combined rate increase

- Perception of higher increase
- Allows added time for media coverage and customer acceptance
- Gives customers added time to alter water use habits

3. Over Allotment Penalties

- Otay Penalty = 2 x Tier II water rate (approx \$1,700/aft) x Otay's share of CWA's overage.
 - Approximately 3 times more than water purchased under the allotment level
 - Only if Otay exceeds its allotment and
 - Only if CWA exceeds its allotment

- Two components:
 - Allotments – To be set shortly
 - Sales Projections – Currently being evaluated

4. Financial Risk Assessment

- Cash Flow Risk – Budget Fluctuations
 - The District has always maintained healthy reserves which protect it from the cash flow risk caused by budget fluctuations.
 - While drought rates provide added flexibility they are not essential to manage cash flow risk.

- Financial Bond Covenants
 - Maintenance of the debt coverage ratio, on the other hand, due to the method of calculation cannot rely on reserves leaving:
 - Penalty pricing – creates a significant uncertainty in the debt coverage ratio
 - Drought rates – key flexibility to modify rates and manage uncertainty
 - Accurate setting of rates – is also key to limiting uncertainty

Penalty Price Impact on Debt Coverage Ratio

■ Historically

- The debt coverage ratio was relatively insensitive to variations from sales projections:
- Water sales > Budget = greater than expected debt coverage ratio
- Water sales < Budget = modestly lower debt coverage ratio due to the reduced purchase cost of water.

■ Prospectively

- The impact of selling less than expected remains modest and unchanged.
- However, with the introduction of an allotment, the impact of selling more than the allotment is substantial.
 - Accurate budgeting to project penalties is essential
 - Monitoring sales to budget is essential
 - Use of drought pricing may be key to managing this new reality