MINUTES OF THE
SPECIAL MEETING OF THE
BOARD OF DIRECTORS
OTAY WATER DISTRICT
March 18, 2013

1. The meeting was called to order by President Lopez at 3:31 p.m.

2. ROLL CALL

Directors Present: Gonzalez, Lopez, Robak and Thompson

Directors Absent: Croucher (due to a work commitment)

Staff Present: General Manager Mark Watton, Attorney Richard Romero, Chief of Information Technology Geoff Stevens, Chief Financial Officer Joe Beachem, Chief of Engineering Rod Posada, Chief of Administration Rom Sarno, District Secretary Susan Cruz and others per attached list.

3. PLEDGE OF ALLEGIANCE

4. APPROVAL OF AGENDA

A motion was made by Director Robak, seconded by Director Thompson and carried with the following vote:

Ayes:	Directors Gonzalez, Lopez, Robak and Thompson
Noes:	None
Abstain:	None
Absent:	Director Croucher

to approve the agenda.

5. PUBLIC PARTICIPATION – OPPORTUNITY FOR MEMBERS OF THE PUBLIC TO SPEAK TO THE BOARD ON ANY SUBJECT MATTER WITHIN THE BOARD'S JURISDICTION BUT NOT AN ITEM ON TODAY'S AGENDA

No one wished to be heard.

WORKSHOP

6. DISCUSSION OF RATE STUDY FINDINGS AND A REQUEST TO DIRECT STAFF TO INCORPORATE THE FINDINGS OF THE STUDY INTO THE FISCAL YEAR 2014 RATE MODEL AND BUDGET

Finance Manager Rita Bell indicated that staff is pleased to present the findings of the District's water and sewer rate study. The purpose of a rate study is to review the District's rate structure every three (3) to five (5) years due to changes in economic factors, price elasticity, and environmental and regulatory changes. The main purpose of the Rate Study is to maintain equity among the District's customer classes based on a Cost of Service Study (COSS), maintain financial stability, and encourage conservation utilizing a tiered rate structure for water and strength and a flow rate structure for sewer.

Ms. Karyn Keese, the District's Rate Study consultant, indicated that there are basically three steps to a Rate Study analysis:

1. Revenue Requirement Analysis: Determining how much of the District expenses must be funded by rates for both water and sewer.

2. Cost of Service Analysis: Allocating costs to the various customer classes based on costs that each customer class *causes* the District to incur (known as *Cost Causative*).

3. Rate Design Analysis: Determine rates based on the studies. The majority of the presentation will focus on this area.

Ms. Keese indicated that the following equation is utilized to determine the District's revenue requirements:

+ Operations and Maintenance Expenses
+ Transfer Payments from Reserve Funds
<u>+ Capital Projects Costs based on Rates</u>
= Total Revenue Requirement
<u>- Miscellaneous Revenues (1% property tax collection, cell site leases, etc.)</u>
= Net Revenue Requirement from Rates

She indicated that the cost allocation for water and sewer is very similar. Costs (fixed and variable) are allocated to the District's different customer classifications (Residential, Multi-family, Commercial/Government, etc.), which then determine the revenue requirement for each customer class. The only difference in allocation between water and sewer is, in sewer, the commodity related costs are broken further into what is referred to as "flow" (biochemical oxidant demand and suspended solids). Ms. Keese indicated that staff will first present the findings of

the Water Rate Study, which will then be followed by the findings of the Sewer Rate Study.

Finance Manager Bell provided a profile of the potable customers and indicated that the District has approximately:

- 48,000 potable customers
  - Majority of the potable customers (44,500) are single family residential with ¾" meters
- 802 multi-family residential with 18,500 dwelling units
- 1400 commercial/publicly owned accounts
- 1200 landscape accounts
- 100 temporary construction accounts

After reviewing the findings of the study, staff is recommended no changes to the following customer classes:

- Residential Attached
  - these customers will continued to be billed under the single-family residential rate structure
- Mixed use multi-residential and commercial
  - Continue to bill under current structure

Also, after reviewing the energy charge, it was found that the District's method of calculating the energy charge was fair and equitable. The energy fee is charged based on every 100 feet of lift and the assignment of zones and rate per lift are accurately assigned.

Ms. Bell presented the areas where changes are recommended:

- Meter Equivalencies
  - Assure that water system charges (system charges and MWD/CWA fixed charges) are utilizing AWWA hydraulic capacity factors which is industry standards
  - The District's capacity fees utilize this standard and the water system charges are being brought in-line with this standard
  - This is an equitable method as the larger metered customers (4" or 6" meters) will now pay a system fee to help pay for the maintenance of the increased water system capacity required by their larger meter.
  - AWWA has standards for each size of meter based on the gallons per minute flow through a 5/8" meter (capacity flow). The 5/8" meter equals "1" meter equivalency. A ¾" meter would equal "1.5" meter equivalency, 1" meter would equal "2.5" meter equivalency, etc. (reference slide number 12 in the attached presentation).
- Adjust Tiers and Break Points

  - Tiers were created to promote conservation. There are currently three (3) tiers for each customer class.
  - Historically, each customer classes' tiers are set so that a certain percentage of billed water flows through each tier. The District wishes to ensure that there is consistency among customer classes by using the same percentages throughout.
  - Staff wishes to retain tiers for commercial classes to allow the District to easily implement drought rates if necessary.
- Create Recycled Commercial Rate
- Update Fire Service Fee

Ms. Bell indicated that staff is recommending that the system fee for ¾" meters be reduced by $.55 and that the MWD/CWA fee be reduced by $.44. This will move Otay WD's bill for 14 units of water down from $73.72 to $72.73, making Otay WD the eighth lowest among the County water agencies. She noted that this is with no future rate increases.

She presented the current recommended tiers for potable water (reference slide number 15 in the attached presentation). She indicated that the District would like to set the break points where approximately 57% of the water billed in each customer class flows through tier I approximately 27% flows through tier II and 16% flows through tier III. The same break points will be set for recycled customers as well. It was indicated that this methodology is based on industry standard.

Currently, the District does not have recycled commercial customers, but is anticipating four (4) such customers in the near future:

- Power Plant requiring a 6" meter
- East Mesa Detention Facility requiring a 2" meter
  - They will be converting their irrigation, laundry and toilet flushing to recycled
- Quarry Operators
  - They are currently in the planning stages and their required meter size is unknown at this time.
- CCA (private prison) requiring a 4" meter

Staff is recommending that the District establish rates for these new customers now and include the new rates within the Proposition 218 notices to be mailed in the fall. As new customers, the District will not have consumption history on which to base their tier rate structure and staff is recommending that the District utilize the commercial potable tier rate structure until history can be established for their water use. Also, by setting their rates at 85% of the potable commercial rate, the District stays in compliance with its contract with CWA regarding recycled credits. It will also encourage the use of recycled water and ensure equity between the user classes as peeking factors for indoor use is much lower than peaking factors for irrigation use.

Ms. Bell reviewed the overall system fire capacity. She stated that the District must size its system to ensure that there is adequate capacity for fire protection system wide. This impacts the size of pipes that must be installed and storage capacity. Fire service capacity is paid by all customers through water rates.

She stated that there is another classification titled, “Private Fire Protection.” This is where a commercial or multi-family customer is required to have a private protection lateral. The lateral is installed by the builder. After installation, the customer is responsible for the maintenance of the backflow device and the fire service lateral after the backflow device. The District is required to maintain, repair and replace the lateral from the backflow device to the street. The private fire service protection fee is based on the cost of service of maintaining this section of the pipe and is recommended as follows:

- Up to a 3” meter the monthly service fee will be set at $21.14.
- For a 4” meter or larger, the monthly service fee will be set at $28.49.

This is a reduction from the current fee of $34.57 for all meter sizes. The proposed charges are a true-up following a review of the cost of service.

In response to an inquiry from Director Thompson, Ms. Bell indicated that the fee has dropped as the District has made a lot of improvements in backflow testing and meter reading which has provided efficiencies. Also, this particular fee had not been reviewed in some time and, up to this point, the fee was adjusted via an economic inflator. The cost of service study reviewed the actual cost today and a true up is being proposed to the actual cost to maintain, repair and service the private fire protection laterals.

Ms. Bell then presented the findings of the Rate Study for sewer services. She indicated that the services provided to Single-Family Residential makes up the largest portion of sewer revenue, with approximately $1.9 million collected. Multi-Family Residential is the second largest customer type with $358,656 collected. The remaining revenue of $426,936 is composed of low, medium, and high strength commercial customers, schools and churches.

She indicated that the sewer rate structure changes recommended are similar to the water services structure changes and are as follows:

- Adjust monthly fixed fees based on meter equivalency to match AWWA standards.
- Make both ¾” and 1” monthly fixed fees the same for Single-Family Residential.
- Base the system fee charge on meter size for Multi-Residential, rather than on per Dwelling Unit.

- Eliminate the ASU (Assigned Service Unit) calculation for Commercial customers.
- Update the strength factors to current State Water Resources Control Board standards for Commercial.
- Change the methodology for Churches and Schools to the same as that for Commercial customers.

Ms. Bell indicated that based on the Cost of Service Study for Single-Family customers, the District wishes to:

- Maintain the “low” strength per State Water Resources Control Board (SWRCB)
- Maintain 85% of this customers’ winter average for flow (January through April)
- Maintain cap of 30 units
- Make the monthly base fee for ¾” and 1” single-family accounts the same

With the above changes, the typical monthly bill increase for Single-Family customers will be $4.20 or 11.6% which is mainly due to more equitable allocations between customer classes. Staff indicated that the board may decide to “phase-in” the increase of the system fee, so the first year the increase in the monthly bill would be $2.97 or 8.2%, excluding the increase in the system fee. It was also noted that this is without the planned rate increase of 7.9% estimated last year for Fiscal Year 2014. She stated that with this increase, the District will be the sixth lowest cost sewer provider in the county with an average monthly cost of $36.15 for those customer utilizing approximately 14 units of water a month.

She indicated that for Multi-Residential customers, based on the Cost of Service Study, the staff recommends that the District:

- Maintain the “low” strength per SWRCB
- Maintain 85% of winter average for flow (January through April)
- Charge a system fee based on meter size, as per industry standards, instead of the number of dwelling units

By incorporating the above changes into the Multi-Residential rate, these customers will see a reduction in their monthly bill of 9.9% to 32.9% (please reference slide 32 of attached presentation).

Ms. Bell indicated that staff is recommending that the methodology for Commercial customers be updated to current industry standards:

- Eliminate the ASU (Assigned Service Unit) calculation for commercial accounts (removing the floor for low water users)
- Create a system fee based on water meter size

- Maintain 85% of their annual average water consumption for the usage charge
- Update sewer strength factor to the current State Water Resource Control Board factors
    - The District's low strength factor will stay at 1 as it matches current industry standard. Its medium strength will change from 1.3 to 2 and high strength will change from 3.2 to 4.

She presented charts showing the District's low and medium strength customers and indicated that the majority will see a decrease in their bills. However, those with larger meter sizes will see an increase in their bill as they will pick-up more of the cost to maintain the system due to their capacity requirements. She stated that all high strength customers' will see a decrease in their bills of between 10.7% and 45.1%.

Ms. Bell indicated that with regard to the School customer class, staff recommends the following changes:

- Eliminate the special formulas for schools and churches based on attendance
- Utilize the Industry Standard Method which uses the methodology for low strength commercial:
    - System fee based on meter size
    - 85% of average annual water consumption times their usage rate

With the above changes, schools will see a decrease in their sewer bill from 23.5% to 76.2% and one school will see a small decrease of .4%. In response to an inquiry from Director Thompson, Ms. Bell indicated that Valhalla High School had a large decrease of 76.2% as the formula for high schools is about twice the strength for elementary kids, thus, they had a very high strength factor. High Schools were being charged more because of the age of the students. The Industry Standard no longer utilizes that factor.

With regard to the Church customer class, staff recommends the following changes:

- The District has four (4) Churches in its sewer District and three (3) of the four (4) will see a decrease in their sewer bills of between 27.6% and 48.1% and one will see an increase of 151.3% (approximately $68.54).

Ms. Bell indicated under the new structures, the District would collect approximately an additional $206,424 annually from Single-Family sewer customers and collect decreases of:

- <$122,028> from Multi-Family Customers
- <$49,656> from Schools
- <$8,772> from Churches

- <$45,804> from Low Strength Customers
- <$12,685> from Medium Strength Customers
- <$23,556> from High Strength Customers

Ms. Bell indicated that if the District implemented the full proposed sewer rate increase, the typical Single-Family customer would see an increase of $4.20 or 11.6%. If the increase was phased in over two (2) years, the typical Single-Family customer would see a $2.97 or 8.2% increase in each of the two (2) years. In this approach, the bill for a Single-Family sewer customer utilizing 14 units of water a month would be approximately $39.12 a month and the District would rank the eighth lowest cost sewer provider within the County. If the board decides on phasing in the increase, it would be noticed in the Proposition 218 notices as a phase-in increase.

Staff is also proposing two (2) additional changes requiring a Proposition 218 hearing. Staff would like to detach and attach Improvement District (ID) 25 to ID 29; and ID 19 to ID 22 (she presented slides showing the location of IDs 19 and 25 [see attached copy of presentation]). She stated that the fees are identical in the IDs and, thus, there is no reason to retain IDs 25 or 19. A Proposition 218 hearing is required to make these changes and the elimination of the two (2) IDs will be included in the Proposition 218 notices.

Ms. Keese noted that the District's sewer rates have not been reviewed in over ten (10) years and is the reason for the many proposed changes. She stated that the rate structures that are currently in place were used widely during the time they were implemented. Staff is proposing changes that will be in line with today's industry standards.

Staff is asking that the board direct staff to incorporate the recommended changes into the Fiscal Year 2014 budget and Rate Model. These changes are revenue neutral and they bring our rate structure in compliance with industry standards. Staff is also requesting direction on whether the board would like to phase in the increase for the Residential Sewer System Fee or to implement the full increase in the first year of implementation.

Director Robak inquired how the encouragement of conservation was factored into the proposed rates. Chief Financial Officer Beachem indicated that the District's tiered rate structure has been implemented for all customer classes and is the District's best driver for conservation. Director Robak further inquired if the District has given any thought to those customers with larger lots who have implemented efficient landscaping, but are still paying the highest tier rate due to their landscape water use. Mr. Beachem indicated that this same issue came up a number of years ago and the board had indicated at the time that customers on larger lots will pay the higher water rate due to their consumption. It is a lifestyle choice. The District had discussed the option that these customers could purchase an irrigation meter which would allow them to purchase a larger amount of water in the middle tiers as

opposed to the highest tiers. However, these customers would need to pay the capacity fee for the meter. It was noted that if a customer already has a large meter and wishes to split the capacity and replace the larger meter with two smaller meters, then it would be considered “equivalent” and there would be no additional cost for the second meter.

In response to another inquiry from Director Robak, Mr. Beachem indicated that the last sewer increase was phased in over a three (3) year period from 2004 to 2006 with a 15% increase implemented in each year. Director Robak inquired if the now proposed sewer increase could be phased in over more years than just two (2). Mr. Beachem indicated that the two (2) year rate increase phase in will actually end up being a three (3) year process, because in the first year, the District will be under collecting and the general fund will cover the underfunding. In the second year, the District is collecting what should be collected, however, there is the deficit that was created and would need to be collected in the third year. The rate would need to be raised slightly higher to reimburse the general fund. Thus, a two (2) year phase in is actually a three (3) year phase in as we would need to reimburse the general fund. He also indicated that those customers who will be receiving a decrease in their billing will likely not be interested in getting a phase in of their reduced bill, they would like to receive it right away. Also, the general fund can cover the underfunding in the first year of the phase in of the residential sewer rate increase. So phasing in the sewer rate decreases is not required.

It was also noted that Proposition 26 made the Cost of Service issue much more clear. The District must charge customers their actual/true costs. If a decrease is phased in, then customers are charged more than their actual cost in the first year of implementation.

In response to an inquiry from Director Robak regarding the monitoring of sewer strength, Mr. Beachem indicated that staff will be presenting a staff report at the next board meeting which discusses staffs’ review of customers and sewer strength factors. Staff will be proposing that eleven (11) customers be reclassified. This process does not require a Proposition 218 hearing process as it is only reclassifying the customer’s by strength factors.

Director Robak also inquired if the District has looked at all the issues regarding water and sewer in terms of equity. Ms. Keese indicated that the District did review everything, including past rate studies. The District did not look at the private fire service cost as it was in-line with other agencies and did not address the equity issues regarding meter sizes. Staff has examined everything thoroughly and it is felt that they have covered everything in this study.

Director Thompson stated that he understands that the District wished to move its overall fee structure to a slightly higher fixed portion and slightly lower per unit portion. He inquired if this was correct. Ms. Keese indicated that staff reviewed doing so, but decided to maintain the 30% based on the Cost of Service Study.

Mr. Beachem further indicated that the benefit of a slightly higher fixed fee charge is it brings greater stability to the District's revenue sources, however, the offset is that the higher the fixed charge the less conservation is promoted. The District wishes to stay at 30% or below as it would impact the District's ability to receive grant funds from the State.

In response to another inquiry from Director Thompson, Ms. Keese indicated that the District looks at the Single-Family classification and determines their winter and summer usage distribution. The District then adds together Single-Family customers who utilize 0-5 units of water a month (conservation tier) to Tier I customers, it equals approximately 57% of total Single-Family customers. Twenty-one percent (21%) of Single-Family customers fall within Tier II and 16% in Tier III. She stated that you also want the same distribution among the District's other user classes. In looking at the Landscape/Agricultural/Construction class, none of the users were hitting the Tier III usage rates, so the consumption blocks were moved downward so that 57% of the customers fell in the first block (tier I), 27% fell in the second block (tier II) and 16% fell in the third block (tier III). You wish to have 10 to 15% of your users within tier III, top water users, to encourage conservation, but you do not want to see an excessive amount in this tier.

Director Thompson inquired about the rate differential between the Single-Family classification tiers. The breakdown is as follows:

Tier I	Usage of 1–5 units	$1.73 per unit (must use less than 10 units of water to receive this rate For the first 5 units of use)
	Usage of 6-10 units	$2.69 per unit
Tier II	Usage of 11-22 units	$3.50 per unit
Tier III	Usage 23+ units	$5.39 per unit

It was indicated that about 14% of users will be in the conservation tier (1-5 units), 14% in the highest penalty tier, and 42% will be in the Tier I use of 6-10 units and 26% in Tier II. This is based on winter average use (10 units or less), summer average use (22 units or less) and use of 23+ units falls within the penalty rate.

Director Thompson indicated, as we look towards conservation in the future, he would like to see a study on how much water would be saved if the rate break points were moved up or down. General Manager Watton indicated that such a study would fall more in line with price elasticity; what usage break points versus cost would encourage more conservation. A representative of the Bureau of Reclamation had presented on price elasticity at a board meeting last year and indicated that he would be doing additional studies on price elasticity. He stated that he would have more information on the price elasticity of water in approximately

one (1) year. It was discussed that it would be good to have the gentleman back to hear about his findings.

Director Thompson indicated that he strongly supported phasing in the sewer rate increase to soften the impact of the rate increase. It was discussed that staff would present that option to the board at the budget workshop. Chief Financial Officer Beachem indicated that staff is requesting that the board direct staff to incorporate the findings of the Cost of Service Study into the Rate Model.

In response to an inquiry from Director Gonzalez, it was indicated that if the sewer rate increase was not phased, the full increase would be $4.20 per month. If it were phased in over three (3) years, the increase would be $2.97 per month in the first year, $1.23 per month in the second year and the third year an additional monthly increase would be implemented to offset the deficit in the first year.

It was indicated that the use of five (5) units per month would equate to approximately 125 GPD in response to an inquiry from Director Robak. The EPA indicates that the average indoor water use is 400 GPD. The District's per capita water use is approximately 134 GPD which is already below its 20/20 State mandated per capita savings. The average monthly Single-Family Residential water use is 14 units per month. The median water use for the Single-Family customer is not far off the average water use per month.

Director Gonzalez stepped out at 5:00 p.m. and returned at 5:03 p.m.

Director Thompson observed with regard to the sewer charge for Multi-Residential, that the larger users' charges are going down substantially. He asked if staff could show how they determined how much they should decrease. Ms. Bell indicated that based on today's rate structure, those customers' with an average of 20 dwelling units (DU), their bill would be calculated as follows:

20 DU X $13.30 (Base Charge) + 84.7 units of water X $1.92 (Commodity Rate) to determine their monthly bill

Based on the Cost of Service Study, staff is proposing:

Fixed Charge of $97.24 plus 84.7 unit of water X $2.17 (Commodity Rate) to determine the customer's monthly bill.

The commodity rate is increasing because the fixed charges are going down. In the Cost of Service Study, a cost allocation of fixed costs was determined without going over 30%. Thirty percent (30%) of the District's fixed costs are allocated into the fixed charge and the remaining is allocated into the commodity charge. By putting more of the cost into the commodity charge, it would make the charges revenue neutral.

The $97.24 is determined similar to how the fixed charge is determined for water. It is based on meter count. By taking fixed costs and multiplying it times the meter equivalencies (reference slide number 12 of staffs' attached powerpoint presentation) where a 5/8" meter equals 1, ¾" meter equals 1.5, etc. Based on each of the District's sewer customers' meter size their meter equivalency is determined. The meter equivalency is divided into the fixed costs, which becomes a measure of one (1). The fixed costs are determined by looking at the budget (revenue requirements) and allocating costs between fixed and variable costs where fixed costs do not exceed 30% of the charges. Ms. Keese indicated that the breakdown of the allocations are in the Rate Model worksheet and staff would be happy to walk through the worksheet with members of the board.

Director Lopez inquired if a Proposition 218 hearing is required to consolidate IDs. It was indicated that it is required under the Proposition 218 requirements. It was noted that there will be no changes to the situation within the IDs and the consolidation would simplify the management of IDs.

A motion was made by Director Thompson, seconded by Director Gonzalez and carried with the following vote:

Ayes:	Directors Gonzalez, Lopez, Robak and Thompson
Noes:	None
Abstain:	None
Absent:	Director Croucher

to approve staffs' recommendation with a request to provide for the phase in of the sewer rate increase.

7. ADJOURNMENT

With no further business to come before the Board, President Lopez adjourned the meeting at 5:20 p.m.

_____
President

ATTEST:

_____
District Secretary