



## ● Proposed water rate alternatives

### Summary

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#### Background

At the January 9, 2012 budget and rates workshop, the Board raised several questions that will be addressed at the committee meeting and budget and rates workshop on February 13, 2012. In particular, the Board requested a discussion of two alternative rate proposals to the 7.5% and 5% rate increase proposal (Exhibit 1) that was recommended in the proposed budget for FY 2012/13 and FY 2013/14. The two alternatives requested were:

Alternative 1: Increase rates by 10% and 5% effective January 1, 2013 and 2014, respectively (Exhibit 2).

Alternative 2: Increase rates by 5% and 5% effective January 1, 2013 and 2014, respectively (Exhibit 3).

Each of these alternatives and related impacts are described below, and a full presentation will be provided at the February 13 committee meeting and board workshop.

#### Alternative 1: 10%/5% water rate increase

This alternative would increase rates by 10% on January 1, 2013 and by 5% on January 1, 2014, compared to the proposed increase of 7.5% and 5%. The higher rate increase of 10% would increase projected revenues by as much as \$34 million in FY 2013/14. This scenario increases Metropolitan's financial flexibility and improves coverage ratios in FY 2012/13 from 1.6 to 1.7. The increase in revenues could be used to increase reserve balances, improving Metropolitan's financial condition and ability to buffer ratepayers from future rate increases, if revenues are lower or expenditures are higher than budgeted. These increased revenues could also be used to increase funding for Other Post Employment Benefits (OPEB) or funding of PAYGO which would result in less debt being issued to finance capital projects.

#### Alternative 2: 5%/5% water rate increases

To lower the January 1, 2013 rate increase to 5% from the 7.5% as recommended in the proposed budget requires a reduction in expenses of \$15 million in FY 2012/13 and \$20 million in FY 2013/14. The following actions could be taken to make these necessary reductions:

Reduce Central Valley storage funding - Reduce funding for Central Valley storage by \$8.8 million and \$7.5 million in FY 2012/13 and FY 2013/14, respectively. This represents the reduced storage fees that could occur if the State Water Project allocation is 5% lower in each fiscal year. While Metropolitan's regional storage levels have improved in recent years, staff does not recommend this reduced funding level for storage as it reduces the flexibility to capture additional supplies as they become available in the next two fiscal years. In total, the current staff proposal represents the lowest Supply Program budget since FY 2003/04.

Reduce conservation funding - Reduce funding levels for conservation incentives by \$5 million in each of the next two fiscal years. Under this scenario, conservation funding would return to \$20 million per year, beginning in FY 2014/15 which may have some upward pressure on projected rate increases for FY 2014/15 and beyond. While the short-term reduction in the conservation budget reflects the recent trend in Metropolitan's conservation expenditures, it is not consistent with the long-term focus on improving water use efficiency throughout the region. As the economy rebounds in the coming years it will be important to maintain regional conservation programs that provide support for residents and businesses to pursue more efficient water use practices.

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In addition to the impacts noted above, the 5%/5% alternative results in reserves remaining at the minimum target level through 2017, and increases the likelihood that rate increases in later fiscal years will be greater than the projected increases of 3% .

### Recommendation

Staff continues to recommend proposed rate increases of 7.5% and 5% for January 2013 and January 2014, striking a good balance between the two alternatives shown above. In particular, the proposed rate increases maintain reserves slightly above the minimum level for the biennial budget period and reserves would continue to grow over the five-year planning horizon. The staff proposal also supports the Board's strategic objectives, including capturing surplus supplies in regional storage and continuing a long-term focus on water use efficiency throughout the region.

By contrast, Alternative 1 would result in much higher reserves that may be difficult to justify given the tight economic times, and Alternative 2 would only meet the minimum reserves and may result in higher rate increases in the later years of the five-year plan.

### **Attachments**

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Exhibit 1 – Proposed rate increase

Exhibit 2 – Alternative 1

Exhibit 3 – Alternative 2





