

November 13, 2015

(Amended November 15, 2015)

Hon. Terry Tornek
 Mayor, City of Pasadena
 100 N. Garfield Avenue
 Pasadena, CA 91109

Dear Mayor Tornek,

This letter provides my comments on the November 16, 2015 Agenda Report (Agenda Report) regarding Agenda Item 13: *Recommendation To Set The Date Of January 11, 2016 To Conduct A Public Hearing To Implement The Water System Capital Improvements Charge Formula Pursuant To Pasadena Municipal Code Chapter 13.20.035* that will be considered by the City Council (Council) on November 16, 2015.

The amount budgeted for CIC projects is vague and perhaps flawed. For purposes of my comments, I refer to the FY 2016-2020 budget document found at <http://cityofpasadena.net/WorkArea/DownloadAsset.aspx?id=8589941502> as the basis for determining which projects are "CIC Projects" (as opposed to "Non-CIC Projects") as follows:

	<u>FY 2016</u>	<u>FY 2017</u>	<u>FY 2018</u>	<u>FY 2019</u>	<u>FY 2020</u>
Total Budget	\$7,699,405	\$18,123,221	\$17,551,150	\$18,145,150	\$12,148,650
Non-CIC Budget					
Customer-driven Meters & Services (customer pays for service request)	\$930,000	\$1,200,000	\$1,200,000	\$1,200,000	\$1,200,000
Arroyo Spreading Basins & Intake Structures (Proposition 84 grant)	\$550,000	\$2,026,579	\$215,000	\$0	\$0
Non-Potable Water Project (financed separately)	\$0	\$1,000,000	\$1,000,000	\$1,000,000	\$1,000,000
Monk Hill Perchlorate Treatment Plant (federal funds)	\$0	\$500,000	\$200,000	\$450,000	\$500,000
Subtotal	\$1,480,000	\$4,726,579	\$2,615,000	\$2,650,000	\$2,700,000
CIC-funded Budget (Total Budget minus Non-CIC Budget)	\$6,219,405	\$13,396,642	\$14,936,150	\$15,495,150	\$9,448,650
Agenda Report Table A-1 (Total)	\$15,300,000	\$18,200,000	\$17,500,000	\$18,100,000	\$12,100,000
Agenda Report Table A-1 (CIC CapEx)	\$9,800,000	\$12,400,000	\$11,900,000	\$13,200,000	\$7,200,000

Correlation between the calculated Total Budget above with that shown in Table A-1 is good except for FY 2016 (the Table A-1 budget is twice as high). The correlation between the CIC-funded Budget with that shown in Table A-1 is weak with my calculated values being consistently higher in FY 2017-2020 (suggesting that there are more Non-CIC projects than I listed) but show the same discrepancies in FY 2016 (the Table A-1 budget of \$9.8 million is \$3.6 million higher). Given the importance of the estimate of Capital Costs to the calculation, a list of the Non-CIC projects should be provided and the significant FY 2016 discrepancy should be explained.

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The description of the language from the Water Rate Ordinance (WRO) regarding calculation of the Capital Improvement Charge (CIC) misrepresents the language in the ordinance. The language in the Agenda Report says:

Per the Water Rate Ordinance, Section 13.05.035(c), adjustments to the CIC shall be adjusted by the following calculation:

$$\text{Capital Improvement Charge} = \frac{((\text{Funding Target Ratio} \times \text{Capital Expenditure}) + \text{Debt Service})}{\text{Water Sales}}$$

Where:

- "Funding Target Ratio" is the ideal debt to equity (cash) funding ratio.
- "Capital Expenditure" is equal to the five-year average annual Water Fund capital expenditure.
- "Debt Service" is the five-year average annual CIC related debt service payment.
- "Water Sales" is the water system projected sales for the next twelve months.

The actual WRO language is as follows:

$$\text{CIC} = \frac{((\text{FTR} \times \text{CE}) + \text{DS})}{\text{WS}}$$

(expressed to the nearest \$0.00001 per hundred cubic feet)

Where: FTR ("Funding Target Ratio") = (A) / (A+B)

Where "A" is the five-year average annual cash required from current-year water rates to fund the CIP as projected by the Department at the time the CIC calculation is made.

Where "B" is the five-year average annual revenue bond funds required to fund the CIP as projected by the Department at the time the CIC calculation is made.

CE ("Capital Expenditure") is the five-year average annual Water Fund capital expenditure as projected by the Department at the time the CIC calculation is made."

The substantive difference is that the Agenda Report defines the terms "DS" and "WS" and does not include the language describing calculation of the Funding Target Ratio (FTR). The WRO also requires that the CIC be calculated to 5 decimal points. The Agenda Report definition of WS defies logic because, unlike all of the other variables in the calculation, the Agenda Report does not use a 5-year projection of water sales.

The establishment of the FTR does not conform to the WRO formula requirement. The Agenda Report says "While PWP normally plans on a cash Funding Target Ratio of 35% for capital investment, a ratio of 30% is recommended for FY2016 only" without explaining why the formula in the WRO is not used. As noted above, the WRO requires that the FTR be evaluated using the following formula (values used are from Table A-1):

$$\text{FTR} = \frac{\text{A}}{\text{A+B}} = \frac{\text{Pay-go CIC CapEx}}{\text{Pay-go CIC CapEx} + \text{Bond funded CIC CapEx}} = \frac{\$3,720,000}{\$3,720,000 + \$7,180,000} = 0.341 \text{ (34.1\%)}$$

Of course, the above calculation will change if the capital budget estimates discussed above change.

FY 2016 estimated sales used in the CIC calculation are flawed. The Agenda Report says (p. 5) that (emphasis added):

PWP's water sales are expected to decrease by 28% in FY 2016 due to PWP customers response to the State's mandate, and a reduced level of customer water usage is expected to be standard going forward based on the significant response to the call to conserve.

The proposed rate adjustment is based on unit sales for FY2016 of 9.6 million billing units, which reflects the annual water sales associated with meeting the 28% water conservation target.

There is no further discussion in the Agenda Report to substantiate the 9.6 million billing units (BU) estimate. More particularly, there is no discussion of the baseline year used to calculate the expected 28% reduction.

The State Water Resources Control Board (SWRCB) has established a regulation that requires a 28% reduction from June 1, 2013 through February 28, 2014 sales in the June 1, 2015 through February, 2016 period (the "State's Mandate" referred to in the Agenda Report). This suggests that it is reasonable to estimate Pasadena's FY 2016 sales by applying Pasadena's actual/projected reduction from FY 2014 sales to the actual sales in FY 2014.

The following demand data has been reported by Pasadena to the SWRCB:

Supplier Name	Stage Invoked	Mandatory Restrictions	Reporting Month	Total Monthly Potable Water Production 2014/2015	Total Monthly Potable Water Production 2013	Units
Pasadena City of	Level 1	Yes	May-15	2184.9	2860.1	AF
Pasadena City of	Level 1	Yes	Apr-15	2291.7	2701.6	AF
Pasadena City of	Level 1	Yes	Mar-15	2253.9	2361.4	AF
Pasadena City of	Level 1	Yes	Feb-15	1868.4	1783.9	AF
Pasadena City of	Level 1	Yes	Jan-15	1897.1	1999.3	AF
Pasadena City of	Level 1	Yes	Dec-14	1709.04	2183.8	AF
Pasadena City of	Level 1	Yes	Nov-14	2221.7	2522.49	AF
Pasadena City of	Level 1	Yes	Oct-14	2882.3	3035.5	AF
Pasadena City of	Level 1	Yes	Sep-14	3038.8	3351	AF
Pasadena City of	Level 1	Yes	Aug-14	3173.5	3534.2	AF
Pasadena City of	Level 1	Yes	Jul-14	3316.43	3475.43	AF
Pasadena City of	Level 1	Yes	Jun-14	3262.2	3240.7	AF

The SWRCB data can be downloaded at

http://www.waterboards.ca.gov/waterrights/water_issues/programs/drought/docs/uw_supplier_data070115.xlsx.

Pasadena has also reported that 2015 demands have been reduced from the SWRCB reporting period by 23%:



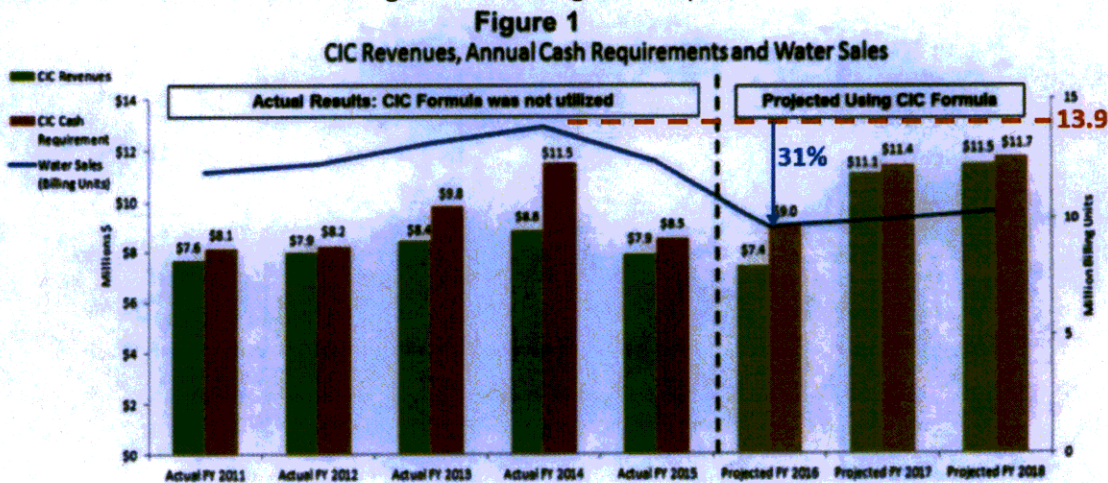
Taken together with the SWRCB data, the following table shows the derivation of FY 2016 sales:

FY 2014 Months	FY 2014 Actual (AF)	FY 2016		Aprox. Reduction required to Achieve 28%	Demand @ 9,600,000 BU	Aprox. Reduction @ 9,600,000 BU
		Sales with 23% Reduction (AF)	Demand required to Achieve 28%			
July 2013	3,475.43	2,676.08	2,676.08	-	2,676.08	-
August 2013	3,534.20	2,721.33	2,721.33	-	2,721.33	-
September 2013	3,351.00	2,580.27	2,580.27	-	2,580.27	-
October 2013	3,035.50	2,337.34	2,337.34	-	2,337.34	-
November 2013	2,522.49	1,942.32	1,942.32	-	1,942.32	-
December 2013	2,183.80	1,681.53	1,485.20	32.0%	1,362.69	37.6%
January 2014*	1,897.10	1,460.77	1,290.22	32.0%	1,183.79	37.6%
February 2014*	1,868.40	1,438.67	1,270.70	32.0%	1,165.88	37.6%
March 2014*	2,253.90	1,735.50	1,532.88	32.0%	1,406.43	37.6%
April 2014*	2,291.70	1,764.61	1,558.59	32.0%	1,430.02	37.6%
May 2014*	2,184.90	1,682.37	1,485.95	32.0%	1,363.38	37.6%
June 2014	3,262.20	2,511.89	2,218.62	32.0%	2,035.61	37.6%
Total AF	31,860.62	24,532.68	22,940		22,038.57	
Million billing Units	13.878	10.686	9.993		9.600000	

* 2015 sales are used as a proxy for 2014 sales

Observations from the above table:

- There is a very good correlation between the above projected FY 2014 demand of 13.878 million BU sales and the information from Figure 1 of the Agenda Report:



- The FY 2016 sales at 23% reduction from FY 2014 are expected to be 10.686 million BU
- To achieve the SWRCB 28% reduction goal, Pasadena sales in the remaining FY 2016 months would have to be reduced from FY 2014 sales by about 32%
- In order to achieve the 9.6 million BUs used in the Agenda Report for calculating the CIC, Pasadena sales in the remaining FY 2016 months would have to be reduced by about 38% from FY 2014 sales

This suggests that \$10.686 million billing units – and not \$9.6 million BU in the PWP reports – are likely to be sold in FY 2016 at a continued 23% conservation level. It also calls into question the assertion in the Agenda Report (p. 7) that "...on average customers are currently using 30% less water than in FY2014..." Even if staff maintained that 28% conservation from FY 2014 levels would be achieved in FY 2016, the above calculations show that would result in 10 million BU being sold.

The calculation of the CIC deserves a fresh look considering the above comments. The CIC calculation must be calculated to 5 decimal points and should use:

- Revised Capital Expenditures based on review of the budget projections
- An FTR that is calculated according to the WRO
- FY 2016 water sales of 10.686 million billing units and - along with modest projected increases shown in Table A-1 - use a 5-year average of sales

Thank you for the opportunity to comment and I would ask that you submit this letter for the record.

Ken Kules
Pasadena Resident (District 4)
3235 Lombardy Road

cc: Margaret McAustin
Chair, Municipal Services Committee

Andy Wilson
Member, Municipal Services Committee

Gene Masuda
Councilmember, District 4

Michael Beck
City Manager

(Transmitted by e-mail)