

RECOMMENDATIONS

Ad Hoc Citizens Advisory Committee

Yorba Linda Water District

Adopted May 4, 2017

INTRODUCTION

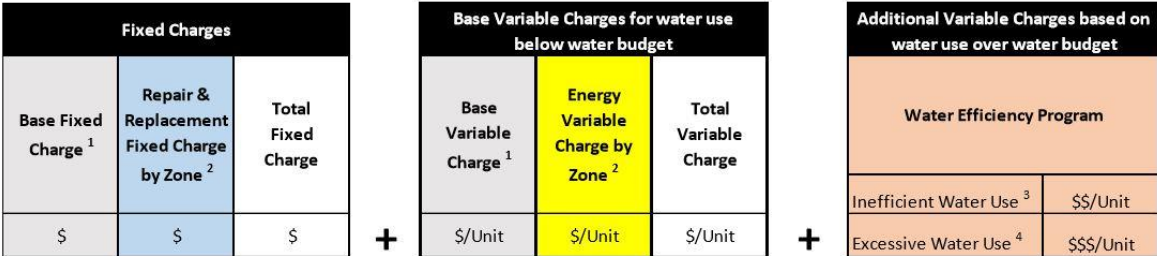
The Ad Hoc Citizens Advisory Committee was charged by the Board of Directors to provide recommendations regarding both the structure and sufficiency of water rates in the Yorba Linda Water District, and we are pleased to offer a set of recommendations here.

Our recommendations are intended to improve the YLWD rate structure by making it more financially stable, more resilient to changing circumstances, easier to understand, and more equitable, while providing the District with the rate revenues needed for the cost of service, including operations, maintenance, capital projects, and maintaining adequate financial reserves.

Our recommendations are intended to promote stability, water efficiency, transparency, and adherence to the letter and the spirit of governing laws. And our recommendations are intended to promote financial accountability to ratepayers through careful budgeting and reconciliation, including providing appropriate refunds to ratepayers.

RECOMMENDATIONS

1. Budget-based Rates



Note:

¹ Amount attributable to the fixed charge and the base variable charge to be determined by Board policy.
² Zones to be defined based on water pressure zones (i.e. Zone 675) to cover energy costs and R&R for that zone.
³ Inefficient water usage would be defined as the amount of water used over a parcels water budget, but less than excessive use.
⁴ Excessive water usage to be defined.

- (a) Explore budget-based water rates using the following proposed rate structure: (See diagram)
 - 1) Base fixed charge
 - 2) Variable water charge based on water budgets to be developed for each property according to land use type. Residential budgets to be based on indoor water use (people per household) and outdoor water use (area of landscaping)
 - 3) Zone-based energy variable charges
 - 4) Zone-based R&R fixed charges
- (b) Develop an appeal and variance system for ratepayers to dispute and resolve potential issues with calculated water budgets.
- (c) Organize a collaborative group of staff and citizens to assist with development and implementation of budget-based rates.

2. Near-Term Rates

- (a) In anticipation of a timely push to adopt tiered budget-based rates, and to avoid the costs of a rate study and Prop 218 analysis, and to avoid further confusion for rate-payers, we recommend no immediate change to the current base rate and commodity rates.
- (b) Until the new budget-based rates are adopted, rate revenue should be reviewed annually against cost-of-service and reconciled with the adopted budget and cash flow projections. Any surplus over-budget should be returned to the customer as a credit to the account. Any deficit should be balanced with the rate stabilization reserve.

3. Refund

- (a) We recommend that YLWD refund \$50-90 per connection in a reconciliation of the FY 2015-2016 budget. The refund should be proportional to the existing fixed fee structure.
- (b) We recommend a detailed public statement by the Board to explain the rationale behind this refund, to help restore the public trust and promote goodwill, to correct any prior misstatements, and to commit to new budget accountability processes moving forward.

4. Implementation and Education Program: Budget-based Rates

- (a) The Board should set a target date for implementing budget based rates. We suggest budget year FY2018/19, but not later than FY2020/21.
- (b) Organize a collaborative group of staff and citizens to assist with development and implementation of budget based rates.
- (c) Apply to SAWPA for available grant funds to defray the cost of developing budget based rates.
- (d) In anticipation of a timely push toward tiered budget-based rates, we recommend that the District begin design and preliminary implementation of a comprehensive rate-payer and water-consumer education and marketing program regarding important details and deadlines for the new rate structure implementation.
- (e) Issues to be addressed by the education program should include (but are not necessarily limited to):
- Values and reasoning behind the structural changes
 - Clear guidance as to what water budgets are and how they are set
 - Clear guidance for variances and appeals processes
 - Tools and resources for all types of users for meeting efficiency targets
 - Provide examples of rate impacts in advance (i.e. provide clear side-by-side sample bills to each customer)

5. Annual Cost of Service Review: Budget-based Rates

As part of the adoption of budget-based rate structure, the District should commit to an annual cost of service review to provide transparency and maintain flexibility, especially during the initial years of the new structure.

6. Administrative Penalties and Efficiency Program

(a) Efficiency Program

(1) In anticipation of a timely push toward tiered budget-based rates, and in anticipation of new permanent state water efficiency standards, we recommend that the District begin a collaborative process for planning and budgeting a robust efficiency program to be funded by inefficient and wasteful tiers of the new rate structure.

(2) Dedicate the Conservation Reserve Fund (currently consisting of penalty funds already collected) to consist of surcharges from inefficient/abusive water sales in the tiered rate system.

(3) Operate the efficiency program's first year out of existing penalty funds in the reserve, while collecting surcharges from first year inefficient/abusive water sales. At the end of first year (and end of every year thereafter) recalculate inefficient/abusive surcharge based on actual program costs and actual past year sales.

(b) Administrative Penalties

As soon as possible, revise existing administrative penalty Ordinance 16-01 to:

(1) Take into account the equitable factors underlying water budget rates (i.e., size of household, size of irrigable area, etc.); and

(2) Explicitly change to a per diem water usage allowance to deal with the different billing period lengths (i.e., explicitly allow larger usage limits for billing periods that exceed 28 days).

7. Transparency: Capital and Repair/Replacement Budgets and Asset Management Plan

(a) For transparency, clearer and more frequent reporting of capital and repair/replacement expenditures is necessary to understand the nature and scope of capital work underway at the District at any given time. A statement on capital improvement and repair/replacement progress should be made available at least quarterly. The statement should clearly show capital expenses and transfers to and from reserves attributable to particular projects.

(b) Capital Improvement Budget – both long term and short term -- should be clearly and quantitatively reconciled annually to demonstrate progress and to anticipate shortfalls in funding for needed capital improvement projects. The capital improvement budget should identify the sources and amounts earmarked to fund each project, i.e. reserves, developer payments, grants, other agencies, etc.

(c) Repair/Replacement Budget - A detailed annual optimized R&R budget should be established and tracked and reported separately from the capital improvement budget. The R&R budget should be reviewed and evaluated annually in comparison with similarly situated water districts, budgets, actuals, and problem areas. The review should be formal and public and transparent.

(d) The Asset Management Plan should be updated as soon as possible, and the District's performance under the previous plan should be evaluated for accuracy of assumptions and projections. The Asset Management Plan should accomplish the following:

- Determine the current replacement cost of all District infrastructure assets
- Calculate the current annual depreciation amount of all infrastructure assets based on expected useful life and straight-line depreciation
- Determine the current backlog of repair/replacement work needed based on expected useful life and straight-line depreciation (The total replacement cost of those assets beyond their expected useful life.)
- Establish a recommended annual repair and replacement schedule incorporating the District's "ugly list" of priority replacement projects
- Recommend a time period and annual optimized budget for catching up on the backlog
- Provide a digital model (i.e. Microsoft Excel) for District staff to update the Asset Management Plan as repair and replacement work is completed and capital improvements are added, no less frequently than quarterly.

8. Transparency: Reserves

(a) The District should deliver clearer and more regular public reporting of reserve balances and line item detail in each reserve category consistent with the reserve policy. In particular, expenditures from an "emergency" reserve should be more clearly attributable to a particular emergency; expenditures from the capital reserve should be more clearly attributable to a particular capital project.

(b) Repair/Replacement Reserves should be reported separately from Capital Improvement Reserves, which are reserves for new construction or upgrades to existing infrastructure.

(c) We believe that the District's current levels of reserves are more than ample to meet the District's current service commitments. In setting future reserve levels, the District should (1) avoid overlap of reserve categories, and (2) consider the District's ability to rely on non-cash reserves such as committed line of credit, property sale-leaseback, etc.

9. Transparency: Financial Reporting

(a) Monthly financial reports should be published on a stand alone basis on the district's website in a way that is easy to find and access (versus the current method of only publishing monthly reports as agenda attachments). The website location should include the most recent as well as historical reports.

(b) A monthly update of the forecasted year end net position compared to the original budgeted year end net position should be added to the monthly budgets to actuals report.

(c) There should be a single monthly report that shows a summary balance sheet portrayal of the district's financial position. This report should list each reserve, debt, and overall cash on hand. Currently, disparate reports have to be viewed to see these items.

10. Strategic Planning

- (a) The District should plan and budget for an update (or complete re-write) of its comprehensive master plan / strategic plan documents.
- (b) The plan should be developed collaboratively with stakeholders (including rate-payers).
- (c) The plan should reflect new realities for efficiency standards, budget-based rates, advanced meters, and modern communications strategies.

11. Low Income / Fixed Income Rate Assistance Study

Due to the short timeframe for the ad hoc committee, we were unable to study rate assistance programs for low income and fixed income rate-payers. We recommend that the District review such programs in other water districts, and evaluate the legality of and need for a similar program in this district, including budget and source-of-funding recommendations.

12. Transparency: Metrics and Benchmarks

Our District: 1) is not subject to state federal or local income or property taxes; 2) receives a tax substantial tax subsidy (over \$1.5 million in FY2016); and 3) neither pays a dividend to its owners nor otherwise provides owners with capital appreciation. There appears to be consensus among customers in general and YLWD that YLWD should remain an independent water agency. To remain independent and avoid takeover, the District must be demonstrably efficient. The rates charged must be compared to other water suppliers taking into account the three advantages listed above and a comparison of operational metrics should be made to demonstrate competitiveness of those rates.

- a) The committee recommends that the Board of Directors formally adopt a set of ratios (management metrics and benchmarks) to be used to gauge district performance. The definition of the denominators and numerators of such metrics should cite specific line items from financial statements, budgets and forecasts, and might include the following:

Numerators: Cash & Short-term investments; unrestricted reserves; restricted reserves; total revenue; operating revenue; total costs; operating costs; District area (acres); District population; salaries and benefits cost; supplies and services costs; variable costs; debt, interest expense and others.

Denominators: miles of mains; asset net book value; asset replacement cost; number of employees; and others.

Other metrics that can be used are debt service coverage; interest coverage; debt.

Comparisons can be made between budget and actual; current year forecast to next year budget; Current year actual to next year budget; as well as to other water suppliers. Comparisons might also be made over multi-year periods to see trends.

b) To assure comparisons of different periods are meaningful, a well-defined methodology of financial budgeting and forecasting must be adopted and adhered to.

13. Staffing Review

(a) The District should consider a comprehensive review of staffing needs and organizational structure. In particular, the District should consider eliminating long-vacant positions, rebalancing workloads, and to minimize overtime. In addition, salaries and benefits should be reviewed for competitiveness in the current regional market, with an eye on uncontrolled liabilities to the District.

14. Professional Services Costs and In-House Planning

(a) To the extent that outside consultants and professional service are necessary to complete planning and engineering documents and rate studies (et cetera), significant contracts must be competitively bid, or the Board must specifically grant a waiver or exception. New qualified providers should be identified. Related documents should be more readily available on the website.

(b) The District should consider, when appropriate and cost-effective, adding permanent in-house planning and engineering staff in an effort to avoid and minimize professional services contracting costs, and to provide oversight of professional services contracting.