



City of Sunnyvale

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REPORT TO COUNCIL

SUBJECT

Proposed Utility Rate Increases for FY 2015/16 Rates of 20% for Water, 8% for Wastewater, and 5% for Solid Waste Utilities for Services Provided to Customers Within and Outside City Boundaries; Finding of CEQA Exemption Pursuant to CEQA Guideline 15273

REPORT IN BRIEF

As part of the yearly process of reviewing the financial condition of the utility enterprise funds, staff recommends that the City Council adopt changes in utility rates. This report presents an analysis of the current utility policy framework, revenues, expenditures, revenue requirements and utility rates for the City's water, wastewater, and solid waste utilities.

Individual rates and monthly bills may vary. However, as a whole, the recommended increases are as follows: 20% increase in water rates, an 8% increase in wastewater rates, and a 5% increase in solid waste and recycling rates. These increases will result in the average single-family residential monthly bill going up by:

Water	\$9.89
Wastewater	\$2.94
<u>Solid Waste and Recycling</u>	<u>\$1.52</u>
Total	\$14.35

The new total average monthly bill will be \$143.23, an increase of approximately 11.1% over the current year. The City's commercial rates will increase by the same overall percentage as residential rates. Detailed single-family rate comparisons are included as Attachment 1 and commercial rate comparisons are provided as Attachment 2. It is important to note that different cities fund different suites of services with their utility fees so care must be taken in comparing them.

The proposed rate increases are included in the FY 2015/16 Recommended Budget that is currently being reviewed by the City Council. Each year, staff provides Council with not only proposed rates, but also planned changes in rates over twenty years. The proposed increase in water rates is 15% higher than previously planned. This increase is necessary to cover sharply rising wholesale water costs and declining revenues due to the current drought, as well as significant rehabilitation costs for water infrastructure. The proposed increase in wastewater rates is the same as previously planned, and is necessary to cover needed infrastructure and capital costs of the City's aging wastewater treatment plant and collection system. The proposed solid waste rate increase is the same as previously planned, and is largely to cover the cost of implementing the City's Zero Waste policy.

The City's two wholesale water providers recently finalized their rate increases, which are less than originally proposed. As a result, the proposed water rate increase of 20% can be reduced by up to

2%. Alternatively, the savings can be applied to the rate stabilization reserve, which would provide additional stabilization to the Water Fund during a time of drought. Regardless of which scenario Council adopts, rate increases have been noticed so that any additional rate increases brought forward by the wholesalers during the fiscal year could be passed on to Sunnyvale water customers in addition to the recommended rate increase.

BACKGROUND

Sunnyvale utility rates are based entirely on the City's costs for operating and maintaining its water, wastewater, and solid waste facilities and services. Each of the utilities is operated as an independent enterprise, and all expenses and revenues for each service are accounted for separately from other funds. In fact, state law requires that all fees collected by each utility be used within that utility and are not allowed to be used for unrelated services.

Each year, as part of the budget process, staff analyzes the current condition of, and long term outlook for, all of the City's utility funds. These analyses are reflected in the Long-Term Financial Plans for each fund. They include a review of available fund balances, state and federal environmental requirements, revenues, anticipated capital, infrastructure and operational requirements, and a detailed inspection of significant expenditure areas (e.g. the anticipated cost of purchased water, environmental regulations related to wastewater discharge, the cost of the City's solid waste collection contract with Bay Counties Waste Services, etc.). The results of these analyses lead to proposed adjustments to rates that will generate the revenues necessary to meet planned expenditures. It is important to note that the practice of long term planning and the use of a Rate Stabilization Reserve enable the City to maintain utility rates at stable levels while providing high quality, reliable, and efficient services by spreading the effects of anticipated operational, capital, and infrastructure costs over multiple years.

Public Noticing Requirements

Sunnyvale continues to comply with the noticing provision for utility rates as required by Proposition 218 and AB 1260. The notice of proposed utility rates was mailed on April 24, 2015.

Proposition 218 requires that should the Council receive written protests from a majority of customers, the proposed rates will not become effective and the current rates will remain in place.

Staff will tabulate protests received prior to the meeting, adding any valid written protests received at the meeting, and summarize the total number for Council. A majority of protests exists if approximately 15,700 valid written protests are received from the properties subject to the proposed fee. One vote will be counted for any property owner or utility customer who submits a protest prior to the end of the noticed public hearing (one protest per parcel). No protest received after that time, even if postmarked prior to that time, will be accepted. Each protest must be in writing and identify the affected property (by assessor's parcel number, street address or utility account number). Oral comments at the public hearing will not qualify as a formal protest unless accompanied by a written protest. Protests received from residents who are not either property owners or utility account holders with the City shall not be counted.

As of the preparation of this report, staff has received 38 protests. These fall primarily into three categories. Seventeen are protests that simply protest the rate increases. Eleven protests state that either rates are too high already or raising rates under the current economic conditions is unreasonable and that the City should lower costs instead. The third category of protests, of which

staff has received ten, base their objection on the protestor's low or fixed income.

EXISTING POLICY

Sunnyvale Municipal Code sections 12.16.020 (Wastewater), 12.24.010 (Water), and 8.16.120 (Solid Waste) authorize the City Council to establish by resolution fees and charges based on cost influencing factors.

Policy 7.11.1a.5 of the Council Policy Manual states "The user fees established for each utility will be reviewed annually and set at a level that will support the total costs of the utility, including direct and indirect costs and contributions to reserves set by Council policy."

ENVIRONMENTAL REVIEW

Public Resource Code Section 21080(b)(8) of the California Environmental Quality Act (CEQA) and CEQA Guideline 15273 provide that CEQA does not apply to the establishment, modification, structuring, or approval of rates, tolls, fares and other charges by public agencies which the public agency finds are for the purposes of (1) meeting operating expenses, including employee wage rates and fringe benefits; (2) purchasing or leasing supplies, equipment or materials; (3) meeting financial reserve needs and requirements; and (4) obtaining funds for capital projects necessary to maintain current service levels.

DISCUSSION

Water Rates

Water rates pay for the safe and reliable delivery of water to the majority of Sunnyvale residents and businesses. The Water Supply and Distribution Fund (Attachment 3) accounts for all revenues and expenses related to the City-operated water utility. Expenses include costs for wholesale water, capital and infrastructure project-related costs, debt service, and other operating costs. Revenues consist of service fees for water and recycled water, water-related public works and construction fees, and interest income. After expenditure levels are developed, water rates are set to collect enough revenue to maintain the fund in a sustainable financial position.

The largest component of the Water Fund's revenue requirement is the cost of purchasing water. As the region is currently experiencing a fourth year of drought conditions, there is greater volatility in both revenues and expenses as the City makes adjustments to manage the water shortage.

Sunnyvale currently receives water from four different sources. For FY 2015/16, approximately 49% of potable water deliveries are projected to come from the Hetch-Hetchy system operated by the San Francisco Public Utilities Commission (SFPUC), 49% from the Santa Clara Valley Water District (SCVWD), and 1% from well water. The remainder (less than 1%) comes from recycled water produced at the City's Water Pollution Control Plant (WPCP). The recycled water production system is currently being rebuilt. When fully operational, the recycled water system will be able to provide a larger percentage of the City's supply. Staff attempts to purchase water at the lowest possible cost. The City's system allows the movement of water from one portion of the City to another and staff monitors and adjusts purchases based on demand and the ability to utilize the most cost effective source, balanced with our minimum contractual requirements for purchases.

Residents and businesses in Sunnyvale have been cutting back on their water consumption. Water sales through March are down nearly 15% compared to FY 2013/14. It is anticipated that water conservation efforts will continue for the foreseeable future. As a result, it is not expected that

Sunnyvale will see its past level of water sales return, and projections have been updated to reflect this change. This overall reduction in demand has reached the point where the City is taking equal to or less than the contractual minimums required by both of the wholesale contracts. So far, the SFPUC and SCVWD have indicated that they will reduce contractual minimums for FY 2014/15 and FY 2015/16 because of the current drought conditions. However, as a practical matter, reduced demand has made the cost to buy water almost a fixed cost, where it used to be more variable. This largely fixed cost makes up a significant portion of the Water Fund’s expenditures at 58% of the budget for FY 2015/16.

Both the SFPUC and the SCVWD provided wholesale rate projections for the next ten years. Their projections have changed significantly over the previous year, as they expect to need additional revenue to make up for lost sales due to water conservation. These projections are in the base rate for the long term rate projections in the twenty-year financial plan. The table below reflects the proposed projections for both agencies.

Projected Increases in Base Wholesale Rates		
Fiscal Year	SFPUC	SCVWD
2015/16*	30.7%	31.5%
2016/17	0.0%	8.0%
2017/18	3.7%	7.8%
2018/19	15.9%	7.5%
2019/20	7.2%	6.2%
2020/21	0.0%	5.7%
2021/22	0.0%	5.2%
2022/23	2.0%	5.1%
2023/24	2.8%	4.9%
2024/25	1.2%	4.8%

*Actual rate increases adopted were 28% for SFPUC and 19.7% for SCVWD.

Based on the rate increases listed above, the anticipated cost of SFPUC Water for FY 2015/2016 was \$1,841 per acre foot per acre foot including meter charges and the BAWSCA debt service surcharge (or \$1,634 without), while SCVWD was expected to charge \$982 per acre foot. The proposed rates for both wholesalers were significantly higher than expected in the previous financial plan. The magnitude of these rate increases coupled with the reduced revenues from the drought cannot be absorbed in the rate assumptions included in the previous financial plan. Therefore, the proposed rate increase for FY 2015/16 increased significantly over the previous financial plan.

The City also receives charges from the SCVWD for pumping ground water from City wells. The unit cost for well water is also influenced by the power costs associated with running the pumps. The projected well water total unit cost (tax plus power) for FY 2015/16 is \$1,096 per acre foot, an increase of 27.7% over the current year unit cost of \$858.

After the City set its recommended budget and issued its utility rate notice, the SFPUC announced a reduction in the proposed FY 2015/16 rate increase from 30.7% to 28.0%, which results in a total cost of \$1,634 per acre foot. SCVWD also finalized lower rate increases than they originally expected

(from 31.5% to 19.7%), with their proposed charge dropping from \$982 per acre foot to \$894 per acre foot. Based on these lower rates, the costs for purchased water are anticipated to be approximately \$1.1 million less than budgeted for FY 2015/16.

This savings realized from the lower than expected increase could be used in two ways. First, it could be used to dial back on the plan's rate increases. If the total savings were used to reduce the rate increase for FY 2015/16, the increase could be lowered by 2%, which would amount to an 18 % water rate increase. This would reduce the typical single family resident's monthly bill by \$1.00 when compared to a 20% rate increase.

Alternatively, the additional money could strengthen the rate stabilization reserve to address the volatility of the City's water revenues. The current financial plan reflects a utilization of the rate stabilization reserves over the next few years to help manage and smooth in customer rate increases. The proposed FY 2015/16 financial plan anticipates a drawdown of reserves through FY 2019/20, down to approximately \$278,000 in FY 2019/20. Should current drought conditions persist into the next few years, the impact to the Water Fund and the rate stabilization reserve could be worse than currently projected. Another uncertainty in the short term is the impact of conservation efforts. Council recently approved over \$230,000 to fund conservation efforts to enforce the state mandated reductions in water use. Should the drought continue, the City may require additional funding to enforce these as well as new restrictions.

It is also important to note that, while not anticipated, it is possible that the wholesalers could adopt a mid-year rate increase as needed due to the drought conditions. Should that occur, a provision was included in the City's required Proposition 218 noticing that would allow the City to pass those costs on to customers. This provision is a pass-through charge, which will pass the higher cost of the water procured for the remainder of the year to the City's water customers. The formula to be used to calculate the surcharge, if needed, is as follows: Total expected cost increase for wholesale water purchases through the fiscal year end divided by the total budgeted expenditures for the purchase of wholesale water for the remainder of the fiscal year. The percentage increase determined by this calculation will be applied to utility bills as a surcharge for each unit of water used for the balance of the fiscal year (ending June 30, 2016). If the wholesalers do not implement any rate increases mid-year, no surcharge will be necessary. While this will prevent any negative impact to the Water Fund from potential mid-year increases, it could result in higher than anticipated utility charges for the City's water customers.

The City's Water Pollution Control Plant (WPCP) provides recycled water, which is wastewater that has been treated to very high standards. Recycled water is currently sold at 90% of water rates to encourage its use. Recycled water costs are funded jointly by the water and wastewater funds. In prior years, the City received a \$115 per acre foot rebate from SCVWD to encourage its use, but this ended in August 2009. Staff and SCVWD have ongoing discussions to partner in significant capital improvement projects that may bring recycled water to more areas of the City. One such project currently in the planning process is the expansion of the recycled water system along Wolfe Road to Homestead Road.

The City of Sunnyvale utilizes a tiered rate structure to encourage water conservation. On April 20, 2015, the fourth district appellate court issued a decision in a lawsuit against the City of San Juan Capistrano. In this case, San Juan Capistrano's tiered rate structure was deemed to violate Proposition 218 because of a failure to calculate the actual costs of service at each tier, and because

San Juan Capistrano did not demonstrate that the higher tiers did not exceed the proportional costs of providing service to each parcel. This decision is contrary to other recent rulings, and is expected to be disputed. It is not final as of this writing. A water cost of service study is scheduled for FY 2015/16, and the outcome of this case will be considered in the study.

Operations and Capital Expenses

The FY 2015/16 Budget for the Water Fund also includes approximately \$6 million in direct operating expenses, which is about 13% of total fund expenses. Of that total, personnel costs account for approximately \$4.2 million and other goods and services costs (e.g. water meters, valves, construction services, equipment costs, etc.) account for the remaining \$1.8 million. The Water Fund also contains annual debt service of approximately \$1.08 million primarily for payment of the City's 2010 Water Revenue Bonds. \$24 million in revenue bonds were issued in 2010 to refund the City's 2001 water and wastewater revenue bonds, as well as provide approximately \$18 million in new funding to address capital and infrastructure needs of the water utility.

Water infrastructure renovation is a major driver of water utility costs. The City has been addressing its aging water utility infrastructure for several years now. Like most municipalities in the state and the country, much of Sunnyvale's water storage and distribution system is over fifty years old and in need of significant rehabilitation. The highest priority has been placed on water pipe replacements. With approximately 350 miles of water lines, many in need of replacement, replacements have been accelerated, with almost \$70 million in replacements planned over the next twenty years. These pipe replacements must be done to minimize water service interruptions due to potential failures of the aging infrastructure. Other notable infrastructure projects include refurbishments of water tanks across the City, starting with the Mary-Carson tank in FY 2015/16, as well as the reconstruction of the Central Water Plant, which has been out of working order since 2007.

A renewed emphasis has been placed on the City's recycled water production and distribution system. Funding for this effort crosses both the water utility and the wastewater utility. \$2.1 million has been budgeted for Sunnyvale's share of a regional project that will include upgrades to the San Lucar Pump Station and extension of the recycled water system along Wolfe Road to Homestead Road. Sunnyvale has entered into a partnership agreement with SCVWD to fund this significant expansion of the recycled water system. This project will provide for the delivery of 0.74 million gallons per day of additional recycled water for use within the City of Sunnyvale and adjacent communities. The project will also serve the new Apple campus, and Apple has contributed funding to the project. The City and District also obtained a State grant for \$4 million for this project and the recycled water improvements at the WPCP.

As required by City policy, the Water Supply and Distribution Fund maintains a Contingency Reserve of 25% of operations and a Rate Stabilization Reserve to normalize rates and provide for the effect of economic cycles. This Fund also contains reserves for revenue funded projects and debt funded projects to manage the flow of these funds against project expenditures that are uneven by nature.

Recommended FY 2015/16 Water Rate Increase

The proposed Water Supply and Distribution Fund Long-Term Financial Plan (Attachment 3) reflects the recommendation that water charges increase by 20%. The projected rate increases anticipated over the remainder of the 20 years are shown at the bottom of the Water Supply and Distribution Fund Long Term Financial Plan. Due to wholesale water rate increases coming in less than planned, the rate increase can be reduced by up to 2%. Alternatively, the savings can be applied to the rate

stabilization reserve, which would provide additional stabilization to the Water Fund during a time of drought. Regardless of which scenario Council adopts, the rate notice sent to customers in accordance with Proposition 218 allows any unanticipated mid-year rate increases implemented by the wholesale water providers to be passed on to the City's water customers in addition to the recommended rate increase. Council may also elect to implement any rate lower than the staff recommendation of 20%. Any increase larger than the staff recommendation would be subject to additional Proposition 218 noticing. .

The detailed Water Rate Survey is presented as Attachment 4. Attachment 1 shows monthly residential utility bill comparisons. The City's residential water rate remains competitive when compared with neighboring cities.

Wastewater Rates

The City owns and operates an extensive system for management of wastewater within City limits and in a small area in northern Cupertino and San Jose. Wastewater rates pay for the safe and reliable removal and treatment of wastewater from all residences and businesses in Sunnyvale and in the area serviced outside the City. Wastewater rates also pay for storm water management, non-point source pollution prevention and other critical public services. The Wastewater Management Fund (Attachment 5) accounts for the revenues and expenses related to the City-operated wastewater collection and Water Pollution Control Plant services.

The system includes approximately 290 miles of sewer pipes, a storm drainage system, and a 29.5 million gallon per day (MGD design capacity) Grade V Water Pollution Control Plant (WPCP). Operations include the transport of sewage to the treatment plant, wastewater treatment, recycled water production, industrial discharge inspection and enforcement, and many other services related to wastewater. It is important to note that the Grade V classification of the City's WPCP is the highest grade, and that the discharge requirements for Sunnyvale are among the most stringent anywhere due to the ecological sensitivity of the South San Francisco Bay.

Operations and Project Expenses

The proposed FY 2015/16 operations expense in the Wastewater Management Fund reflects personnel, chemicals, and other costs. Additionally, the City's street sweeping program is funded equally by the Wastewater and Solid Waste Funds to reflect the benefits that street sweeping provides in clearing litter and debris off the streets and preventing that debris from entering the storm drainage system.

The wastewater utility is facing even larger infrastructure challenges than the water utility. The most significant is the renovation of the City's WPCP. The recommended FY 2015/16 Budget includes planned infrastructure expenditures of approximately \$442 million over twenty years, with \$316 million (or 73%) allocated to the WPCP renovation project. With the completion of the Plant Master Plan this summer, the costs and schedule will be updated. And, parallel planning is in progress should the Water District ultimately decide to move forward with the projects designed to utilize WPCP effluent for potable reuse.

The most significant of the WPCP renovation projects to date is approximately \$116 million to design and construct new primary treatment facilities. This includes a new head works facility, which removes large debris from incoming sewage and pumps the sewage into new primary treatment tanks which, in turn, slow down the wastewater to settle out large solids. The current influent sewage

pump station has reached the end of its useful life and the gas-powered influent engines will be non-compliant with air regulations effective January 2016. The City anticipates building the new head works and primary facilities at the current bio-solids drying operation location, adjacent to the current influent pump station. As a result, this project displaces the current bio-solids drying operations and will likely require alternate operation (such as vendor contracted drying operations) until new bio-solids facilities are constructed.

Additional WPCP renovation projects include \$28 million for Program Management Services and \$5.8 million for the completion of the WPCP Master Plan. These projects will fund the identification of future secondary and tertiary treatment processes, the development of conceptual designs for future projects within the reconstruction program, the preparation of the programmatic environmental impact report, and oversight of the implementation of the reconstruction program over the next 12 years.

Work also continues on certain critical projects which were previously identified as necessary in the short-term to address the most advanced areas of deterioration and are in increasing danger for failure. These projects fall primarily into two categories 1) projects in which technology has not changed significantly since they were originally built and will therefore become part of the new plant, and 2) projects that address infrastructure that may be replaced with different technology or processes, but that will not last the interim period and therefore must be repaired or replaced. Examples include a project to replace the gaseous chlorine disinfection system with a much safer liquid hypochlorite system and the rehabilitation of the WPCP's digester facilities. These critical projects should wrap up in the next year as the WPCP renovation projects get under way.

In addition to the work on the WPCP, a high priority has been placed on sewer and storm pipe and facility replacements. The wastewater collection system consists of approximately 613 miles of sewer and storm mains, and seven pump or lift stations. The system has five major sewer trunk lines that terminate at the WPCP where sewage is treated.

The City's wastewater collection systems are in need of significant rehabilitation due to their age. The recommended FY 2015/16 Budget includes approximately \$41 million in projects related to sewer and storm water. Major projects include \$22 million for sewer and storm pipe improvements, \$6.4 million for rehabilitation of the Lawrence Expressway trunk line, and \$4.6 million for sewer and storm pump and lift station rebuilds.

There is over \$2.8 million in the proposed budget for new projects to address stormwater concerns. The City stormwater system operates under the terms of a Municipal Stormwater National Pollutant Discharge Elimination System (NPDES) permit. These projects would implement trash reduction programs and other maintenance activities in order to meet permit requirements. The funds will provide additional street sweeping in the City, provide outreach and enforcement efforts, and fund retrofit projects that would redirect stormwater to biotreatment areas.

The debt service payments are largely for the Wastewater Revenue Bonds, issued in 2010 for \$35 million to refund the existing bonds and provide \$22.5 million in new funds for capital and infrastructure projects. As discussed earlier, some of the bond proceeds are funding the initial efforts for the renovation of the WPCP. As a placeholder, future debt has been reflected with debt service payments noted in the *New WPCP Debt Service* line item. The actual amount and structuring of the financing will be determined as the plan is further defined. However, it is important to note that over time, the City will be issuing bonds to fund this program. At its completion, the City will be paying

significant annual debt service, anticipated to be approximately \$24 million each year, over 36% of the fund's total expenses.

The Wastewater Management Fund by policy maintains a Contingency Reserve of 25% of operations and a Rate Stabilization Reserve to normalize rates and provide for the effect of economic cycles. The Fund also contains reserves for revenue funded projects and debt funded projects to manage the flow of these funds against project expenditures that are uneven by nature.

Wastewater Rates for Customers Outside the City

In addition to the City's wastewater customers within the city limits, there are 1,876 properties located outside the city limits that are serviced by the City's wastewater collection and treatment system. In accordance with legal requirements for the collection of fees on the property tax roll, tonight's public hearing also includes the proposed charges for wastewater services provided by the City of Sunnyvale to properties located outside the City limits. Details of the charges for each property outside the City are included as Attachment 10. A map of the service area outside the City is provided as Attachment 11.

In the mid 1950s, an area known as Rancho Rinconada was being developed as a mostly single-family residential area. At the time, this area was in a pocket of the county that had no direct access to a sewer collection system. The City of Sunnyvale entered into a series of agreements with the developers that allowed the Rancho Rinconada sewer system to be tied into a 15-inch City sewer main that was extended 1.7 miles for that purpose. The agreements required developers to construct sewers that met the City's standards and allowed the City to collect fees from the homeowners for the purpose of reimbursing the City for its costs of providing on-going sewer service.

Proposed charges for all customers in the outside sewer area are equal to the City's proposed charges for customer inside City limits plus a 1% administrative fee charge by the County for processing.

Recommended FY 2015/16 Wastewater Rate Increase

The rate increase proposed for Wastewater services for FY 2015/16 is 8%, which is as projected in last year's budget. Annual rate increases for the remainder of the planning period are shown at the bottom of the Wastewater Management Fund Long-Term Financial Plan (Attachment 5).

The City's detailed Wastewater Rate Survey is presented as Attachment 6. As shown in Attachment 1, Monthly Utility Bill Comparisons - Single Family Residential, the City's residential wastewater rate is competitive when compared with neighboring cities.

Solid Waste Rates

The Solid Waste Management Fund (Solid Waste Fund) accounts for the revenues and expenses related to collection, recycling, and disposal of solid waste generated within the City of Sunnyvale. A private company, Bay Counties Waste Services, doing business in Sunnyvale as Specialty Solid Waste & Recycling (Specialty), has been issued an exclusive franchise for collection of solid waste and recyclable materials through 2021, and these contract costs are reflected in the Solid Waste Management Fund. Operations of the Sunnyvale Materials Recovery and Transfer Station (SMaRT Station) and disposal of refuse at the Kirby Canyon Landfill are included in a separate fund, and the City's share of these expenses and revenues is reflected in the Solid Waste Management Fund.

The City's contract with Specialty for the collection of solid waste and recyclables throughout the City is the largest single expense within the Solid Waste Fund. Specialty is paid on a monthly basis, but its payment is determined for a year based largely on formulas that take actual expenses in the last completed fiscal year and adjust them for inflation and apply a profit. Therefore, the contractor payment for the following fiscal year is driven primarily by actual expenditures from the last full fiscal year, adjusted by various indexes as identified in the contract. The projected FY 2015/2016 contractor payment is \$20 million, which is essentially unchanged from the current FY 2014/15 contractor payment.

City operations costs in the Solid Waste Fund account for approximately 13% of total fund expenses. City operations include contract administration costs for the City's solid waste collection, transfer and disposal contracts, recycling program outreach and administration costs, and administrative and regulatory compliance costs associated with maintaining the closed Sunnyvale landfill. As with the wastewater utility, continued tightening of regulations related to air quality and post closure landfill maintenance are placing upward pressure on the solid waste utility's costs.

The Fund also includes a project to implement the City's Zero Waste policy. The project has been updated to include \$29 million over twenty years to fund new practices aimed at meeting the Zero Waste Strategic Plan goals of 75% diversion by 2020. This project does not incorporate the costs necessary to reach the goal of 90% diversion by 2030 due to uncertainty regarding legal and technical barriers to meeting the 90% goal. Methods planned to increase the diversion rate include implementation of new SMaRT equipment, pilot programs related to food scraps and commercial yard trimmings, and the implementation of City-wide multi-family recycling. The additional diversion is expected to generate approximately \$460,000 per year in operating savings due to a reduction in landfill expenditures.

The Solid Waste Management Fund Long-Term Financial Plan reflects two inter-fund loans that were advanced from the General Fund between FY 1985/1986 and 1998/1999. Additionally, in order to help bridge the gap of depressed cash flow from the recession to recovery, the Solid Waste Management Fund reflects a \$2 million loan from the Wastewater Management Fund at 4.5% interest. Payment is deferred to FY 2015/2016 and then repaid over a six-year period. This helps the Solid Waste Fund with cash it needs now, and then helps the Wastewater Management Fund in the future as its cash needs increase to fund the new WPCP.

Debt service expenditures reflect Sunnyvale's portion of the debt service for the original cost of the SMaRT Station facility and replacement equipment, as well as the estimated portion of debt which is anticipated to be issued in FY 2021/22 for a new materials recovery system.

Solid Waste Cost of Service

Solid waste rates are set to recover the City's cost of providing service to our customers. To verify that the cost of service provided is accurately reflected for each customer group in the City's utility rates, staff periodically conducts rate studies for each of the City's enterprise funds. A solid waste cost of service study was completed in FY 2013/14. The FY 2014/15 fee schedule incorporated changes to debris bin collection rates, but the other shifts resulting from the fee schedule were planned to be implemented in FY 2015/16.

The study showed that residential collection rates needed to be adjusted. Since the last cost of service study, there have been a few changes that impact rates. First, the number of residential

routes was decreased by one route, resulting in cost savings to the City. Second, the allocation of recycling costs has shifted, which reduced the amount of recycling revenue allocated to residential service. The recommended changes include shifting rates across customer classes to better account for the fixed costs of solid waste collection. As a result, smaller cart and bin sizes see a higher percentage increase than larger cart and bin sizes.

On the commercial side, there are some services that will see a price reduction based on the study. On-call extra services for four cubic yards or smaller commercial bins are reduced by as much as 14.3%. This occurred due to a reduction in commercial routes that resulted in cost savings to the City. Compactor services rates will decrease for seven cubic yard or larger bins. This occurred because the study found that the total pounds per loose cubic yard have dropped significantly from the previous study, leading to a reduction in disposal costs.

All changes that were recommended in the cost of service study have been incorporated into the FY 2015/16 financial plan. Cost of service studies are conducted every five years for each utility, and the next solid waste study is planned for FY 2018/19.

Sunnyvale Materials Recovery and Transfer (SMaRT) Station Fund

In 1992, the City of Sunnyvale entered into a Memorandum of Understanding (MOU) with the cities of Palo Alto and Mountain View for the operation of the SMaRT Station. The three cities that participate in the SMaRT Station have individual agreements with Waste Management, Inc. for landfill disposal at the Kirby Canyon Landfill in San Jose. Sunnyvale and Mountain View agreed to deliver all of their garbage and residential recyclables, including yard trimmings, to SMaRT. In 1992, at the start of the MOU, Palo Alto operated its own landfill and facilities for yard trimmings, compost, and recycling. Palo Alto thus committed to deliver only specific amounts of garbage that vary from year to year. The SMaRT Station is operated by a private company under contract with the City. Last year, the City Council awarded a new contract for operation of the SMaRT Station to Bay Counties Waste Services. Bay Counties Waste Services has been operating the SMaRT Station since 2008, and their new contract runs through 2021.

Sunnyvale's share of SMaRT station costs is included in the Solid Waste Fund. At current garbage delivery rates, Sunnyvale is responsible for about half of the SMaRT Station operating expenditures and receives about half of the revenues earned by the cities from recyclables removed from the garbage. The capital cost of the SMaRT Station was financed by the sale of revenue bonds by Sunnyvale. The debt service on the bonds is shared among the three cities as specified in the MOU. In FY 2014/15, the 2003 and 2007 Solid Waste Revenue Bonds were refinanced to take advantage of interest rate savings. This resulted in a savings of over \$600,000 in present dollars, which is split between the three cities.

The SMaRT Station Operations Fund was established to account for operations at the facility. It receives revenue from the charges to the cities of Sunnyvale (Solid Waste Fund), Mountain View, and Palo Alto, and from the sale of recyclables. Major operating cost components include the SMaRT Station operator contract and disposal fees and taxes collected by the Kirby Canyon Landfill. The fund is managed so that annual revenues and expenditures are in balance and that no fund balance, with the exception of a small debt service reserve, is carried forward to the next year.

The SMaRT Station Replacement Fund provides for the replacement of City-owned SMaRT Station equipment. The three participating cities contribute to these efforts and to payment of debt service

based on fixed percentages established by the SMaRT Station MOU. Debt service reflects payment through FY 2020/21. Funding is projected for a new materials recovery system and any other improvements needed to the SMaRT Station Facility in FY 2021/22, with annual debt service of \$2 million. Funding is also provided for planning and inter-jurisdictional coordination in FY 2016/17 through FY 2019/20. The project could involve a replacement for the SMaRT Station or implementation of some other solution for the management of solid waste and recyclables in the City.

Recommended FY 2015/16 Solid Waste Rate Increase

The rate increase proposed for solid waste and recycling services for FY 2015/16 is 5%, as planned in last year's budget. The projected increases for the remainder of the planning period are reflected at the bottom of the Solid Waste Management Long-Term Financial Plan (Attachment 7).

The detailed Solid Waste Rate Survey is presented as Attachment 8. As shown in Attachment 1, Monthly Utility Bill Comparisons - Single Family Residential, the City's residential solid waste and recycling rate is competitive when compared with neighboring cities.

FISCAL IMPACT

The proposed utility rate changes are necessary to maintain the City's utilities in a sound financial and operational condition. Even with the proposed changes, Sunnyvale's utility rates remain competitive when compared to current rates charged in other cities.

PUBLIC CONTACT

Public contact was made by posting the Council agenda on the City's official-notice bulletin board outside City Hall, at the Sunnyvale Senior Center, Community Center and Department of Public Safety; and by making the agenda and report available at the Sunnyvale Public Library, the Office of the City Clerk and on the City's Web site.

As detailed in the background section of this report, Sunnyvale continues to comply with the noticing provision for utility rates as required by State law.

ALTERNATIVES

1. Find that the project is exempt from CEQA pursuant to Public Resources Code Section 21080 (b)(8) and CEQA Guideline 15273 because it approves rates and charges for the purposes of (1) meeting operating expenses, including employee wage rates and fringe benefits; (2) purchasing or leasing supplies, equipment or materials; (3) meeting financial reserve needs and requirements; and (4) obtaining funds for capital projects necessary to maintain current service levels.
2. Adopt the attached resolution increasing water rates by 20%, wastewater rates by 8%, and solid waste rates by 5% for FY 2015/16. Allocate any savings realized from lower wholesale purchase rates to the Water Fund's Rate Stabilization Reserve.
3. Adopt a 2% lower water rate increase than proposed due to the savings from lower wholesale purchase rates. This alternative would result in a 17.5% water rate increase, 8% wastewater increase, and 5% solid waste rate increase for FY 2015/16.
4. Adopt rates other than those proposed. Take no action on rates and leave the existing rates in effect.
5. Continue the hearing to a future date to consider rates higher than those proposed, which would require additional Proposition 218 noticing.

STAFF RECOMMENDATION

Alternatives 1 and 2: 1) Find that the project is exempt from CEQA pursuant to Public Resources Code Section 21080(b)(8) and CEQA Guideline 15273 because it approves rates and charges for the purposes of (1) meeting operating expenses, including employee wage rates and fringe benefits; (2) purchasing or leasing supplies, equipment or materials; (3) meeting financial reserve needs and requirements; and (4) obtaining funds for capital projects necessary to maintain current service levels; and 2) Adopt the attached resolution increasing water rates by 20%, wastewater rates by 8%, and solid waste rates by 5% for FY 2015/16. Allocate any savings realized from lower wholesale purchase rates to the Water Fund's Rate Stabilization Reserve.

Water rates can be increased by less than 20%, down to 18%, without fiscal impact to the long term water plan. However, staff does not recommend this due to volatility with the drought and the need for strong reserves to deal with potential revenue loss and unanticipated costs for conservation efforts.

Prepared by: Janice Broussard, Utility Billing Manager
Reviewed by: Grace K. Leung, Director of Finance
Reviewed by: Robert A. Walker, Assistant City Manager
Approved by: Deanna J. Santana, City Manager

ATTACHMENTS

1. Combined Monthly Utility Bill Comparisons - Single Family Residential
2. Utility Rate Comparisons - Commercial
3. Recommended FY 2015/16 Water Supply and Distribution Fund Long Term Financial Plan
4. Water Rate Survey
5. Recommended FY 2015/16 Wastewater Management Fund Long Term Financial Plan
6. Wastewater Rate Survey
7. Recommended FY 2015/16 Solid Waste Management Fund Long Term Financial Plan
8. Solid Waste Rate Survey
9. Proposed Resolution
10. Tax Roll Detail for Wastewater Services Provided Outside the City Limits
11. Map of Wastewater Service Area Outside the City Limits