



PUBLIC WORKS DEPARTMENT

CITY HALL

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CITY COUNCIL STAFF REPORT

Meeting Date: October 2, 2018

Subject

Factors affecting water rates in Cupertino.

Recommended Action

Accept presentation on water rates.

Background and Discussion

The issue of water rates and conservation became important to many Cupertino residents in California's historic drought. While previous droughts had been experienced, it was during the four year drought of 2012-16 that many water utilities imposed drought surcharges, which carried noticeable financial impacts for customers.

In Cupertino, water customers are served by three water systems that approximately divide the City into thirds. One system is owned & operated by California Water Service (Cal Water), another is owned & operated by San Jose Water Company (San Jose Water), and the third system is the Cupertino Municipal System, owned by the City and operated through a lease by San Jose Water. Both Cal Water and San Jose Water are investor owned utilities (IOU), while the Cupertino Municipal System is a government owned utility (GOU), with full operations of the system provided through a lease to San Jose Water.

IOUs and GOUs have a different public process to determine rates. For IOUs the meter charge, volume charge, and surcharges are proposed to the California Public Utilities Commission (CPUC) through a general rate case (GRC) application process. GRC applications are filed about 18 months in advance of their proposed implementation date to allow for the CPUC and the California Public Advisors Office (Cal PA, formerly the Office of Ratepayer Advocates) review and for public input. Charges established in the GRC cover a three year period. Advice Letters are periodically submitted to the CPUC for consideration to adjust rates established in the GRC and other decisions. The 2018 Tax Cut and Jobs Act is an example of a previous Advice Letter filed by both Cal Water and San Jose Water. Another filing made by IOUs is referred to as Cost of Capital. The purpose of the Cost of Capital is to set the rate of return for dollars invested into the

utility. Customers of IOUs are charged for their meter/service, water consumed and surcharges. The purpose of the surcharge is to account for the costs of specific programs and changes to rates, some of which occur outside of the GRC process. Surcharges can include costs such as low income rate assistance, increased costs of wholesale water from the Santa Clara Valley Water District (SCVWD) and other regulatory fees.

GOU's follow a different rate setting process. GOU's, instead of being regulated by the CPUC, follow a State of California process known as Proposition 218. GOU's periodically review their costs and adjust their rates accordingly. Per the lease agreement between the City of Cupertino and San Jose Water, rates in the Cupertino Municipal System are authorized by the City of Cupertino and generally follow those established by the CPUC authorized rates of San Jose Water.

Charges for meter/service and water consumed vary for both IOUs & GOU's. Most all utilities have established tiered rates based on water consumed. The below table shows current charges for the three Cupertino systems and three adjacent GOU's for a residential customer.

	5/8x3/4" Meter/Service Charge	Tiered Rate Thresholds (Ccf)	Volume Rates by Tier (per Ccf)
Cal Water	\$17.97	0 - 10	\$5.24
		11 - 27	\$5.58
		28+	\$6.69
San Jose Water	\$25.28	0 -3	\$4.22
		4 - 18	\$4.68
		18+	\$5.15
Cupertino Municipal System leased to San Jose Water	\$23.98	0 -3	\$4.06
		4 - 18	\$4.51
		18+	\$4.95
Sunnyvale	\$14.05	0 - 5	\$4.39
		6+	\$5.36
Mountain View	\$15.15	0 - 3	\$5.15
		4 - 15	\$6.87
		16+	\$10.99
Santa Clara	\$17.87	0+	\$5.98

The average residential customer in Cupertino uses 11ccf (1 Ccf=748 gallons) of water per month. Using the meter/service charge, tiers and rates shown above, the below table shows how total water costs for the average Cupertino customer vary among the IOUs and GOUs.

	5/8x3/4" Meter/Service Charge	11 Ccf Charge	Surcharge	Total
Cal Water	\$17.97	\$58.01	\$7.46	\$83.44
San Jose Water	\$25.28	\$50.58	\$13.06	\$88.93 ¹
Cupertino Municipal System leased to San Jose Water	\$23.98	\$48.25	\$11.83	\$84.06 ²
Sunnyvale	\$14.05	\$54.11	0	\$68.16
Mountain View	\$15.15	\$70.41	0	\$85.56
Santa Clara	\$17.87	\$65.78	0	\$83.65

¹Rates are effective August 2018

² Rates have not increased since 2016

Water utility rates typically increase annually. Cal Water's revenue requirement, which is the foundation of rates paid by customers, is anticipated to increase by 3.4% in 2019; 3.7% in 2020 and 5.1% in 2021. San Jose Water is anticipated to have rate increases of 9.76%, 3.7% and 5.1% for the same period. GOUs are also expected to have increases. A portion of the increases is driven by SCVWD wholesale water increases. As an example, wholesale water costs increased 19.9%, 9.6% and 9.7% for 2016 through 2018. This caused retail water consumption costs to increase approximately 8%, 4% & 4% for this same time period. These increased wholesale costs are eventually added to other costs to operate the utilities and are descriptive to how increasingly expensive water is becoming.

Overbilling of San Jose Water Company Customers

On June 6, 2017 AL No. 510 was submitted by San Jose Water Company to the CPUC to reconcile billing errors made from January 2014 through December 2016. At issue is when

San Jose Water Company billed their customers for CPUC authorized rate changes. By submitting this AL, San Jose Water Company admitted that it was billing customers a CPUC authorized rate prior to the effective date of the rate change.

The rate impact of AL No. 510 was a proposed one-time refund of \$5.70 to residential customers with a 3/4" meter. Customers with larger meters and commercial customers would receive more. In total, San Jose Water Company calculated \$1.794 million in refunds to its customers. Since the error also occurred to customers of the Cupertino Municipal System, a refund to these customers will also be required and will be addition to the \$1.794 million.

On June 23, 2017 Cal PA recommended to the CPUC that AL No. 510 be rejected and a formal hearing be considered. City staff agreed with the Cal PA recommendation and sent a similar request to the Water Director of the CPUC on July 26, 2017 and a second letter dated August 9, 2018 to the CPUC Administrative Law Judge presiding over the issue. The CPUC responded to the City's letter on August 7, 2017 by stating that AL No. 510 was suspended pending further investigation and coordination with complaint number C.17-06-009 filed by Water Rate Advocates for Transparency, Equity and Sustainability.

On September 13, 2018 the CPUC opened a formal investigation into San Jose Water Company's billing practices. This action was due to an informal Cal PA investigation that alleges that for at least 30 years, San Jose Water Company failed to pro-rate its customer bills when a change to its service charge went into effect in the middle of a customer billing cycle. Additionally, Cal PA alleges that San Jose Water Company double-billed its customers when it converted from billing its service charge in advance to billing in arrears. The Cal PA report recommends that San Jose Water Company implement a credit to its customers of approximately \$2 million for the time period of January 1, 2014 to December 31, 2016, as well as another \$1.9 million to reflect the 1987-2013 time period. Additionally, Cal PA calculated that the total amount of double billing amounts to nearly \$5 million in overcharges.

The formal investigation by the CPUC will provide a forum to consider evidence and argument on these issues from CPUC staff, San Jose Water Company, and other parties to the proceeding. Evidence taken in the proceeding will be the basis for findings, conclusions, and CPUC orders, including whether San Jose Water Company should provide refunds to customers as well as whether the company should face additional financial penalties, reparation and other remedies.

It would be premature at this time for the City to cause San Jose Water Company to credit the customers of the Cupertino Municipal Water System for their amount of overbilling. Instead, City staff recommends that the issue be monitored to see by how much the CPUC changes or adds to the Cal PA recommendation to credit \$8.9 million. As it is unknown how long this investigation will take, City staff will create and keep updated a webpage on the City website to assist Cupertino water customers in being timely informed of this issue.

A presentation will be provided to the City Council at the October 2, 2018 Water Rate Study Session. City Council and public input is invited.

Fiscal Impact

Millions of dollars are spent annually by water customers in Cupertino. The City alone expended approximately \$1.09 million for water last year. Any increase in the cost of water impacts the budget of all consumers. When the issue of AL No. 510 is concluded by the CPUC for customers of San Jose Water Company, customers of this system will likely receive a one-time credit. Customers of the Cupertino Municipal System leased to San Jose Water Company will also receive a refund. Increases in water costs for FY18/19 have been included in the FY18/19 Operating Budget. No adjustment has been made to the FY18/19 Operating Budget for refunds that may be received as a result of overbilling of City water accounts. No additional appropriations are requested.

Sustainability Impact

None.

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Attachments: None