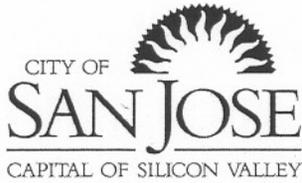


Council Agenda: 2-8-05
Item: 3.5



Memorandum

TO: HONORABLE MAYOR AND
CITY COUNCIL

FROM: Larry D. Lisenbee

**SUBJECT: COUNCIL REFERRAL:
WHOLESALE WATER COSTS
VS. RETAIL REVENUES**

DATE: February 4, 2005

Approved

Date

2/7/05

On June 22, 2004, the City Council approved Municipal Water rate increases and directed staff to return during the Mid-Year Budget Review with a report on projected and actual wholesale cost increases versus retail revenues generated by the rate increase. This response to the Council referral is being released under separate cover as noted in the 2004-2005 Mid-Year Budget Review, scheduled to be discussed at the February 8, 2005 City Council meeting (Item 3.5).

LARRY D. LISENBEE
Budget Director

Memorandum

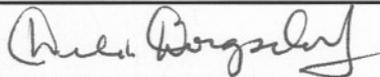
TO: HONORABLE MAYOR AND
CITY COUNCIL

FROM: Carl W. Mosher

**SUBJECT: WHOLESALE WATER COSTS
VS. RETAIL REVENUES**

DATE: January 31, 2005

Approved



Date

2-4-05

INFORMATION

BACKGROUND

On June 22, 2004, the City Council adopted Resolution No. 72183 to increase Municipal Water System's rates by \$0.08 per hundred cubic foot. This amounted to a 4% increase on the average customer bill and reflected a blending of the rate increases set by the two water wholesalers that supply our customers.

Staff was directed to return during the Mid-Year Budget cycle with a report on projected and actual wholesale cost increases versus retail revenues generated by the rate increase. This memo provides that analysis as well as the formula used to determine these calculations.

ANALYSIS

The formula used to determine the appropriate rate setting strategy for Municipal Water customers is based on the projected volume of wholesale water to be purchased during the year, the ratio of water purchased from each of the two wholesalers, and any rate increases projected to be adopted by the governing bodies of the two water wholesalers.

Water Volume and Ratio Purchased: Meters at each turnout measure on a monthly basis the actual amount of water purchased from the two wholesalers. The amount purchased varies from year to year, largely depending on whether summers were hotter or cooler than normal. Historically, the ratio of water that Muni purchases amounts to approximately 75% from the Santa Clara Valley Water District and 25% from the San Francisco Public Utilities Commission (SFPUC) through the Hetch Hetchy reservoir system.

Rate Increase Projections: Since the budget approval cycle for the three agencies is similar, Muni relies on staff from the Water District and San Francisco to provide information on any anticipated rate increases for the next fiscal year.

January 31, 2005

Subject: Information - Wholesale Water Costs Vs. Retail Revenues

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Summary of Calculations: Tables 1 and 2 below summarize (1) projections for the full year and (2) actual data for the first six months of fiscal year 2004-05 covering volumes of water purchased, total cost increases, and cost increases per hundred cubic feet.

**TABLE 1 – PROJECTED ANNUAL
Wholesale Water Amounts and Costs
July 1, 2004 - June 30, 2005**

<u>Agency</u>	<u>Wholesale Water Purchases HCF*</u>	<u>2003-04 Rate \$/HCF</u>	<u>2004-05 Rate \$/HCF</u>	<u>Ratio of Water (%)</u>	<u>Total Cost</u>	<u>Total Cost Increase</u>	<u>Increase \$/HCF</u>
<u>SFPUC</u>	2,287,215	\$1.10	\$1.20	24.3%	\$2,866,734**	\$228,722	\$0.10
<u>SCVWD</u>							
Treated Water	6,822,509	\$1.056	\$1.136	72.6%	\$7,750,371	\$545,800	\$0.08
Wells, Zone 2	258,442	\$0.860	\$0.930	2.8%	\$240,352	\$18,090	\$0.07
Wells, Zone 5	<u>28,105</u>	<u>\$0.367</u>	<u>\$0.459</u>	<u>0.3%</u>	<u>\$12,900</u>	<u>\$2,529</u>	<u>\$0.09</u>
TOTAL	9,396,271			100%	\$10,748,281	\$795,141	\$0.08

*1 HCF = 748 gallons

**Includes a monthly meter charge of \$10,173 (Table 1 and 2)

**TABLE 2 – ACTUAL AT MIDYEAR
Wholesale Water Amounts and Costs
July 1, 2004 - December 31, 2004**

<u>Agency</u>	<u>Wholesale Water Purchases HCF*</u>	<u>2003-04 Rates \$/HCF</u>	<u>2004-05 Rates \$/HCF</u>	<u>Ratio of Water (%)</u>	<u>Total Cost</u>	<u>Total Cost Increase</u>	<u>Increase \$/HCF</u>
<u>SFPUC</u>	1,208,725	\$1.10	\$1.13	23.3%	\$1,426,897**	\$36,246	\$0.03
<u>SCVWD</u>							
Treated Water	3,845,717	\$1.056	\$1.136	74%	\$4,370,132	\$309,000	\$0.08
Wells, Zone 2	120,567	\$0.860	\$0.930	2.3%	\$13,730	\$8,211	\$0.07
Wells, Zone 5	<u>20,969</u>	<u>\$0.367</u>	<u>\$0.459</u>	<u>0.4%</u>	<u>\$9,099</u>	<u>\$2,048</u>	<u>\$0.09</u>
TOTAL	5,195,977			100%	\$5,919,858	\$355,505	\$0.07

HONORABLE MAYOR AND CITY COUNCIL

January 31, 2005

Subject: Information - Wholesale Water Costs Vs. Retail Revenues

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As of December 31, 2004, the actual amount of water purchased totals 5,195,977 hundred cubic feet (this represents more than half the annual projection because three of the four warm weather months are in the first half of the year). This results in an actual increase in wholesale water costs totaling \$355,505, which translates to a cost of \$0.07 per hundred cubic feet compared to the \$0.08 increase per HCF projected by staff (see the last column in each table).

This variance occurred mainly because the SFPUC raised its rates by only 2.7%, rather than the 9% projected earlier by its staff in information provided to Muni. As noted above, the three agencies are on similar rate setting and budget approval cycles, and City calculations are based on the best available information as we progress through our budget processes.

In the worst-case scenario, this variance generated additional retail revenue of \$60,173 for the first six months (5,195,977 HCF multiplied by \$0.08). For the full year, this would total \$108,500 (less water is sold in the second half of the year since June is the only warm weather month). The actual additional revenue will be slightly less since all water systems experience "losses" (leaks, water used for fire fighting, and failure of some customers to pay their bills).

IN CLOSING

Overall, the total amount of additional retail revenue would equate to about \$0.15 monthly on the average customer bill, and represents less than one-half of 1% on Muni's total annual sales of over \$21 million. Since FY 1996-97, Muni Water has passed through only 75% of its total wholesale water cost increases, resulting in a total customer savings of \$7,386,000. Consequently, Muni Water's average monthly bills are 24% lower than the average bill of the two private companies serving San Jose.

Nonetheless, the \$0.01 differential that appears to be occurring this year will be taken into consideration while determining the five-year rate strategy for the Municipal Water System during the City's FY 2005-06 annual budget process.

Questions or clarifications regarding the information in this report can be addressed during the Mid-Year Budget review process.



CARL W. MOSHER

Director, Environmental Services Department

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