



Memorandum

TO: HONORABLE MAYOR AND
CITY COUNCIL

FROM: Carl W. Mosher

SUBJECT: SEE BELOW

DATE: 6-3-04

Approved

Date

**SUBJECT: PROPOSED WHOLESALE RECYCLED WATER RATE INCREASE
FOR FY 2004-05**

RECOMMENDATION

Adopt a resolution to:

- Increase the wholesale recycled water basic rate from \$240 per acre-foot (AF) to \$405/AF;
- Index the basic rate to the Santa Clara Valley Water District's wholesale untreated water costs;
- Provide a \$165/AF discount for recycled water delivered to water retailers for landscape irrigation use; and
- Provide a \$365/AF discount for recycled water delivered to water retailers for industrial and agricultural uses.

BACKGROUND

The City of San José is the administering agency for the San José/Santa Clara Water Pollution Control Plant (Plant). It has entered into agreements with water retailers to provide wholesale recycled water service through South Bay Water Recycling (SBWR). The agreements stipulate that the wholesale rate for recycled water shall provide an economic incentive to recycled water customers and shall be identified in a rate schedule to be established by the City Council of the City of San Jose.

In 1997, Council adopted wholesale rates for the sale of recycled water to water retailers in San Jose, Santa Clara, and Milpitas. The rates were designed to allow water retailers to sell water to

their customers at a discount relative to the cost of untreated potable water, which at that time was \$240 per AF, while maintaining profits consistent with those made on the resale of potable water. The discount structure created a financial incentive for water retailers to market recycled water as well as for customers to use the water.

ANALYSIS

As referenced above, Council established the Basic Rate for recycled water in 1997 (Resolution No. 67182) at \$240/AF. Resolution No. 67182 also provides that the basic wholesale price for recycled water should be increased to track any future price increases for untreated water from the Water District. Since 1997 the District has raised its rates for untreated water by 56% from \$240/AF to \$375/AF and is proposing to increase the price of untreated water to \$405/AF for FY 2004/05.

The following table provides an historical overview of the District’s wholesale rates:

<u>Year</u>	<u>District Untreated Water (AF)</u>	<u>SBWR Basic Rate** (AF)</u>
97-98	\$240	\$240
98-99	\$260	\$240
99-00	\$285	\$240
00-01	\$310	\$240
01-02	\$330	\$240
02-03	\$340	\$240
03-04	\$375	\$240
04-05	\$405*	\$405*

* Proposed

** Note that SBWR’s Basic Rate is not the price that water retailers pay for wholesale recycled water. The discounted rates are explained below.

Resolution No. 67182 also established discounted wholesale rates for water delivered by retailers to customers for landscape irrigation, industrial and agricultural uses. These discounted rates were established to facilitate customer connection to SBWR and to provide adequate price incentives to ensure that flows to San Francisco Bay were maintained below 120 million gallons per day (mgd).

Over the last seven years, both wholesale and retail potable water rates have risen to reflect increases in wholesale water prices from the District. On the other hand, wholesale rates for

recycled water delivered to landscape irrigation, industrial and agricultural customers have remained the same. The recommended rates in this Resolution would allow recycled rates to rise automatically with any increase in the District’s wholesale untreated water costs, while still maintaining fixed price discounts to provide a sufficient incentive to encourage use of recycled water.

A higher discount is recommended for agricultural customers primarily due to their access to very low-cost well water. The higher discount will also be retained for industrial customers, to continue to provide a substantial incentive to encourage these customers to consider recycled water as an option. The incentives will continue to allow the retailers to earn profits on the resale of recycled water that are consistent with the profits that they would make on the resale of potable water.

Rate Comparison

<u>Year</u>	<u>District Untreated Water Rate (AF)</u>	<u>SBWR Basic Rate (AF)</u>	<u>SBWR Irrigation Rate (AF)</u>	<u>SBWR Industrial/Agricultural Rate (AF)</u>
Current	\$375	\$240	\$180	\$20
04-05*	\$405	\$405	\$240	\$40

* Proposed

Implementation of the new wholesale rates will raise revenues by approximately \$360,000 annually. This figure is based on selling approximately 6,000 AF of recycled water during FY 04-05.

This additional revenue will offset the costs paid by sewer ratepayers for producing and delivering recycled water.

Impact on Customers

In accordance with Resolution 68377, the Municipal Water System plans to increase retail recycled rates by the same proportion as the increase in wholesale rates. This equates to \$.14/HCF (HCF equals 748 gallons) except for former well users whose rates will go up by \$0.05/HCF. The other water retailers (San Jose Water Company, City of Santa Clara, and City of Milpitas) are expected to follow suit.

Attachment A provides a comparison of current and predicted potable and recycled water rates among the four water retailers.

PUBLIC OUTREACH

Discussions of this proposal have been held with the water retailers, and they are in concurrence.

Additionally, in November 2001, Fairbanks, Maslin, Maullin and Associates conducted two focus groups with a targeted sampling of recycled water customers. Customers walked through a variety of potential rate scenarios with rates between 80% and 100% of potable water rates. They indicated that they would be less inclined to use recycled water without any cost savings, but that their use was based on other motivations as well, including the assurance of reliable water deliveries during periods of drought and being known as “good corporate citizens.”

A retail price of 80% of the retail price of potable water was generally seen as an acceptable rate for recycled water. The recommended wholesale rate with discounts will result in retail recycled water prices that are approximately 69% of the retail price for potable water.

COORDINATION

This memo has been coordinated with the City Attorney’s Office and the City Manager’s Budget Office. This item is scheduled to be heard at the June 10, 2004, Technical Advisory Committee (TPAC) meeting.

CEQA

Not a project.

CARL W. MOSHER
Director, Environmental Services Department