



COUNCIL AGENDA: 06-17-08

ITEM: 7.3

Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

FROM: John Stufflebean

**SUBJECT: RECYCLED WATER RATE
DISCOUNT REDUCTION**

DATE: 05-27-08

Approved

Date

5-28-08

COUNCIL DISTRICT: Citywide

RECOMMENDATION

Adopt a resolution setting wholesale recycled water rate discounts over a three year period for landscape irrigation of \$145 per acre-foot (2008-09), \$125 per acre-foot (2009-10), and to \$105 per acre-foot (2010-11) and setting a discount over a one year period of \$345 per acre-foot (2008-09) for recycled water used for industrial and agricultural use.

OUTCOME

Reducing the discount as proposed will: (1) generate between \$150,000 and \$200,000 in additional revenue the first year; increase revenue to about \$500,000 after three years; and (3) move the operation of the system toward a more "cost recovery" basis.

BACKGROUND

The City is the administering agency for the San José/Santa Clara Water Pollution Control Plant (Plant) and South Bay Water Recycling (SBWR), which provides recycled water to south bay cities including San José, Santa Clara, and Milpitas.

On March 4, 1997, Council adopted Resolution 67182 setting a basic wholesale recycled water rate of \$240 per acre-foot (AF), and discounts of \$60/AF for recycled water used for landscape irrigation and \$220/AF for recycled water used for industrial and agricultural use. At this time, \$240/AF was equal to the untreated water rate set by the Santa Clara Valley Water District (SCVWD) and was not expected to increase.

The basic discounts were designed to encourage the use of recycled water by making it less costly than potable water. The discount for landscape irrigation was designed to make recycled water available at a cost (10-20%) lower than what customers were paying at that time for potable water. The steeper discount for industrial users was designed to cover the additional treatment costs that these customers would incur. The following year, SCVWD began increasing the untreated water rate, resulting in a corresponding increase in the basic wholesale recycled water rate. However, the net wholesale rates for recycled water charged to the systems' retailers

based on the 1997 resolution, effectively increasing the discount and corresponding cost savings over potable water each year.

On June 15, 2004, Council adopted Resolution 72167 revising the basic wholesale recycled water rate to reflect the then current SCVWD untreated water charge of \$405/AF, and fixing the discounts offered, which by then had reached \$165/AF (\$105 additional discount) for recycled water used for landscape irrigation and \$365/AF (\$145 additional discount) for recycled water used for industrial and agricultural use.

SCVWD has continued to increase the untreated water charge annually, resulting in the basic wholesale recycled water rate rising to the current \$475/AF. The proportion of imported water is anticipated to continue to increase which will compel the SCVWD to raise the untreated water charge by an estimated \$45/AF for FY 2008-09, which would result in the basic wholesale recycled water rate rising to \$520/AF effective July 1, 2008.

ANALYSIS

Recycled water has been widely used in the SBWR service area for over ten years, with more than 540 customers using in excess of 10,000 AF per year annually (9 million gallons per day). In view of the growing acceptance of recycled water, the current discount rate appears to be greater than that needed to encourage recycled water use.

The present action proposes to reduce the discount for irrigation use by \$60/AF per year over three years, from the current level of \$165/AF to \$105/AF. The present action also proposes to reduce the discount for industrial use by \$20/AF, from the current level of \$365/AF to \$345/AF. As a result, for FY 2008-09 the discount for landscape irrigation use would be reduced to \$145/AF, and the discount for industrial and agricultural use would be reduced to \$345/AF. For FY 2009-10, the discount for landscape irrigation use would be further reduced to \$125/AF, while for FY 2010-11, the discount for landscape irrigation use would be reduced to \$105/AF. Recommendations for any further changes to the discount given to industrial and agricultural users will be determined after additional discussion with water retailers and implementation of the current Cooling Tower Conversion program. The table below shows the effect of this change on the final wholesale cost of recycled water per acre-foot, based on projected wholesale potable rates through 2012:

Year	District Untreated Water	Irrigation Discount	Irrigation Wholesale Rate	Industrial Discount	Industrial Wholesale Rate
2004-2005	\$405	\$165	\$240	\$365	\$40
2005-2006	\$420	\$165	\$255	\$365	\$55
2006-2007	\$435	\$165	\$270	\$365	\$70
2007-2008	\$475	\$165	\$310	\$365	\$110
2008-2009	\$520	\$145	\$375	\$345	\$175
2009-2010	\$565	\$125	\$440	\$345	\$220
2010-2011	\$610	\$105	\$505	\$345	\$265

**projected*

The reduction in the discount is necessary to bring the revenue from the sale of recycled water closer to the service delivery cost. In addition, the discount levels currently in place should be brought closer to their original levels, as the current level of incentive appears to be unnecessary. (See table below). By taking into account the increase in rates that is expected to occur because of the increase in untreated water rates set by the SCVWD, the net wholesale recycled water rate for FY 2008-09 would likely be \$375/AF for irrigation use, and \$175/AF for agricultural and industrial use, a net increase of \$65/AF. Notwithstanding these increases, irrigation customers will continue to realize a savings of \$245/af for irrigation use and \$445 for industrial use.

It is anticipated that this rate structure will continue to provide sufficient incentive for customers to use recycled water as well as allowing the SBWR program to reach cost recovery. The impact on customers of the proposed discount reduction is presented in the table below:

Type of Customer	Water Use (AFY)	Potable Water (\$/year)	Current discount (\$/year)	Reduced discount (\$/year)	Change in Savings (\$/yr)
Irrigation-large	280	\$252,000	\$ 176,000	\$ 182,000	\$ 5,600
Irrigation-small	11	\$9,900	\$ 6,900	\$ 7,100	\$ 200
Industrial-large	1120	\$1,008,000	\$ 493,000	\$ 515,000	\$ 22,200
Industrial-small	22	\$19,800	\$ 9,700	\$ 10,100	\$ 400

EVALUATION AND FOLLOW-UP

South Bay Water Recycling will track costs and revenues and make additional recommendations as needed to operate the utility onto a cost recovery basis. Additionally, we will continue to meet with water retailers and recycled water customers to confirm the appropriateness of our rate structure.

PUBLIC OUTREACH

This issue was presented to the Transportation and Environment Committee on September 17, 2007, and was discussed with SBWR retailers at the February 28, 2008, Recycled Water Retailers Meeting.

COORDINATION

This item has been coordinated with the City Attorney's Office. This item is scheduled to be heard at the June 12, 2008 meeting of the Treatment Plant Advisory Committee.

COST IMPLICATIONS

Existing funds are available for this purpose. No appropriation action is required.

HONORABLE MAYOR AND CITY COUNCIL

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BUDGET REFERENCE

Fund: 513 Treatment Plant Operating Fund

Amount: NA

Budget Document: NA

CEQA

Not a project.



JOHN STUFFLEBEAN

Director, Environmental Services Department

For questions please contact Mansour Nasser, Deputy Director, at (408) 277-4218.