

Item No. 14-1

“To Be Delivered” Material

For

City of Sacramento

City Council

Financing Authority

Housing Authority

Redevelopment Agency

Agenda Packet

Submitted:

For the Meeting of: January 26, 2010

The attached materials were not available at the time the Agenda Packet was prepared.

Title: Department of Utilities-Proposition 218 Update

Contact Information: Marty Hanneman, Director, 916-808-7508

Please include this “To Be Delivered” material in your agenda packet. This material will also be published to the City’s Internet. For additional information, contact the City Clerk Department at Historic City Hall, 915 I Street, First Floor, Sacramento, CA 95814-2604, (916) 808-7200.



REPORT TO COUNCIL

City of Sacramento

915 I Street, Sacramento, CA 95814-2604
www. CityofSacramento.org

Staff Report
January 26, 2010

Honorable Mayor and
Members of the City Council

Title: Department of Utilities- Proposition 218 Update

Location/Council District: All

Recommendation: Receive and file.

Contact: Marty Hanneman, Director, Department of Utilities 808-7508

Presenters: Marty Hanneman, Director, Department of Utilities

Department: Utilities

Division: Administration

Organization No: 14001011

Description/Analysis

Issue: On January 6, 2010, the Sacramento County Grand Jury released a report regarding potential Proposition 218 violations in regards to the City's utility rates. Staff has been requested by the City Council and the City Manager's Office to report back to the Council on potential Proposition 218 issues and their status.

This report provides a brief background of Proposition 218 and how it relates to the Department of Utilities and its operations and rate setting. This report then discusses the Sacramento County Grand Jury Report and the issues identified in the Report, describes the actions already taken to address some issues and efforts underway to address remaining issues, and provide a timeline of events since this issue was raised within the Department in 2007.

City staff continues to work on a proposed implementation plan to address all potential Proposition 218 violations and will return to the City Council with regular updates. The City is required to provide a written response to the findings and recommendations in the Grand Jury report by April 6, 2010, and staff plans to present to the City Council its recommended response to the Grand Jury report in March.

Policy Considerations:

Proposition 218 issues will continue to change how the Department of Utilities charges for its services to other City Departments, while continuing to provide high quality water, sewer, drainage and solid waste services.

Environmental Considerations:

California Environmental Quality Act (CEQA):

Under the CEQA guidelines, continuing administrative activities do not constitute a project and are therefore exempt from CEQA review.

Sustainability Considerations: There are no sustainability considerations associated with this report.

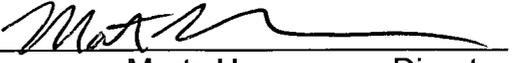
Commission/Committee Action: None

Rationale for Recommendation: No recommendations are provided in this report. Staff will present its recommended response to the Grand Jury report for City Council consideration in March.

Financial Considerations: There will be some implications to the General Fund as the Department of Utilities increases charges for certain services to other City Departments.

Emerging Small Business Development (ESBD): No goods or services are being purchased under this report.

Respectfully Submitted by: 
Marty Hanneman, Director

Approved by: 
Marty Hanneman, Director

Recommendation Approved:


Ray Kerridge
City Manager

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Attachment 1

BACKGROUND

Proposition 218:

Proposition 218 was adopted by California voters in 1996 to add provisions to the California Constitution to govern the adoption of taxes, assessments and property-related fees by local agencies. With respect to property-related fees, Proposition 218 established procedural requirements that must be followed prior to adopting or increasing such fees, as well as the following substantive requirements that apply to the determination of the fee amount and the use of fee revenues:

- Revenues derived from a property-related fee or charge cannot exceed the funds required to provide the property-related service.
- Revenues may not be used for any purpose other than that for which the fee or charge was imposed.
- No fee or charge may be imposed for general governmental services available to the public at large.
- The amount of a fee or charge imposed upon any parcel or person as an incident of property ownership must not exceed the proportional cost of the service attributable to the parcel.
- The fee or charge may only be imposed for service that is actually used by, or is immediately available to, the owner of the property in question.

How Utilities Rates are Set:

Utility rates are calculated based on the cost of operating and maintenance expenses such as labor, supplies and materials, equipment, capital expenditures for infrastructure debt service payments on bonds and other debt, and adequate reserves for meeting all capital and operating needs. The historical and projected costs are input into a financial rate model using reasonable assumptions for future growth and inflation. The financial rate models are used to determine the utility rates needed to meet all current and projected cost obligations. The main objective of rate development is to make sure the

utility is completely self-sufficient and the rates charged cover the full cost of each service delivered.

On an annual basis, the Department of Finance coordinates the development of a cost allocation plan with the assistance of outside consultants. The cost allocation plan identifies the indirect and direct costs for each department and calculates a cost rate that can be used to cover the full cost of providing a service. The Department of Utilities meets with the Budget Office and the consultants each year to review the methodology and documentation used to develop the allocation of these costs to DOU. The cost allocation is incorporated in the financial rate model discussed above.

The Department of Utilities (DOU) is currently working with consultants to develop a more robust and accurate rate modeling system for all its funds.

Timeline of Events:

In 2007, the City Manager's Office and DOU requested a legal opinion from the City Attorney's Office whether certain past and ongoing practices were consistent with the substantive requirements of Proposition 218. Some of the ongoing practices predated the adoption of Proposition 218.

In March of 2008, the City Attorney's Office issued a confidential opinion memorandum to the City Manager's Office and DOU that provided legal advice and recommendations with respect to the various issues presented by DOU.

Subsequent to receipt of the City Attorney opinion memorandum, DOU retained Nolte Associates to review cost data associated with practices identified by DOU as potential Proposition 218 violations and prepare a report quantifying the cost associated with various practices identified by DOU. Nolte Associates provided DOU with a draft report in May of 2008.

A timeline of events pertaining to potential Proposition 218 issues and DOU can be found

in Attachment 2.

Proposition 218 Issues Raised in Grand Jury Report:

The Grand Jury report issued on January 6, 2010 indicates that the Grand Jury received a complaint in July of 2009, which led to the Grand Jury's investigation into whether some uses of the DOU ratepayers funds complied with the substantive mandates of Proposition 218. The Grand Jury investigation and report utilized information from the Nolte Associates draft report to identify the following practices as City programs that improperly benefited from DOU ratepayer subsidies:

- Providing water service to City parks and other City facilities at a significantly discounted rate.
- Providing solid waste disposal services for City facilities and events without reimbursement from the general fund.
- Utilizing approximately \$2,000,000 of drainage rate revenues to help fund the City's purchase of property for the proposed "Natomas Auto Mall" site.
- Contributing ratepayer funds on a periodic basis to an economic development capital improvement program to help fund utility infrastructure for development projects.
- Utilizing DOU personnel and equipment to perform work for non-DOU facilities without reimbursement.

Actions Taken:

Several actions already taken with respect to DOU charges and services have reduced or eliminated any subsidy occurring as a result of some of the practices described in the Grand Jury report, including the following:

- DOU has worked closely with the Parks Department to incrementally eliminate special water rates over the course of the next 15 years. This phased approach was undertaken to lessen the significant general fund impact.
- DOU went to the Utilities Rate Advisory Commission in 2009 to restructure water rates and City Council approved these in June 2009.

- As of FY2010, DOU no longer provides services for events without reimbursement.
- As of FY2010, DOU no longer contributes ratepayer funds to the economic development capital improvement program to fund utility infrastructure for development projects.
- As of FY 2010, DOU reduced the citywide illegal dumping service in half.
- As of FY 2010, DOU no longer allows use of its personnel or equipment to perform work for non-DOU facilities without reimbursement of funds or trade of in-kind services.
- As of FY2011, DOU will no longer provide solid waste disposal services to City facilities without reimbursement.

Issues Still Pending:

Staff has identified several other potential Proposition 218 issues through its continuing probe. With the implementation of the Customer Information System (CIS), the Department has new tools to identify, audit and address billing issues.

Ten service impacts by Prop 218 pending resolution will be addressed in the upcoming budget process for FY2011 (see Attachment 3), including:

- **Subsidized Water Rates:** An MOU is in place to phases Parks to the full rate in 15 years. DOU is working with the departments of Transportation and Convention, Culture and Leisure to convert to the standard rate in FY2011.
- **Solid Waste/Recycling Service to City Departments:** A review of accounts is being completed. Staff will be working with affected Departments to bill services beginning in FY2011.
- **Drainage Billing for Parks:** Recent auditing conducted by DOU indicates that City parks are being undercharged for drainage service. Staff is completing an analysis of Parks accounts and will be working with Parks to have all accounts accurately billed.

- Illegal dumping pickup and litter containers citywide.

Next Steps:

- Staff continues to work on a proposed implementation plan to address all remaining subsidy issues and will return to City Council with regular updates.
- Staff will bring forward recommendations to all unresolved items to City Council as part of the FY2011 budget development process.
- Staff will also return in March 2010 to City Council with recommended responses to the Grand Jury report.

The Department of Utilities intends to continue to review its policies and practices to ensure that any further potential 218 issues that may arise are addressed and brought to City Council's attention.

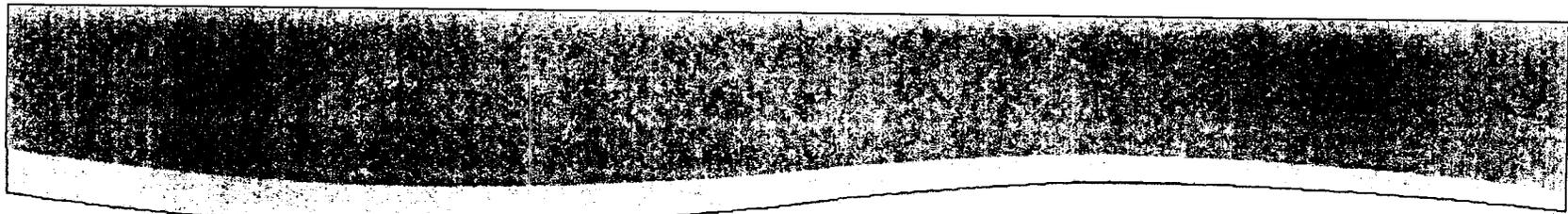
TIMELINE OF EVENTS[Back to Table of Contents](#)**Attachment 2**

Summer 2007	City Manager and DOU request legal opinion from City Attorney's Office regarding past and ongoing practices in regards to Proposition 218.
March 2008	<ul style="list-style-type: none"> • City Attorney's Office issues a memo on 3/18/08 with a legal opinion regarding the issues raised by DOU and City Manager's Office. • DOU Director requests Division Managers and staff to compile a list of potential 218 violations • DOU retains Nolte Associates to review potential violations and quantify the costs of the potential violations to the Utilities funds.
May 2008	Nolte Associates provides draft report to DOU
September 2008	DOU Staff begins to review special water rates, such as Parks and SMUD rates and works with Parks Department to create an MOU to bring Parks up to paying the standard water rate.
December 2008	DOU Staff presents Water Rate Restructure that would eliminate special water rates for outside agencies. Council does not approve the rate restructure.
June 2009	<ul style="list-style-type: none"> • Council approves Water Rate Restructure that eliminates special water rates except for City Parks and Medians • DOU signs MOU with Parks Department to convert Parks to the standard water rate over the next 15 years
July 2009	Complaint is filed with the Sacramento County Grand Jury
January 6, 2010	Sacramento County Grand Jury releases report
January 15, 2010	Howard Jarvis Taxpayers Association and Sacramento County Taxpayers League file a lawsuit against the City of Sacramento
January 26, 2010	DOU provides Council with an update of potential 218 issues
February 11, 2010	DOU anticipates bringing forward issues impacting General Fund to Council as part of the Budget process
March, 2010	DOU anticipates bringing a proposed response to the Sacramento County Grand Jury Report to Council
April 6, 2010	Sacramento County Grand Jury response due.

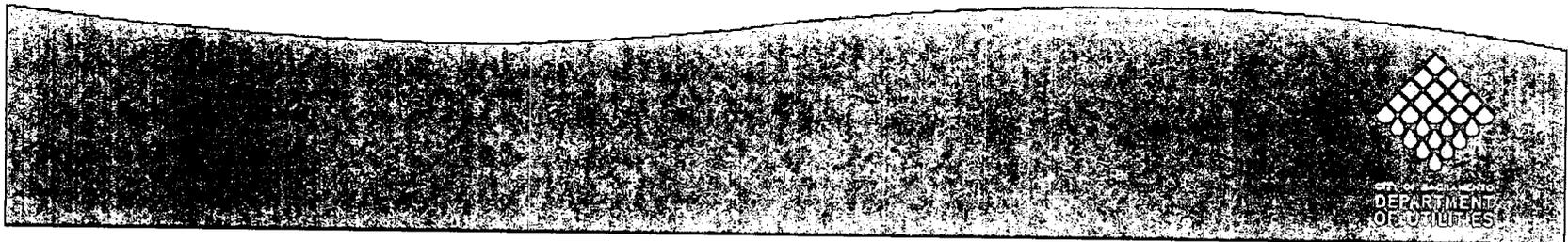
SERVICE IMPACTS BY PROP 218 - FY2010/11

Attachment 3

Ongoing Cost of Service Issues	Notes:
Subsidized Water Rates	Parks and DOU have currently a 15 year phase-in plan.
Solid Waste/Recycling Service to City Facilities	Comprehensive service audits being performed to verify the costs to the various departments.
Illegal Dumping Citywide Service	Currently one crew only. Reduced in half FY09/10.
Brown Autolift Toters	Throughout City
Concrete Litter Cans - Manual	Throughout City
Drainage billing to Parks	Comprehensive audits will be conducted to verify costs.
Recycling in the Parks	Service Audits are being conducted.
Miscellaneous Unfunded Development Review	
Green Waste downtown - Seasonal "leaf season"	For Downtown leaf collection
One Time Cost of Service Issues	Notes:
Natomas Automall	Drainage Funds used in Dec 2002 to acquire proposed AutoMall property. Land swap in 2005 for Youth baseball complex- One Time cost



Department of Utilities and Proposition 218 Update



Agenda

- Background
- Time Line
- Issues and Status
- Next Steps



CITY OF SACRAMENTO
DEPARTMENT
OF UTILITIES

Background

- Proposition 218
- Grand Jury Report
- How Utilities Rates are Set



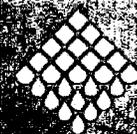
CITY OF SACRAMENTO
DEPARTMENT
OF UTILITIES

Timeline

Summer 2007	City Manager and DOU ask CAO for a legal opinion regarding potential 218 violations
March 2008	<ul style="list-style-type: none">•CAO responds with memo•DOU Director requests staff compile list of potential violations and hires Nolte to compile a report
Sept 2008	Staff works with DPR to put together MOU for DPR to pay full water rate
June 2009	<ul style="list-style-type: none">•Council approves new water rates that eliminate special rates, except for Parks•DOU/DPR MOU is finalized, Park will transition to full rate in 15 yrs
July 2009	Grand Jury Complaint filed
Jan 6, 2010	Grand Jury Report released

Actions Taken

- Working with affected Departments to move them to standard rates
- Fee for service
- No contribution to Economic Development CIP



CITY OF SACRAMENTO
DEPARTMENT
OF UTILITIES

Remaining Service Impacts

- Subsidized rates
- Garbage/Recycling Service for City Departments
- Recycling in the Parks
- Drainage for Parks
- Illegal Dumping
- Unfunded Development Review
- Garbage removal (brown toters and concrete containers)
- Downtown Green Waste Removal
- Use of Drainage Funds to purchase land (one time impact)



Next Steps

- Provide Recommendation for FY2010/2011 Budget Process
- Return to Council in March with Grand Jury Response
- Provide regular updates

