Dublin San Ramon Services District
Water, wastewater, recycled water

Policy

Policy No.: P400-16-1	**Type of Policy:** Finance
Policy Title: Rate Policies and Guidelines	
Policy Description: Provides guidance and consistency in decision-making for developing and adopting rates.	
Approval Date: 6/7/2016	**Last Review Date:** 2016
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It is the policy of the Board of Directors of Dublin San Ramon Services District:

To ensure that rates are developed using a generally-accepted methodology, to provide financial stability, to achieve rate stability, to ensure public well-being and safety and with consideration of the rate impact as outlined in the following guidelines.

The Rate Policies and Guidelines are attached hereto and made a part hereof as if written in full in this policy.

The following rate policies and guidelines have been developed to provide guidance and consistency in decision-making for the District's management team. These policies and guidelines will assist the District in achieving financial and rate stability from year-to-year for the water and wastewater Enterprises. The proposed policies and guidelines should be reviewed periodically to determine if they are still relevant and appropriate. The policies framework is shown below:

Dublin San Ramon Services District
Rate Policies and Guidelines

Rate Setting Methodology

1. **Rates Should Be Established Utilizing a "Generally Accepted" Rate Setting Methodology.**

First and foremost, rate setting must conform to all legal constraints established for the District. In addition, when reviewing rates it is important to use a methodology that is "generally accepted" in the financial and rate setting community as well as the water and wastewater industries. This will assure a legally defendable approach as well as consistency of the analysis over time.

1.1. It is recommended the District use the following "generally accepted" approaches to establish rates.

- Revenue requirement analysis
- Cost of service analysis
- Rate design analysis

REVENUE REQUIREMENTS:

1.1.1 Revenue requirements will be established on a "cash basis" approach. The "cash basis" approach includes operation & maintenance (O&M) expenses, taxes/transfer payments, debt service (P&I), and funding for replacement of capital assets. The revenue requirements, as defined herein, are the basic components. Revenue requirements should also include any other cost items requiring funding (e.g. bond reserves) or needed to operate the Enterprise on a financially stable basis (e.g. accumulation or reduction in working capital).

1.1.2 Currently, revenue requirements include the impact of capacity fee “buy in” revenue. This “buy in” will be eliminated at District buildout. The District should plan accordingly and gradually eliminate the impact of the revenue from the “buy in” component on revenue requirements. The funding for asset replacements should be 100% funded by rate revenue by the end of the 10 year planning period (2027).

1.1.3 Costs associated with each of the District’s funds (i.e. Enterprise, Replacement, Expansion, etc.), for both water and wastewater, shall be tracked and budgeted separately for use within the revenue requirements.

1.1.4 At a minimum, revenues and costs will be projected for a six-year projected test period.

1.1.5 Projections of O&M costs should include any estimated incremental O&M costs associated with future capital improvements.

1.1.6 Costs associated with mandated program requirements will be identified and included within the cash basis approach.

COST OF SERVICE:

1.2.1 A cost of service study will be utilized to allocate costs equitably to customer classifications of service.

1.2.2 The cost allocation methodology will utilize techniques that are “generally accepted” by the industry (e.g. American Water Works Association, American Public Works Association, etc.).

1.2.3 The water cost of service will, at a minimum, consider the following cost components:

- ✓ *Commodity costs* – those costs that vary with the total amount, or flow of water consumed by a customer over an extended period of time (e.g. electricity and chemicals).
- ✓ *Capacity costs* – those costs that vary with maximum demand, or the maximum rates of flow to customers (e.g. sizing facilities to meet peak demands).
- ✓ *Public fire protection costs* – those costs related to the public fire protection function (e.g. hydrants and over-sizing of mains).
- ✓ *Customer related costs* – those costs that vary with the number of customers on the system (e.g. postage, meter maintenance expense).
- ✓ *Revenue related costs* – those costs associated with the amount of revenue received by the water enterprise fund (e.g. a gross proceeds tax, delinquent fees).

1.2.4 The wastewater cost of service will, at a minimum, consider the following cost components:

- ✓ *Volume costs* – those costs that vary with the total flow of wastewater contributed by a customer over an extended period of time.

- ✓ *Strength costs* – those treatment-related costs associated with the strength of wastewater (e.g. biochemical oxygen demand and suspended solids) will be determined separately and will depend on the class of service and type of service provided (local vs. regional).

- ✓ *Customer related costs* – those costs that vary with the number of customers on the system (e.g. postage).

- ✓ *Revenue related costs* – those costs associated with the amount of revenue received by the Wastewater Enterprise fund (e.g. a gross proceeds tax, delinquent fees).

RATE DESIGN:

1.3.1 Rate designs will be reflective of the District's needs and also reflect the greater public purpose and policy goals of the District's Board (e.g. economic development, conservation, ability to pay, etc.).

1.3.2 Rate structures will recognize the appropriateness of both a fixed charge and a variable charge in order to provide the correct price signal to the District's customers. Fixed charges provide the District with a level of revenue stability and they are preferred by rating agencies as the method to best ensure debt coverage, while customers generally prefer variable charges, which allow them to control the amount of their bill. The balancing of these two competing rate components should be considered when reviewing rate structures. For water rates, variable rates will be established at no less than 70% of the total revenue requirement while the District remains subject to CUWCC BMP 11.

1.3.3 Rates will be set at a level that recovers necessary costs, by classification, yet flexible enough to accomplish the District's objectives (e.g. public purpose programs).

1.3.4 Rates should be designed to be equitable and detailed to a level to reflect the service provided (e.g., private fire protection, multi-family services, etc.).

1.3.5 Rates will be set at a level to ensure that bond covenants are met without reliance on capacity fees.

Financial Stability

2. The District Should Continue to be Managed to Maintain Financial Stability Over Time.

The District, like any other business, should strive to maintain financial stability over time, as it has done in the past. Financial stability is not only a prudent financial management goal; it can also minimize financial costs in the long-term (e.g. unnecessary borrowing). Above all, financial stability will provide the community with the confidence of knowing a strong, consistent management team is managing the Enterprise.

2.1 Financial Policies and Measures Will be Developed to Measure, Manage, and Achieve Financial Stability.

RESERVES:

2.1.1 The minimum and target reserve levels in the Enterprise funds (as defined in the Financial Reserves policy) are indicators of the financial health of the Enterprise and will be used to determine when certain actions should be taken.

- ✓ **Fund is below the target working capital level** - If the Enterprise fund's working capital is projected to go below the minimum reserve level and stay below that level in the subsequent year, a rate increase shall be considered in order to maintain the financial stability of that fund.

- ✓ **Fund is above the target working capital level and revenues exceed expenses** - If the Enterprise fund's working capital is projected to be in excess of the working capital target and the rate revenues in the fund exceed the sum of the O&M expenses and replacement transfer, a rate decrease shall be considered to bring the working capital target between the minimum and target levels.

- ✓ **Fund is above the target working capital level and expenses exceed revenues** - If the Enterprise fund's working capital is projected to be in excess of the working capital target and the rate revenues in the fund are less than the sum of the O&M expenses and replacement transfer, the excess reserves will be used to cover expenses. In these circumstances, current rates are not covering current costs, and it is likely that a rate increase will be needed in future periods.

CASH FLOW:

2.2.1 Except as noted in section 2.1, each Enterprise should have annual net income (total revenue less O&M, taxes, debt service, and replacement funding) greater than or equal to zero unless the Board has made a policy decision to utilize Rate Stabilization Reserves.

DEBT SERVICE COVERAGE:

2.3.1 The Debt Service Coverage Ratio is an important financial measure that is reviewed by banks and bond companies to show the Enterprise's ability to make debt payments. The ratio is the Enterprise's Net Operating Income over the Total Debt service. Net Operating Income is gross income less operating and maintenance expense. For financial planning purposes, the annual debt service coverage ratio shall be the highest ratio, by Enterprise, for the District's current debt covenants.

2.3.2 For all debt issues with a legal bond covenant, when the debt service coverage ratio falls below the legal requirement the District's Board will abide by the specific covenants related to the bond issue.

2.3.3 While rates will be developed to achieve contractual debt coverage levels, the overall target for debt service coverage is 1.60, and will include revenue received from capacity reserve fees.

CAPITAL IMPROVEMENT FUNDING FROM RATES:

2.4.1 Each Enterprise should adequately fund through its rates, an amount sufficient for the replacement of District assets.

2.4.2 Replacement funding is determined based upon capital asset replacement needs and Capital Projects to be in compliance with Financial Revenues policy P400-15-1.

Rate Stability

3. Rates Should be Stable Over Time.

Financial stability of an Enterprise also provides rate stability. Rate stability reinforces that costs are being managed and controlled, thereby gaining customers' confidence of the management team's credibility.

3.1 Rates Should Not Only be Stable in Their Ability to Generate Sufficient Revenues, but also in the Customer's Perception of the Rate Changes from Year to Year.

3.1.1 The District should review rates during the biennial budget process to assure that they provide sufficient revenues. This does not imply that rates must be adjusted, simply that the rates are reviewed in the context of these policies to assure that they are adequately funding each Enterprise.

3.1.2 Rate reviews will consider a six-year projected period to attempt to stabilize and minimize rates over time.

3.1.3 The District will attempt to minimize impacts to customers when rate adjustments are needed.

3.1.4 A comprehensive rate study will be conducted at least every five years in order to assess the fairness of the rates to the District's ratepayers and to ensure that the necessary revenue is available for the District's operating and replacement needs.

Public Well-Being and Safety

4. The District will maintain its facilities at a level that will provide for the public well-being and safety of the residents.

The District's facilities will be maintained at a level that assures system reliability and efficiency. A well thought out renewal and replacement program will extend the life of the system that will in turn reduce infrastructure costs in the long-term.

4.1 Sufficient funding should be made available to provide for adequate renewal and replacement of capital assets and equipment.

4.2 The District will adequately fund costs for meeting current industry standards and regulations (e.g. Safe Drinking Water Act, Clean Water Act, NPDES II, etc.).

4.3 The District will fund improvements according to an adopted Capital Improvement Program.

5. The District will consider the impacts of rates on their customers and financial and operating needs will be balanced against the rates and financial impacts.

Rates are one of the most important ways in which the District communicates with its customers, and should follow these guiding principles.

5.1 Rates will be easy to understand and the District will attempt to keep the frequency and magnitude of rate adjustments to a minimum.

5.2 Rates will be reviewed for their overall competitiveness.

5.3 Rates will be balanced to meet the varying competing needs.