

FREQUENTLY ASKED QUESTIONS REGARDING THE TOWN'S WATER RATES

What do the Town's water service charges fund?

The Town operates and maintains a potable water distribution system to serve its residents and water users. It is a complex system with varying topography and 21 separate but interconnected pressure zones. The infrastructure network includes 108 miles of water mains, 18 water tanks, 14 water pump stations and over 7,500 various assets such as water meters, fire hydrants, and valves. The Town purchases its water from the San Francisco Public Utilities Commission (SFPUC). The Town pumps and delivers water to approximately 4,270 customers, nearly all of whom are single-family residential customers.

The revenue collected from the Town's water service charges is used to pay for the cost of providing water service, and may not be used for any other purpose. The cost of providing water includes not only the water we purchase, but the infrastructure that treats and delivers the water, water utility personnel, and our water conservation and efficiency and water demand management programs to ensure that there is safe and reliable water to meet the demands of all of our water customers twenty-four hours a day, seven days a week.

Why is the Town considering increasing its water rates?

The Town is entirely reliant on the SFPUC for its potable water supply. The SFPUC manages a complex water supply system stretching from the Sierra to the City of San Francisco and featuring a complex series of reservoirs, tunnels, pipelines, and treatment systems. The Hetch Hetchy watershed, an area located in Yosemite National Park, provides approximately 85% of SFPUC's total water needs. The SFPUC delivers treated wholesale water to the Town primarily from its Hetch Hetchy system, but also delivers water from local watersheds in Alameda County and the Peninsula.

Historically, the SFPUC's annual rates have increased greater than the rate of inflation because of the Hetch Hetchy Water Supply Improvement Plan (WSIP). The WSIP is a nearly \$5 billion capital improvement plan that improves the infrastructure reliability of the regional Hetch Hetchy water supply facilities. The recent improvements done by the SFPUC were seismic improvements, including the addition of a 5th transmission line crossing the bay, and significant dam rehabilitation.

The cost of purchased water is approximately 40% of the Town's cost to operate the water system. The per unit cost that SFPUC charges its 26 wholesale water customers, including the Town, has nearly doubled since 2011. The Town has increased its water rates over the past several years to help fund these water purchase cost increases and to fund needed water capital improvements, with increases of 14% in April 2011, and 13% in January 2012 through 2015. In addition to these cost increases, the Town has experienced other increases in the costs of providing water service.

The Town is committed to providing the highest quality water at the lowest possible rates for our customers. To meet this commitment, the Town engaged HF&H Consultants, LLC (HF&H) to perform an independent water rate study, and evaluate the infrastructure needs, programs, and operations and maintenance costs of the Town's water services and the rates necessary to recover the costs for those services for the next five years. A cost of service and rate study demonstrates what it costs the Town to provide water service and the appropriate rates to fairly and appropriately allocate the costs of providing water to our customers. Based on the HF&H

rate study, the Town has determined that adjustments in and increases to the rates of its current water service charges are necessary to fully fund its water services. Customers will be receiving a notice in the mail of the proposed rates and a public hearing to be held by the City Council on February 13, 2017, to consider those rate increases.

What action did the Town take in response to the statewide drought?

California is currently in the grips of an extreme drought with record low precipitation. This five-year drought has caused severe impacts across the State, including community water sources running dry, the loss of agricultural production and jobs, depletion of groundwater basins, widespread tree death, and impacts to fish and wildlife. In April 2015, Governor Jerry Brown issued Executive Order B-29-15 mandating State-wide water conservation in response to the persistent, record-setting, severe drought conditions. Under drought regulations established by the State Water Resources Control Board (SWRCB) pursuant to the Executive Order, the Town was ordered to reduce its water consumption by 36% compared to its 2013 water use. The State's compliance period began on June 1, 2015. If the Town failed to meet the 36% reduction mandate, it was potentially subject to fines by the State of up to \$10,000 per day.

In response to the SWRCB regulations, and to avoid the imposition of any State fines, the Town took immediate action to reduce water consumption by adopting an urgency ordinance that established mandatory water use restrictions. The urgency ordinance also included volumetric penalties for violating the Town's excessive water use regulations beginning in June 2015. Under the Town's water conservation ordinance, customers were given an allotment of water appropriate for efficient indoor and outdoor water usage. If a customer exceeded their allotment, they were subject to a volumetric penalty based on the amount of water used in excess of their allotment. The penalties were imposed to gain compliance with the Town's water shortage contingency plan in effect under the urgency ordinance and the state-mandated water use restrictions, and to encourage customers to change their water consumption behavior during this critical period. The volumetric penalties that were adopted by the Town are fully authorized to be imposed pursuant to State law (California Water Code section 377).

If requested, is the Town required to disclose the name, credit history, water usage data, home address, or telephone number of water customers?

High water use customers should be aware that under the California Public Records Act (Government Code section 6254.16(d)) the Town is required to release the name, home address and water usage data of customers using water inconsistent with or in violation of the Town's water shortage regulations, such as those set forth in its Municipal Code and the June 2015 urgency ordinance, if that data is requested pursuant to a Public Records Act request. If the Town receives a valid public records request for information about any such violations, the Town is required to and will comply with the request, and the media may publish that information. The Town fully understands and is sensitive to customers' concerns about the release of their private information. To that end, the Town will only release information which is required to be released by law. The Town takes customer privacy very seriously and has a practice of never voluntarily releasing customer information to a third party unless required to do so by law.

What impact did the drought have on the Town's water rates and revenues?

The Town achieved a 42% reduction in water usage from 2013 in response to the Governor's Executive Order and the SWRCB water reduction mandates. The 42% reduction in water

demand had a significant impact on the revenues that the Town received from its water service charges. To offset this reduction in revenues, in January 2016, the Town added a Revenue Stabilization Charge to its existing volumetric water service charges, and increased its fixed monthly water charges by \$10 per month to stabilize water revenue during the drought. The Revenue Stabilization Charge allowed the Town to continue to operate the water system and provide safe and reliable water service during this period by helping to pay for the lost revenue resulting from the reduction in water use.

Recognizing persistent yet less severe drought conditions throughout California, on May 18, 2016, the SWRCB adopted an emergency water conservation regulation that replaced the prior emergency regulation. The May 2016 regulation that is in effect from June 2016 through January 2017 requires locally developed conservation standards based upon each agency's specific circumstances. It replaces the prior percentage reduction-based water conservation standard with a localized "stress test" approach. Based on the Town's current local conditions, on June 13, 2016, the Town ended mandatory water rationing and implemented voluntary water conservation. The voluntary water conservation period extends through January 31, 2017, with a goal of reducing water usage by 10% compared to 2013 water usage within the Town.

In November 2016, the City Council reviewed the need for the Revenue Stabilization Charge and determined that based on current, improved rainfall conditions, the Revenue Stabilization Charge no longer needs to be imposed. The cessation of the charge will be reflected in customers' December 2016 water bills. The City Council thanks our residents for the significant actions they have taken and sacrifices they have made to conserve water during this historic drought; your achievements are reflected in the 42% reduction in water use the Town was able to achieve while the mandatory restrictions were in place.

What impact did the drought have on the Town's proposed water rates?

The Town is currently in the process of conducting a comprehensive water cost of service and rate study that carefully analyzes the revenues that are necessary to continue to provide our customers with safe and reliable water for the next five years. There have been in-depth reviews of the proposed water rates and rate structure by the City Council at two public study sessions held on September 12, 2016 and November 2, 2016.

Based on the analysis performed by the independent rate consultant, HF&H, it has been determined that the multi-year drought has resulted in both temporary and permanent changes in water demand by our customers. These changes have impacted not only water revenues but the costs of providing water service. Consequently, the Town is proposing some adjustments to the rate structure of the volumetric service charges that it imposes.

The impact of the rate changes for any one ratepayer will vary depending on their particular usage for any given month. The City Council will be reviewing the proposed rates at a public hearing to be held on February 13, 2017. Customers will receive a notice of when the City Council will be holding the public hearing on the proposed rates as well as a detailed explanation of the proposed rates. A copy of the HF&H water cost of service and rate study is available on the Town's website at <http://www.hillsborough.net/186/Water-Sewer-Services>. The City Council welcomes and encourages public input and participation in this process.

Why are the Town's rates higher than those imposed in neighboring communities?

Comparing rates among neighboring jurisdictions is never an “apples-to-apples comparison.” Rate structures and annual operating costs vary significantly among jurisdictions. The unique qualities of the Town's topography, size, and household density, among other things, reasonably result in the Town's rates being higher than surrounding communities. The Town's water system is complex for a system its size. The steep topography results in numerous pressure zones, which in turn require more storage reservoirs and pumps. The operation of these storage reservoirs and pumps must be coordinated with sophisticated instrumentation and staff, leading to higher costs per household than neighboring communities. Most notably, lot sizes in Hillsborough are more than twice as large as our neighboring communities. Sparser development means that there is more infrastructure required per household, which raises the cost of service, but with fewer customers with whom to spread the cost.

In addition, capital improvement spending to renew and replace aging infrastructure differs significantly among communities depending on the system's size, age, and where in the spending cycle the neighboring communities may be. During the five-year planning period of HF&H's cost of service and rate study, the Town is investing heavily in its aging water system infrastructure to improve reliability (e.g., reduce pipeline breaks and leaks). Delaying these needed improvements would result in higher costs to our customers in the future.

Do the Town's water rates comply with Proposition 218?

Yes, the Town believes that our current and proposed water rates comply with two constitutional mandates—Article XIII D, section 6, commonly referred to as Proposition 218, and Article X, section 2 of the California Constitution. Proposition 218 mandates that we proportionately allocate and not charge our customers more than the cost of providing water service. Article X, section 2 mandates that we protect and conserve the water resources of our state. Our current and proposed rate structures proportionately allocate the costs of providing water service to those who place the most demands on our water system by using greater amounts of water, and, therefore, generate additional costs to the Town for providing water service.

Our rates are also structured to comply with state law requirements. We have an obligation to develop long-term water management strategies that incorporate water conservation and resource management as key components of preserving our water supplies.

In 2009, the state legislature adopted SB 7X7 which proposes to protect water supplies by mandating a statewide twenty percent reduction in urban per capita water use by 2020. Urban retail water suppliers such as the Town are required to reduce per capita water use within their service area by twenty percent by 2020. Tiered rates send water users a “price signal” that by using more water they will pay a higher price for it, thereby indirectly encouraging customers to conserve.

In addition to current constitutional and legislative mandates, under a new plan being considered by the SWRCB, urban water agencies such as the Town would face an increasingly expansive set of water conservation laws and regulations. The plan, which also addresses water use in agriculture and other sectors, was developed jointly by five state agencies, including the SWRCB and the Department of Water Resources.

The draft plan was developed in response to Executive Order B-37-16, which Governor Brown issued May 9, 2016, to address drought preparedness and long-term water conservation. While

a number of the draft plan's provisions would be implemented under already existing authorities, other elements would require either rulemaking by state agencies or new legislation.

During the past two years, water supply agencies have had to deal with challenging emergency water conservation regulations adopted by the SWRCB in the face of a lingering and serious statewide drought. The draft plan moves away from the piecemeal emergency regulatory approach by calling for a new permanent water conservation regime for the State.

A key element of the draft plan involves a requirement that the State's 410 urban water suppliers meet new water use targets, which would be set locally based on state standards applied to unique local conditions. The proposed new approach is designed to take into account the unique climatic, demographic, geographic and land-use characteristics of each urban water agency's service area. The Executive Order requires that the new water use targets build on existing statutory requirements that the State achieve a twenty percent reduction in urban water usage by 2020. Under the proposed regime, DWR and the SWRCB would develop new standards by 2020 to address four sectors:

- Indoor residential per capita water use
- Outdoor irrigation
- Water lost through leaks
- Commercial, industrial and institutional water use

Local urban water suppliers would calculate their own unique water use targets based on the state standards, and would be required to achieve compliance by 2025.

The draft plan implementing the Executive Order contains a number of other elements, including:

- Potential extension of the SWRCB's current emergency water conservation regulations, which are in effect through February 2017, for an additional 270 days, depending on ongoing drought conditions.
- Establishment of permanent monthly urban water use reporting requirements and permanent prohibitions on wasteful water practices, such as hosing down sidewalks, through SWRCB rulemaking.
- New measures achieved through rulemaking by several agencies to reduce water lost through leaks.
- New legislation requiring urban water suppliers to submit "Water Shortage Contingency Plans" to the State, to conduct a "Five-Year Drought Risk Assessment" every five years, and to submit a water budget forecast annually to the State.
- New actions to improve drought preparation among small water suppliers and rural communities.
- New legislation placing water use efficiency and drought planning requirements, such as water budgets and water management plans, on suppliers of water to agricultural users.

Information on the draft plan is available on the SWRCB's website at <http://www.water.ca.gov/wateruseefficiency/conservation/>. If the draft plan is implemented, the Town's proposed rates will also assist the Town in meeting these new regulatory requirements.

Are tiered water rates legal and does the Town intend to continue to impose tiered water rates?

The legality of tiered water rates under Proposition 218 was recently reviewed and affirmed by a court of appeal in *Capistrano Taxpayers Association v. the City of San Juan Capistrano*. In reviewing the constitution, the court of appeal stated numerous times throughout the opinion that tiered rates are legal under Proposition 218. However, in that case, the city's rate study failed to demonstrate that its tiered rates aligned with its costs of providing water service. The Town believes that our current and proposed rates fully comply with Proposition 218. The tiers are designed to recover the incremental costs incurred by the Town in sizing, operating and maintaining our water system to meet the demand of those who use the most water and place the greatest demands on our water system—i.e., more pipe and pumping capacity to maintain a high peak water demand when people are using large volumes of water. The rates also incidentally encourage people to conserve by sending a price signal that the more they use the more they will pay.

Additionally, we take a proactive approach with regard to our rates. We continually monitor our costs and expenses to achieve savings for our customers and ensure that we are able to provide safe and reliable water service. After determining our revenue needs, we evaluate whether rate increases are necessary and how best to fairly and appropriately allocate those costs. We have engaged an independent rate consultant, HF&H, to prepare a water cost of service and rate study to determine the best rates to meet our future costs, manage our water resources, and meet the needs of our customers. Based on the recommendations in the HF&H water cost of service and rate study, the Town is proposing to continue to impose tiered rates. A copy of the study is available on the Town's website at <http://www.hillsborough.net/186/Water-Sewer-Services>.

How can I learn more about the proposed water rates and water conservation?

The HF&H water cost of service and rate study is available on the Town's website at <http://www.hillsborough.net/186/Water-Sewer-Services>. For additional information on the Town's water conservation and efficiency program, please visit our website at <http://www.hillsborough.net/249/Water>.