



# Santa Clara Valley Water District

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**File No.:** 20-1020

**Agenda Date:** 11/24/2020

**Item No.:** 5.1.

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## BOARD AGENDA MEMORANDUM

### **SUBJECT:**

Overview of the FY 2021-22 Groundwater Production Charge Setting Process and Review of 10-Year Water Rate Projection Assumptions.

### **RECOMMENDATION:**

- A. Receive an overview of the Fiscal Year 2021-22 Groundwater Production Charge setting process; and
- B. Review and provide feedback on the 10-year Water Rate Projection Assumptions.

### **SUMMARY:**

This agenda item presents the Fiscal Year (FY) 2021-22 groundwater production charge setting process and provides an update on key issues that pertain to setting the charges that would take effect July 1, 2021 (Attachment 1).

Each year, the Board establishes groundwater production charges for four zones of benefit (Zone W-2 in the North County and Zones W-5, W-7, and W-8 in the South County) in accordance with Section 26 of the District Act. Although not specified under the District Act, the Board also sets surface water charges, recycled water charges, treated water surcharges, and the amount of the State Water Project cost to be recouped through the State Water Project tax, within the framework of the groundwater charge setting process.

The Water Utility taxing and pricing policy, Resolution 99-21 (Attachment 2) and legal requirements, guide staff in the development of the overall structure for these charges.

The FY 2021-22 surface water charge setting process will be conducted consistent with Proposition 218's requirements for property-related fees for water services as detailed in Board Resolution 12-10 (Attachment 3).

In late 2017, the State Supreme Court found that proposition 218 is not applicable to groundwater production charges. However, the Court did determine that Proposition 26 does apply to groundwater charges. This means that for the groundwater charge to qualify as a nontax fee under Proposition 26, it must satisfy both of the following requirements:

1. That the groundwater charge be established in an amount that is no more than necessary to cover the reasonable costs of the government activity, and

2. The manner in which those costs are allocated to a payor bear a fair or reasonable relationship to the payor's burdens on, or benefits received from the government activity.

The FY 2021-22 groundwater production charge setting process will be conducted consistent with Proposition 26 requirements. Procedural requirements for property related fees and charges under Proposition 218 like holding a public hearing and noticing well owners are consistent with the District Act and would continue.

Under the District Act, Section 26.6, an annual report referred to as the Report on Protection and Augmentation of Water Supplies (PAWS) is to be filed with the Clerk of the Board on or before the first Tuesday in April. A public hearing must be held on or before the fourth Tuesday in April and it must be noticed to the public in a newspaper of general circulation at least 10 days in advance. In addition, all well owners and well operators on record are notified of proposed groundwater production increases in writing, and of the public hearing at least 45 days in advance. Groundwater production charges must be determined for the ensuing fiscal year prior to July 1 of the ensuing fiscal year. For each zone of benefit, groundwater production charges must be fixed and uniform per acre-foot for agricultural water and fixed and uniform per acre-foot for all water other than agricultural water.

Under the District Act, Section 26.3, groundwater production charges are to be used for the following purposes:

1. Pay for construction, operation, and maintenance of imported water facilities;
2. Pay for imported water purchases;
3. Pay for constructing, maintaining, and operating facilities which will conserve or distribute water including facilities for groundwater recharge, surface distribution, and purification and treatment; or
4. Pay for debt incurred for purposes 1, 2 and 3.

The Board may establish groundwater benefit zones in accordance with the District Act. The objective of establishing various groundwater benefit zones is to recover costs for the benefits resulting from District activities within that zone. The benefits and costs which are apportioned to zones by customer class are presented in the annual PAWS report.

The groundwater production charge reflects the benefit of District activities to protect and augment groundwater supplies and is applied to water extracted from the groundwater basin in Zones W-2, W-5, W-7, and W-8. Zone W-2 encompasses the Santa Clara groundwater subbasin north of Metcalf Road or the North County. Zone W-5 overlays the Llagas subbasin from northern Morgan Hill south to the Pajaro River. Zone W-7 overlays the Coyote Valley south of Metcalf Road to northern Morgan Hill, and W-8 encompasses the area below Uvas and Chesbro Reservoirs.

The District protects and augments water supplies for the health, welfare, and safety of the community. County-wide, groundwater replenished by the District makes up, on average, two-thirds of the groundwater used by residents, retailers, and businesses. The District replenishes the groundwater basins with local water and purchased water imported from the Sierra Nevada mountains and conveyed thru the San Francisco Bay Delta Estuary. The activities undertaken by the District to acquire, monitor, recharge, and protect the water supply are funded, in part, through

groundwater production charges.

### **Water Usage Trend**

District managed water use for FY 2019-20 is estimated to be approximately 232,000 acre-feet (AF), roughly 7,000 AF lower than budgeted, but 16,000 AF higher than prior year, due to a dry winter and dry spring. If the dry winter and dry spring were to repeat for the current year FY 2020-21, then there would be a 2,000 AF water usage excess versus budget, which would translate to an estimated \$3.2 million in revenue. The current projection for FY 2021-22 is 232,000 AF, which is flat compared to the FY 2019-2020 estimate.

Staff will carefully monitor monthly water use actuals and work closely with the water retailers during the upcoming rate setting process to modify the water usage forecast as necessary.

### **FY 22 Planning Scenario Ideas**

Staff anticipates the need to provide several groundwater charge projection scenarios for Board consideration during this rate setting cycle. Staff would appreciate Board feedback on the following assumptions and scenario ideas:

Baseline assumptions:

- Delta Conveyance SWP portion at 2.73%
- Purified Water Expansion (9 to 12kAF) via P3 by FY26
  - Assume 100% debt financed by P3 entity
- Los Vaqueros (Transfer Bethany Pipeline)
- FY22 increase in Agricultural Rate as a percentage of non-agricultural rates
- Pacheco Reservoir Expansion

Scenarios:

- Delta Conveyance SWP portion at 5% (CVP)
- Sites Reservoir Expansion
- Los Vaqueros Reservoir Expansion
- Pacheco Reservoir Expansion Funding Alternatives

Based on Board feedback, various groundwater charge projection scenarios will be provided for Board consideration.

### **Open Space Credit**

The Valley Water Board has historically recognized that agriculture brings value to Santa Clara County in the form of open space and local produce. In an effort to help preserve this value, the District Act limits the agricultural charge to be no more than 25% of the M&I charge. In 1999, to further its support for agricultural lands, the Board put a policy in place to further limit the agricultural groundwater production charge to no more than 10% of the M&I charge. The agricultural community

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currently benefits from low groundwater charges that are 2% of M&I charges in North County Zone W -2 and 6% of M&I charges in South County Zone W-7. The FY 2020-21 agricultural groundwater production charge is \$28.86/AF, or 6% of the Zone W-7 M&I charge of \$481.00/AF. According to Section 26.1 of the District Act, agricultural water is “water primarily used in the commercial production of agricultural crops or livestock.”

The credit to agricultural water users has become known as an “Open Space Credit.” It is paid for by fungible, non-rate related revenue. To offset lost revenue that results from the difference between the adopted agricultural groundwater production charge and the agricultural charge that would have resulted at the full cost of service, Valley Water redirects a portion of the 1% ad valorem property taxes generated in the Water Utility, General and Watershed Stream Stewardship Funds.

In April 2019, the Board directed staff to eliminate the discretionary portion of the Open Space Credit starting in FY 2021-22, after a two-year period in which a coalition of agricultural industry and other stakeholders would work to pursue an alternative revenue source to replace the discretionary portion of the Open Space Credit (See Attachments 4 and 5). As such the agricultural groundwater charge would increase to the maximum allowed by the District Act at 25% of the M&I charge for FY 2021-22. Doing so will require an update to the Board’s Pricing Policy which currently limits the agricultural groundwater production charge to 10% of the M&I Charge.

### **Planned Groundwater Charge Setting Schedule**

Below are the key dates for the groundwater charge setting process as tentatively scheduled. The schedule calls for adopting the budget and groundwater production charges on May 11, 2021.

- Jan 4: Agricultural Advisory Committee Meeting (Preliminary Groundwater Production Charge Analysis)
- Jan 12: Board Meeting (Preliminary Groundwater Production Charge Analysis), CIP Work Study
- Jan 13: Water Retailers Meeting (Preliminary Groundwater Production Charge Analysis)
- Jan 20: Water Commission Meeting (Preliminary Groundwater Production Charge Analysis)
- Feb 9: Board Meeting (Review draft CIP & Budget development update)
- Feb 26: File “Report on Protection & Augmentation of Water Supplies” (PAWS) with District Clerk of the Board & mail well owners and surface water users notice
- Mar 17: Water Retailers Meeting (Groundwater Production Charge recommendation)
- Mar 23: Board Meeting - Budget development update (2nd Pass)
- Mar 30: Landscape Committee Meeting (Groundwater Production Charge recommendation)
- Apr 5: Agricultural Advisory Committee Meeting (Groundwater Production Charge recommendation)
- Apr 7: Water Commission Meeting (Groundwater Production Charge recommendation)
- Apr 13: Board Meeting (Open Public Hearing on Groundwater Production Charges)
- Apr 15: Board Meeting (Continue Public Hearing on Groundwater Production Charges to South County)
- Apr 27: Board Meeting (Continue and Conclude Public Hearing)
- Apr 28-29: Board Meetings (Budget Work Study Sessions)
- May 11: Board Meeting (Adopt Groundwater Production Charges, Budget & CIP)

**FINANCIAL IMPACT:**

Depending on the direction provided by the Board, there could be a future financial impact to the Water Utility.

**CEQA:**

CEQA Guidelines Section 15273: CEQA does not apply to establishment or modification of water rates.

**ATTACHMENTS:**

Attachment 1: PowerPoint

Attachment 2: SCVWD Resolution 99-21

Attachment 3: SCVWD Resolution 12-10

Attachment 4: April 2019 memo from Director's Hsueh, Estremera and Varela

Attachment 5: Memo on Research of Feasible Revenue Alternatives

**UNCLASSIFIED MANAGER:**

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