

REPORT FROM

## OFFICE OF THE CITY ADMINISTRATIVE OFFICER

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Date: October 14, 2011

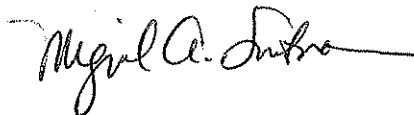
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Council District: All

To: The Council

From: Miguel A. Santana, City Administrative Officer



Reference: City Administrative Officer report dated July 29, 2011 relative to Clean Water Program Rate Adjustments

Subject: **ADDITIONAL REPORT BACKS ON PROPOSED CLEAN WATER PROGRAM RATE ADJUSTMENTS**

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### SUMMARY

At the meeting of the Energy and Environment Committee held on September 13, 2011, the Committee requested the following information from staff:

1. Identify additional reductions that can be made to bring the Clean Water Program (CWP) rate proposal to the lowest level of increases possible but maintaining sufficient funding for the capital program and deferred maintenance.
2. The Chief Legislative Analyst, with assistance of the City Administrative Officer as required, initiate an Independent Infrastructure Integrity Review of all Clean Water capital projects. Given extensive time and efforts involved to produce a comprehensive study, we recommend this item move on a separate track.
3. Review options to achieve bill clarity for the customer, that is, better distinction of the charges relating to sewer, water, electric and trash service. It is our understanding that the Bureau of Sanitation will report on this item.

This report identifies opportunities for the reduction of costs in operations and maintenance (O&M) as requested. The O&M component with the highest cost burden is staffing. Therefore, the reduction opportunities are focused on the containment of staffing costs. The opportunities vary in severity and relative impact and are summarized as follows:

ENERGY & ENVIRONMENT

BUDGET & FINANCE

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Will have no impact on existing staffing levels or the salaries of existing employees

- Eliminate all 222 vacant positions and funding (includes vacancies in capital labor).
  - (\$17.2 million; est. first year rate impact - 3.3 percent)
  - This would require an adjustment in the salary savings rate.
- Adjust position authority and funding for positions filled in lieu to the level occupied.
  - (\$1.1 million; est. first year rate impact - 0.2 percent)
  - This will reduce promotional opportunities for employees.
  - However, this will not impact operations as the Director of the Bureau of Sanitation has already determined that the duties and levels of positions are appropriate.

Will reduce existing staffing levels but will not impact salaries of existing employees

- Adjust funding for anticipated attrition.
  - (Up to \$8.2 million annually; est. first year rate impact - 1.5 percent)
  - If this opportunity is adopted and combined with the elimination of vacancies, it would be recommended that a targeted attrition program be developed at a lower dollar amount, such as \$5 million, in order to assure that critical plant and collection system operations are maintained.
  - This could also be used instead of layoffs.

Will reduce existing staffing levels and will impact salaries of existing employees

- Layoffs.
  - (Undetermined amount and first year rate impact)
  - If this opportunity is adopted, a targeted layoff program should be utilized in order to assure that critical plant and collection system operations are maintained.

It is intuitive to assume that each of the reduction opportunities listed above could be used to reduce potential rate requirements. This is especially true because the Department of Public Works is operating and maintaining the sewer system without major incidents. However, two other important factors must also be considered:

Existing costs are increasing rapidly.

- Costs of labor, health care and pensions are increasing significantly.
- Estimated growth costs over the next three fiscal years are represented in Figure 1 which depicts a net increase of approximately \$74 million in salaries and overheads (compared to the current cost of \$156 million).

<b>Figure 1 - Labor Growth Costs</b>					
	2011-12	2012-13	2013-14	2014-15	Total
Labor Increase	\$ 156,211,829	\$ 23,822,304	\$ 23,244,320	\$ 26,501,024	\$ 73,567,648
SCM Salaries	156,211,829	180,034,133	203,278,453	206,535,157	745,059,572

Improvement is required in the capital program.

- Deferred maintenance can not be ignored. Both public safety and economic concerns justify enhancing the ability to address deferred maintenance on a more timely basis.
- Current funding provides for a 168-year replacement cycle. Pipes have an estimated 80-year useful life. Plants have an estimated 30 to 50-year useful life (depending on components).

Therefore, while the identified reduction opportunities will save money in the first year, just the increasing costs of the existing work force will almost immediately offset the reduction – without providing extra funding to improve the capital program. This means that additional reductions must occur or rates must be increased to maintain stability within the system. While significant attrition and/or layoffs could be implemented to create more savings, those are limited term solutions whose financial impact will be also quickly exceeded by increasing costs.

A minimum rate increase of approximately 3.3 percent annually is required to fund the escalation in existing costs. Therefore, the Bureau's ten year proposal with 4.5 percent increases at the beginning, will not provide a significant increase for the capital program or the ability to increase jobs significantly.

We recommend an increase of 5.5 percent for each of the first three years and 6.5 percent for each of years four and five, which is one percent below our July 29, 2011 proposal. To minimize the potential for layoffs, we also recommend that the Council and Mayor eliminate all vacant positions and funding, adjust position authority and funding for positions filled in lieu to the level occupied and implement a targeted attrition program of \$5 million focused on non-critical positions. This would still augment the capital program by approximately \$11.5 million annually from a \$200 million base level targeted in the prior proposal, which we recommend be established as a minimum level of funding through the rate period. Management flexibility will continue to be provided by the availability of substitute and in lieu position authority and by exempting CWP positions from the Managed Hiring Process.

## **RECOMMENDATIONS**

That the Council and Mayor:

1. Delete 222 vacancies in the Clean Water Program as noted in Attachment A, and direct the City Administrative Officer to work with the Mayor's Office in preparing the necessary implementing actions in the Mayor's Proposed Budget;
2. Direct the City Administrative Officer and the Chief Legislative Analyst to work with the Bureau of Sanitation to implement a targeted attrition program of \$5 million for the Bureau of Sanitation Clean Water Program and report back on the progress with each Financial Status Report;
3. Exempt positions that are directly funded more than 90 percent (of the total of direct and indirect costs) by the Sewer Construction and Maintenance Fund (Schedule 14 of the Adopted Budget)

from the Managed Hiring process. Positions that are currently filled in-lieu will remain subject Managed Hiring until position authority has been adjusted;

4. Approve a minimum level of funding of \$212 million annually for the Clean Water capital program through the period of rate increases;
5. Instruct the Bureau of Sanitation to:
  - a. Increase the Sewer Service Charge (SSC) annually for a period of five years by 5.5 percent beginning as early as January 1, 2012, and 5.5 percent effective July 1 in each of fiscal years 2012-13 and 2013-2014, and 6.5 percent effective July 1 in each of fiscal years 2014-2015 and 2015-2016;
  - b. Develop a proposed Sewer Connection Loan Program based on stakeholder input and report back with program details;
  - c. Adjust the low-income surcharge from the current rate of 0.84 percent to 1.64 percent to fully fund the low income subsidy provided to SSC customers, as required by the Clean Water Act;
  - d. Adjust the SSC of public agencies to eliminate exemption of the capital component of the SSC so they are billed on the same basis as all other customers;
  - e. Adjust the Quality Surcharge Fee (QSF) for the amounts specified in Table A-2 of the July 29, 2011 CAO report, subject to any changes necessary to conform to the revised SSC rates presented herein in consultation with the Bureau of Sanitation and City Attorney;
  - f. Modify the Industrial Waste Fees for increased cost recovery, as specified in Table A-3 of the July 29, 2011 CAO report, subject to any changes necessary to conform to the revised SSC rates presented herein in consultation with the Bureau of Sanitation and City Attorney;
  - g. Modify the Septage Fees for full cost recovery, as specified in Table A-4 of the July 29, 2011 CAO report, subject to any changes necessary to conform to the revised SSC rates presented herein in consultation with the Bureau of Sanitation and City Attorney;
  - h. Modify the Sewerage Facilities Charge, as specified in Table A-5 of the July 29, 2011 CAO report, subject to any changes necessary to conform to the revised SSC rates presented herein in consultation with the Bureau of Sanitation and City Attorney;
  - i. Print and distribute notices to all affected customers in compliance with Proposition 218;
  - j. Assume the eligibility verification process for SSC low-income subsidies from the Department of Water and Power;

- k. Evaluate, with the assistance of the City Administrative Officer and Chief Legislative Analyst, strategic options to minimize future rate impacts by increasing revenue and/or reducing costs for the Clean Water program, as included in Appendix F of the July 29, 2011 CAO report;
6. Request the City Attorney to prepare and present ordinances for pertinent fee adjustments, and finalize ordinances for approval after required public hearings have been held; and,
7. Reduce a General Fund obligation of \$10 million in SCM expenditures for Northridge earthquake recovery by \$4 million (reflects an offset of prior years related cost adjustments from 2008-09 and 2009-10), thereby reducing the Northridge obligation to \$6 million (with intent to address this amount over the next four years).

## **FISCAL IMPACT**

The Sewer Construction and Maintenance Fund is a special enterprise fund with no reliance on the General Fund. Proposed rate adjustments for various components of the Clean Water Program, inclusive of the Sewer Service Charge will increase rates over a five year period by 5.5 percent in the first two years and 6.5 percent in the following three years.

The recommendations are in compliance with the City's Financial Policies in that user charges and fees are proposed at a level to support the full cost of operations for the Clean Water Program, including operating, capital and financing costs. The recommendations also reduce a pending General Fund obligation of \$10 million to the SCM by \$4 million, and indicate the intent of the City to address the remaining obligation of \$6 million over the next four years. Revenue adjustments for vacant positions and attrition would be done in the normal course of evaluating planned versus actual staffing levels which for the Sewer Construction and Maintenance Fund is typically handled in the Financial Status Report.

*MAS:ER:06120040*

Attachment

**Background**

There are three major categories of funding in the CWP: the capital improvement program, debt amortization and O&M. To bring the proposed rates down and maintain sufficient capital funding, it is necessary to consider the other major cost areas in the CWP. Debt service on wastewater bonds is non-discretionary and is driven by the amount of outstanding bonds and new issuances. Some savings can be achieved with re-fundings although the proposed rate structure already reflects recent transactions. The City regularly conducts reviews for refunding opportunities; however, current market conditions do not support a refunding at this time. It is anticipated that conditions will improve later this fiscal year, supporting a refunding of approximately \$200 million, with annual savings of approximately \$250,000.

O&M is funded at \$318 million and comprises 44 percent of the total CWP program budget of \$717 million. O&M includes the various staffing and overhead costs for implementing bureaus and departments, contract services, utilities, and other project and operation-related expenses. The O&M component with the highest cost burden is staffing, which comprises \$161 million, including salaries and related costs, of the \$318 million total. Capital labor is an additional \$62 million, for a total of \$223 million budgeted in the CWP for staffing and overhead costs. Estimated growth costs over the next three fiscal years are represented in Figure 1 which depicts a net increase of approximately \$74 million in salaries and overheads based on current appropriations and expected cost trends.

	2011-12	2012-13	2013-14	2014-15	Total
Labor Increase	//////	\$ 23,822,304	\$ 23,244,320	\$ 26,501,024	\$ 73,567,648
SCM Salaries	156,211,829	180,034,133	203,278,453	206,535,157	//////

Following is additional information on incremental options for staffing cost reductions:

a. Eliminate all vacant positions and funding.

There are a total of 222 vacancies across all CWP implementing departments which include both O&M and capital labor. The vacancy classifications for each department are included in Attachment A. The data in Figure 2 includes vacancies necessary to achieve budgeted salary savings which vary across departments. Elimination of all vacancies would achieve \$18 million in ongoing salary savings and \$8 million in foregone related cost obligations, for a total reduction of \$26 million (not adjusted for salary savings). Sanitation and Engineering both have a salary savings rate of four percent for SCM. This scenario assumes that the salary savings rate for Sanitation and Engineering is reduced to zero (in the following budget year).

Department	Positions	Salaries	Related Costs	Total
Board of Public Works	1	\$ 65,709	\$ 69,750	\$ 135,459
Bureau of Engineering	41	3,513,893	1,219,672	4,733,565
Bureau of Sanitation	180	14,085,049	6,749,555	20,834,604
<b>Total</b>	<b>222</b>	<b>\$ 17,664,651</b>	<b>\$ 8,038,978</b>	<b>\$ 25,703,629</b>

Figure 3 reflects vacancies with sufficient salary funding in the budget due to the salary savings rate, which represents 143 funded positions and 79 unfunded. Both Sanitation and Engineering have a salary savings rate of four percent for SCM which amounts to \$4.5 million for Sanitation and \$1.3 million for Engineering, for a total of \$5.8 million. Factoring in related costs of \$2.7 million, the total savings rate equivalent is \$8.5 million. Thus, in the option to delete all vacant positions, the total labor cost of \$25.7 million would incorporate a savings rate adjustment of \$8.5 million (and reduce the savings rate to zero going forward) for a net reduction of \$17.2 million.

**Figure 3 - SCM Vacancies (excludes positions required for salary savings)**

Department	Positions	Salaries	Related Costs	Total	Est. Rate Impact
Board of Public Works	1	\$ 65,709	\$ 69,750	\$ 135,459	0.0%
Bureau of Engineering	22	2,167,858	752,464	2,920,322	0.6%
Bureau of Sanitation	120	9,586,353	4,593,780	14,180,133	2.7%
<b>Total</b>	<b>143</b>	<b>\$ 11,819,920</b>	<b>\$ 5,415,994</b>	<b>\$ 17,235,914</b>	<b>3.3%</b>

It should be noted that Sanitation has been operating with significant vacancies in the following operations classes (Figure 4). However, to our knowledge minimum service levels are being met under current staffing albeit with overtime usage and as-needed support exceeding budgeted levels. Should additional staffing or management flexibility be needed to address peak workload situations or extraordinary circumstances, the Bureau has at its disposal other mechanisms to augment staffing needs such as substitute and as-needed position authority.

**Figure 4**

<u>Class</u>	<u>Vacancies</u>	<u>Vacancy Rate within Class</u>
Wastewater Collection Worker II	26	12%
Wastewater Treatment Operator I	15	15%
Wastewater Treatment Electrician I	11	39%
Wastewater Treatment Mechanic I	10	30%
Instrument Mechanic	9	29%
Mechanical Helper	10	36%
Laboratory Technician II	10	23%
Total	91	

In BOE, all CWP staffing is in the capital program. Approximately 10 positions provide administrative and engineering support and may be less critical to operations. The remaining vacancies are in engineering, surveying and construction management functions. We are not in a position to determine the appropriate staffing level for a \$200 million-plus capital program but given the fiscal pressures on the SCM fund, we would support the deletion of all vacancies and assist BOE in meeting any critical staffing voids in these areas through interim means, such as substitute authority, as needs arise.

Impacts:

- Maintains current staffing levels in SCM-funded departments.
- Savings achieved with no negative impact on existing personnel.
- Reduces promotional opportunities within Sanitation’s clean water operations.
- May reduce management flexibility in plant and administrative operations.
- May require some departmental reorganization.

b. Lower position authority and funding for positions filled in lieu to the level occupied.

There are approximately 80 positions in Sanitation’s CWP that are filled at a lower classification or pay grade which results in savings of up to \$1.1 million annually. Maintaining a freeze on all positions at the current classification or pay grade would contribute to O&M cost containment.

**Figure 8 - SCM Posiitons Filled In-lieu (salaries reflect savings rates)**

Dept.	Salaries	Related Costs	Total
Bureau of Sanitation	\$ 758,294	\$ 363,374	\$ 1,121,668

The following are the more prominent examples of positions filled in lieu with a lower class or pay grade and exclude those carried out for training and recruitment purposes, such as Wastewater Collection Worker II (filled at I level) and Wastewater Treatment Operator I (filled with Plant Equipment Trainee):

<u>Class</u>	<u>Filled In Lieu</u>
Senior Clerk Typist	Clerk Typist
Management Analyst I/II Environmental/	Management Assistant/Management Analyst I
Civil Engineering Associate III Laboratory Technician II	Environmental/Civil Engineering Associate II Laboratory Technician I

Impacts:

- Maintains current staffing levels in SCM-funded departments.
- Savings achieved with no negative impact on existing personnel.
- Limits promotional opportunities within Sanitation’s CWP.

c. Attrition

Sanitation attrition patterns were reviewed over a five-year period. The average annual attrition is 129 positions with commensurate salaries funding of \$9.6 million (it should be noted that 2009 and 2010 were somewhat anomalous given ERIP). Only Sanitation was reviewed for attrition because it has by far the largest share of O&M funding (70 percent). Most of the remaining 11 departments with O&M funding have staffing of between one and 20 positions and would be adversely impacted by sustained attrition. Attrition includes positions that were vacated for a variety of reasons, including but not limited to promotions within or outside the Bureau, internal



transfers, terminations, etc. Thus, the labor cost escalation could be offset by as much as \$14.3 million if all Sanitation CWP positions were subject to a hard freeze.

Year	Positions	Salaries	Related	Total
2010	159	12,113,466	5,804,773	17,918,239
2009	103	7,533,036	3,609,831	11,142,866
2008	136	10,374,801	4,971,605	15,346,406
2007	124	9,411,789	4,510,129	13,921,919
2006	121	8,738,290	4,187,389	12,925,678
Average (2006-10)	129	\$ 9,634,276	\$ 4,616,745	\$ 14,251,022

Recognizing, however, the need to maintain minimum staffing levels in some functions, particularly in plant and field operations, we recommend a targeted attrition program of \$5 million for the Bureau of Sanitation CWP and report back on the progress with each Financial Status Report. The \$5 million is a reasonable target given average attrition of \$8.2 million (Figure 6) in the CWP that excludes critical operations classes with high vacancies and/or turnover incidence noted in Figure 4.

Year	Positions	Salaries	Related	Total
2010	84	6,427,583	3,080,098	9,507,681
2009	48	3,477,143	1,666,247	5,143,390
2008	75	5,655,053	2,709,901	8,364,954
2007	77	5,945,908	2,849,279	8,795,187
2006	84	6,353,993	3,044,833	9,398,826
Average (2006-10)	74	\$ 5,571,936	\$ 2,670,072	\$ 8,242,008

Even with deletion of vacancies (Figure 7), targeted attrition would cover about one third of growth costs, resulting in approximately \$18 million (three-year growth average minus attrition) in annual unfunded obligatory costs for this period. This approximates a 3.3 percent rate adjustment.

Department	2011-12	2012-13	2013-14	2014-15	Total
Labor Increase	////	\$ 21,989,220	\$ 21,455,711	\$ 24,461,818	\$ 67,906,749
SCM O&M Staffing	144,191,607	166,180,827	187,636,538	190,642,645	////

**Impacts:**

- Reduces staffing from current levels as an alternative to layoffs.
- Salary reductions implemented in the current fiscal year (beyond a planned staffing level) would impact budgeted revenue for related cost reimbursements to the General Fund (i.e., 48 percent of any salary reduction or up to \$2.7 million for attrition).
- Could be tailored to focus on non-critical support systems (e.g., administrative, clerical and systems).

### Other Funding Opportunities

In addition to reduction measures, it is also important to recognize any leveraging opportunities for the Clean Water Program. Leaders of the House Transportation and Infrastructure Committee on October 11, 2011 introduced the bipartisan Water Quality Protection & Job Creation Act of 2011, which would invest \$13.8 billion in the clean water state revolving fund (CWSRF) and would ensure the long-term financing of wastewater infrastructure through the establishment of a Clean Water Trust Fund. We will monitor this proposal and the funding potential for City clean water projects. The Obama administration's proposed American Jobs Act of 2011 that sought to create a national infrastructure bank was voted down by the Senate.

SCM Vacancies as of August 2011					
ClassPG	Class	Sanitation	Engineering	PW Board	Total
15132	ACCOUNTANT II			1	1
12232	ACCOUNTING CLERK II	1			1
79263	ARCHITECTURAL ASSOC III		1		1
33440	CARPENTER	1			1
78332	CHEMIST II	5			5
72370	CIVIL ENGINEER		1		1
72462	CIVIL ENGRG ASSOC II		8		8
72463	CIVIL ENGRG ASSOC III	1	9		10
72464	CIVIL ENGRG ASSOC IV		1		1
31272	CONSTR & MAINT SUPV II	1			1
72302	CONTRL SYS ENG ASSC II	1			1
31560	CUSTODIAN	1			1
11211	DELIVERY DRIVER I	1			1
15934	DEPT CHIEF ACCT III				0
11940	DIR CASH MGMT SERVICES				0
75252	ELECTRCL ENGRG ASSC II	1			1
72172	ENGRG DESIGNER II		1		1
42920	ENV COMPLIANCE INSP	5			5
78720	ENVIRONMENTAL ENGINEER	4			4
78712	ENVIRONMENTAL ENGRG ASSC II	4			4
78713	ENVIRONMENTAL ENGRG ASSC III	1	1		2
73103	ENVIRONMENTAL SPEC III	1			1
73041	ENVIROMENTAL SPVR I		1		1
72280	FIELD ENGINEER AIDE		2		2
72141	GEOG INFO SYS SUPVR I		2		2
23300	INDUSTRIAL HYGIENIST	1			1
38430	INSTRUMENT MECH	9			9
38441	INSTRUMENT MECH SUPV I	1			1
78542	LABORATORY TECH II	10			10
72830	LAND SURVEYING ASST		1		1
37630	MACHINIST	2			2
37662	MACHINIST SUPVR II	1			1
31150	MAINT & CONSTR HELPER	1			1
31120	MAINTENANCE LABORER	3			3
91841	MANAGEMENT ANALYST I	2	1		3
91842	MANAGEMENT ANALYST II	3			3
75542	MECH ENGRG ASSC II	1	1		2
37710	MECH HELPER	10			10
72123	OFFICE ENGRG TECH III		1		1
34230	PAINTER	1			1
35580	POWER SHOVEL OPERATOR	1			1
17311	PERSONNEL ANALYST I	1			1
17312	PERSONNEL ANALYST II		1		1
12010	PR CLERK	1	1		2
78750	PR ENVIRONMENTAL ENGR	1			1
41281	SANIT WSTWTR MGR I	1			1
41282	SANIT WSTWTR MGR II	2			2
11160	SECRETARY		1		1
72421	SHIFT SUPT W/W TRMT I	2			2

SCM Vacancies as of August 2011					
ClassPG	Class	Sanitation	Engineering	PW Board	Total
78300	SR CHEMIST	3			3
13680	SR CLERK TYPIST	2			2
94850	SR CIVIL ENGINEER		2		2
72890	SR CONSTR ENGINEER		1		1
78740	SR ENVIRONMENTAL ENGINEER	2			2
91712	SR MGMT ANALYST II	2	1		3
91671	SR PERSONNEL ANALYST I	1	1		2
94250	SR STRUCTURAL ENGINEER		1		1
15971	SR SYSTEMS ANALYST I	1			1
15972	SR SYSTEMS ANALYST II	2			2
41240	SR W/W TREATMENT OPER	3			3
72862	SURVEY PARTY CHIEF II		1		1
15962	SYSTEMS ANALYST II	1			1
14551	SYSTEMS PROGRAMMER I				0
14552	SYSTEMS PROGRAMMER II	1			1
14553	SYSTEMS PROGRAMMER III	1			1
41130	W/WTR COLL SUPERVISOR	1			1
41102	W/WTR COLL WORKER II	26			26
56151	W/WTR TRMT ELEC I	11			11
56152	W/WTR TRMT ELEC II	1			1
56130	W/WTR TRMT ELEC SUPVR	1			1
56141	W/WTR TRMT MECH I	10			10
56142	W/WTR TRMT MECH II	4			4
41231	W/WTR TRMT OPER I	15			15
41232	W/WTR TRMT OPER II	2			2
41233	W/WTR TRMT OPER III	4			4
78562	WATER BIOLOGIST II	3			3
37960	WELDER	1			1
	TOTAL	180	41	1	222