

7. RESPONSE TO COUNCIL RECOMMENDATIONS

On September 19, 2012, the Los Angeles City Council (Council) Energy and Environment Committee adopted a report with ten recommendations associated with third-party review of LADWP's Incremental Electric Rate Ordinance. The full Council adopted the same recommendations in connection with its approval of the Incremental Electric Rate Ordinance on October 2, 2012. Many of these recommendations stemmed from the recommendations found in Appendix E of the "Los Angeles Department of Water and Power (LADWP) - Power System Financial Review and Rate Restructuring Analysis" report issued to the City Council on August 23, 2012 (RPA Power Report).

A summary of the activities and status for each of the applicable recommendations is included in this report. While these recommendations were directed at the LADWP Power System, several also have relevance to the Water System. Therefore, a summary of the activities and status for each of the applicable recommendations is included in this report to the extent the specific item directly impacts the Water System's operations and revenue requirement.

LADWP has made significant progress towards addressing each item, including working collaboratively with the Ratepayer Advocate (RPA), Chief Legislative Analyst (CLA) and Chief Administrative Officer (CAO).

As shown in the table below, formal programs or other activities are underway to address all of the recommendations, and LADWP has made significant progress in each area.

Response to City Council Recommendations

a. Conduct negotiations with labor to find common ground that allows for greater flexibility to contract out effectively and bring salaries and benefits closer to other power utility providers.

In December of 2013, the Council approved a new Memorandum of Understanding (MOU) with IBEW Local 18 that provides significant savings to LADWP ratepayers and makes significant progress towards addressing this recommendation. Specifically, the new MOU makes progress in the following major areas:

- MOU term was extended from 10/1/14 to 9/30/17
- Defer the existing 2.9% COLA from 10/1/13 to 10/1/16
- Create new lower (Tier 2) pension benefits for new employees
- Entry level salaries are reduced for 34 common classes

- Contracting out overtime restriction – reduction from 10% to 5%
- Sick time medical certification requirement for three days rather than the previous five days

As a result of these changes, LADWP is projected to reduce labor costs by \$456 million over the next four years.

Key MOU Components	Four-Year Savings Estimate
Defer COLA from 10/1/13 to 10/1/16	\$385.0
Entry Level Salary Reduction for 34 Common Classes	\$15.0
Sick Time Medical Certification Requirement	\$12.0
Contracting Out Overtime Restriction - Reduction from 10% to 5%	\$3.0
Retirement Plan Tier 2 For All New Hires	\$41.0
Total Estimated Savings over four years	\$456.0

b. Re-evaluate and consider replacing the surcharge-based restructuring approach with fully restructured permanent rates once legal considerations allow.

(This item is specific to the Power System and is therefore not discussed in this appendix)

c. Conduct a new formal cost of service study in order to prepare for future power rate restructuring.

LADWP has new cost of services studies for both the Water and Power Systems. These studies are based on marginal cost principles to allocate the overall water & power revenue requirement to each major customer class.

The new cost of service studies by themselves have no impact on the overall revenue requirements; however, they will be used to allocate revenues between customer classes and provide guidance on rate design. This methodology is consistent with industry best practice and leads to the most efficient use of utility resources by LADWP customers. This methodology is also consistent with the requirements of Proposition 218.

d. Conduct a benchmarking assessment to review the cost per project for the repowering program and the Power Reliability Program to ensure cost reasonableness.

(This item is specific to the Power System and is therefore not discussed in this appendix)

e. Identify opportunities to contract out and explore the potential savings, including the benchmarking of staffing and outsourcing levels against utility peers.

As part of the recent LADWP reorganization by the General Manager, a new Corporate Performance function has been created. This new function will focus on:

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- High-level benchmarking: As of February 2015, the Department has completed its initial high-level benchmarking. The study identifies areas where LADWP is comparable or better than industry performance and where there are opportunities for improvement. This high-level study provides a “roadmap” for follow-up in-depth studies to be conducted. Key findings of the benchmarking study for the Water System include:
 - Total O&M costs: The Water System total O&M costs on a per customer and per gallon basis are 2nd/3rd quartiles. This includes the \$56 million of O&M for the Los Angeles Aqueduct that most water utilities do not have. If this cost was excluded, these metrics would improve by one full quartile.
 - Reliability metrics: LADWP is 2nd quartile for both planned and unplanned service disruptions, as well as system losses.
 - The LADWP’s key financial metrics are in line with industry peer sets.
 - Customer Service O&M: The Water System benchmark for customer service O&M per account fell into the 4th quartile. This result could be lower as a result of business strategies for mostly publicly owned utilities within the AWWA peer set.
 - LA Metro wage rates - Compared to other regions of the US, wage rates for the LA Metro area can range from 13% to 33% higher than peer utilities. The labor component, including overtime and benefits, represents 73% of the Water System’s total O&M expense.
 - Regional water rate - LADWP’s rates remain competitive with neighboring water utilities in all customer classes for FY 2012-13. Water utilities in California are increasing rates in response to both State and Federal regulatory requirements as well as much needed water storage and recycling infrastructure programs.
 - Real system losses - This metric benchmarks in the 2nd and 3rd quartile and shows that the Water System losses are roughly in line with the median of the peer set.
 - Total unplanned service disruptions per customer - LADWP 2nd quartile result is a favorable benchmark relative to both National and Western Regional peers.
 - Total planned service disruptions per customer - LADWP’s 1st and 2nd quartile results are favorable benchmarks relative to National and Western Regional peers, respectively.
 - Follow-up in-depth studies: As a result of the high level benchmarking study, there will be a number of areas that require further study and analysis. While the specific areas to be studied will be identified after completion of the initial study, some potential components of this study will be:
 - Determine number of employees and overtime.
 - Provide contracting amounts as a percent of total for various functions and sub functions.
 - Conduct more detailed salary/pension/healthcare benchmark study with adjustments for cost of living in the greater Los Angeles area.
 - Identify areas/processes where benchmarking data shows that there is room for improvement. These areas/processes will be the subject of future business process improvement studies.
 - Determine financial impacts of the significant policies that increase LADWP’s costs.
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- Business process mapping studies: As a result of the above studies, there will be a number of areas that will present opportunities for significantly improving financial and/or Departmental performance. These functions will be the subject of specific business process mapping studies. These studies will compare industry best practices and evaluate what steps need to be taken for LADWP to move towards the best practice.

f. Review overtime expenses allocation, as well as the Department’s contractual requirements that have an impact on overtime.

The current MOU with IBEW Local 18 has key provisions in it for reducing overtime as a consequence of obtaining contracting services. Overtime at a utility is affected by several factors; many of which are operational in nature and in some cases outside the immediate control of the utility; for example, emergency mainline breaks or regulator station call-outs.

Additionally, overtime is considered a safe and cost effective means of obtaining needed resources when used in moderation. In general, it is good utility practice to use overtime at the rate of roughly 15% of regular labor costs. Currently, LADWP is limited in its ability to recruit replacement employees in a timely manner. This is resulting in somewhat higher overtime levels. For the Water System, overtime was higher than the budget at 15.6% for FY 2013-14, this is offset by underspending in regular labor due to the slow hiring process. The approved budget for overtime for the Water System in FY 2014-15 is 8.4% with a proposed five-year average of 9.8%.

g. Complete a rigorous review of the Department’s hedging plan to lock in low fuel prices.

(This item is specific to the Power System and is therefore not discussed in this appendix)

h. Establish a plan for energy efficiency that maintains expenditure levels at an achievable and cost effective level.

(This item is specific to the Power System and is therefore not discussed in this appendix)

i. Seek greater Departmental efficiencies by pursuing process improvement efforts across a range of areas and practices.

In FY 2011-12, LADWP initiated a Department-wide \$459 million, three-year cost reduction program. The final results from the cost reduction plan, concluded in June 2014, exceeded the total \$459 million cost reduction plan target. The source of the cost savings has changed somewhat, and the Department has saved more through non-labor and capital budgets; however, LADWP has managed the overall portfolio of savings opportunities and exceed the original target by \$7.8 million.

Source (\$M)	Original Target	Total Savings	Feb. 2011 - June 2012 Savings	FY 12-13 Savings	FY 13-14 Savings	Difference between target
Total	\$459.1	\$466.9	\$188.7	\$168.5	\$109.8	\$7.8

LADWP has created a new Corporate Performance function. This function will first seek to evaluate the overall performance by conducting a high-level benchmarking study, followed by a

more in-depth follow-up study to specifically evaluate where there are opportunities to improve cost, reliability, and/or customer service performance of LADWP. Ultimately, the results of these studies will result in a number of business process mapping studies where LADWP operations can be compared to and moved toward industry best practice. Some potential changes could require the “meet and confer” process, as well as require subsequent MOU changes.

Additionally, consistent with the Mayor’s goal of making City government more efficient and effective, LADWP will be implementing the COMSTAT key performance indicator tool and process throughout the Department, beginning with a soft launch in April 2015. COMSTAT is built on a single platform with four tiers of performance indicators, each tailored to the appropriate audience. The targeted data monitors and manages dozens of key performance indicators at the Departmental, System, and Division levels, and the integrated COMSTAT platform enables LADWP to evaluate and verify the integrity of the indicators. The goal of the COMSTAT system is to define a “single source of truth” for key indicators and enable transparency for the Mayor, the City, and the public. LADWP expects the COMSTAT tool to be fully operational by the end of 2015.

As a result of these cost reduction efforts, LADWP had no rate ordinance changes for both Water and Power Systems in FY 2014-15. It should be noted that LADWP has used cost containment programs to limit rate actions in the past. Results of these programs are:

- Water System: The Water System has not had a base rate increase for five years, with the last base rate increase taking place in FY 2009-10. The last rate ordinance change took place with the Water Quality Improvement Adjustment factor cap increase in FY 2011-12.
- Power System: Over the five-year period, Power System has gone through three of the years (FY 2010-11, FY 2011-12, and FY 2014-15) without any base rate increase. The last rate ordinance change was a two-year rate action for FY 2012-13 and FY 2013-14.

j. Submit a semi-annual report to the Mayor and Council regarding the status of the Renewable Portfolio Standards program and its impact on rates.

(This item is specific to the Power System and is therefore not discussed in this appendix)