



**DATE:** June 5, 2018

**TO:** Mayor and City Council

**FROM:** Director of Utilities & Environmental Services

**SUBJECT:** Consideration of Resolution Opposing the State Water Tax Provisions of the Safe and Affordable Drinking Act Budget Trailer Bill

### **RECOMMENDATION**

That the Council adopts a resolution opposing the Safe and Affordable Drinking Water Act budget trailer bill in its present form, which would impose a State water tax on Hayward's water customers, and encouraging consideration of other potential funding mechanisms to assist disadvantaged communities with access to safe and affordable drinking water supplies.

### **SUMMARY**

The Governor is proposing to include the Safe and Affordable Drinking Water Act as a budget trailer bill (BTB) to his proposed State budget for Fiscal Year 2018-19. The BTB closely resembles Senate Bill 623, which was introduced during the 2017 legislative session and has not been amended since August 21, 2017. The BTB would establish the Safe and Affordable Drinking Water Fund to provide financial assistance to disadvantaged communities that do not have access to safe drinking water because of contamination. The BTB would require local water agencies to collect a State tax on water customers, based on meter size, and remit the monies to the State Water Board to fund the financial assistance. Hayward fully supports the State's objectives to ensure that every Californian has access to safe and affordable drinking water.

Staff recommends, however, that the City Council adopt a resolution opposing the BTB unless it is amended to remove provisions related to the State water tax. Staff is concerned about the burden a State water tax would place upon Hayward water customers, some of whom are economically disadvantaged families, and the precedent of using a water tax as a method to fund other State initiatives. Other funding options are available to the State and should be considered in lieu of a State water tax.

## BACKGROUND

Existing California law establishes the right of every human being to “safe, clean, affordable, and accessible water adequate for human consumption, cooking and sanitary purposes.” In some California communities, however, access to safe drinking water is a challenge due to contaminants caused by human activities and natural conditions and a lack of financial resources to implement mitigation measures. The State Water Board estimates that there are about 300 public water systems, serving approximately 200,000 statewide, and an unquantifiable number of very small water systems and households reliant on domestic wells, that cannot access nor afford to pay for safe drinking water. Many of these water systems cannot charge water rates that are both affordable and sufficient to supply drinking water that complies with federal and state water quality standards.

During the 2017 legislative session, State Senator Bill Monning (D-Carmel) introduced Senate Bill (SB) 623 – Safe and Affordable Drinking Water Act. This legislation would establish the Safe and Affordable Drinking Water Fund to assist disadvantaged communities with clean water initiatives. SB 623 would impose taxes on residential and commercial water bills, as well as fees on fertilizers and dairies. The water taxes would be collected by water purveyors and remitted to the State. SB 623 has been in the committee process since last August.

Governor Brown has placed a significant focus on addressing the problem of contaminated drinking water in disadvantaged communities. A modified version of SB 623 has been proposed as a budget trailer bill (BTB) to the Governor’s proposed State budget for Fiscal Year 2018-19. Though not yet formally introduced, it is expected that the BTB language will be placed into a bill as part of the legislature’s budget process and that the BTB will replace SB 623 as the vehicle for advancing the Safe and Affordable Drinking Water legislation. Both SB 623 and the BTB require a two-thirds vote in the legislature because of the proposed tax on drinking water. The full text of the BTB can be viewed at:

[http://www.dof.ca.gov/Budget/Trailer\\_Bill\\_Language/documents/SafeandAffordableDrinkingWater.pdf](http://www.dof.ca.gov/Budget/Trailer_Bill_Language/documents/SafeandAffordableDrinkingWater.pdf)

The BTB is intended to address the issue of access to safe drinking water for all Californians, ensure the long-term sustainability of drinking water service and infrastructure, and provide a stable and sustainable funding source. Like SB 623, the BTB would establish the California Safe Drinking Water Fund and appropriate monies to the State Water Board to expend in the form of grants, loans and services for short- and long-term solutions to contaminated or failing water systems in disadvantaged communities. The funding mechanisms would include:

- 1) A State water tax to be collected by local water agencies, including Hayward, for drinking water delivered to residential, business, industrial, and institutional customers, and
- 2) Agricultural-related fees on confined animal facilities, fertilizers, and dairy.

A presentation made to the Bay Area Council in July 2017 indicates that a total of \$90 to \$110 million per year would be collected from retail water customers throughout the State for an indefinite period. An additional \$30 million is expected to be generated from agriculture-related fees for 15 years, and from that time forward, the total revenue would not exceed \$10 million.

## **DISCUSSION**

### Council Sustainability Committee Action

Staff provided an oral update on the BTB to the Council Sustainability Committee (CSC) on May 14. No action was requested.

### Bill Analysis

Staff's review of the BTB focused on potential impacts to Hayward water customers. If approved by the legislature, the BTB would impose a monthly tax on each retail water customer, based on meter size, ranging from \$0.95 for meters of 1 inch and smaller to \$10.00 for meters that are larger than 4 inches, beginning July 1, 2019. The BTB includes exemptions for low-income households and meters used for fire flow or non-potable purposes, such as recycled water. For the first two years, the local water agency would have the ability to exempt customers who are already enrolled in a low-income rate assistance program from paying the tax. After July 1, 2021, the low-income exemption would only apply to customers with household incomes equal to or less than 200% of the federal poverty level.

As of July 1, 2021, the amount of the water tax would be determined by the State Water Board, although the tax would be capped at the amounts shown in the BTB. The taxes would be collected on water bills and remitted to the State Water Board for the purposes described in the BTB. The maximum tax amount could be increased in the future by a two-thirds vote of the legislature.

Staff estimates that the annual amount collected in Hayward, based on the current number of meters, would be in the range of \$500,000. This is an estimate only. The actual revenue collected may be less because of the uncertainty of how many Hayward customers would qualify long-term for an exemption from the tax. A small portion of the revenue, 4% until 2021 and 2% thereafter, could be retained by the City for administrative costs.

Regarding the impact on customers, staff has calculated that an average single-family customer would see a monthly increase of about 2% as a result of the water tax, based on average usage of 14 hundred cubic feet, or 175 gallons per day. The annual impact to City customers will range from \$11.40 to \$120, depending on meter size, and may be considered significant by some customers living on limited incomes. Although the City will not benefit from the tax, customers will likely view it as a City charge and it may affect the City's ability to increase water rates sufficiently to cover operational costs in the near-term.

The City is committed to providing safe and affordable drinking water for Hayward customers, which is demonstrated by the City's efforts to maintain water rates as low as possible while providing reliable water service. Though none of Hayward's customers lack access to safe drinking water, the City also understands the importance of ensuring access to safe drinking water in disadvantaged communities throughout the State. The intended beneficiaries of the BTB do not have the ability to pay and that funding support is needed. While staff supports the objectives of the BTB, staff has identified several concerns with the tax provisions of the BTB, as described below, that should be considered by the Council:

- Taxing a resource that is essential to human existence may not be sound public policy.
- Requiring local water agencies to collect a State tax sets a precedent that could lead to other taxes fees being added to water bills by the State or other entities.
- While the taxes, as proposed in the BTB, are relatively modest, there are no guarantees that they won't be increased in future years, placing a burden on the City's ratepayers, which include families with limited economic resources.
- The cost burden does not appear to be equitable between urban and agricultural users. Under the current provisions of the BTB, urban users would bear the predominant burden of funding the Safe and Affordable Drinking Water Fund, although agricultural use accounts for a larger portion of water consumption in the State. Some agricultural users would pay into the fund; however, their contribution is significantly less than their proportional use of water resources. Overall, the proposal would allocate about 78% of the cost burden to urban water users initially, and ultimately the potential share could reach 90%.

For these reasons, staff recommends that the City Council oppose the BTB in its present form and request that the Governor and legislature consider other sustainable funding sources to provide needed assistance to affected communities. The Association of California Water Agencies (ACWA), a coalition of public water agencies, has identified other viable funding mechanisms to address this critical need, such as the use of federal safe drinking water funds, general obligation bond funds, a limited amount of State General Fund monies, lease revenue bonds, and an allocation from the Cap and Trade program. These sources, or combination of sources, would be appropriate alternatives to the proposed water tax.

As signatories to the letter submitted by ACWA (see Attachment III), the following nearby agencies have indicated their opposition to the BTB unless it is amended: Alameda County Water District; Contra Costa Water District; Dublin San Ramon Services District; and Zone 7 Water Agency. The East Bay Municipal Utility District and San Francisco Public Utilities Commission have not taken a formal position on the BTB.

#### Schedule

The timing of when the BTB will be heard and voted on in committee is uncertain. Proponents of the BTB would like to see the bill move as early as June as part of the budget process. However, other indications are that because of the two-thirds majority required to pass the BTB, discussions may extend into late summer. If the effort to move the BTB is unsuccessful, SB 623 could also be amended and advanced during the 2018 legislative session.

## **ECONOMIC IMPACT**

As noted above, if the BTB is approved, the proposed State water tax is estimated to result in the collection of about \$500,000 per year from Hayward customers. The impact on single-family customers is estimated to be an increase of about 2%. These funds would be remitted to the State and would provide no direct benefit to Hayward customers.

The BTB includes exemptions for low-income customers. For the first two years, all customers receiving a reduced water service fee as part of the City's low-income exemption program could qualify for an exemption from the water tax. As a reminder, 2650 single-family customers with household income below the "Alameda County – Very Low Income" threshold, as determined by the State of California, are eligible for the low-income exemption and pay a reduced service fee. Beginning in 2021, only customers whose household income is equal to or less than 200 percent of the federal poverty level would be exempt from the tax. This could result in some Hayward customers enrolled in the low-income exemption program no longer qualifying for an exemption from the water tax.

## **FISCAL IMPACT**

If the BTB is approved, there would be some administrative cost to update the customer billing system to account for the collection of the tax and on-going annual costs to collect the tax and remit the revenue to the State. As noted in the discussion, the City would be able to retain a small portion of the tax to cover administrative costs. Staff is still reviewing potential fiscal impacts of the BTB, but they are not expected to be significant. There would be no impact on the General Fund.

## **STRATEGIC INITIATIVES**

This agenda item does not directly relate to one of Council's Strategic Initiatives.

## **SUSTAINABILITY FEATURES**

Hayward supports access to safe, affordable and sustainable water supplies within Hayward and beyond its borders. While the objective of the BTB has merit, other funding mechanisms are available for consideration.

## **PUBLIC CONTACT**

Staff did not conduct public outreach regarding this item. If the BTB were to be enacted, outreach would be needed to notify Hayward water customers of the State tax prior to adding

it to water bills.

## **NEXT STEPS**

If Council concurs with the recommendation, staff will prepare a letter for the Mayor's signature to be sent to the Chairs of the Senate and Assembly Budget Committees, with copies to local State representatives. Staff will continue to monitor the progress of the Safe and Affordable Drinking Water BTB and SB 623 and will report new developments to the CSC and Council.

*Prepared by:* Jan Lee, Water Resources Manager

*Recommended by:* Alex Ameri, Director of Utilities & Environmental Services

*Approved by:*

A handwritten signature in black ink, appearing to read 'K. McAdoo', is positioned above a horizontal line.

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Kelly McAdoo, City Manager