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10 **SUPERIOR COURT OF THE STATE OF CALIFORNIA**
11 **FOR THE COUNTY OF SAN DIEGO, CENTRAL DISTRICT**

13 Case No: 37-2021-00030939-CU-WM-CTL

14 **CLASS ACTION**

15 BARRY ALLRED, on behalf of himself
16 and all others similarly situated,

17 Plaintiff and Petitioner,

18 v.

19 CITY OF SAN DIEGO;
20 CITY OF SAN DIEGO PUBLIC
21 UTILITIES DEPARTMENT; DOES 1-10,
22 INCLUSIVE,

23 Defendants and Respondents.

14 **VERIFIED PETITION FOR WRIT OF MANDATE**

17 **AND**

19 **CLASS ACTION COMPLAINT FOR:**

- 20 **1. PETITION FOR WRIT OF MANDATE;**
- 21 **2. VIOLATION OF CALIFORNIA CONSTITUTION,**
22 **UNLAWFUL MUNICIPAL TAXES AND FEES;**
- 23 **3. MONEY HAD AND RECEIVED;**
- 24 **4. BREACH OF EXPRESS WARRANTY;**
- 25 **5. BREACH OF IMPLIED WARRANTY;**
- 26 **6. NEGLIGENCE.**

27 *Allred v. City of San Diego, et al.*

28 **VERIFIED PETITION FOR WRIT OF MANDATE AND CLASS ACTION COMPLAINT**

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1 Barry Allred (“Plaintiff” and “Petitioner”), on behalf of himself and all others similarly situated,
2 by and through his undersigned counsel, hereby brings this action against Defendant the City of San Diego
3 and Defendant the City of San Diego Public Utilities Department (collectively “Defendants”), and upon
4 information and belief and investigation of counsel, alleges as follows:

5 **I. INTRODUCTION**

6 1. This action alleges that the City of San Diego Public Utilities Department (“SDPUD”)
7 unlawfully charges and collects service fees from residential and commercial (“R&C”) account customers
8 for wastewater services that are actually provided to SDPUD’s industrial customers throughout the
9 utility’s service area including industrial customers outside of San Diego.

10 2. These excess charges levied on R&C customers are illegal taxes under the California
11 Constitution as well as unlawful fees under California’s Government Code.

12 3. These fees imposed on residential and commercial customers unlawfully subsidize
13 SDPUD’s industrial wastewater customers, which pay far less than the actual cost of their service
14 throughout the service region.

15 4. Because the SDPUD fails to collect from industrial users all but a fraction of the cost of
16 the service provided to those customers, including accounts outside the City of San Diego, those costs are
17 imposed on R&C customers within the City of San Diego instead.

18 5. This practice unlawfully subsidizes selected private industrial wastewater-discharging
19 businesses at the expense of City of San Diego R&C customers.

20 6. The SDPUD is required, by state law, by the California Constitution, and by its own
21 published rate policy, to impose on R&C customers only such fees as are reasonably related to the cost of
22 wastewater services actually provided to those customers’ properties.

23 7. The excess fees that SDPUD imposes on its R&C customers to make up for the agency’s
24 failure to collect service fees from industrial users are unrelated to the cost of providing service to R&C
25 customers and are therefore not only an improper fee but an illegal tax as well. California Const. Art. XIII
26 D.

27 8. This Writ Petition and proposed Class Action accordingly seeks to compel the City of San
28 Diego to cease these illegal and unconstitutional practices and to reimburse its residential and commercial

1 account ratepayers for illegal taxes and fees that the SDPUD has charged and continues to charge those
2 customers.

3 **II. JURISDICTION AND VENUE**

4 9. Plaintiff, individually and on behalf of all others similarly situated, brings this action in
5 this Court pursuant to the California Constitution, Article VI, Section 10, and Section 382 of the California
6 Civil Code. This Court has subject matter jurisdiction over both the Writ Petition and the proposed class
7 action.

8 10. Defendants are governmental entities located in and acting within the State of California
9 and the County of San Diego. The exercise of personal jurisdiction over these Defendants by this Court is
10 therefore proper.

11 11. Venue is proper in this Court because each Defendant is a governmental entity located and
12 operating in this county. All of the decisions, transactions, and illegal taxes and fees complained of herein
13 occurred in this county including specifically the transactions between Plaintiff and Defendants.

14 **III. PARTIES**

15 13. Plaintiff and Petitioner Barry Allred lives in and is a resident of the City of San Diego.

16 14. Mr. Allred is currently and has during the proposed Class Period been a customer of the
17 City of San Diego PUD.

18 15. Plaintiff has paid and continues to pay SDPUD for sewer and wastewater service to a
19 residential property during the proposed Class period described herein.

20 16. Plaintiff has standing to assert the claims set forth herein on his own behalf and for a
21 proposed class of similarly situated persons.

22 17. Plaintiff has exhausted all administrative or other remedies available before commencing
23 this action. Plaintiff further has public interest standing to prosecute the claims of all other individuals
24 constituting the proposed Class.

25 18. Defendant City of San Diego is a California Charter city and municipal corporation
26 located in San Diego County.

27 19. Defendant the San Diego Public Utilities Department (SDPUD) is the City of San Diego
28 department responsible for, among other services, wastewater and sewer services provided to residents,

1 commercial businesses, industrial users, and others within the SDPUD service area, which includes but
2 is not limited to the City of San Diego.

3 20. The true names and capacities of Defendants sued as Does 1 through 10 are unknown to
4 Plaintiff at this time. Plaintiff therefore sues said Defendants by such fictitious names. Plaintiff will
5 amend this Complaint to allege the true names and capacities of Does 1 through 1,000 when ascertained.
6 Plaintiff is informed and believes, and thereupon alleges, that each of the Doe Defendants, jointly and
7 severally, are in some manner responsible for the damages alleged herein. Any reference to “Defendant”
8 includes Doe 1 though 10, inclusive.

9 **IV. GOVERNMENT CLAIMS REQUIREMENTS**

10 21. On June 3, 2021, Plaintiff/Petitioner presented to Defendants a written claim, using the
11 required city form, for a refund of excess and unlawful fees and illegal taxes paid to the City of San Diego
12 for wastewater services to date as described herein, on behalf of himself and others similarly situated.

13 22. That written claim complied with the requirements of the California Government Claims
14 Act, Cal. Gov’t Code §910, *et seq.*

15 23. Defendants failed to respond to those claims within the statutory 45-day period.

16 24. Plaintiff has exhausted all meaningful administrative remedies available to him.

17 25. Plaintiff therefore has complied with the Government Claims Act and accordingly has
18 standing to present the claims described herein.

19 **V. FACTUAL ALLEGATIONS**

20 26. The City of San Diego, through its Public Utilities Department (SDPUD), provides
21 wastewater sewerage and wastewater treatment services to residential, commercial, and industrial
22 customers within its designated service area.

23 27. That service area includes both the City of San Diego and several additional municipal
24 service areas and participating utility agency service areas. Table 1, below, shows municipalities and
25 agencies contracting for wastewater treatment services from outside the City of San Diego.

26 28. The SDPUD is a department of the City of San Diego that is mandated to provide sewerage
27 and wastewater treatment services to customers, and to bill customers for those services consistent with
28 its published fee rates and policies.

1 29. Administratively, SDPUD separates “Industrial” wastewater-discharging customers from
2 “Residential and Commercial” (“R&C”)wastewater customers; the latter two are grouped together.

3 30. Because industrial wastewater discharges are in general significantly different in both
4 quality and quantity from R&C discharges, industrial accounts are handled separately under SDPUD’s
5 Industrial Wastewater Control Program (IWCP).

6 31. The IWCP service area extends beyond the City of San Diego boundaries.

7 32. The IWCP program collects and processes wastewater from additional municipal service
8 areas and water districts within the county of San Diego but outside the City of San Diego. Participating
9 San Diego County municipalities and agencies are listed below in Table 1.

10 33. Through the IWCP, SDPUD in theory is required to levy sufficient fees for wastewater
11 collection and treatment service on industrial wastewater discharging customers to fully cover the cost
12 of providing service to those customers.

13 34. In fact, however, the IWCP continually fails to collect all but a fraction of the necessary
14 fees from industrial discharge customers.

15 35. Because SDPUD has no legitimate means by which it can make up for its failure to assess
16 and collect fees from its industrial customers, the agency makes up that deficit by collecting unlawful
17 excess fees from SDPUD’s Residential and Commercial customers.

18 36. SDPUD also fails to collect adequate service fees from its customers outside the City of
19 San Diego. This shortfall is also improperly charged to San Diego R&C customers.

20 37. Table 1, below, shows municipalities and agencies outside the City of San Diego to which
21 SDPUD also provides wastewater sewerage and treatment services.

22 Table 1: Municipalities and Agencies Contracting with SDPUD for Wastewater Service

23

24 Chula Vista	National City
25 Coronado	Poway
26 Del Mar	Alpine Service Area
27 El Cajon	East Otay Mesa Service Area

28

Imperial Beach	Lakeside Service Area
La Mesa	Spring Valley Service Area
Lemon Grove	Winter Gardens Service Area

A. Public utilities in California, including San Diego PUD, are required by law to assess property-related service fees only for the cost to provide that service to that property.

38. Public utility agencies in California operate under express requirements set forth in the state Government Code and the California Constitution for cost allocation and rate setting for any fees that are “property-related.” California Constitution, Art. XIII D, Section 2(h).

39. These constitutional requirements were established by a public referendum entitled Proposition 218 which amended the California Constitution.

40. As established by Proposition 218, any such “property related” fees must be proportional to and must not exceed the cost of providing those services to that property and must be used by the municipality to defray the actual cost of providing those services.

41. Further, California’s Government Code Section 54999.7 requires that any fees assessed by public agencies must be proportional to the cost of the services provided.

42. Government Code Section 54999.7 requires that fees for public utility service other than electricity or gas “must not exceed the reasonable cost of providing the utility service.”

43. In addition, and more specifically, Government Code Section 50076, adopted pursuant to Proposition 13, states that any charge or fee is a “special tax” unless “the fee does not exceed the reasonable cost of providing the service or regulatory activity for which the fee is charged[.]”

44. Government Code Section 50076 further requires that any fees assessed must not be used to collect money “for general revenue purposes.” If the proceeds from a fee are used for general revenue purposes the fee is a tax.

45. Sewer and wastewater treatment services are billed to property owners with their annual

1 property tax bills and are assessed upon and collected for each property. These fees are assessed in San
2 Diego on an address- or location-specific basis and are collected along with annual property taxes on that
3 property.

4 46. Sewer and wastewater treatment services are property-related services.

5 47. Wastewater and sewerage service fees are therefore “property-related” fees under the
6 California Constitution.

7 48. All fees for sewer and wastewater service must therefore comply with the constitutional
8 requirements of Proposition 218.

9 49. Under Proposition 218, any revenues from a property-related fee or charge cannot exceed
10 the cost of providing the service for which the fee is assessed.

11 50. Further, Proposition 218 also requires that revenues derived from the fee cannot be used
12 for any purpose other than that for which the fee is assessed. *See*, Cal. Const. Art. XIII D, Section 6(b)(1)-
13 (3).)

14 51. Government agencies that assess fees for property-related services bear the burden of
15 demonstrating that each of these requirements is met. Cal. Const Art. XIII C, Section 1.

16 52. Any fee assessed by a public wastewater utility must therefore bear a direct relationship
17 to the cost of the service provided. Such fees must not exceed the cost of providing that service to the
18 property assessed, and the funds derived from the fees must not be used for any purpose other than
19 delivering to that property those services for which the fees are assessed.

20 53. Wastewater service fees charged by SDPUD to Residential and Commercial customers
21 violate all of these criteria and are therefore both illegal fees and illegal taxes under California law.

22 **B. A 2013 city audit found that SDPUD failed to collect sewer and wastewater fees from**
23 **industrial wastewater dischargers and was charging excess fees to residential and**
24 **commercial customers to compensate for the agency’s shortfall.**

25 54. In 2013, the City of San Diego Office of the City Auditor (OCA) conducted an audit of
26 SDPUD’s Industrial Wastewater Control Program (IWCP).

27 55. The IWCP is the administrative program within SDPUD that is responsible for issuing
28 sewer permits to industrial users and for recommending, billing, and collecting fees for sewer and

1 wastewater treatment services provided to those users.

2 56. IWCP permittees are exclusively industrial wastewater dischargers.

3 57. Because industrial wastewaters may be orders of magnitude greater in volume and may
4 contain substances and contaminant loads that place greater demands on treatment infrastructure, the
5 permitting process is far more resource-intensive for such users and wastewater treatment is typically far
6 more expensive on a per-property basis.

7 58. It is essential for that reason that SDPUD accurately assess, account for, and collect the
8 fees owed to it from industrial users.

9 59. The OCA found in 2013, however, that the IWCP was characterized by “outdated fees,
10 billing lapses, and inadequate controls [that] limited program cost recovery from IWCP permittees.”¹

11 60. In its 2013 report, the Audit Committee found that “IWCP did not achieve adequate cost
12 recovery” from industrial wastewater dischargers.

13 61. Further, because of the agency’s error-riddled billing and collection practices the IWCP
14 has repeatedly failed to collect even the small fraction of fees for service that it does assess on Industrial
15 discharge customers.

16 62. The 2013 Audit disclosed that “between FY 2010 and FY 2012, billable costs exceeded
17 revenues by about \$8.3 million – meaning that only 15 percent of billable costs were recovered through
18 program fees charged to regulated businesses.”²

19 63. The remaining 85% of costs for the IWCP industrial discharge program services, the Audit
20 found, “were offset by charges to other ratepayers, including residential and commercial customers” and
21 that “the vast majority of program costs were being passed on to non-IWCP users via wastewater
22 rates[.]”³

23 64. The Audit therefore concluded in 2013 that illegal taxes or fees already “may have been
24 charged” to R&C customers to offset millions of dollars that should have been collected from IWCP
25

26 _____
27 ¹ City of San Diego, Office of the City Auditor: “Follow Up Performance Audit of the Industrial
Wastewater Control Program”, July 2020; OCA-21-001.

28 ² Id. at Page 1.

³ Id. at Page 2.

1 customers but were not.⁴

2 65. In its 2013 Audit Report - the public version - the OCA made 13 separate findings of
3 practices that SDPUD was required to implement to correct the agency’s critical failures in financial
4 controls, billing, and fee collection.

5 66. These were recommendations SDPUD was required to implement to correct the agency’s
6 improper and “possibly illegal” collection of excess fees from its R&C customers.

7 67. In a 2020 follow up to the 2013 Audit, however, the OCA found that at least ten of the
8 thirteen of the audit’s required recommendations had never been implemented and that as a result the
9 improper fee collection practices had continued essentially unchanged between 2013 and 2020.

10 **C. The city’s 2020 follow-up report found that SDPUD had failed to correct its**
11 **improper fee collection practices, and that Residential and Commercial customers**
12 **were still being overcharged to make up for the agency’s failure to collect fees from**
13 **IWCP accounts.**

14 68. In 2020 the OCA performed a follow-up assessment to its 2013 audit.

15 69. The OCA found in 2020 that after seven years the IWCP had failed to implement nearly
16 all of the 2013 audit recommendations and had failed in general to correct any of the fee calculation,
17 billing, and fee collection errors found in 2013.

18 70. OCA concluded that SDPUD had essentially made no progress on correcting its 2013
19 audit findings of improper fee collection from Residential and Commercial customers.

20 71. The OCA found in 2020 that between the years of 2010 and 2019, \$33.3 million in fees –
21 86% of total IWCP fees during that period – that should have been collected from IWCP accounts had
22 been charged to and collected from R&C customers instead.

23 **D. SDPUD continues to overcharge Residential & Commercial customers in violation**
24 **of California law to offset chronic shortfalls in fees collected from Industrial users.**

25 72. The OCA found in its 2013 Audit that the IWCP was failing to collect fees from industrial
26 users and instead charged excess fees to R&C customers to compensate for this ongoing failure.

27 _____
28 ⁴ The city auditor was careful not to include in its 2013 public report the explicit legal conclusion that
SDPUD was collecting illegal taxes, but rather “raised the possibility.” The OCA instead issued a
confidential memorandum to the Mayor of San Diego discussing this “possibility” in greater detail.

1 73. The 2020 Audit found that “the issues we identified in 2013 remain largely unaddressed.”

2 74. In its 2020 review, OCA concluded not only that at least \$33.3 million of the fees assessed
3 by the SDPUD on Residential and Commercial customers between 2010 and 2019 were improper, but
4 that SDPUD continued to fail to match the fees charged to R&C customers to the cost of providing service
5 to those customers and instead continued to overcharge R&C customers to offset undercharges and under-
6 collection of fees from SDPUD’s IWCP customers.

7 75. The 2020 follow up audit report found that unless SDPUD quickly implemented
8 significant corrective actions the improper and unlawful fee collections practices were likely to continue
9 as they had for well over a decade.

10 76. Among other findings, the OCA found in 2020 that “although City regulations and
11 policies require fees to be regularly reviewed and updated, we found that many IWCP fees had not been
12 updated *since as far back as 1984.*” (emphasis added)

13 77. From FY 2010 through FY 2019, IWCP costs of providing service to Industrial discharge
14 customers totaled approximately \$38.8 million.

15 78. Of those costs, only \$5.5 million, or 14%, was recovered from IWCP (industrial)
16 permittees.

17 79. The remaining \$33.3 million – 86% of the costs attributable to the industrial discharger
18 program – had been passed on to other wastewater customers in the form of excessive and unlawful rates
19 and fees.

20 80. The \$33.3 million in improper fees collected from R&C customers between 2010 and
21 2019 constitute illegal fees under state and municipal regulations, and SDPUD policy, and an illegal tax
22 under the California Constitution.

23 81. The OCA found that “these cost recovery practices remain out of compliance with City
24 regulations and policies” and that “more seriously, the possibility remains that, by passing on most
25 program costs to other wastewater customers, the City may not be complying with Prop. 218.”⁵

26 82. SDPUD’s fees to R&C customers in fact continue to violate Government Code Sections

27 _____
28 ⁵ See Footnote 2, above.

1 54999.7 and 50076, and the California Constitution, as well as violating the terms of service warranted
2 by SDPUD to its R&C customers.

3 83. The OCA further found that these subsidies “came exclusively from San Diego [R&C]
4 wastewater customers, even though IWCP serves the larger metro area” which includes additional
5 wastewater service areas and authorities (see Table 1).

6 84. The 2020 Audit found that “[SD]PUD has again failed to bill many IWCP permittees
7 [dischargers] outside the City [of San Diego.]” OCA 21-001, Jul 2020.

8 85. Because of SDPUD’s unlawful fee setting and negligent collection practices, R&C
9 customers have been subsidizing selected private businesses, both within the City of San Diego and in
10 surrounding areas, for over a decade.

11 86. On March 25, 2021, the City of San Diego PUD announced that it was planning on
12 increasing sewer charges for all customers by a staged series of fee increases over the years 2022 – 2025.

13 87. SDPUD’s proposed fee increases will not compensate Plaintiff or the proposed class for
14 the years of illegal taxes and unlawful fees that the SDPUD has collected from R&C customers or correct
15 that continuing wrong.

16 88. This action therefore seeks to compel the City of San Diego and SDPUD to cease
17 assessing and collecting improper fees and illegal taxes from R&C customers and to refund to R&C
18 customers all such improper fees and taxes illegally collected during the proposed Class Period.

19 **VI. DELAYED DISCOVERY**

20 89. Plaintiff did not discover until May 2021 that the fees he paid to SDPUD for sewer and
21 wastewater services for his property were unlawful and were not being used solely to provide service to
22 his and class members’ properties but to subsidize industrial wastewater dischargers instead.

23 90. Plaintiff is a reasonably diligent consumer of public utility services who exercised
24 reasonable care in paying his SDPUD sewer and wastewater bills.

25 91. Nevertheless, he would not have been able to discover Defendants’ deceptive and unlawful
26 practices and lacked the means to discover them given that, like nearly all consumers, he relies on and is
27 entitled to rely on the city and agency’s obligations to conduct its operations and impose fees on customers
28 only in compliance with its published policies, city and state law, and the California Constitution.

1 92. Furthermore, Defendants’ opaque practices and procedures impeded Plaintiff’s and the
2 Class members’ abilities to discover the deceptive and unlawful practices throughout the Class Period.

3 93. Because Defendants actively concealed the illegal conduct, preventing Plaintiff and the
4 Class from discovering the contractual violations and violations of state law and the state Constitution,
5 Plaintiff and the Class are entitled to delayed discovery and an extended Class Period tolling the
6 applicable statute of limitations.

7 **VII. CLASS ACTION ALLEGATIONS**

8 94. Plaintiff brings this action on behalf of himself and all others similarly situated (the
9 “Class”) pursuant to California Civil Code Section 382.

10 95. The Class is defined as follows:

11 All San Diego SDPUD customers who paid bills assessed by the SDPUD for wastewater
12 service provided to a residential or commercial account at an address within the City of
13 San Diego, on or after January 1, 2009 and until the date the Class is certified by the
14 Court, excluding Defendants and Defendants’ officers, directors, employees, agents, and
15 affiliates, and the Court and its staff.

16 96. During the Class Period, Defendants unlawfully imposed fees and taxes on Class members
17 which subsidized industrial wastewater dischargers at the expense of R&C customers, in violation of the
18 city’s stated and warranted rate policy, state law, and the California Constitution.

19 97. Class members during the proposed Class Period paid these illegal taxes and fees and
20 incurred the same injuries as alleged herein for the Plaintiff.

21 98. The proposed Class meets all criteria for a class action, including numerosity, typicality,
22 superiority, and adequacy of representation; there is a well-defined community of interest in questions of
23 law and fact common to the Class.

24 99. The proposed Class satisfies numerosity. R&C accounts within the City of San Diego
25 number over one hundred thousand. Individual joinder of the class members in this action is impractical.
26 Addressing the class members’ claims through this class action will benefit Class members, the parties,
27 and the courts.

28 100. The proposed Class satisfies typicality. Plaintiff’s claims are typical of and are not

1 antagonistic to the claims of other Class members. Plaintiff and the class members all paid San Diego
2 SDPUD sewer account bills which included the above-described excess and illegal taxes or fees and were
3 deprived of money as a result.

4 101. The proposed Class satisfies superiority. A class action is superior to any other means for
5 adjudication of the Class members' claims because each class member's claim is modest, estimated to be
6 on the order of \$50.00. It would be impractical for individual class members to bring individual lawsuits
7 to vindicate their claims. If this action is not brought as a class action, Defendants can continue to deceive
8 their customers, impose illegal fees and taxes, violate the state Constitution, and retain monies illegally
9 collected from the Class.

10 102. Because Defendants' unlawful fees and taxes were collected uniformly from all R&C
11 account included in the Class, all Class members including Plaintiff were deceived and unlawfully billed.

12 103. The proposed Class representative satisfies adequacy of representation. Plaintiff is an
13 adequate representative of the Class as he seeks relief for the Class, his interests do not conflict with the
14 interests of the Class members, and he has no interests incompatible with those of other class members.
15 Plaintiff has retained counsel competent in the prosecution of consumer fraud and class action litigation.

16 104. There is a well-defined community of interest in questions of law and fact common to the
17 Class, and these predominate over any individual questions affecting individual Class members in this
18 action.

19 105. Questions of law and fact common to Plaintiff and the Class include:

- 20 a. Whether Defendants failed to collect the full cost of service from industrial
21 wastewater dischargers;
- 22 b. Whether Defendants charged excess fees to R&C customers in the City of
23 San Diego to compensate for the resulting shortfall instead;
- 24 c. Whether those fees collected from the Class constituted improper fees under
25 published City of San Diego SDPUD fee-setting policy;
- 26 d. Whether those fees collected from the Class constituted improper fees under
27 California's Government Code;
- 28 e. Whether those fees collected from the Class violated the State of

1 California's Constitution under Proposition 218;

2 f. Whether excess fees collected from the Class were illegal taxes under
3 Proposition 218/California Const. Art. XIII D;

4 g. Whether Defendants' conduct abridged Plaintiff's and the Class's state
5 constitutional rights;

6 h. Whether Defendants should be required to refund illegal taxes collected
7 from the Class;

8 i. Whether the statute of limitations should be tolled on behalf of the Class
9 due to Defendants' deliberate and knowing deceptive conduct in concealing
10 that they were imposing unlawful taxes and fees;

11 j. Whether Plaintiff/Petitioner is entitled to a Writ of Mandate;

12 k. Whether Plaintiff and the Class are entitled to restitution, rescission, actual
13 damages, attorney fees and costs of suit, and injunctive relief; and

14 l. Whether members of the Class are entitled to any such further relief as the
15 Court deems appropriate.

16 106. Class members lost money as a result of Defendants' unlawful behavior.

17 107. Further, Defendants have acted on grounds applicable to the entire Class, making final
18 declaratory or injunctive relief appropriate for the Class as a whole.

19 108. Class treatment is therefore appropriate for this Action.

20 **VIII. CAUSES OF ACTION**

21 **First Cause of Action: Petition for Writ of Mandate**

22 100. Plaintiff/Petitioner realleges and incorporates by reference each of the allegations made
23 elsewhere in the Complaint as if set forth in full herein.

24 101. Defendants/Respondents are required by state law to comply with the California
25 Constitution, Article XIII D, Section 6(b), as compelled by Proposition 218.

26 102. Under those provisions, Respondents are now and were at all times relevant required to
27 assess on and collect from R&C customers only such fees for wastewater services as are necessary to
28 offset the actual costs to provide those services, and to use all monies collected exclusively to provide

1 those services to R&C customers.

2 103. Respondents violated and continue to violate these provisions of Proposition 218 and the
3 California Constitution.

4 104. Defendants are and at all times relevant were aware that the fees assessed to R&C
5 customers included charges to offset uncollected costs of providing sewer service to IWCP customers
6 both within and outside the City of San Diego.

7 105. As a result of Respondents' violations, Plaintiff and the Class suffered and continue to
8 suffer ascertainable losses in the form of the excess fees they paid and continue to pay, which they would
9 not if Defendants had complied with Proposition 218.

10 106. Petitioner has a present right to Defendants' compliance with the California Constitution
11 and California state law, and therefore to Defendants' performance of the required fee-setting and levying
12 of duties.

13 107. Defendants' violations are continuing.

14 108. Defendants have the power and ability to rectify these violations.

15 109. Plaintiff therefore petitions for a writ of mandate pursuant to California Code of Civil
16 Procedure 1085 compelling Defendants to comply with these mandatory duties to comply with the
17 California Constitution and reimbursing to Plaintiff and the proposed Class all fees unlawfully collected.

18 110. Plaintiff and the proposed Class have no plain, speedy, and adequate remedy at law.

19 **Second Cause of Action: Violation of California Constitution, Proposition 218**

20 **Declaratory, Injunctive, and Equitable Relief**

21 111. Plaintiff realleges and incorporates by reference each and every allegation contained
22 elsewhere in this Complaint as if fully set forth herein.

23 112. Defendants' conduct violated the California Constitution, Article XIII D, because the fees
24 that Defendants charged to and collected from Plaintiff and the proposed Class for wastewater services
25 at their properties were an illegal tax exceeding the cost to provide those services to those properties.

26 113. The fees Defendants charged to Plaintiff and the proposed Class further violate the
27 California Constitution, Article XIII D, section 6, subsections (b)(1) and (b)(2), because those fees were
28 used to compensate for monies uncollected from the provision of wastewater services to industrial users,

1 a purpose other than the use for which those fees were collected from Residential and Commercial users.

2 114. Defendants' conduct further violated the California Constitution, Article XIII D, section
3 6, subdivision (b)(3), because the fees that Defendants charged to and collected from Plaintiff and the
4 proposed Class for wastewater services at their properties were an illegal tax exceeding the proportional
5 cost to provide those services attributable to the parcel to which the fees were assessed.

6 115. These constitutional violations are the direct result of Defendants' actions and may be
7 redressed by Defendants' correction of those actions, retrospectively and prospectively.

8 116. This is an active controversy between the parties. Defendants unlawfully retain fees that
9 were collected from Plaintiff and the proposed Class in violation of the California Constitution and
10 continue to collect such fees unlawfully.

11 117. Plaintiff does not have an adequate remedy at law.

12 118. Plaintiff therefore seeks declaratory and injunctive relief.

13 119. Plaintiff seeks declaratory relief declaring the rights of and obligations the parties in this
14 active conflict.

15 120. Plaintiff seeks a declaration that the fees described above in this action that have been
16 imposed and continue to be imposed on Plaintiff and the proposed Class violate the California
17 Constitution.

18 121. Plaintiff further seeks injunctive relief and restitution, to prevent Defendants from
19 continuing to impose these unconstitutional and unlawful fees and to return to Plaintiff and the proposed
20 Class all such fees illegally collected during the proposed Class period.

21 122. Unless enjoined by this Court, Defendants will continue to impose and collect unlawful
22 fees from Plaintiff and the proposed Class.

23 123. Plaintiff and the proposed Class have sustained damages as a direct result of Defendants'
24 constitutional violations.

25 124. The Court has the equitable power to return to Plaintiff and the proposed Class all such
26 monies unlawfully collected.

27 **Third Cause of Action: Money Had and Received**

28 109. Plaintiff realleges and incorporates by reference the allegations made elsewhere in the

1 Complaint as if set forth in full herein.

2 110. Defendants received excess monies from Plaintiff and the Class as a result of improper
3 fees and unlawful taxes assessed for property-related services in violation of the California Constitution
4 and California state law.

5 111. Defendants benefitted from receipt of this money.

6 112. As a result of Defendants' violations, Plaintiff and the Class suffered ascertainable losses
7 in the form of the cost premiums they paid for wastewater services to compensate for fees that SDPUD
8 improperly failed to collect from IWCP customers.

9 113. Under principles of equity and good conscience, Defendants should not be permitted to
10 retain this money.

11 114. Plaintiff and the members of the Class are thus entitled to recovery of the funds they
12 expended which were used to unlawfully subsidize the services provided to IWCP permittees.

13 **Fourth Cause of Action: Breach of Express Warranty**

14 115. Plaintiff realleges and incorporates by reference the allegations found elsewhere in the
15 Complaint as if set forth in full herein.

16 116. Defendants warranted to Plaintiff and the proposed Class, as a promise and statement of
17 fact, that the fees charged to R&C customers would not exceed the actual cost of providing those services.

18 117. As described herein, Defendants breached that warranty.

19 118. Defendants charged Plaintiff and the Class fees that included a preponderance of the cost
20 of service provided to industrial account customers instead of only the cost of service attributable to R&C
21 customers' properties.

22 119. This violated Defendants' warranty to Plaintiff and the Class that the fees charged would
23 reflect only the costs of service to R&C customers.

24 120. Plaintiff took reasonable steps to notify Defendants within a reasonable time that the fees
25 charged were not as represented and warranted.

26 121. Defendants actually received such notice.

27 122. Defendants failed to remedy the excessive fees charged.

28 123. Plaintiff and the Class were harmed thereby.

1 124. Defendants' failure to abide by their warranty for rate setting was a substantial factor in
2 causing Plaintiff's harm.

3 125. It is not necessary for Defendants to have intended to create a warranty.

4 126. These promises became part of the basis of the bargain between the parties and thus
5 constituted an express warranty which Defendants breached.

6 127. Defendants sold the services to Plaintiff and the other Class members who bought the
7 services from Defendants.

8 128. Plaintiff and the Class did not receive services as warranted by Defendant.

9 129. As a proximate result of this breach of warranty, Plaintiff and the Class have been
10 damaged in an amount to be determined at trial.

11 130. Plaintiff and the Class are entitled to injunctive and equitable relief, restitution, and an
12 order for the disgorgement of the funds by which Defendants were unjustly enriched.

13 **Fifth Cause of Action: Breach of Implied Warranty**

14 131. Plaintiff realleges and incorporates the allegations made elsewhere in the Complaint as if
15 set forth in full herein.

16 132. Defendants' published policy statements and representations also created implied
17 warranties under California law that the fees charged to R&C customers complied with municipal policy
18 and state law and the California Constitution. Defendants breached these implied warranties as well.

19 133. As alleged in detail above, at the time of the services were provided Defendants had reason
20 to know that Plaintiff, as well as all members of the Class, were relying on Defendants to provide services
21 in compliance with municipal policy and state law including Prop 218 and the California Constitution.

22 134. This became part of the basis of the bargain between the parties.

23 135. Based on that implied warranty, Defendants provided these services and charged Plaintiff
24 and other Class members for the services, who bought the services from Defendant.

25 136. At the time of purchase, Defendants knew or had reason to know that Plaintiff and the
26 Class members were relying on Defendants' skill and judgment to set and collect fees in accordance with
27 Proposition 218 and state and municipal policy and SDPUD policy, and Plaintiff and the Class justifiably
28 relied on Defendants' skill and judgment.

1 137. Because of the multiple violations alleged herein, the services were not provided in
2 accordance with this warranty.

3 138. Plaintiff purchased the services believing they had the qualities Plaintiff sought, but the
4 services as provided to Plaintiff did not comply with those warranties.

5 139. As a result of this breach, Plaintiff and the other Class members did not receive sewer
6 service at the rates impliedly warranted by Defendant.

7 140. Within a reasonable amount of time after Plaintiff discovered that the Products breached
8 these warranties, Plaintiff notified Defendants of such breach.

9 141. As a proximate result of this breach of warranty, Plaintiff and other Class members have
10 been damaged in an amount to be determined at trial.

11 142. As a result, Plaintiff and the Class are entitled to injunctive and equitable relief,
12 restitution, and an order for the disgorgement of the funds by which Defendants were unjustly enriched.

13 **Sixth Cause of Action: Negligence**

14 143. Plaintiff realleges and incorporates the allegations made elsewhere in the Complaint as if
15 set forth in full herein.

16 144. Defendants, individually and collectively, had throughout the propose Class period and
17 currently have a mandatory duty to Plaintiff and the proposed Class to assess and collect only such fees
18 for wastewater services as are required to deliver those services to each respective property-related
19 account.

20 145. Defendants breached that duty because Defendants assessed on and collected from
21 Plaintiff and proposed Class members wastewater fees that were inflated to compensate for Defendants'
22 failure to assess and collect adequate fees from SDPUD Industrial dischargers under the IWCP program.

23 146. Defendants failed to assess and collect these fees from IWCP accounts and assessed and
24 collected excess fees from R&C account customers to compensate for the shortfall.

25 147. SDPUD Residential and Commercial customers were damaged by paying excess fees to
26 make up for Defendants' failure to properly collect fees from Industrial account customers.

27 148. Defendants' actions were the proximate cause of those damages.

28 149. Plaintiff and the proposed Class are therefore entitled to a return of all excess fees

1 collected from them as damages proximately resulting from Defendants' negligence.

2 **IX. PRAYER FOR RELIEF**

3 WHEREFORE, Plaintiff, on behalf of himself and all others similarly situated, prays for judgment
4 against Defendants as follows:

- 5 A. An order declaring that the conduct complained of herein violates California Constitution;
- 6 B. An order declaring that the conduct complained of herein violates California state law;
- 7 C. An order declaring that the conduct complained of herein violates Defendants' express
8 written rate-setting policy;
- 9 D. An order issuing a Writ of Mandate as requested herein;
- 10 E. An order certifying that this action is properly maintainable as a class action as defined
11 above, appointing Plaintiff and his undersigned counsel to represent the Class, and
12 requiring Defendants to bear the cost of class notice;
- 13 F. An order permanently enjoining Defendants' unlawful and improper fee collection
14 practices;
- 15 G. An order requiring Defendants to disgorge any benefits received from Plaintiff and the
16 Class and any unjust enrichment realized as a result of the illegal taxes or improper fees;
- 17 H. An order requiring Defendants to pay restitution to Plaintiff and Class members so that
18 they may be restored any money which was acquired by means of any illegal, unfair,
19 deceptive, unconscionable or negligent acts;
- 20 I. An order declaring that the conduct complained of herein breached Defendants' warranted
21 obligations to Plaintiff and the Class;
- 22 J. An order finding that Defendants' conduct in charging excess fees was negligent with
23 respect to Plaintiff and the Class.
- 24 K. An order requiring Defendants to inform class members about the conduct described
25 herein;
- 26 L. An order finding that this proceeding is brought in the public interest to vindicate
27 important public rights and for the broad benefit of residents of San Diego who directly
28 or indirectly pay for residential or commercial wastewater services.

1 M. An award of attorney fees, pursuant to California Code of Civil Procedure section 1021.5
2 or the Court's inherent powers, and costs;

3 N. An award of pre-judgment and post-judgment interest; and

4 O. Such other and further relief as this Court may deem just, equitable, or proper.

5 **X. JURY DEMAND**

6 Plaintiff demands a trial by jury on all claims for damages. Plaintiff does not seek a jury trial for
7 claims sounding in equity.

8
9 DATED: July 20, 2021

Respectfully Submitted,

10
11 /s/ Ronald A. Marron

12 **LAW OFFICES OF**
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VERIFICATION

I, BARRY ALLRED, am the Petitioner/Plaintiff in this action.

I have read the above Petition For Writ Of Mandate and Class Action Complaint and believe the allegations in that Petition and Complaint to be true of my own knowledge based on investigation of counsel, except matters stated on information and belief, and as to them I believe them to be true. I declare under penalty of perjury that the foregoing is true.

Executed in San Diego, California on 7/19/2021



Barry Allred

EXHIBIT 1

FOLLOW-UP PERFORMANCE AUDIT OF THE PUBLIC UTILITIES DEPARTMENT'S INDUSTRIAL WASTEWATER CONTROL PROGRAM

The Public Utilities Department's
Cost Recovery Practices Remain Out
of Compliance with City Regulations
and Policies and Possibly State Law

Office of the
City Auditor

City of San Diego



Follow-Up Performance Audit of the Industrial Wastewater Control Program

The Public Utilities Department's Cost Recovery Practices for IWCP Remain Out of Compliance with City Policies and Possibly State Law

Why OCA Did This Study

The Public Utilities Department's (PUD) Industrial Wastewater Control Program (IWCP) permits, monitors, and inspects a variety of industries across the City and 12 other Participating Agencies to detect and minimize the discharge of toxic substances into the sewerage system.

In 2013, we issued a [performance audit of IWCP](#). At that time, we found that outdated fees, billing lapses, and inadequate controls limited program cost recovery from IWCP permittees. Most program costs were passed on to other wastewater customers who were not IWCP permittees. In addition, we issued a confidential memorandum raising the possibility that these cost recovery practices were not in compliance with Proposition 218 (Prop 218).¹ The objective of the current audit was to review the status of the recommendations we made in 2013.

What OCA Found

We found that the issues we identified in 2013 remain largely unaddressed.

Finding 1: While an IWCP fee update is in progress, it has not been completed, and many program fees remain unadjusted since 1984. As a result, from FY 2010 to FY 2019, program costs totaled about \$38.8 million, of which only \$5.5 million (14 percent) was recovered from fees charged to IWCP permittees. The remaining \$33.3 million (86 percent) was passed on to other customers via wastewater rates. By not regularly reviewing IWCP fees and presenting them to the City Council for approval, PUD's IWCP cost recovery practices remain out of compliance with City regulations and policies. In addition, the continuance of these practices again raises the possibility of non-compliance with Prop 218.¹

Finding 2: PUD continues to use overly-complex billing processes for IWCP, which is inefficient and has caused billing lapses. Even though PUD implemented our 2013 recommendation to recover unbilled costs from FY 2008 to FY 2012, we found that, since FY 2017, PUD has again failed to bill many IWCP permittees outside the City.



Source: U.S. Environmental Protection Agency

What OCA Recommends

We make a total of 9 recommendations to correct the issues we identified, which are similar to the public and confidential recommendations we made in 2013.

Specifically, we recommend that PUD:

- Document procedures to track IWCP costs and revenues;
- Complete the current IWCP fee study, consult with the City Attorney's Office to develop a fee proposal that is in compliance with City regulations, policies, and state law, and present the proposal to the City Council for approval;
- Document policies and procedures for periodically reviewing and updating IWCP fees moving forward;
- Consolidate and simplify the billing process for IWCP fees; and
- Seek recovery of IWCP fees that went unbilled since FY 2017.

PUD agreed with all 9 recommendations and has taken several steps towards implementation.

For more information, contact Kyle Elser, Interim City Auditor at (619) 533-3165 or cityauditor@sandiego.gov

¹ We do not reach any legal conclusions in our report regarding Proposition 218, and nothing in our report should be interpreted as any type of legal conclusion.



THE CITY OF SAN DIEGO

July 15, 2020

Honorable Mayor, City Council, and Audit Committee Members
City of San Diego, California

Transmitted herewith is a follow-up performance audit report on the Public Utilities Department's Industrial Wastewater Control Program. This report was conducted in accordance with the City Auditor's Fiscal Year 2020 Audit Work Plan, and the report is presented in accordance with City Charter Section 39.2. The Results in Brief are presented on page 1. Audit Objectives, Scope, and Methodology are presented in Appendix B. Management's responses to our audit recommendations are presented after page 49 of this report.

We would like to thank staff from the Public Utilities Department and the City Attorney's Office. All of their valuable time and efforts spent on providing us information is greatly appreciated. The audit staff members responsible for this audit report are Shadi Matar, Luis Briseño, Danielle Knighten, and Andy Hanau.

Respectfully submitted,

Kyle Elser
Interim City Auditor

cc: Kris Michell, Chief Operating Officer
Jeff Sturak, Assistant Chief Operating Officer
Johnnie Perkins, Deputy Chief Operating Officer, Public Utilities/Infrastructure
Shauna Lorange, Director, Public Utilities Department
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Lisa Celaya, Assistant Director, Public Utilities Department
John Stufflebean, Assistant Director, Public Utilities Department
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Charles Modica, Deputy Director, Public Utilities Department
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Matthew Helm, Chief Compliance Officer
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Jessica Lawrence, Director of Policy and Council Affairs, Office of the Mayor
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Results in Brief

The Public Utilities Department's (PUD) Industrial Wastewater Control Program (IWCP) represents a key element of the City of San Diego's (City) environmental management efforts. IWCP permits, monitors, and inspects a variety of industries across the City and 12 other Participating Agencies (PAs) to detect and minimize the discharge of toxic substances into the metropolitan sewerage system. The sewage is treated by the City's wastewater treatment plants before being discharged into the Pacific Ocean.

Summary of Previous Audit Findings

In August 2013, we issued a public performance audit of IWCP that assessed the extent to which the program's permit and inspection fees and billing processes met legal requirements, achieved appropriate cost recovery, and ensured timely collection. We found that outdated fees, billing lapses, and inadequate controls limited program cost recovery.

Specifically, although City regulations and policies require fees to be regularly reviewed and updated, we found that many IWCP fees had not been updated since as far back as 1984. Moreover, PUD was not tracking program costs.¹ As a result, IWCP did not achieve adequate cost recovery. We estimated that between FY 2010 and FY 2012, billable costs exceeded revenues by about \$8.3 million—meaning that only 15 percent of billable costs were recovered through program fees charged to regulated businesses. The other 85 percent of costs were offset by charges to other ratepayers, including residential and commercial customers. In addition, we found that IWCP had not issued bills to many permittees for a five-year period, from FY 2008 to FY 2012, totaling \$850,000.

In addition to our public audit report, we raised additional legal concerns in a confidential memorandum to the Mayor,

¹ As reported in our August 2013 audit, PUD was not able to precisely determine recoverable program costs because it did not maintain sufficient data to do so and because a formal workload study to identify program costs had not been conducted.

PUD, and the City Attorney's Office in May 2013.² Specifically, the fact that the vast majority of program costs were being passed on to non-IWCP users via wastewater rates created the possibility that PUD's cost recovery practices were out of compliance with Proposition 218 (Prop 218).³ Adopted by California voters in 1996, Prop 218 generally requires that "property related fees and charges"—including charges for water and sewer service—not exceed the cost of providing the service.

We made a total of 8 recommendations in our public audit and an additional 5 recommendations in our confidential memorandum to ensure that program costs are tracked; fees are regularly reviewed and updated; billing is timely; and cost recovery practices comply with City regulations and policies as well as state law. Since 2013, we have kept the Mayor, the City Council, and the Audit Committee informed of PUD's progress in implementing these recommendations via periodic recommendation follow-up reports. During this time, PUD only provided evidence to demonstrate that 3 of the 13 recommendations were fully implemented.⁴

² This memorandum was issued confidentially because cost recovery at the time was unclear (because program costs were not being tracked); additional City analysis was needed to determine whether there was a risk of Prop 218 non-compliance; and because the memorandum contains sensitive and privileged information. While that memorandum remains confidential because it contains sensitive and privileged information, given the time that has passed and the new information that has become available, we have determined that it is in the public interest to raise the pertinent issues here so that management and oversight bodies can act to quickly and appropriately resolve them as needed. Any reference to the 2013 confidential memorandum is not intended in any way to waive the confidentiality of the report itself or to otherwise make the confidential report or any portion of it subject to disclosure.

³ We do not reach any legal conclusions in this report regarding Proposition 218, and nothing in this report should be interpreted as any type of legal conclusion.

⁴ OCA reports on the status of outstanding public audit recommendations on a six-month interval and reports on the status of outstanding confidential recommendations periodically, the most recent of which we completed in June 2019. During the follow-up process, OCA reviews information provided by management to determine whether a recommendation has been implemented.

The Issues We Identified in 2013 Remain Largely Unaddressed, and PUD's Cost Recovery Practices Remain Out of Compliance With City Regulations and Policies and Possibly State Law

Given the serious issues that were identified in 2013, and the apparent lack of progress in implementing our recommendations, we conducted this follow-up audit to evaluate the current state of PUD's cost recovery efforts for IWCP. Specifically, our audit objectives were to review the implementation status of our 2013 recommendations and publicly report on the issues we had identified in 2013 through both our public audit and our confidential audit memorandum.

We found that, while some progress has been made, the issues we identified in 2013 remain largely unaddressed. PUD began tracking IWCP costs in 2014 in an effort to facilitate an update to program fees. PUD has also commissioned several consultant fee studies, although two of these studies were cancelled after we identified methodological issues during our recommendation follow-up process, and none have yet been finalized and presented to the City Council for approval. A new fee study is nearing completion, and PUD plans to present the results to the City Council by January 2021. As a result, many fees still remain unadjusted since 1984, and program cost recovery remains very low. From FY 2010 through FY 2019, IWCP costs have totaled approximately \$38.8 million. Of these costs, only \$5.5 million (14 percent) was recovered from IWCP permittees while the remaining \$33.3 million (86 percent) was passed on to other wastewater customers, such as residential and commercial customers, via wastewater rates.

These cost recovery practices remain out of compliance with City regulations and policies. More seriously, the possibility remains that, by passing on most program costs to other wastewater customers, the City may not be complying with Prop 218.⁵ We also identified an additional concern with Prop 218 compliance that is created by complexities in PUD's wastewater accounting and its agreement with regional PAs. Specifically, due to these complexities, the \$33.3 million needed to subsidize IWCP between FY 2010 and FY 2019 came

⁵ As previously noted, we do not reach any legal conclusions in this report regarding Proposition 218, and nothing in this report should be interpreted as any type of legal conclusion.

exclusively from City of San Diego wastewater customers, even though IWCP serves the larger metro area, including 12 PAs.

Additionally, even though PUD implemented our 2013 recommendation to recover the approximately \$850,000 in costs that went unbilled from FY 2008 to FY 2012,⁶ we found that, since FY 2017, PUD again failed to bill many IWCP permittees outside the City. As in 2013, we found this was largely due to overly-complex and labor-intensive billing processes and a breakdown in billing oversight.

We make a total of 9 recommendations to address the issues identified above, which are similar to the public and confidential recommendations we made in 2013. Specifically, we recommend that PUD document its procedures to track IWCP costs and revenues; complete the current fee study and work with the City Attorney's Office to develop a fee proposal in compliance with City regulations, policies, and state law, and present these fees to the City Council for approval; document policies and procedures for periodically reviewing and updating fees moving forward; and consolidate and simplify its IWCP billing process. Management agreed to implement all 9 recommendations.

⁶ Prior to the completion of our 2013 audit, PUD sent invoices for unbilled charges accrued during FY 2008 and FY 2009. Then, in our office's Audit Recommendation Follow-up Report for the period ending June 30, 2014, we verified that PUD invoiced for previously unbilled permits and monitoring services for FY 2010 through FY 2012, totaling about \$628,000.

Background

The Public Utilities Department’s (PUD) Industrial Wastewater Control Program (IWCP) represents a key element of the City of San Diego’s (City) environmental management efforts. Implemented in 1982, IWCP is a pretreatment and pollution prevention program intended to minimize toxic discharges to the metropolitan sewerage system. To that end, IWCP operates an industrial wastewater discharge permit, monitoring, and enforcement system for the City and 12 other jurisdictions, referred to as Participating Agencies (PAs), within the County of San Diego. The sewage is treated by the City’s wastewater treatment plants before being discharged into the Pacific Ocean. IWCP’s budgeted staffing and expenses for recent years are summarized in **Exhibit 1**.

Exhibit 1

Industrial Wastewater Control Program Budgeted Staffing and Expenses, 2017 – 2020

	2017	2018	2019	2020
Positions	29	26	32	32
Expenses	\$3,814,965	\$3,356,631	\$3,971,596	\$3,971,596

Notes: Figures in the table reflect total budgeted staffing and expenses for all sections of the program (permits, enforcement, supportive services, and sampling). According to PUD, this does not include costs from the Environmental Chemistry Services section (ECS), which analyzes user samples for IWCP, because this is not a core ECS function. According to PUD, IWCP samples make up only about 6 percent of ECS’s total expenses.

Figures for 2017 through 2019 reflect information from PUD’s Annual Wastewater Pretreatment Program Reports, which is reported on a calendar year basis. Figures for 2020 reflect budget information from the City’s enterprise resource planning system, which is recorded on a fiscal year basis.

Source: Auditor generated based on information from PUD and the City’s enterprise resource planning system, SAP.

IWCP Operational Focus IWCP was created in July 1982 after being formally approved by the U.S. Environmental Protection Agency (EPA). IWCP applies and enforces federal pretreatment regulations set forth by the EPA pursuant to the Code of Federal Regulations⁷ and the Clean Water Act. In addition, under state and federal regulations—and as described in the Point Loma Wastewater Treatment Plant’s NPDES⁸ Permit—the City must implement the federal Industrial Pretreatment Program to control the discharges of all Significant Industrial Users (SIUs).⁹ The NPDES Permit additionally requires the City to implement a non-industrial Source Control Program to regulate the discharge of toxic pollutants and pesticides into the system from non-industrial sources.

In general, IWCP’s primary focus is to minimize toxic discharges to the sewerage system. The program consists of:

1. An industrial wastewater discharge permit system to establish industrial discharge limits and requirements;
2. Periodic facility inspections and unannounced sampling;
3. Enforcement procedures to deter violations and bring noncompliant dischargers back into compliance with discharge standards and requirements; and

⁷ Title 40, Part 403, 1981.

⁸ Created in 1972 by the Clean Water Act, the National Pollutant Discharge Elimination System (NPDES) permit program is authorized to state governments by EPA to perform many permitting, administrative, and enforcement aspects of the program. NPDES addresses water pollution by regulating point sources that discharge pollutants to waters of the United States.

⁹ According to PUD, SIUs are all industrial users that are subject to categorical pretreatment standards set forth in Title 40 of the Code of Federal Regulations, Chapter I, Subchapter N, Parts 405 - 471. The term “SIU” includes industrial users that: discharge an average of 25,000 gallons per day of process wastewater (excluding sanitary and “dilute wastewater,” as defined at 40 CFR 403.6 e(1)(i) under “FD”); contributes a process waste stream that makes up 5 percent or more of average dry weather hydraulic or organic capacity of the publicly-owned treatment works; or is determined to have reasonable potential for adversely affecting the publicly-owned treatment works’ operation or for violating any pretreatment standard or requirement.

4. Industrial user guidance and permit conditions designed to encourage pollution prevention and waste minimization.

**IWCP Industrial
Wastewater Discharge
Permits**

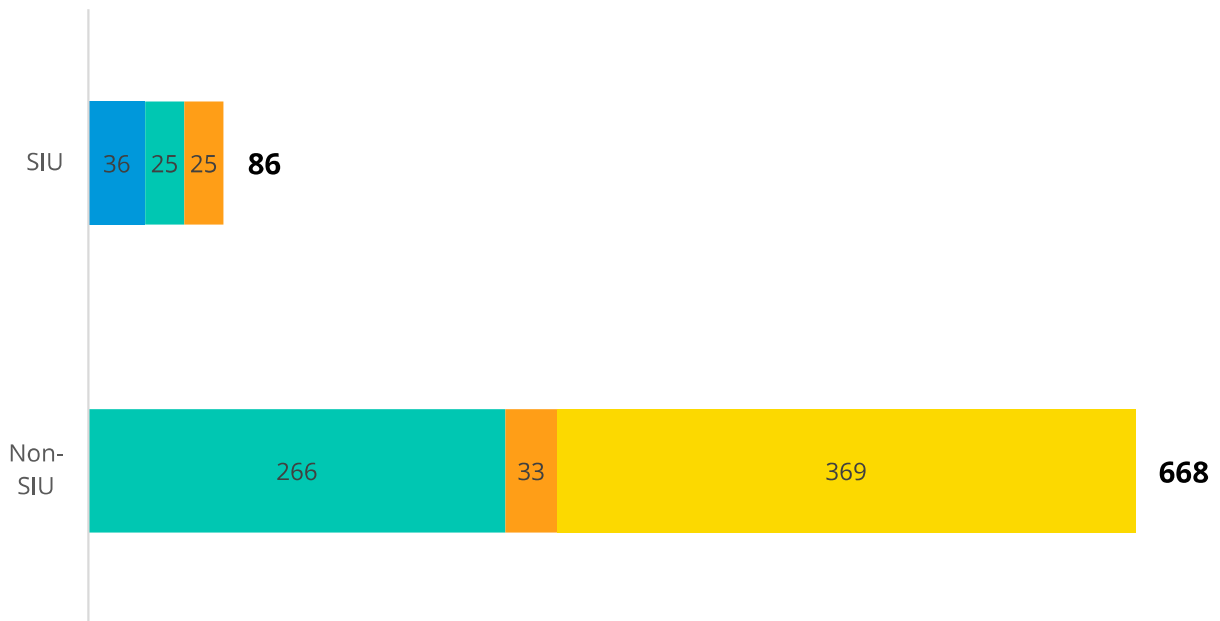
IWCP regulates various types of industries,¹⁰ primarily by issuing a variety of permits to businesses based on industry type and amount of wastewater discharge.¹¹ According to the program's annual report, IWCP had an inventory of almost 900 active permits as of December 31, 2019. **Exhibit 2** below provides a breakdown of the number of SIU and non-SIU permits as of December 31, 2019 and an explanation of the associated permit types.

¹⁰ These include aerospace manufacturing; metal forming, casting and finishing; pharmaceutical manufacturing; hospitals and medical centers; film processors; laundries and dry cleaners; and a variety of laboratories.

¹¹ [Exhibit 2 in the 2013 audit](#) summarizes IWCP's various permit types.

Exhibit 2

The Industrial Wastewater Control Program’s SIU and Non-SIU Permit Inventory as of December 31, 2019



Legend	Permit Classification	Permit Description
■	Class 1	Issued to certain industries whose composition and amounts of discharge are subject to federal standards
■	Class 2	Issued to targeted industrial sectors that have some toxic discharge, but are not subject to federal standards
■	Class 3	Issued to targeted industrial sectors to regulate conventional pollutants
■	Best Management Practices (BMP)	These authorizations include requirements followed by a certification of compliance for management and discharge of silver-rich solutions or dry-cleaning solvents

Note: Trucked waste permits are excluded from the chart because these are not the main focus of IWCP’s regulation of industrial businesses through permitting, monitoring, and enforcement activities.

Source: Auditor generated based on information from PUD’s Point Loma Wastewater Treatment Plant’s 2019 Pretreatment Report.

In the past, IWCP’s primary focus was regulating SIUs, which are subject to stringent federal standards because of the potential risks these types of industries pose to the sewerage system and the environment. Accordingly, SIUs require

additional monitoring and routine sample testing. However, according to PUD management, IWCP has recently shifted resources to also focus on regulating non-SIU businesses through its Enhanced Source Control Program. This change is intended to assist in the City's implementation of the Pure Water program, since IWCP's activities are critical to protect source water quality for that program.¹²

IWCP Jurisdictions

IWCP's pretreatment program encompasses the metropolitan wastewater area; this includes not only the City, but also the unincorporated areas and the incorporated municipalities within San Diego County that utilize the City's wastewater treatment system. To regulate industries outside City limits, IWCP operates under the auspices of interjurisdictional pretreatment agreements (IJAs) between the City and each of the PAs in the County and in the incorporated municipalities. IJAs are important because they:

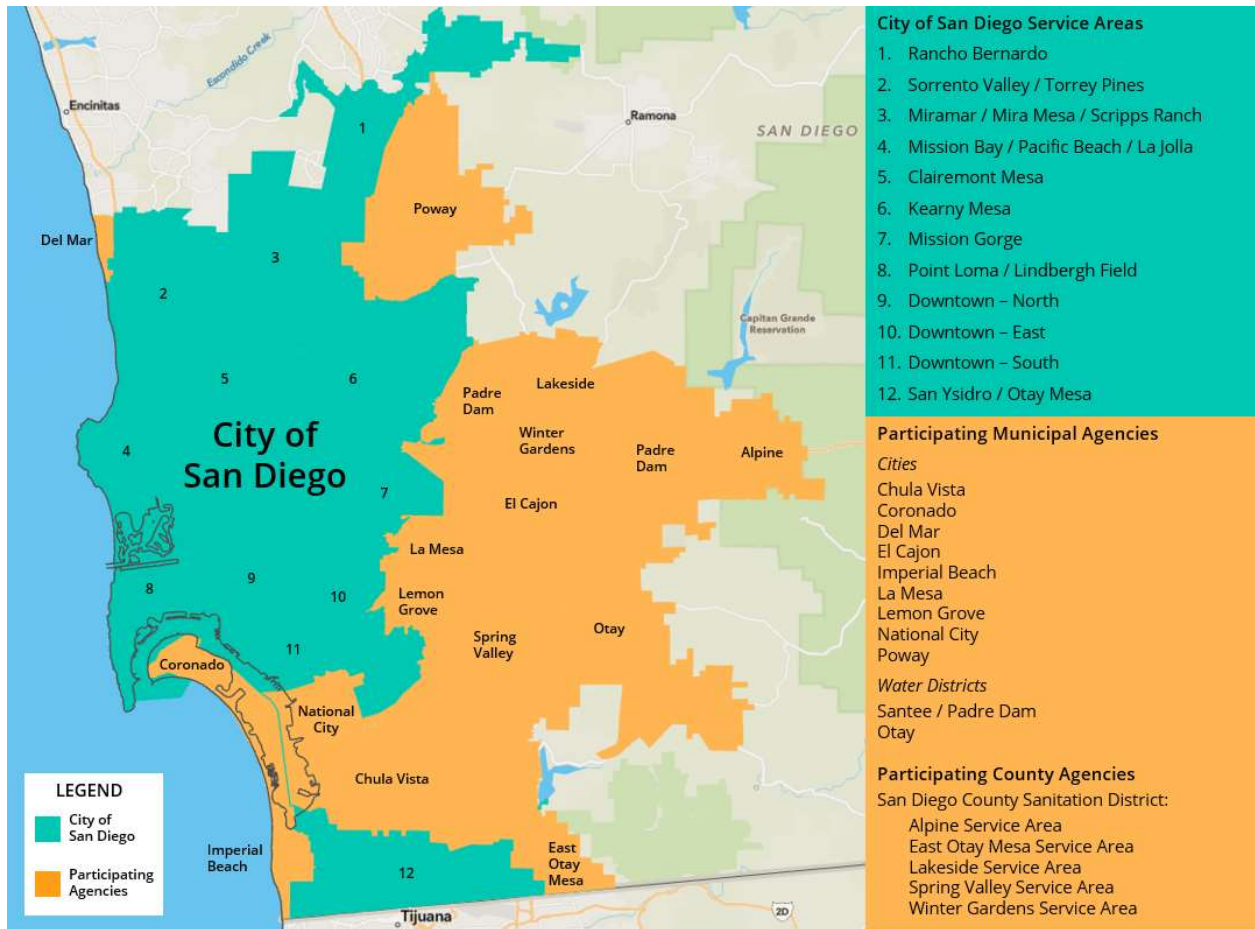
- Require PAs to promulgate ordinances that comport with federal standards and parallel City ordinances regarding pretreatment standards for waste discharge;
- Authorize the City, through IWCP, to permit, inspect, and monitor facilities in each of the PAs; and
- Establish permit and monitoring fees with the PAs to recover applicable IWCP costs associated with these activities.

IWCP regulates industrial businesses located within the jurisdictions shown in **Exhibit 3**.

¹² The City's phased, multi-year Pure Water program started in 2015 and is expected to provide one-third of San Diego's water supply when fully implemented by the end of 2035. Pure Water uses recycled water to produce a water supply and reduce wastewater discharge into the ocean.

Exhibit 3

The Industrial Wastewater Control Program’s Service Area Extends Beyond the City of San Diego



Note: Labels are approximate.

According to PUD, the service areas listed under “Participating County Agencies” were previously separate sewer districts. In July 2011, those entities were incorporated into the newly formed San Diego County Sanitation District. Therefore, these service areas are considered part of a single Participating Agency, the San Diego County Sanitation District.

Source: Auditor generated based on SanGIS data and information from PUD.

Most businesses regulated by IWCP are located within the City, but about one-third of them are spread across the PAs, as shown in **Exhibit 4**.

Follow-up Performance Audit of the Industrial Wastewater Control Program

Exhibit 4

Number of Permittees per IWCP Service Area

Area	Class 1	Class 2, 2C, 2Z	Class 3, 3C, 3Z	BMP	Total Permits	Total Percentage
City of San Diego	22	227	48	213	510	67.6%
City of Chula Vista	1	15	2	31	49	6.5%
City of Coronado	0	1	0	7	8	1.1%
City of Del Mar	0	0	1	2	3	0.4%
City of El Cajon	3	14	0	36	53	7.0%
City of Imperial Beach	0	0	0	4	4	0.5%
City of La Mesa	0	5	0	21	26	3.4%
City of National City	0	9	1	18	28	3.7%
City of Poway	4	4	3	11	22	2.9%
Santee / Padre Dam Municipal Water District	4	6	0	12	22	2.9%
City of Lemon Grove	0	2	0	5	7	0.9%
Total Within Municipal PAs	12	56	7	147	222	29.4%
Alpine Service Area	0	0	0	2	2	0.3%
Lakeside Service Area	0	4	1	3	8	1.1%
Spring Valley Service Area	1	2	1	4	8	1.1%
Winter Gardens Service Area	0	1	0	0	1	0.1%
East Otay Mesa Service Area	1	1	1	0	3	0.4%
Total Within County PA	2	8	3	9	22	3.0%
Grand Total	36	291	58	369	754	100.0%

Note: Trucked waste permits are not included in this table.

Source: Auditor generated based on 2019 Point Loma Pretreatment Report.

**IWCP Fees, Cost Recovery,
and Enforcement**

San Diego Municipal Code Section 64.0508 states that Industrial Wastewater Discharge Permit Fees should be established periodically by resolution of the City Council. Accordingly, IWCP charges annual permit fees to regulated industries within the City. The IJAs establish the permit and monitoring fees within the PAs. Permit fees range from \$25 to \$3,180 per year and are based on the permit classification, amount of wastewater discharged, and various business characteristics, as well as where the business is located (City vs. PAs). Additionally, Council Resolution No. 260133, adopted

March 1, 1984, states that the fees should recover PUD's costs for inspecting, monitoring, and sampling permitted facilities.

IWCP also has a variety of enforcement mechanisms available. When a permittee violates discharge limits, an enforcement action is initiated through a Notice of Violation and additional sampling. IWCP bills violating industries directly to recover violation, sampling, and administrative fees. IWCP is also authorized to seek administrative civil penalties.

Billing arrangements for permit and monitoring fees vary by jurisdiction, as shown below in **Exhibit 5**.

Exhibit 5

Billing Arrangements for Permit and Monitoring Fees Vary by Jurisdiction

	City of San Diego	County Participating Agencies	Municipal Participating Agencies
Fee Structure	Flat Rate - Established by 1984 Council Resolution establishing IWCP permit fees	Line Item (Individual Charge for Each Activity) - Established in 1999 Agreements with County Agencies	Hourly - IWCP/IWL staff should track labor hours for each project, and PUD staff add overhead rates to generate invoice amounts
Permit Fee Range	\$25 to \$2,000 per year, based on class and flow	\$135 to \$3,180 per year, based on class, complexity, and whether self-monitoring is required	Varies based on labor hours charged
Are the businesses billed directly?	Yes	Yes	No
Is the participating agency billed directly?	N/A	No	Yes ¹
Are SIUs billed for additional lab monitoring fees?	No, because this cost is included in annual permit fee	Yes	Yes, but PUD does not track individual user costs
Are non-SIUs billed for additional lab monitoring fees?	No, because this cost is included in annual permit fee	Yes	Yes, but varies based on labor hours charged

¹ The City of Coronado bills industries directly and is therefore an exception.

Source: Auditor generated summary based on Interjurisdictional Pretreatment Agreements and IWCP information, as of May 20, 2020.

IWCP utilizes the Pretreatment Information Management System (PIMS) to administer information related to the inventory of permitted facilities. Specifically, IWCP uses PIMS to track Industrial User permit information; inspection, monitoring, and violation data; and to charge most IWCP fees. For businesses within the City and/or County PAs, fees charged in PIMS are automatically transferred to the Citywide financial system, SAP. For businesses within the Municipal PAs, violation fees are automatically transferred to SAP while fees for permitting and monitoring are manually entered in SAP. These differences are shown in **Exhibit 11**.

**Summary of Previous
Audit Findings**

In August 2013, our office completed a performance audit of IWCP to assess the extent to which permit and inspection fees and billing processes met legal requirements, achieved appropriate cost recovery, and ensured timely collection. The audit found that outdated fees, billing lapses, and inadequate controls limited program cost recovery.

Specifically, IWCP fees were outdated—having not been updated since as far back as 1984. Moreover, program costs were not tracked.¹³ As a result, IWCP did not achieve adequate cost recovery. We estimated that between FY 2010 and FY 2012, billable costs exceeded revenues by about \$8.3 million—meaning that only 15 percent of billable costs were recovered through program fees charged to regulated businesses. The other 85 percent of costs were offset by charges to other ratepayers, including residential and commercial customers.

IWCP's cost recovery level is ultimately a decision that should be made by the Mayor and the City Council, in accordance with San Diego Municipal Code Section 64.0508, Council Policy 100-05, and Administrative Regulation 95.25. However, because PUD never reviewed fees or prepared proposals to the City Council for updating them, these policymakers were likely not aware that IWCP was not recovering its costs through permit fees.

¹³ As reported in our August 2013 audit, PUD was not able to precisely determine recoverable program costs because it did not maintain sufficient data to do so and because a formal workload study to identify program costs had not been conducted.

The first audit finding included five recommendations, summarized below:

1. Track all billable costs so that fees (cost recovery rates) can be determined.
2. Review fees annually and conduct detailed fee studies not less than every three years; present fee proposals to the City Council.
3. Conduct a fee study to determine fee levels for full cost recovery; ensure fee calculation methodology meets applicable legal requirements.
4. Revise agreements with outside agencies to include fees that achieve cost recovery and mechanisms to adjust fees in response to changes in the cost of service.
5. Develop a proposal to update program fees within the City that achieve cost recovery and include mechanisms to adjust fees in response to changes in the cost of service.

In addition, the audit found that, in the five-year period between FY 2008 and FY 2012, PUD failed to invoice over \$850,000 to numerous regulated entities for IWCP services. This was primarily caused by unnecessarily complex billing processes, system programming errors, and a lack of established accountability for billing and review of financial information. Moreover, according to PUD, the failure to bill was caused by turnover in staff and initial confusion resulting from the implementation of the SAP financial system in FY 2010.

The second audit finding included three recommendations, summarized below:

6. Seek recovery of all unbilled costs related to IWCP activities.
7. Establish a centralized billing process and standardize billing policies and procedures across all IWCP activities.
8. Review all PIMS settings to ensure invoices are generated accurately and in a timely manner.

PUD originally agreed to implement all 8 recommendations by January 31, 2014.

Our Confidential Memorandum Raised the Possibility that IWCP's Cost Recovery Practices Were Not in Compliance with Prop 218

Prior to publishing our August 2013 audit, our office distributed a confidential audit memorandum to City management, the City Attorney's Office, and the Mayor in May 2013. While that memorandum remains confidential because it contains attorney-client privileged information, given the time that has passed and the new information that has become available, we have determined that it is in the public interest to raise the pertinent issues here so that management and oversight bodies can act to quickly and appropriately resolve them as needed. The confidential memorandum raised the same issues that were reported publicly in the August 2013 audit but went further by identifying the possibility that, by passing most costs on to other classes of users, IWCP was not in compliance with Proposition 218 (Prop 218).¹⁴ Adopted by California voters in 1996, Prop 218 focuses on taxes, fees, or charges that are directly associated with property ownership; known as "property related fees and charges," these include charges for water and sewer service. Prop 218's rules generally require that rates not exceed the cost of providing the service and that rate proceeds be used only to provide the service. However, as reported in 2013, approximately 85 percent of IWCP costs were being passed on to other classes of users via sewer service charges—raising the possibility that IWCP's cost structure was not in compliance with Prop 218 requirements.

The 5 recommendations made in the confidential memorandum are similar to the 5 recommendations made in Finding 1 of the public audit, except they include ensuring that cost recovery practices also be reviewed for compliance with Prop 218. Following the issuance of our confidential audit memorandum in 2013, PUD worked to determine potential corrective measures related to these issues.

¹⁴ As previously noted, we do not reach any legal conclusions in this report regarding Proposition 218, and nothing in this report should be interpreted as any type of legal conclusion.

Our office issued the memorandum confidentially at the time because actual cost recovery was unclear (since program costs were not being tracked), because additional analysis would be required to determine a whether any corrective action was necessary, and because the memorandum contains attorney-client privileged information. We recommended that the City further study this issue and take corrective action if necessary. Since issuing the confidential memorandum and the public audit report, our office has kept the Mayor, the City Council, and the Audit Committee apprised of PUD's progress implementing the recommendations by periodically issuing recommendation follow-up reports.

PUD Has Made Some Efforts to Address Previous Audit Recommendations, but Past Missteps Have Slowed Progress

Since our 2013 audit, PUD has continuously been engaged in efforts to address substantive issues identified by the audit. However, at the time we initiated this follow-up audit, the City had fully implemented only 3 of a total of 13 recommendations made by our office in 2013.¹⁵

In FY 2014, PUD created a cost center specific to IWCP to better track program revenues and expenditures. However, the cost center still includes some line items that are unrelated to IWCP permitting, monitoring, and enforcement activities. Therefore, determining precise revenues and expenditures for these activities—which is necessary to understand what program fee levels would achieve cost

¹⁵ As of December 2019, the City had implemented 1 of the 8 recommendations made in the public audit report and 2 of the 5 recommendations made in the confidential audit memorandum.

The only recommendation that was implemented from the public report was Recommendation 6, which had to do with seeking recovery—to the greatest extent possible allowed by law—of all unbilled IWCP costs related to application review, permitting, inspection, and monitoring. Our 2013 audit found that PUD had not billed numerous regulated entities for IWCP services in the five-year period between FY 2008 and FY 2012 and that unbilled amounts totaled more than \$850,000. PUD sent invoices for unbilled charges accrued during FY 2008 and FY 2009 prior to the completion of our 2013 audit. Then, in our office's Audit Recommendation Follow-up Report for the period ending June 30, 2014, we reported that PUD had submitted evidence of having invoiced for previously unbilled permits and monitoring services for FY 2010 through FY 2012, totaling about \$628,000.

The two recommendations from the confidential audit memorandum that have been implemented pertain to delaying the Wastewater Cost of Service Study until additional analysis of IWCP's cost recovery practices is completed. Our office has verified that these recommendations have been implemented.

recovery—is still not as straightforward as we recommended in the audit report. Nevertheless, PUD has recently made progress toward developing and documenting a methodology to track program costs and revenues, which will be used in the future to update fees. This is discussed further in Finding 1.

Although PUD Commissioned Several Fee Studies Since the Audit, They Were Never Finalized or Sent to the City Council for Approval in Accordance with City Policies and to Ensure Compliance with Proposition 218

In April 2016, a consultant for PUD, Black & Veatch (B&V), completed a draft IWCP fee study, which found that IWCP fees would—in certain scenarios—need to be increased significantly to achieve full cost recovery.¹⁶ These results were consistent with our 2013 audit findings that cost recovery was only about 15 percent. Even though the fee study cost approximately \$150,000, it was never finalized. Current PUD management speculates this was because the consultants' fee structure was too complicated, but this cannot be verified due to the significant change in PUD management staff since 2016. The results of this fee study were never presented to the City Council and were not provided to OCA during our biannual recommendation follow-up process.

Around the time PUD decided not to move forward with the results of that fee study, PUD provided the same consultant (B&V) with IWCP cost and revenue data and asked if the amount of costs being passed on to other customers was material. Based on the data PUD provided, B&V concluded that IWCP costs were being fully recovered and that raising permit fees would not have a material effect on wastewater revenues or wastewater rates for non-IWCP permittees. PUD provided a letter from B&V to OCA to this effect and asked that we close the remaining IWCP recommendations because the costs were not material. However, upon a closer review, OCA identified that the data PUD provided to B&V significantly overestimated revenues. Specifically, it included revenues for items such as “trucked waste,” which is revenue for treatment of waste trucked into PUD dumping locations (such as waste

¹⁶ Not all fees in this fee study were directly comparable with current fees because the study recommended creating many different classes of permittees with different rates. However, some of the proposed fees in the study were directly comparable to current fees and showed a significant increase in certain scenarios.

from portable toilets), and unrelated to IWCP inspections and monitoring.

In July 2018, PUD retained another consultant (Raftelis) to study IWCP fees again—this time at a cost of \$30,000.¹⁷ Again, using data and assumptions from PUD, Raftelis concluded that only about \$500,000 of IWCP's costs were not being recovered from IWCP permittees. Further, Raftelis concluded these unrecovered costs were not significant in the sense that increasing fees to achieve cost recovery would not have a material effect on rates, and the reduction to wastewater charges (presumably for other, non-industrial customers) would be less than one cent.¹⁸ Our office again questioned the assumptions used to reach this conclusion, and PUD subsequently acknowledged that unrecovered costs totaled approximately \$3.3 million per year while asserting that this amount was immaterial given the size of wastewater revenues.

PUD is awaiting the results of a new fee study, at a cost of \$21,090,¹⁹ which is intended to determine what full cost recovery fees would be and how much of those costs can be justifiably passed along to non-IWCP ratepayers. As discussed in more detail below, PUD plans to recommend updated fees to the City Council by January 2021 to correct some of the remaining cost recovery issues with the program.

Exhibit 6 summarizes key events related to our audit since 2013.

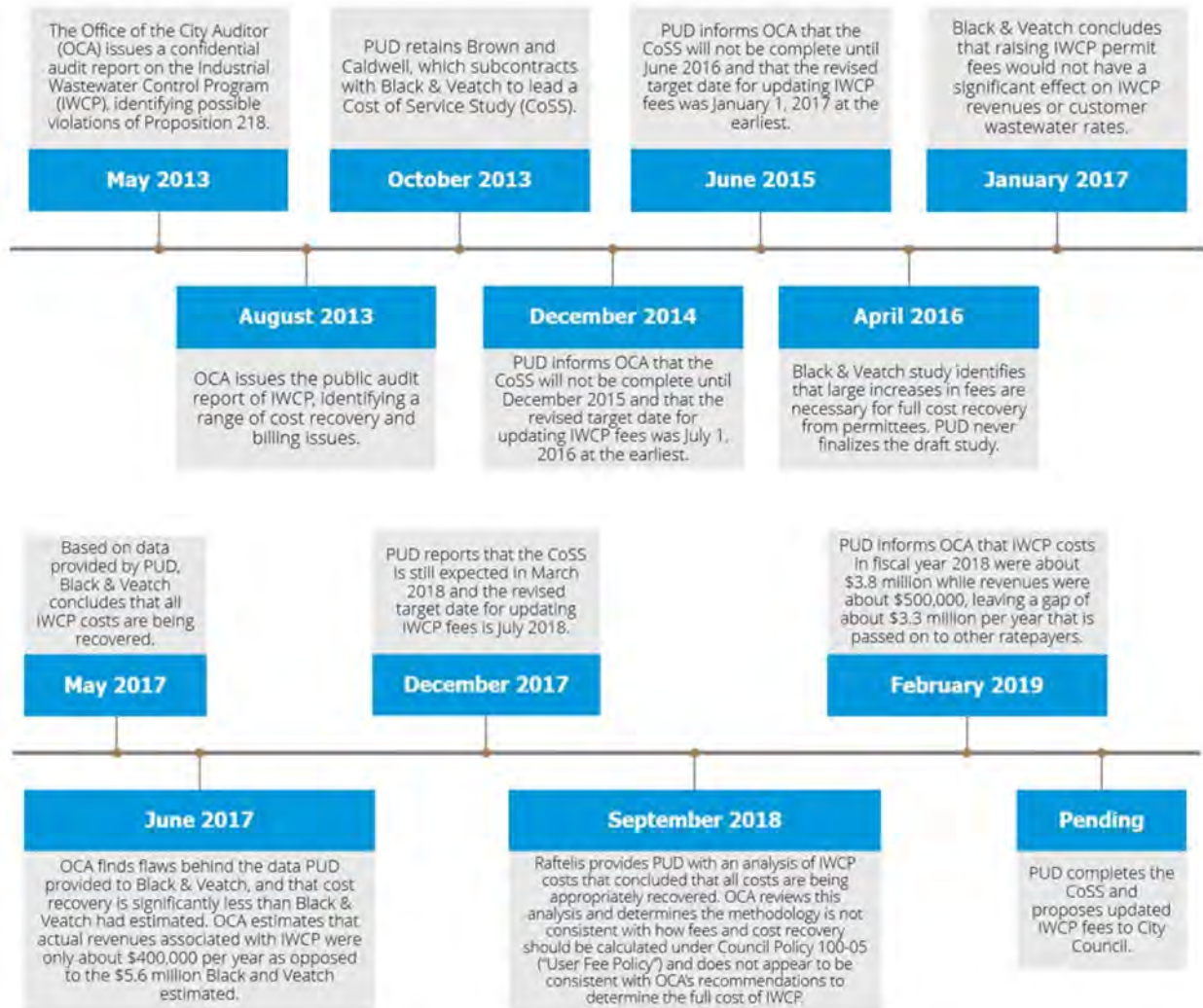
¹⁷ This is a line item amount set aside for this work in a larger contract with the consultant. Actual invoice payments total \$18,910 as of July 8, 2020.

¹⁸ The consultant did not specify a time or unit interval when making this estimation; therefore, it is unclear whether this one cent applies monthly, annually, per unit of water used, etc.

¹⁹ The allocated amount for the current fee study is \$21,090; about \$18,400 of that has been invoiced as of July 8, 2020.

Exhibit 6

Timeline of IWCP Events Since 2013



Source: Auditor generated based on communications between OCA, PUD, and the City Attorney's Office.

New Audit Underway

In addition to this follow-up report, our office plans to complete another audit of IWCP; the tentative objectives of that audit will focus on operational issues of the program, such as permitting, monitoring, and enforcement.

IWCP Organizational Changes Since 2013 Audit

In June 2018, IWCP engaged a consultant team to review and assess staffing levels, organization, and workflow. The resulting consultant report made a total of 22 recommendations across 6 program areas. According to the

schedule in the report, changes to the program would be implemented between May 2019 and October 2020.²⁰ Among these changes is an organizational restructuring to facilitate the Enhanced Source Control Program's (ESCP) workflow.²¹ Previously, inspections for both SIUs and businesses that fell within ESCP were handled by the same work group, while enforcement activities, including the issuance of Notice of Violations (NOVs), were handled by a separate work group. As shown in **Exhibit 7**, SIU inspection activities have been assigned to one group of inspectors while non-SIU businesses have been assigned to two groups: Source Control-North and Source Control-South. Enforcement activities are being incorporated into the workload of inspectors in both the SIU and Source Control work groups.²²

In addition, according to PUD, the Support Services group was set up to develop, update, and maintain Standard Operating Procedures (SOPs) for IWCP. Support Services is also tasked with assisting in groundwater permitting and supporting the clerical needs of the program. PUD management informed us that program staff has been working on developing SOPs during the COVID-19 pandemic while working remotely.

Moreover, five new full-time equivalent positions were created in the FY 2020 budget. One of these was an unclassified Program Manager position to oversee the program because, according to PUD management, the increased importance of IWCP as Pure Water is implemented warrants leadership at a higher level. The position was filled in October 2019. The addition of these positions further increases IWCP's program costs.

²⁰ It is unknown whether this timeline will change based on operational impacts from the COVID-19 pandemic.

²¹ ESCP was created in 1998 in response to regulatory requirements associated with the waiver from secondary treatment granted to the City's Point Loma Wastewater Treatment Plant. As the City begins implementing the first phase of the Pure Water Program, ESCP will be important to regulate the discharge of toxic pollutants and pesticides into the system from non-industrial sources.

²² We observed inspectors in both work groups in March 2020. Based on our observations, it appears IWCP has a large backlog of inspections for both SIU and ESCP permittees. We may explore this issue further in our forthcoming audit of IWCP's permitting and enforcement processes.

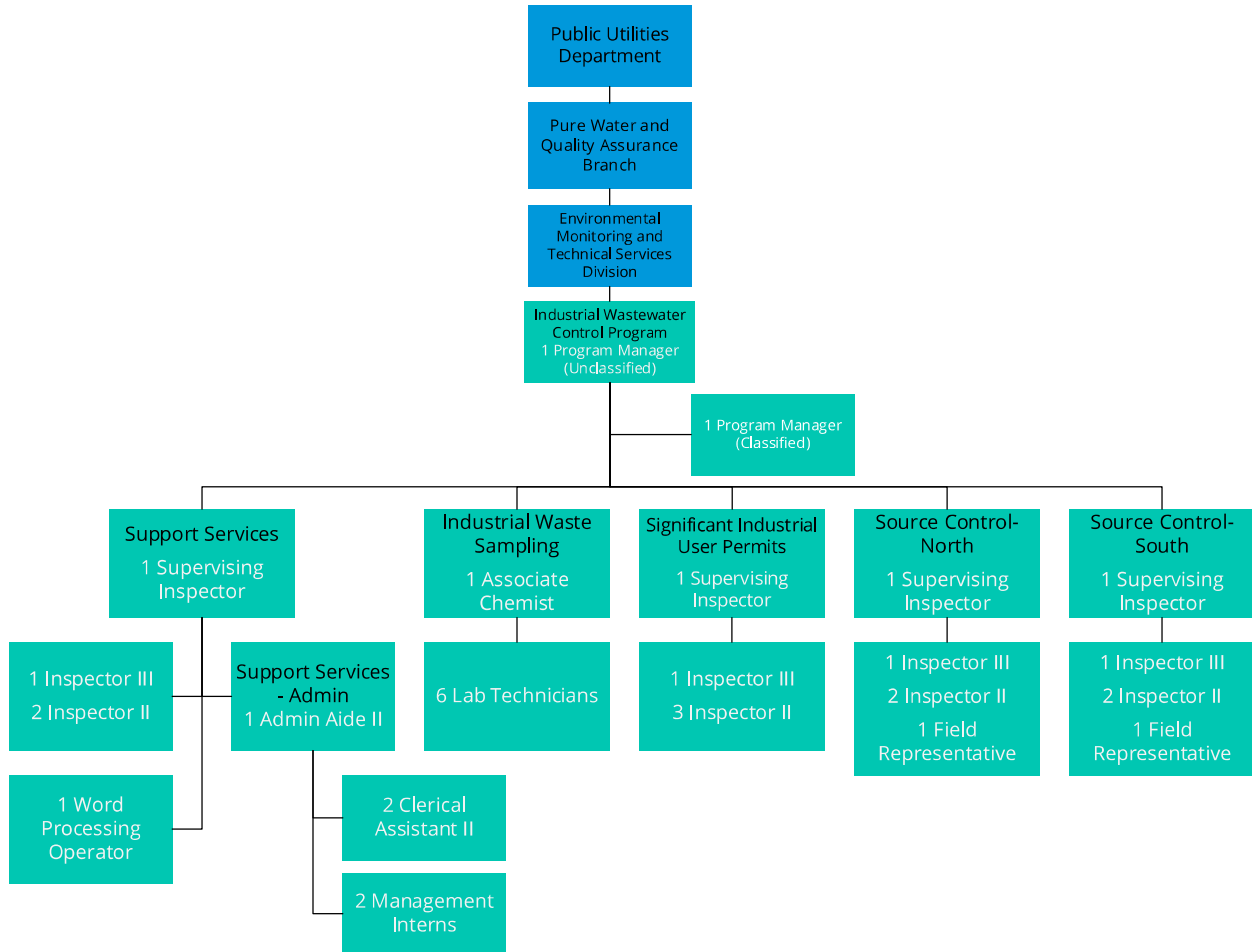
In February 2019, PUD requested a Special Salary Adjustment (SSA) of 20 percent for the Industrial Wastewater Pretreatment Inspector series (Inspector I, II, and III) to address retention issues in the Program, the differential in salary created by prior SSAs for Chemists and Lab Techs, and to increase the incentive for staff to remain with the City and IWCP. According to PUD, the SSA was approved, and new salaries were effective July 2019.

These changes are significant to the program's restructuring, but it is important to note that additional staffing will also increase the program's costs. Therefore, if program fees remain the same, there is a risk that cost recovery could become even lower.

IWCP implemented its new organizational structure in April 2020; the most current version is shown in **Exhibit 7**.

Exhibit 7

Industrial Wastewater Control Program Organizational Structure as of June 2020



Source: Auditor generated based on information provided by PUD.

Audit Results

Finding 1: The Public Utilities Department Has Not Adjusted Many IWCP Permit Fees Since 1984, and its Cost Recovery Practices Remain Out of Compliance with City Policies and Possibly State Law

Finding Summary

While the Public Utilities Department (PUD) has made some progress, the issues we identified in our 2013 audit of the Industrial Wastewater Control Program (IWCP) remain largely unaddressed. Many fees have still not been adjusted since 1984, and program cost recovery remains very low. For example, while program costs totaled approximately \$38.8 million between FY 2010 and FY 2019, only about \$5.5 million (14 percent) was recovered through program fees charged to regulated businesses. The remaining \$33.3 million (86 percent) of program costs were passed on to other wastewater customers, including residential and commercial customers, via wastewater rates.

These cost recovery practices remain out of compliance with City regulations and policies. More seriously, the possibility remains that, by passing most program costs on to other wastewater customers, the City may not be complying with Proposition 218 (Prop 218).²³ We also identified an additional concern with Prop 218 compliance that is created by complexities in PUD's wastewater accounting and its agreement with Participating Agencies (PAs). Specifically, due to these complexities, the \$33.3 million needed to subsidize IWCP between FY 2010 and FY 2019 came exclusively from City of San Diego wastewater customers, even though IWCP serves the larger metro area, including 12 PAs.

²³ As previously noted, we do not reach any legal conclusions in this report regarding Proposition 218, and nothing in this report should be interpreted as any type of legal conclusion.

Follow-up Performance Audit of the Industrial Wastewater Control Program

PUD has options to ensure IWCP’s cost recovery practices comply with City policies and state law and has recently made progress to this end. However, several of these efforts are still underway; therefore, our office will continue to monitor these developments as they apply to the recommendations we make in this report.

**From FY 2010 to FY 2019,
86 Percent of IWCP
Costs—Totaling More
Than \$30 Million—Were
Passed on to Other
Wastewater Customers**

Our 2013 audit identified that many IWCP fees had not been updated since 1984 and others since 1999. That issue remains unaddressed since our 2013 audit, which now means that many program fees have not been adjusted for 36 years.

As a result, the vast majority of IWCP costs continue to be passed on to other wastewater customers. As **Exhibit 8** and **Exhibit 9** show, unrecovered IWCP costs averaged about \$3.3 million—or 86 percent—per year, totaling \$33.3 million in the ten-year period between FY 2010 and FY 2019. Those costs were offset by revenues from non-IWCP sources, including wastewater rates charged to residential and commercial customers.

Exhibit 8

IWCP Revenues, Expenses, and Cost Recovery, Fiscal Years 2010-2019

	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015
Violation Fees	\$21,250	\$23,483	\$20,153	\$16,877	\$14,824	\$16,306
Discharge Fees*	\$89,216	\$101,411	\$95,136	\$293,578	\$536,840	\$168,797
Lab Monitoring Fees	\$14,587	\$12,685	\$15,326	\$149,097	\$471,710	\$86,454
Trucked Waste Fees^	\$177,957	\$192,466	\$170,336	\$171,231	\$169,906	\$230,036
Misc. Revenues			\$3,003			
Total Revenues†	\$303,010	\$330,045	\$303,954	\$630,783	\$1,193,280	\$501,593
Total Billable Expenses	\$3,137,974	\$3,190,876	\$3,465,149	\$4,250,040	\$5,153,584	\$4,946,787
Unrecovered Costs	(\$2,834,964)	(\$2,860,831)	(\$3,161,195)	(\$3,619,257)	(\$3,960,304)	(\$4,445,194)
Percent Cost Recovery	10%	10%	9%	15%	23%	10%

Follow-up Performance Audit of the Industrial Wastewater Control Program

	FY 2016	FY 2017	FY 2018	FY 2019	Total
Violation Fees	\$14,925	\$12,820	\$31,340	\$27,975	\$199,953
Discharge Fees	\$95,005	\$323,133	\$108,550	\$108,730	\$1,920,396
Lab Monitoring Fees	\$8,564	\$169,256	\$82,155	\$3,618	\$1,013,452
Trucked Waste Fees	\$281,422	\$312,813	\$295,559	\$327,630	\$2,329,356
Misc. Revenues					\$3,003
Total Revenues	\$399,916	\$818,022	\$517,604	\$467,953	\$5,466,160
Total Billable Expenses	\$4,187,460	\$3,590,548	\$3,601,533	\$3,253,635	\$38,777,587
Unrecovered Costs	(\$3,787,544)	(\$2,772,525)	(\$3,083,928)	(\$2,785,683)	(\$33,311,426)
Percent Cost Recovery	10%	23%	14%	14%	14%

Notes: **Exhibit 5** in our 2013 audit report includes a similar table for FY 2010 through FY 2012. The corresponding figures in this table originate from that exhibit, but we have adjusted them as follows:

* In the 2013 table, "Discharge Fees" were classified as "Permitting Fees."

^ In the 2013 table, "Trucked Waste Fee" amounts were included as part of the "Permitting Fees" and "Monitoring Fees" categories. We adjusted the figures and separated out Trucked Waste revenues here for FY 2010 through FY 2012 to be consistent with other years in the table.

† In the 2013 table, "Total Revenues" included an estimated amount in each of the years (FY 2010 through FY2012) for certain permitting and monitoring revenues that had not actually been recovered at the time. After our 2013 audit, and in our office's Audit Recommendation Follow-up Report for the period ending June 30, 2014, we reported that PUD invoiced for previously unbilled permits and monitoring services for FY 2010 through FY 2012. The invoices totaled about \$628,000. Therefore, we removed the estimated revenue amounts for FY 2010 through FY 2012 from this table so as to not double count the actual revenues PUD recovered subsequent to our 2013 audit.

Source: Auditor generated based on information from PUD (FY 2010 through FY 2012) and PUD (FY 2013 through FY 2019).

IWCP's Cost Recovery Practices Remain Out of Compliance with City Policies and Possibly State Law

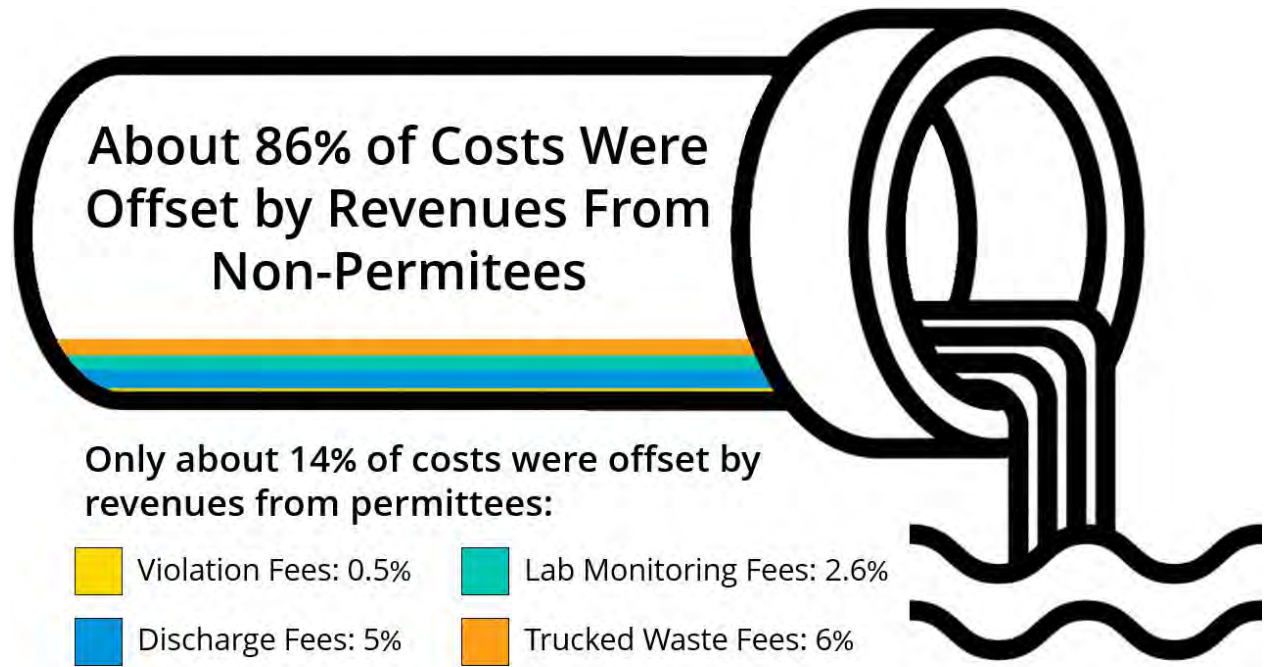
By not studying fees and presenting them to the City Council on a regular basis, PUD is not complying with multiple City regulations and policies. Specifically, San Diego Municipal Code Section 64.0508 states that Industrial Wastewater Discharge Permit Fees should be established periodically by a resolution of the City Council. In addition, the City has several policies and procedures in place requiring periodic review and updating of fees to ensure adequate cost recovery. For example, according to Administrative Regulation 95.25, the City's policy is to annually review fees to ensure that all reasonable costs incurred in providing these services are being recovered. In addition, Council Policy 100-05 also states that fees should achieve full cost recovery, except in certain cases where the intent is to provide a specific benefit to recipients (such as recreation center or library fees). The policy also requires in-depth fee studies every three years, with interim adjustments to fees taking place on an annual basis. Finally, the policy requires City Council approval for changes to fees in Enterprise Fund departments (including PUD). Because updated IWCP fees still have not been proposed to the City Council for approval, PUD is still out of compliance with these policies.

More importantly, evidence gathered since 2013 indicates an increased likelihood that the City's cost recovery practices for IWCP remain potentially out of compliance with the requirements of Prop 218, which essentially states that utility ratepayers can only be charged in accordance with the benefit they receive.²⁴ Since FY 2010, IWCP has cost over \$38 million. IWCP permittees benefit from the program by being allowed to operate businesses that may potentially discharge harmful substances into the metropolitan wastewater system. However, they have only paid about \$5.5 million via IWCP fees (about 14 percent of IWCP costs) during this time. The other 86 percent of IWCP costs, or about \$33.3 million, has been passed along to other City wastewater customers that are not IWCP permittees, such as residential customers, via higher wastewater rates.

²⁴ As previously noted, we do not reach any legal conclusions in this report regarding Proposition 218, and nothing in this report should be interpreted as any type of legal conclusion.

Exhibit 9

Between Fiscal Years 2010 and 2019, Only About 14 Percent of IWCP’s Costs Were Offset by Revenues from IWCP Permittees



Source: Auditor generated based on information from PUD.

While Prop 218 does not necessarily require full cost recovery, PUD does need to thoroughly analyze the benefits of IWCP and allocate costs equitably between IWCP permittees and other wastewater customers. There are clearly benefits to the average customer—such as avoiding secondary treatment at the Point Loma wastewater treatment facility, which PUD estimates would cost ratepayers almost \$2 billion.²⁵ However, PUD needs to analyze and quantify these benefits and then seek City Council approval for updated fees, which PUD has not historically done. According to PUD, this analysis is currently in process. Thus, the longer PUD takes to perform

²⁵ Secondary treatment is the second stage in most wastewater treatment systems in which bacteria consume the organic matter in wastewater. The Clean Water Act requires that municipal wastewater treatment plants meet a minimum of secondary treatment. However, the City has for decades operated under a waiver from secondary treatment under Sections 301(h) and 301(j)(5) of the Clean Water Act, and PUD has noted that IWCP helps ensure the City’s ongoing eligibility to receive this waiver. Absent this waiver, which must be renewed every five years, the City would need to upgrade the Point Loma wastewater treatment facility to provide secondary treatment. According to PUD, the estimated cost to ratepayers for upgrading the plant to secondary treatment is almost \$2 billion.

this analysis, the longer the City is potentially out of compliance with Prop 218 and potentially subject to legal liability.

While PUD has recently acknowledged that cost recovery issues are substantial—averaging \$3.3 million per year passed on to other customers between FY 2010 and FY 2019—PUD has still maintained that this is not a material amount given total wastewater revenues. For example, revenue from sewer service charges—which is used to offset IWCP’s unrecovered costs—was approximately \$267.1 million in FY 2018.

Therefore, unrecovered costs of \$3.3 million would represent just over 1 percent of that revenue. PUD also estimated that recovering an additional \$3.3 million in IWCP fees in FY 2018 would have lowered the typical single-family residential customer’s total sewer bill by just 1.3 percent. Using this information, we estimate that recovering an additional \$3.3 million in IWCP fees would roughly translate to approximately \$5 per year in savings for the average single-family residential customer.

While the amount of unrecovered costs may be very small compared to overall wastewater revenues, the City is not meeting certain obligations by allowing revenues from other customers to offset unrecovered IWCP costs. For example, the City has an obligation under Prop. 218 to ensure its ratepayers are not paying more than their fair share of wastewater expenses and to accurately allocate expenses within the appropriate funds. In addition, legal compliance with Prop 218 is the minimum requirement the City must meet when setting fees appropriately. Prop 218 issues aside, not adjusting fees for up to 36 years and applying revenues from residential customers to offset costs created by certain industrial users may create inequity, represents poor stewardship of customer revenues, and can damage public perception of the organization. While there are many aspects and potential effects to consider, a decision on an appropriate cost recovery level—including how much should be passed on to other customers—should ultimately be made by the Mayor and the City Council.

Even Though the City Provides Wastewater Services—including IWCP—in the Metro Area, City Ratepayers Alone Are Subsidizing IWCP

We uncovered an additional cost recovery issue since our 2013 audit that is caused by complexities in PUD's wastewater accounting structure and the City's agreement with the Participating Agencies (PAs). PUD uses two funds to account for wastewater activities: the Municipal Wastewater Fund (Muni Fund) and the Metropolitan Wastewater Fund (Metro Fund).²⁶ Only City customers contribute to the Muni Fund, while the Metro Fund includes revenues from both City customers and customers in the PAs. In addition, the current Regional Wastewater Disposal Agreement between the City and the PAs prohibits any IWCP costs from being passed on to PAs.²⁷ Accordingly, IWCP's revenues and expenses are budgeted exclusively within the Muni Fund, even though IWCP regulates businesses throughout the metro wastewater area—both within and outside of the City.²⁸ This means costs incurred by the program that are not recovered through fees charged to regulated businesses—which average to about 86 percent of program costs since FY 2010—are offset by revenues generated *only* from City customers. Thus, because IWCP does not recover all of its costs, and because IWCP is budgeted in the Muni Fund, the average single-family residential customer in the City pays about \$5 per year to subsidize IWCP while similar residential customers in the PAs pay nothing to subsidize IWCP—even though approximately

²⁶ The Muni and Metro Funds have different revenue and expense sources and support different capital improvement projects. The Muni Fund receives revenues from sewer service charges; wastewater fees; and grants to cover expenses for maintaining, collecting, and transporting wastewater. The Metro Fund receives revenues from sewer service charges; wastewater fees; grants; and the sale of electricity generation. Importantly, revenue from Participating Agencies is used exclusively in the Metro Fund.

²⁷ In December 2018, the City Council and the Mayor approved an Amended and Restated Regional Wastewater Disposal Agreement; this agreement states that the City and the Participating Agencies intend to negotiate within a year of the effective date to address, among other things, the issue of IWCP costs and whether and to what extent those will be shared among the parties. We learned from the City Attorney's Office that the Amended and Restated Disposal Agreement is not in effect because two Participating Agencies have not signed it. Nevertheless, according to the City Attorney's Office, the parties are moving closer to getting the Amended and Restated Agreement fully authorized. In the meantime, the previous Disposal Agreement—which became effective in 1998—is still in effect.

²⁸ The metro wastewater area includes the City of San Diego plus 12 Participating Agencies. Refer to **Exhibit 3** for a map of IWCP's service area.

one-third of businesses regulated by IWCP are located outside the City. Exhibit 10 illustrates that only revenue from City customers is used to offset unrecovered costs, even though IWCP serves the larger metro area.

Exhibit 10

City Customers Alone Subsidize IWCP's Costs, Even Though IWCP Serves the Larger Metro Area



*Not all Participating Agencies appear in this graphic. Refer to Exhibit 3 for a complete representation of Participating Agencies.

Source: Auditor generated based on information provided by PUD.

**PUD Has Options to
Ensure Compliance with
City Cost Recovery
Policies and Proposition
218**

The simplest way to ensure compliance with the City's cost recovery policies and the requirements of Proposition 218 is to thoroughly study IWCP costs, develop fees that achieve full cost recovery, and present them to the City Council for approval and implementation. Assuming PUD were to achieve full cost recovery, this approach would also eliminate the need to move IWCP's budget from the Muni Fund to the Metro Fund, since IWCP permittees would be directly offsetting all program costs.

However, a different and more comprehensive approach—one that allows for less than full cost recovery—would be for PUD to thoroughly study the costs *as well as the benefits* of the program. PUD could then develop fees that achieve a desired level of cost recovery from IWCP permittees while being able to justify passing on the unrecovered costs to other wastewater customers (based on the quantifiable benefits those other customers receive from the program). In this scenario, the costs passed on to other customers must not be more than the benefits they receive from the program; therefore, the quantifiable benefits of the program would dictate the program's minimum cost recovery level.

However, this second option is more complicated because it requires PUD to complete additional analysis before setting program fees. For example, in addition to studying costs, PUD would need to thoroughly analyze and quantify the benefits that IWCP provides to non-IWCP customers—which may be difficult to accomplish, especially if those benefits are not easily quantifiable. Moreover, this option may potentially increase the risk of non-compliance if a court were to find the City's analysis overestimated the relative benefit of the program to non-IWCP customers. Finally, the second option is more complicated because PUD would also need to move IWCP's budget from the Muni Fund to the Metro Fund to ensure that any unrecovered costs are shared between the City and the Participating Agencies.

For comparative purposes, we reviewed the cost structures of other agencies' IWCP-like programs to compare cost recovery rates and other elements relating to IWCP improvements. We compared IWCP to the Orange County (CA) Sanitation District,

the City of Portland's Industrial Pretreatment Program, the City of San Jose's Industrial Discharge Program, and King County's (WA) Industrial Waste Program.²⁹ We found that cost recovery varies for the other agencies—from 10 percent to 100 percent. In San Diego, cost recovery averaged 14 percent between FY 2010 and FY 2019. In addition, other agencies update their permit fees regularly and have methods to track billable costs clearly, accurately, and explicitly related to industrial wastewater.

PUD Has Recently Made Progress in Implementing Some of the Recommendations from Our 2013 Audit and to Ensure Compliance with City Cost Recovery Policies and Proposition 218

In response to Recommendation 1 from our 2013 audit report, PUD recently drafted a process narrative for calculating all billable IWCP costs and program revenues so that PUD staff can determine IWCP fee levels and appropriate cost recovery rates. The draft process narrative is supplemented by screenshots and a spreadsheet to assist staff in calculating IWCP costs and revenues. While the process narrative and supplemental materials are still in draft form as of June 2020, they appear to substantively address Recommendation 1 from our 2013 audit report. Our office will make a final determination on the status of this recommendation after PUD finalizes the process narrative and approves it for use.³⁰

In addition, and according to PUD, the department is pursuing the second approach described above to ensure compliance with the City's cost recovery policies and the requirements of Prop 218. PUD has engaged a consultant to complete a cost of service study and assist the department in developing updated IWCP fees for approval by the City Council. According to PUD, their consultant is also working to quantify the benefits of IWCP so that PUD may better understand whether a portion of the program's costs can be justifiably passed on to other customers. In addition, the department intends to move IWCP's budget from the Muni Fund to the Metro Fund at some point in the future. Finally, PUD has developed a draft fee

²⁹ All comparable programs were chosen based on similarities to the City of San Diego's IWCP. However, the City of San Diego is the only program that participates in the 301(h) waiver program. In addition, Portland and King County are not located in California, and thus are not subject to the provisions of Prop 218.

³⁰ After we reviewed the draft process narrative, PUD management informed us that the final version will likely be in the form of a department instruction.

model; this draft model allows staff to determine fee levels that would be necessary to fully recover IWCP's program costs. The draft fee model; the analysis by PUD's consultant; the determination on a proposed cost recovery level; and the proposal of updated program fees to the City Council for approval are all pending as of June 2020. We note that these items and actions collectively touch on several of the recommendations we made in our 2013 audit report—specifically Recommendations 2, 3, 4, and 5. Therefore, our office's final determination on the status of these recommendations is pending completion of these items.

Recommendations

Given that the same issues we identified in 2013 are largely still taking place and that PUD has not implemented the recommendations we made at that time, we make the same recommendations in this follow-up report. The following recommendations were made in our 2013 public audit and have been modified to include the potential Prop. 218 issues we raised in our 2013 confidential memo. We note that Recommendations 4 and 6 depend on negotiating with the Participating Agencies; we encourage the City to negotiate terms that allow these recommendations to be implemented as stated.

Specifically, in order to ensure that cost recovery practices for IWCP are brought into compliance with City policies and state law as quickly as possible, we recommend:

Recommendation 1

The Public Utilities Department should establish policies and procedures to track all billable IWCP related costs so that fee levels and appropriate cost recovery rates can be determined effectively. (Priority 1)

Recommendation 2

The Public Utilities Department should establish policies and procedures to periodically review fee levels and present fee proposals to the City Council. These reviews and fee studies should include calculation of the rate of cost recovery achieved by current fees. Reviews should be conducted on an annual basis, and detailed fee studies should be conducted not less than every three years, in accordance with Council Policy 100-05 and Administrative Regulation 95.25, and

proposed fees and cost recovery levels should comply with Proposition 218. (Priority 1)

Recommendation 3 The Public Utilities Department should perform a fee study to determine fee levels that achieve full cost recovery for all IWCP activities, including all labor and materials required for application review and permitting, inspections, monitoring, and sample analysis, as well as overhead and non-personnel expenses. The Public Utilities Department should ensure that methodologies used to calculate fees are adequately documented and consult with the Office of the City Attorney to meet all applicable legal requirements, including those established by Proposition 218. (Priority 1)

Recommendation 4 Upon completion of the fee study, the Public Utilities Department should work with the Office of the City Attorney and the Participating Agencies to review and revise, as appropriate, Interjurisdictional Agreements to include fees for service that achieve appropriate cost recovery under the guidelines of Council Policy 100-05 and Administrative Regulation 95.25, as well as Proposition 218. The revised agreements should include mechanisms to adjust fees in response to changes in the cost of service. (Priority 1)

Recommendation 5 Upon completion of the fee study, the Public Utilities Department, in consultation with the City Attorney's Office, should develop a proposal for consideration by the City Council to update fees for Industrial Users within the City of San Diego. This proposal should include fees that achieve appropriate cost recovery under the guidelines of Council Policy 100-05 and Administrative Regulation 95.25, as well as Proposition 218. The revised fee schedules should include mechanisms to adjust fees in response to changes in the cost of service. (Priority 1)

In addition to the recommendations we made in 2013, we make the following new recommendation to ensure that any IWCP programs costs that are not recovered through program fees from regulated businesses are divided equitably between City customers and customers within the Participating Agencies. As previously noted, and per the Amended and Restated Disposal Agreement, this requires the City to negotiate with the Participating Agencies.

Recommendation 6 The Public Utilities Department should move the Industrial Wastewater Control Program's budget from the Municipal Wastewater Fund to the Metropolitan Wastewater Fund.
(Priority 1

Finding 2: Billing Lapses Have Reoccurred Due to Overly Complex and Inefficient Processes and a Breakdown in Oversight

Finding Summary

Even though the Public Utilities Department (PUD) implemented our 2013 recommendation to recover costs that went unbilled between FY 2008 and FY 2012,³¹ we found that, since FY 2017, PUD again failed to bill many IWCP permittees outside the City. As in 2013, we found this was largely due to overly-complex and labor-intensive billing processes and a breakdown in billing oversight.

PUD management stated that adopting a standardized billing process for all program fees, regardless of jurisdiction, is ultimately their goal. However, according to PUD management, this is something that would need to be negotiated as part of updated agreements with Participating Agencies (PAs). In addition, PUD must still propose updated program fees to the City Council for approval. Therefore, implementing a single billing procedure will likely take place further in the future.

IWCP Still Uses Multiple Billing Processes, which is Inefficient and Increases the Risk of Billing Errors

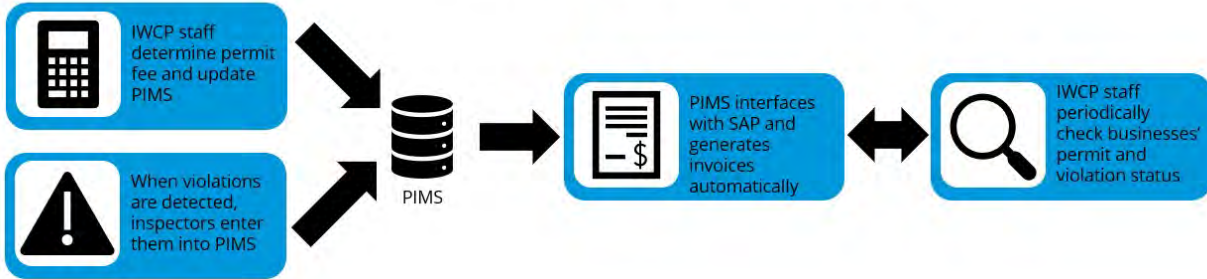
As show in **Exhibit 11** below, our 2013 audit found that PUD used three different billing processes for different industrial businesses, depending on the jurisdiction in which they were located.

³¹ Prior to the completion of our 2013 audit, PUD sent invoices for unbilled charges accrued during FY 2008 and FY 2009. We later verified that PUD invoiced for previously unbilled permits and monitoring services for FY 2010 through FY 2012.

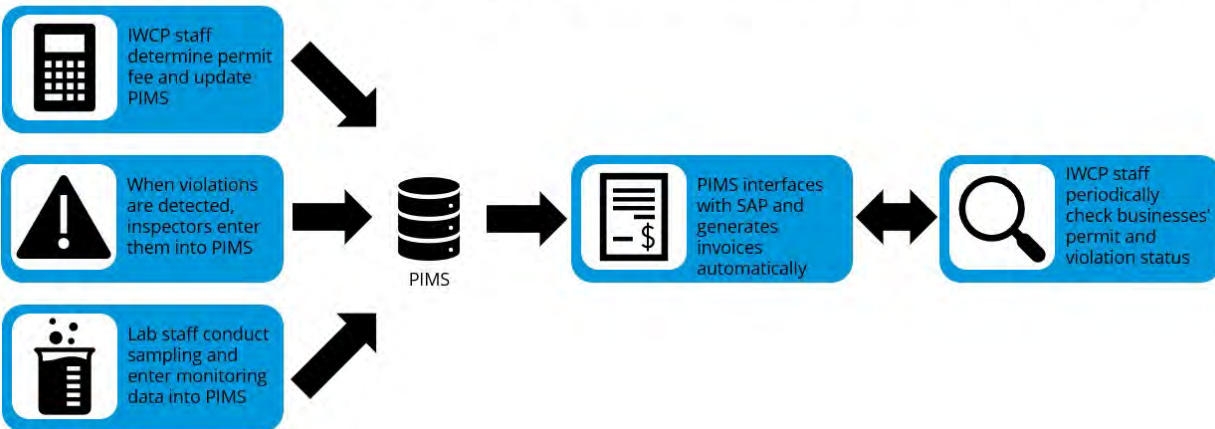
Exhibit 11

Summary of IWCP's Multiple Billing Processes

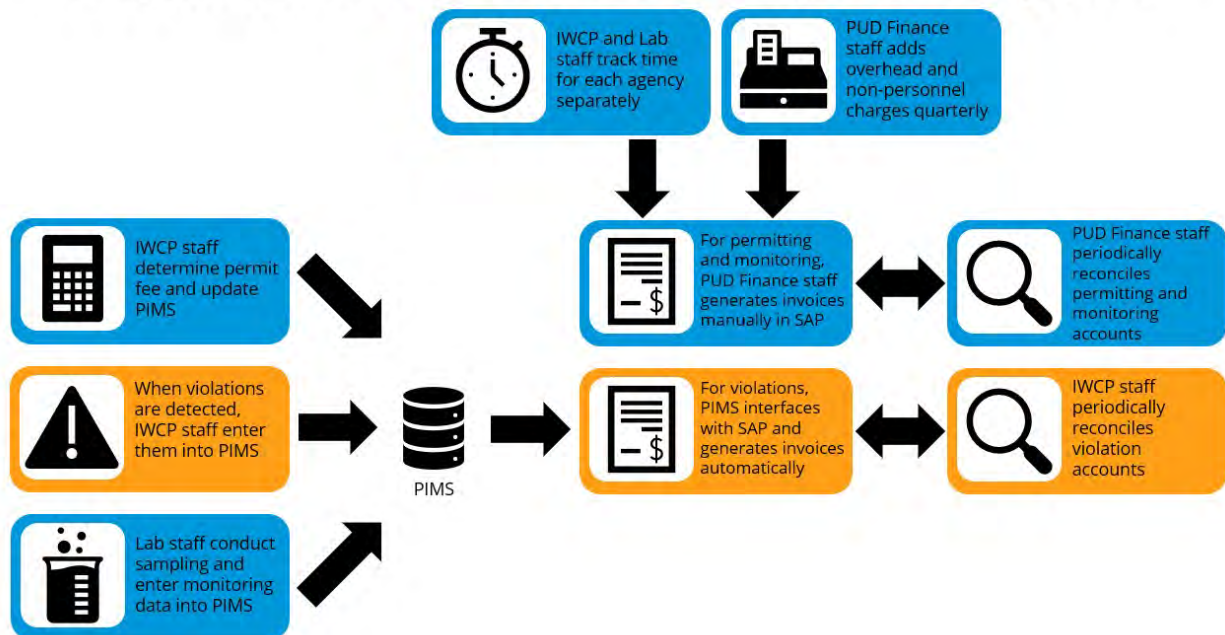
Billing Process for Industrial Users Within the City



Billing Process for Industrial Users Within the County Participating Agencies



Billing Process for Industrial Users Within the Municipal Participating Agencies



Source: Auditor generated summary of PUD information.

This approach created unnecessary complexity, making it difficult for IWCP staff to ensure the timely and accurate billing and reconciliation of accounts. In fact, we found that IWCP failed to bill approximately \$850,000 to some regulated entities located outside the City during the five-year period between FY 2008 and FY 2012. This indicated both a lack of understanding of billing practices on the part of staff as well as a significant breakdown in billing oversight. We recommended that PUD develop a single, standardized billing process for all IWCP fees. That recommendation, however, has not been implemented since the 2013 audit.

Instead, we learned that IWCP still follows multiple billing processes depending on the jurisdiction in which an industrial business is located. We also learned that billing lapses have reoccurred, and IWCP has not billed all industrial businesses outside of the City since FY 2017.³² According to PUD, this is a result of not having enough staff to accomplish the billing for all municipal PAs. In addition, as in 2013, we conclude that the use of multiple billing processes is a major contributing factor to these lapses, as the current billing processes are overly complex, confusing, and inefficient. When asked whether IWCP would adopt a standardized billing process for all fees regardless of jurisdiction, PUD management stated that this is ultimately the goal and is something that would need to be negotiated as part of updated agreements with PAs. However, according to PUD management, billing procedures are only one aspect of those agreements—updated fees, for example, would also need to be addressed—so implementing a single billing procedure will likely take place further in the future.

For comparison, in the City of Los Angeles, the Bureau of Sanitation's Industrial Waste Division administers the Pretreatment Program, which regulates the discharge of industrial wastewater into the city's publicly-owned treatment works system. The Pretreatment Program's service area includes 19 contributing jurisdictions and 8 contract cities. According to Financial Management staff from the City of Los Angeles's Industrial Waste Division, the largest participating

³² The total amount that has gone unbilled is yet to be determined.

agencies have signed onto a Universal Terms Agreement (UTA). Under the UTA, the city treats the wastewater and the participating agencies must follow certain procedures relating to enforcement and regulation. The UTA also provides that the City of Los Angeles will charge participating agencies the same rates it charges users in the City of Los Angeles. Thus, the City of Los Angeles uses a singular billing process for all participating jurisdictions and may avoid the billing inefficiencies created by using multiple and complex billing processes.

Because the billing process issues identified in our 2013 audit have not been corrected, and because billing lapses have reoccurred, we again make the following recommendations to standardize IWCP's billing process, ensure accurate and timely billing, and improve efficiency:

Recommendation 7 The Public Utilities Department should work with the Office of the City Attorney to seek recovery, to the greatest extent possible allowed by law, of all unbilled costs related to Industrial Wastewater Control Program application review, permitting, inspection, and monitoring. (Priority 1)

Recommendation 8 The Public Utilities Department should establish a centralized billing process and standardized billing policies and procedures for all IWCP fees and charges. These policies and procedures should be documented in a process narrative and should:

- a. Establish responsibilities and timelines for generating and sending invoices for all IWCP fees and charges;
- b. Establish responsibilities and timelines for performing a periodic reconciliation of all IWCP revenue accounts;
- c. Establish guidelines and procedures for recording labor time, if necessary to determine invoice amounts;
- d. Establish guidelines and procedures for calculating invoice amounts; and
- e. Ensure that appropriate Separation of Duties controls are enforced. (Priority 1)

Recommendation 9 The Public Utilities Department should perform a comprehensive review of all PIMS settings and invoice calculating features to ensure that invoices are automatically generated by PIMS and sent in a timely manner. (Priority 1)

Conclusion

IWCP is an important City program. It is a key component of the City's environmental management efforts; plays a critical role in the City's compliance with wastewater regulations; helps to protect wastewater infrastructure and limit replacement costs; is important for protecting source water quality for the Pure Water Program; and is critical for the City's ongoing eligibility for the waiver from secondary wastewater treatment, which helps preclude the need to make about \$2 billion worth of upgrades to the Point Loma Wastewater Treatment Plant.

We believe that conducting this follow-up audit was in the public interest, given the importance of the program, the length of time that passed since our 2013 audit, and the numerous delays in implementing both the public and confidential audit recommendations. Even though the City has made some progress toward implementing these, we found that many of the same substantive issues remain largely unaddressed:

- Program fees have still not been updated for decades;
- Program cost recovery is still very low—only about 14 percent between FY 2010 and FY 2019;
- Unrecovered program costs are still offset by charges to other ratepayers, including residential and commercial customers, which creates the possibility that PUD's cost recovery practices do not comply with Proposition 218;³³ and
- Billing lapses reoccurred as a result of overly-complex and labor-intensive billing processes and a breakdown in billing oversight.

In addition to the issues we raised in 2013, this report identifies an additional concern with Proposition 218

³³ As previously noted, we do not reach any legal conclusions in this report regarding Proposition 218, and nothing in this report should be interpreted as any type of legal conclusion.

compliance: City wastewater customers alone are subsidizing program costs, even though the program serves customers in the larger metro area, including customers in the Participating Agencies.³⁴

Making changes to the program per our recommendations is important to ensure that program fees are regularly reviewed and updated; cost recovery is monitored; billing is timely; and cost recovery practices are equitable and comply with City policies and state law.

We will continue to monitor the City's progress in addressing the issues identified by our audits.

³⁴ As previously noted, we do not reach any legal conclusions in this report regarding Proposition 218, and nothing in this report should be interpreted as any type of legal conclusion.

Recommendations

- Recommendation 1** The Public Utilities Department should establish policies and procedures to track all billable IWCP related costs so that fee levels and appropriate cost recovery rates can be determined effectively. (Priority 1)
- Recommendation 2** The Public Utilities Department should establish policies and procedures to periodically review fee levels and present fee proposals to the City Council. These reviews and fee studies should include calculation of the rate of cost recovery achieved by current fees. Reviews should be conducted on an annual basis, and detailed fee studies should be conducted not less than every three years, in accordance with Council Policy 100-05 and Administrative Regulation 95.25, and proposed fees and cost recovery levels should comply with Proposition 218. (Priority 1)
- Recommendation 3** The Public Utilities Department should perform a fee study to determine fee levels that achieve full cost recovery for all IWCP activities, including all labor and materials required for application review and permitting, inspections, monitoring, and sample analysis, as well as overhead and non-personnel expenses. The Public Utilities Department should ensure that methodologies used to calculate fees are adequately documented and consult with the Office of the City Attorney to meet all applicable legal requirements, including those established by Proposition 218. (Priority 1)
- Recommendation 4** Upon completion of the fee study, the Public Utilities Department should work with the Office of the City Attorney and the Participating Agencies to review and revise, as appropriate, Interjurisdictional Agreements to include fees for service that achieve appropriate cost recovery under the guidelines of Council Policy 100-05 and Administrative Regulation 95.25, as well as Proposition 218. The revised agreements should include mechanisms to adjust fees in response to changes in the cost of service. (Priority 1)

- Recommendation 5** Upon completion of the fee study, the Public Utilities Department, in consultation with the City Attorney's Office, should develop a proposal for consideration by the City Council to update fees for Industrial Users within the City of San Diego. This proposal should include fees that achieve appropriate cost recovery under the guidelines of Council Policy 100-05 and Administrative Regulation 95.25, as well as Proposition 218. The revised fee schedules should include mechanisms to adjust fees in response to changes in the cost of service. (Priority 1)
- Recommendation 6** The Public Utilities Department should move the Industrial Wastewater Control Program's budget from the Municipal Wastewater Fund to the Metropolitan Wastewater Fund. (Priority 1)
- Recommendation 7** The Public Utilities Department should work with the Office of the City Attorney to seek recovery, to the greatest extent possible allowed by law, of all unbilled costs related to Industrial Wastewater Control Program application review, permitting, inspection, and monitoring. (Priority 1)
- Recommendation 8** The Public Utilities Department should establish a centralized billing process and standardized billing policies and procedures for all IWCP fees and charges. These policies and procedures should be documented in a process narrative and should:
- a. Establish responsibilities and timelines for generating and sending invoices for all IWCP fees and charges;
 - b. Establish responsibilities and timelines for performing a periodic reconciliation of all IWCP revenue accounts;
 - c. Establish guidelines and procedures for recording labor time, if necessary to determine invoice amounts;
 - d. Establish guidelines and procedures for calculating invoice amounts; and
 - e. Ensure that appropriate Separation of Duties controls are enforced. (Priority 1)

Recommendation 9 The Public Utilities Department should perform a comprehensive review of all PIMS settings and invoice calculating features to ensure that invoices are automatically generated by PIMS and sent in a timely manner. (Priority 1)

Appendix A: Definition of Audit Recommendation Priorities

The Office of the City Auditor maintains a priority classification scheme for audit recommendations based on the importance of each recommendation to the City, as described in the table below. While the City Auditor is responsible for providing a priority classification for recommendations, it is the City Administration’s responsibility to establish a target date to implement each recommendation, taking into consideration its priority. The City Auditor requests that target dates be included in the Administration’s official response to the audit findings and recommendations.

Priority Class ³⁵	Description
1	Fraud or serious violations are being committed. Significant fiscal and/or equivalent non-fiscal losses are occurring. Costly and/or detrimental operational inefficiencies are taking place. A significant internal control weakness has been identified.
2	The potential for incurring significant fiscal and/or equivalent non-fiscal losses exists. The potential for costly and/or detrimental operational inefficiencies exists. The potential for strengthening or improving internal controls exists.
3	Operation or administrative process will be improved.

³⁵ The City Auditor is responsible for assigning audit recommendation priority class numbers. A recommendation that clearly fits the description for more than one priority class shall be assigned the higher priority.

Appendix B: Audit Objectives, Scope, and Methodology

In accordance with the City Auditor's Fiscal 2020 Audit Work Plan, we conducted a follow-up audit of the Public Utilities Department's (PUD's) Industrial Wastewater Control Program (IWCP).

Objectives and Scope

Given the serious issues identified in 2013 through both our public audit report and our confidential audit memorandum, and the apparent lack of progress in implementing our recommendations, we conducted this follow-up audit to evaluate the current state of PUD's cost recovery efforts for IWCP. Specifically, our audit objectives were to review the implementation status of our 2013 recommendations and publicly report on the issues we had identified in 2013 through both our public audit and our confidential audit memorandum.

Methodology

To do this, and in addition to the routine efforts we have made since 2013 as part of our office's normal recommendation follow-up process, we requested and reviewed pertinent program documents from PUD. These included policies and procedures related to IWCP's operations; recent permitting data; program expenses and revenues; service contract documents related to cost of service studies; current organizational charts; several annual wastewater pretreatment reports; and a program assessment report completed in 2019.

Data Reliability and Internal Controls

We updated several key components from our 2013 audit report based on information provided by PUD, including the cost recovery table presented in **Exhibit 8**. For figures in the cost recovery table that PUD provided to us, we reviewed PUD's methodology for calculating them, but we did not perform detailed data reliability testing. Our testing of internal controls was limited to reviewing PUD's documentation for tracking costs and revenues.

We also reviewed correspondence between our office, PUD, and the City Attorney's Office to better articulate the sequence of notable events that took place since our 2013 public audit report and confidential audit memorandum.

In addition, we conducted several interviews with department management and program staff to discuss past developments and efforts to address our 2013 recommendations; the current state of the program, including field observations to better understand the permitting and inspection process; and management's recent progress in implementing our past recommendations, including the current cost of service study and other pending items that will impact the program and its cost recovery practices in the future.

Compliance Statement

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.



THE CITY OF SAN DIEGO

M E M O R A N D U M

DATE: July 9, 2020

TO: Kyle Elser, Interim City Auditor, Office of the City Auditor

FROM: Shauna Lorance, Director, Public Utilities Department

SUBJECT: Management Response to Follow-Up Performance Audit of Public Utilities Department's Industrial Wastewater Control Program

The purpose of this memorandum is to provide Management's response to the City Auditor's report entitled *Follow-Up Performance Audit of Public Utilities Department's Industrial Wastewater Control Program: PUD's Cost Recovery Practices Remain Out of Compliance with City Regulations, Policies, and Potentially State Law*.

Public Utilities Department (Department) management agrees with recommendations included in the audit and has made considerable progress toward completing several of this audit's recommendations over the past year. Under the leadership of Mayor Faulconer, a new management structure and team are now in place and we are committed to continuous improvement throughout our operations. Those improvements include the initial steps necessary to respond to this audit's recommendations, including a cost of service analysis for the Industrial Wastewater Control Program (IWCP) and development of a clear and documented process for tracking IWCP expenses and revenues to fully capture *all* of that program's financial impacts.

The Department has worked diligently with a rate consultant to prepare an IWCP cost recovery model that can be used to prepare updated fee proposals on both a near-term and long-term basis, and the model has sufficient usability and flexibility to adapt to future changes to the program's operations and budget. As noted in the audit and in our responses below, the Department's rate consultant is continuing to work to determine the appropriate portion of IWCP expenses that should be recovered directly through IWCP fees and those that should be recovered from system-wide users who indirectly benefit from the program. This work, along with the IWCP cost recovery model, will be used as the basis for a proposal the City Council can consider to adjust existing IWCP fees.

While over two decades have passed since IWCP fees were last updated, we have documented through our responses how we will periodically update fees to ensure that they remain appropriate and comply with all applicable regulations.

Page 2 of 7
Kyle Elser, Interim City Auditor, Office of the City Auditor
July 9, 2020

We appreciate the opportunity to provide comments on this audit and thank the City Auditor's team for their cooperation and professionalism throughout the audit process. Our responses to the audit recommendations are below.

RECOMMENDATION #1: The Public Utilities Department should establish policies and procedures to track all billable IWCP related costs so that fee levels and appropriate cost recovery rates can be determined effectively.

Management's Response: Agree. The IWCP is budgeted in multiple fund centers (an IWCP Fund Center and an Environmental Chemistry Services Fund Center) which requires the use of multiple data sources to accomplish this recommendation. The Department has prepared a draft Department Instruction that clearly documents processes and procedures for extracting IWCP expense and revenue data using SAP Business Objects and the Pretreatment Information Management System (PIMS). The draft Department Instruction clearly lays out the processes needed to extract budget information from SAP, and the steps needed to apply PIMS data, in order to capture specific IWCP expenses and revenues.

The information derived from this process provides total IWCP expenses and revenues that can be used in combination with the IWCP Cost Recovery Model (see Recommendations 2 and 3), to determine fee levels to achieve appropriate cost recovery.

Target Implementation Date: Tracking IWCP related costs, using SAP and PIMS, has been implemented. The Department Instruction will be finalized and put into effect by December 30, 2020, including training of all applicable team members. As new employees involved in this program are hired, additional training on the Department Instruction will be provided during the onboarding process.

RECOMMENDATION #2: The Public Utilities Department should establish policies and procedures to periodically review fee levels and present fee proposals to the City Council. These reviews and fee studies should include calculation of the rate of cost recovery achieved by current fees. Reviews should be conducted on an annual basis, and detailed fee studies should be conducted not less than every three years, in accordance with Council Policy 100-05 and Administrative Regulation 95.25, and proposed fees and cost recovery levels should comply with Proposition 218.

Management's Response: Agree. The response to Recommendation 1 provides the process necessary to identify total IWCP expenses and revenues that can be used in combination with the IWCP Cost Recovery Model (see Recommendation 3, to determine appropriate fee levels to achieve appropriate cost recovery, which will be executed annually). Additionally, the City contracted with Raftelis Financial Consultants, Inc. (Raftelis Consulting) to prepare a fee model that can allocate IWCP expenses to various IWCP functions and tasks, and that can be used to update IWCP permitting and violation fees. This model is substantially complete, and Raftelis Consulting is further preparing a user manual for the model that will allow the Department to update total expenses and the allocation of those expenses in order to propose updated fee levels on a periodic basis. The fee proposal consideration by the City Council is discussed in Recommendation 3.

As noted in the audit, the IWCP does provide benefits to non-industrial customers, and therefore it may be appropriate to not recover all IWCP costs from IWCP fees. Raftelis

Consulting is currently evaluating and quantifying these system-wide benefits to determine the appropriate level of direct cost-recovery through fees under Proposition 218.

Target Implementation Date: Most elements of this recommendation have been implemented. The Department Instruction will be finalized and operationalized by December 30, 2020, including training of all appropriate team members. An initial fee proposal will be developed in Fiscal Year 2021, and any implemented fee proposal will be reviewed to generate an updated fee proposal by Fiscal Year 2024.

RECOMMENDATION #3: The Public Utilities Department should perform a fee study to determine fee levels that achieve full cost recovery for all IWCP activities, including all labor and materials required for application review and permitting, inspections, monitoring, and sample analysis, as well as overhead and non-personnel expenses. The Public Utilities Department should ensure that methodologies used to calculate fees are adequately documented and consult with the Office of the City Attorney to meet all applicable legal requirements, including those established by Proposition 218.

Management's Response: Agree. As noted in the response to Recommendation 2, the Department has engaged Raftelis Consulting to create a fee model and user manual that will be used to develop fees for appropriate cost recovery of IWCP activities by allocating all expenses (including labor, materials, overhead, and non-personnel expenses) to specific IWCP functions and tasks. The model is substantially complete.

Raftelis Consulting is currently evaluating the appropriate level of direct cost recovery for the program. Upon completion of its evaluation, the Department will work with the City Attorney's office to ensure that any ensuing fee proposals will meet all legal requirements.

Target Implementation Date: Raftelis Consulting and the Department will complete work on the fee study, to prepare a proposal for revised fees for consideration by the City Council by January 30, 2021, and the Department will work with the City Attorney to ensure all legal requirements are met.

RECOMMENDATION #4: Upon completion of the fee study, the Public Utilities Department should work with the Office of the City Attorney and the Participating Agencies to review and revise, as appropriate, Interjurisdictional Agreements to include fees for service that achieve appropriate cost recovery under the guidelines of Council Policy 100-05 and Administrative Regulation 95.25, as well as Proposition 218. The revised agreements should include mechanisms to adjust fees in response to changes in the cost of service.

Management's Response: Agree. As noted in the audit, a portion of IWCP expenses and revenues are derived from permittees that are outside of City limits and that are in the jurisdiction of Participating Agencies (PAs) of the Metropolitan Wastewater Joint Powers Authority (Metro JPA). The Department intends to seek permit fees for IWCP functions and tasks that are uniform regardless of the location of the permittee.

The PAs of the Metro JPA are currently in the process of approving an amended and restated agreement that describes wastewater expenses they are responsible for paying. That amended and restated agreement explicitly notes that upon its effective date, the City and the PAs intend to negotiate in good faith on additional matters, including the proportion of

IWCP costs that PAs are ultimately responsible for (the existing agreement precludes using IWCP costs to determine overall PA payments for use of the City's wastewater treatment infrastructure). Negotiations on this are anticipated to begin immediately after the amended and restated agreement is approved by all PAs, which is currently anticipated by November 2020. Any revisions to Metro JPA agreements will be subject to negotiations, and while the Department will seek an appropriate and timely outcome regarding IWCP costs, the Department cannot guarantee a specific outcome or timeframe.

Target Implementation Date: The Department anticipates entering negotiations on further amendments to the Metro JPA Agreement by November 2020.

RECOMMENDATION #5: Upon completion of the fee study, we recommend the Public Utilities Department, in consultation with the City Attorney's Office, should develop a proposal for consideration by the City Council to update fees for Industrial Users within the City of San Diego. This proposal should include fees that achieve appropriate cost recovery under the guidelines of Council Policy 100-05 and Administrative Regulation 95.25, as well as Proposition 218. The revised fee schedules should include mechanisms to adjust fees in response to changes in the cost of service.

Management's Response: Agree. As noted in our response to Recommendation 3, the Department has engaged Raftelis Consulting to create a fee model that can be used to determine fees for full cost recovery of IWCP activities by allocating expenses to specific IWCP functions and tasks. This model is substantially complete.

Raftelis Consulting is currently evaluating the appropriate level of direct cost recovery for the program. Upon completion of its evaluation the Department will work with the City Attorney's office to ensure that any ensuing fee proposals will meet all legal requirements. While the Department may propose updated fees, the decision to actually implement those fees rests with the City Council.

Target Implementation Date: Raftelis Consulting and the Department will complete work on the fee study, and prepare a proposal for revised fees for consideration by the City Council by January 30, 2021, and the Department will work with the City Attorney to ensure all legal requirements are met.

RECOMMENDATION #6: The Public Utilities Department should move the Industrial Wastewater Control Program's budget from the Municipal Wastewater Fund to the Metropolitan Wastewater Fund.

Management's Response: Agree. As the IWCP is a treatment program, it is appropriate for it to be budgeted in the Metropolitan Wastewater Fund. Metropolitan Wastewater Fund expenses are shared by the City and the PAs. The City's current agreement with the PAs precludes the City from charging PAs for general IWCP expenses; however, as noted in the response to Recommendation 4, the Department intends to enter negotiations with the PAs of the Metro JPA to determine an appropriate share of IWCP expenses that to be borne by the PAs. Upon completion of these negotiations, it will be appropriate to move the IWCP budget from the Municipal Sewer Fund to the Metropolitan Wastewater fund.

Moving the IWCP budget requires reallocating IWCP expenses and revenues through the City's restructure process. Requests for restructures generally must be submitted by operating departments to the Department of Finance by October in order for them to be implemented in the following fiscal year's budget.

Target Implementation Date: The Department intends to include the IWCP's budget in the Metropolitan Sewer Fund after completing negotiations with the PAs. If this is completed by the fall of 2021, in accordance with DoF's schedule, this should then be reflected in the FY 2023 budget. If negotiations with the PAs do not conclude by the fall of 2021, the budgetary transition may not be possible until the following fiscal year (Fiscal Year 2024).

RECOMMENDATION #7: The Public Utilities Department should work with the Office of the City Attorney to seek recovery, to the greatest extent possible allowed by law, of all unbilled costs related to Industrial Wastewater Control Program application review, permitting, inspection, and monitoring.

Management's Response: Agree. While bills for IWCP permitting and sampling performed for Metro JPA PA customers have not been sent since FY 2017, the Department is able to determine the unbilled parties and amounts.

While PAs are not billed for general IWCP costs, as discussed in Recommendations 4 and 6, PAs do pay for their share of the Metro Wastewater system's treatment expenses. On an annual basis, PAs make initial payments for their anticipated use, and then after a reconciliation of their anticipated and actual use, they are issued refunds or additional bills to true-up those initial payments. The Department intends to send bills for unbilled IWCP fees to the appropriate PAs at the same time that it sends its true-up refunds/invoices.

Target Implementation Date: The Department is working to notify PAs of amounts due; it anticipates sending invoices for unbilled amounts by December 30, 2020.

RECOMMENDATION #8: The Public Utilities Department should establish a centralized billing process and standardized billing policies and procedures for all IWCP fees and charges. These policies and procedures should be documented in a process narrative and should:

- a. Establish responsibilities and timelines for generating and sending invoices for all IWCP fees and charge;
- b. Establish responsibilities and timelines for performing a periodic reconciliation of all IWCP revenue accounts;
- c. Establish guidelines and procedures for recording labor time, if necessary to determine invoice amounts;
- d. Establish guidelines and procedures for calculating invoice amounts; and

Ensure that appropriate Separation of Duties controls are enforced.

Management's Response: Agree. While there is an existing process for billing City of San Diego businesses, billing businesses that fall outside of the City's boundaries and in the boundaries of the various PAs is complicated. In some cases, those businesses are billed directly, and in others the PA in whose jurisdiction those businesses are located is billed. The

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Department's past practices have not been clearly documented, and the Department is currently evaluating its past processes while developing instructions and guidelines for calculating the appropriate yearly costs to PAs and permittees that are located outside the City. This includes:

- Developing instructions and documenting a standard operating procedure for current sampling and permitting fees charged to PA's using PIMS data (expected to be complete in December 2020);
- The Environmental Monitoring and Technical Services (EMTS) and Finance Divisions working to ensure the methodology for PA fees are appropriate for billing (expected to be complete in January 2021); and
- EMTS completing the reorganization of the IWCP and assigning the responsibility of annually billing PAs to the Support Services Group (expected to be complete in October 2020, with bills annually to PAs or outside permittees annually in October).

Note that implementation of this process will require negotiations with PAs, as is indicated in the responses to Recommendations 4 and 6.

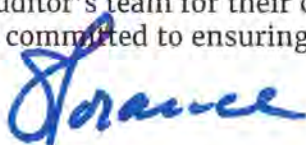
Target Implementation Date: The Department's Environmental Monitoring and Technical Services Division is working in conjunction with its Finance Division to complete these operating procedures by January 30, 2021.

RECOMMENDATION #9: The Public Utilities Department should perform a comprehensive review of all PIMS settings and invoice calculating features to ensure that invoices are automatically generated by PIMS and sent in a timely manner.

Management's Response: Agree. The Department currently invoices City of San Diego and County businesses automatically with approved fees pursuant to the 1984 Council Resolution or County agreement. As described in our response to Recommendation 8, PA bills require annual calculations. The process described in our response to Recommendation 8 will contain approved timelines. Additionally, the Department is developing a PIMS replacement program through the RFP process; the bidding period is expected to open in September 2020. This new PIMS will have documented billing invoice processes that sync with SAP system.

Target Implementation Date: The Department anticipates the new PIMS system to be implemented by June 2021. This timeline may need to be modified depending on the implementation timelines of respondents to the RFP to ensure successful implementation.

Again, we appreciate the opportunity to provide comments on this audit, and thank the City Auditor's team for their cooperation and professionalism throughout the audit process. PUD is committed to ensuring substantial progress is made on addressing these findings.



Shauna Lorance
Director

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