

**WATER RATE AND FINANCIAL POLICY
TACOMA PUBLIC UTILITIES
WATER DIVISION**

~~November 2022~~

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WATER RATE AND FINANCIAL POLICY

I. PURPOSE

The Water Rate and Financial Policy gives direction to planning decisions and helps ensure that the Department of Public Utilities provides for an adequate supply of safe, clean water to all customers efficiently, reliably and at the lowest possible cost consistent with prudent utility management.

II. GUIDING OBJECTIVES FOR WATER RATE DECISIONS

- A. Water Rates Should Ensure ~~Adequate Supply~~ Water Quality and Robust Supply.
- B. Water Rates Should Be As Low As Is Responsible.
- C. Water Rates Shall Be Fair and Equitable.
- D. Water Rates Should Be Based on Long-Term Financial Planning and Adjusted Gradually.
- E. Water Rates Should Be the Product of Customer Involvement.

III. POLICIES

- A. Water Rates Should Ensure ~~Adequate Supply~~ Water Quality and Robust Supply
 - 1. Water rates must be designed to adequately fund the acquisition of new resources and conservation consistent with local, state and federal laws and regulations and consistent with the responsibility of Tacoma Water as a regional purveyor for identified portions of Pierce and South King Counties as described in the Tacoma Second Diversion Water Right, Pierce County Coordinated Water System Plan, Tacoma Water System Plan, Second Supply Agreement, and any other official planning document as appropriate.
 - 2. Rate adjustments will be proposed in amounts sufficient to meet reasonable Tacoma Water budgets, while minimizing the long-run costs to the rate-payer. Since some actions such as supply

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development can influence the level of revenue needed over a period of years, staff will estimate both the short-run and long-run rate impacts of proposals presented to the Public Utility Board for consideration.

3. The revenue requirements analysis will study the projected revenue, expenses and capital improvements for the period to be covered by the rate change.
4. Modeling assumptions used in the estimation of water consumption and revenue for the rate review shall use industry standards, generally accepted econometric models, relevant forecasted local data, or a combination thereof.
5. Water rates will be designed to promote conservation as a long-term resource that will extend the use of the existing source of supply.
6. Water rates will be adequate to maintain the quality of the environment and balance the needs of customers (including the personal, aesthetic, recreational, and business objectives of customers) with the preservation of sensitive ecosystems at the source of supply.
7. Water rates will support a reasonable plan for replacement of aging water supply, distribution and storage infrastructure.
8. Climate change and equity will be incorporated when planning for investments and improvements to the water system.
9. Water rates will be designed to preserve and protect water quality. This includes the maintenance of sources of supply, infrastructure, facilities, and personnel to meet or exceed regulatory requirements.

B. Water Rates Should Be As Low As Is Responsible

1. Rate revenue together with other revenue sources, will cover current costs and meet or exceed all bond and other requirements necessary to maintain financial sufficiency.
2. Tacoma Water will secure the least costly means of financing for capital improvement projects based on evaluation of the Utility's financial position and capital needs. Financing mechanisms may include the use of revenue funding, unallocated operating or capital reserves, low interest loans, revenue bond funding and other means as deemed prudent.

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3. Senior Debt Service Coverage will be maintained above 1.50, exceeding Tacoma Water's bond covenant requirement of net revenue at least 1.25 times annual senior debt service. All-In Debt Service Coverage will be maintained above 1.25 except when cash reserves are budgeted to meet the annual revenue requirement, when it will be maintained above 1.00.

Major capital investments and other commitments that would significantly affect costs, rates or prices for Tacoma Water services will be evaluated against costs and benefits and documented before commitments are made. Such evaluations will address both short- and long-term, as well as potential or uncertain, impacts on costs and revenues.

4. Rates shall be set at levels such that projected current fund (fund 4600) cash balances will be ~~equal to~~ more than 60 days of current budgeted expenditures in each year of the planning period. It is recognized, however, that seasonal fluctuations may cause balances to be below recommended levels, but rates should be set such that the minimum cash balance in any month does not drop more than 40 percent below the recommended level. Operating surpluses may be applied to the Operating Reserve, capital construction or the Capital Reserve Fund.
5. Tacoma Water will exercise responsible cost control of department administration and overhead expenses consistent with industry standards.
6. Tacoma Water maintains two types of special funds that provide flexibility in ensuring timely acquisition, replacement and upgrade of the Utility's water system infrastructure and capital assets. Expenditures from these funds, subject to the limitations discussed below, may be used to offset the impact of rate increases.

The Water Capital Reserve Fund can be budgeted on a biennial basis as revenues become available for appropriate capital projects. A minimum balance of 1% of original cost plant-in-service will be maintained in the Fund.

The System Development Charge Fund is intended to provide capital funding for source development, transmission, storage, and related facilities. A minimum balance of \$2,000,000 will be maintained in the Fund to deal with unforeseen emergencies and contingencies, which would be authorized by separate Public Utilities Board approval.

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7. A special contract water rate may be developed in lieu of a system development charge for short-term temporary facilities provided sufficient surplus water is available for the term of proposed use. For purposes of this policy, short-term will generally be considered to be twenty years or less.
8. As rate adjustment proposals are developed, we will monitor the affordability of our rates and assess ways to mitigate impacts to our customers.

C. Water Rates Shall Be Fair and Equitable

1. Rates charged for each class of customer will be set to reflect the cost of supplying service to that class. Any exceptions to cost-of-service principles will be explicitly noted in this policy document.
2. An embedded cost-of-service study will determine the cost of serving each customer class, allocation of class responsibility for the projected expenses, and proposed rates sufficient to equitably recover projected expenses.
3. A short-term market based rate may be considered for marketing surplus water to industrial or wholesale customers if such a rate would increase net revenue to the Utility and no other customer class would be adversely impacted.
4. Conformance with responsible water use standards will be encouraged by the use of rate design and/or special charges.
5. A rate may be designed that would include an amount of water in the ready to serve charge.
6. Incentives will be considered for construction and conversions incorporating water conservation measures.
7. A rate surcharge may be proposed under unusual conditions, such as a drought, to ensure adequate revenues.
8. A rate surcharge may be proposed to improve acquired water systems which do not meet current Tacoma Water standards. This surcharge will apply to the service area of the sub-standard system and be used solely for the purpose of bringing that system up to standard.

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9. Rates for retail customers located outside the corporate boundaries of the City of Tacoma will be 20 percent higher than rates for inside City customers.
10. The assignment of costs of existing water supply resources to customers will be based on how those resources are used to meet system demands at the time of the current rate study.
11. The assignment of costs for new resources will reflect the anticipated use characteristics of those resources in either supplying normal water flows or providing extra water during times of peak usage.
12. Rates for new or additional water demand in excess of 1 million gallons a day (MGD) within any 12-month period may be designed to recover up to the full additional source of supply costs, less credit for any system development charge paid. *The use of water efficient technology will be a key consideration in the application of this provision.*
13. New customer hook-ups and enlarged services will be charged at current cost of main extension, including the cost of mains, inspection fees, services, meters, and any necessary fire protection service. A system development charge will be imposed on new or expanded services and may include charges for additional source of supply, transmission, storage, and pumping facilities. Adequate provisions shall be made to permit those who develop new services to recover main extension costs from those who subsequently use those water mains.
14. Periodic checks of actual revenues collected should be compared to projected revenue requirements by class. If the collections are not within an appropriate range, demand projections will be reviewed.
15. Inter-class revenue requirements adjustments significantly in excess of the system average may be allocated proportionately to the remaining customer classes. Subsequent increases for the subsidized class will be set equitably and appropriately until cost-of-service rates are reestablished.
16. The needs of low-income, senior, and disabled water customers will be considered when establishing rates, providing bill assistance, developing and implementing customer programs, and offering financial education.

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D. Water Rates Should Be Based on Long-Term Financial Planning and Adjusted Gradually

1. To the extent possible, rate adjustments will not exceed general inflationary trends. Phased-in adjustments over a limited time period may be used for projects requiring a considerable change in rate levels.
2. The number of rate schedules will be minimized by combining customers of reasonably similar use and cost-of-service characteristics.
3. Each rate schedule, except irrigation, will contain a monthly customer charge that will reflect, at a minimum, administrative and billing cost.
4. For revenue stability purposes, customer charges may be designed to recover up to 65 percent of revenue requirements for customer classes with strong seasonal consumption patterns.
5. Regular reviews will be performed to determine the adequacy of rates, and a full revenue requirements study will be performed every two years.
6. Seasonal rate design may be used to promote conservation during periods of greatest consumption. The second tier of a seasonal rate may be set to reflect the marginal cost of supply for the Utility.

E. Water Rates Should Be the Product of Customer Involvement

1. Any decision to revise rate-making policies will be done in an orderly fashion and formalized by resolution.
2. The Public Utility Board must review the existing rate policy well in advance of consideration of each rate adjustment. Any proposed changes require formal Board and City Council resolutions.
3. Tacoma Water will gather citizen input and provide equitable access to information about its rate-making process. Any proposal to be discussed will be made available as far in advance of its public hearing as is practical.
4. If an emergency rate adjustment becomes necessary due to drought or other unforeseen conditions, the emergency nature of the rate surcharge (or rollback) may necessitate a recommendation to the City Council using a reduced public involvement schedule. Such an

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emergency adjustment shall be followed by a reevaluation of the change in accordance with the formal procedures outlined in this policy.

5. A professional rate expert may be hired to represent the interests of the residential class during the rate process.
6. The Utility staff will respond to requests from the Neighborhood Councils and other local organizations to the Community and Media Services section of the Utility and provide equitable access to information on water rates, rate policy or rate assistance programs.
7. To the extent practicable, services and associated rates and fees will be designed to offer maximum choice and flexibility to meet customer needs and desires.