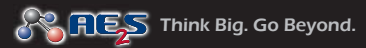


UTILITY ENTERPRISE MANAGEMENT

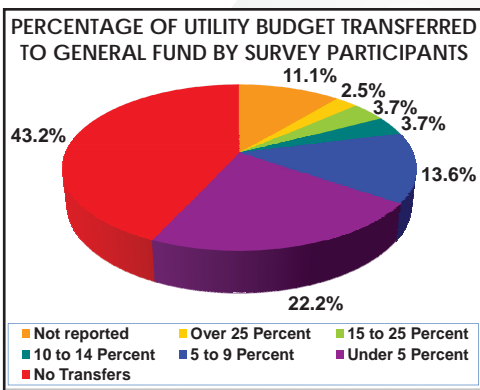
The Source

4th Quarter 2009



Rate Survey Data – General Fund Transfers

As part of the 2009 North Central Region Utility Rate Survey, responding utilities were asked what percentage of utility revenues are transferred to the owner municipality's General Fund. The chart below illustrates the results from 81 responding utilities.



Results ranged from zero to as high as 48 percent. It should be noted that the transfer of surplus utility funds is specific to each state. In North Dakota, up to 20 percent of annual utility revenues may be transferred to another fund. State laws in Minnesota, Montana, and South Dakota leave discretion to the governing body provided that the surplus utility funds are not otherwise pledged. It should be further noted that, although the industry standard is to strive for full cost recovery while charging an appropriate rate to allow the utility to break even after funding operation, maintenance, debt services, and either capital replacement/expansion costs or depreciation, the degree to which utility enterprises subsidize other City services or other City funds subsidize

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For Minnesota water systems serving greater than 1,000 people, the deadline for implementing a conservation rate structure is approximately one month away. Minnesota systems are not alone when it comes to encouraging water users to reduce water usage, as systems across the country are implementing such rate structures as part of comprehensive, long-term water system planning efforts.

A review of the literature finds that benefits associated with conservation rate structures include rewarding efficient users, reducing operating costs, delaying

Conservation Rates: Issues and Trends

capital expenditures associated with system expansion, drought preparedness, water supply conservation, reduced

wastewater discharge to watersheds, and flexibility for customers to control individual bills based on household choices. Potential drawbacks to conservation rate structures include revenue instability, possible reduction in revenues, difficulty with acceptance and implementation, and source substitution where allowed in some parts of the country. Overall, however, it appears that utilities are finding that the benefits outweigh the drawbacks when conservation structures are properly implemented. Regulators appear to agree, as evidenced by the Minnesota State Statute 103G.291 and funding requirements for some agencies that do not allow the continued use of declining block rate structures for funding recipients.

So, what about the impact to utility revenues? This is a valid concern, as the reduction of water use and the need for stable and adequate revenues can be competing objectives. The literature suggests that the price elasticity associated with water consumption is relatively small. Although little data is available, price elasticity has been found to be higher in areas of the country where irrigation is common. Elasticity also appears to rise with an increase in rate levels. As a result, when implementing conservation structure it is important to understand the usage patterns of the community so as to appropriately anticipate the potential change in water use.

To get an idea of rate structure trends in our region, rate survey statistics from the AE2S North Central Regional Utility Rate Surveys from 2005 to 2009 were reviewed. The table below shows the use of three block rate structures by utilities in our region (excluding the Minneapolis Metro area): Constant (or Uniform) Block, Increasing Block, and Declining Block. Inclining and Declining Block rate structures consist of two or more rate tiers and the Constant Block rate structure consists of one tier.

	2005	2006	2007	2008	2009
No. Respondents	62	74	79	82	81
Constant Rate	67.7%	62.1%	67.1%	70.7%	64.2%
Declining Block	21.0%	23.0%	16.6%	11.0%	12.3%
Inclining Block	11.3%	14.9%	16.6%	18.3%	23.5%

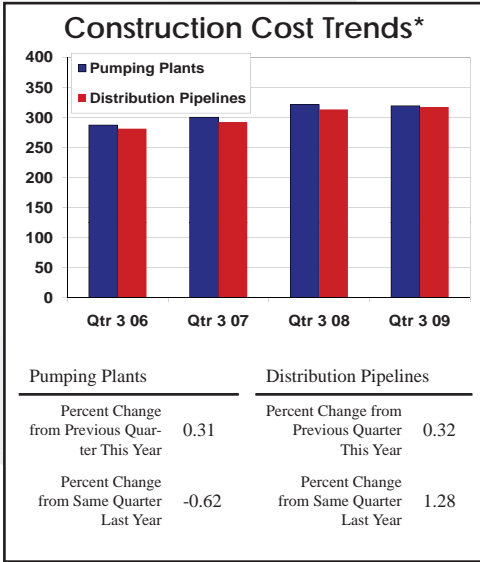
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(Rate Survey continued from first page)
 water and sewer utility services varies greatly based by municipality dependant on what is local policy. ■

(Conservation Rates: Issues and Trends continued from first page)

Although the systems responding each year are not necessarily the same, the table on the previous page shows that for the rate structures reported by survey respondents, the use of Constant Block structure has remained fairly stable. It appears there is a trend away from the Declining Block and toward the Inclining Block structure. Even though the Constant Block rate structure is not considered a conservation structure, Constant Block rates are simple, easy to implement, have a greater effect on deterring water use than Declining Block rates, and promote stable revenues. Inclining Block rates have the greatest ability to affect consumer responsiveness to rate changes, as users know that higher levels of use result in higher prices. The literature suggests that an Inclining Block rate with steep price blocks can be the best solution in addressing rate equitability, and can increase the incentive to conserve without increasing the price burden to low income users. Efforts to minimize potential revenue instability associated with Inclining Block structures can be implemented by carefully considering potential water sale reductions.

Reference: "Conservation and Drought Water Rates: State-of-the-art practices and their application," April 2009, Colin Rawls and Tatiana Borisova, University of Florida. ■



*Based on information from the Bureau of Reclamation

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