



**SANTA ANA
WATERSHED
PROJECT
AUTHORITY**

**The pricing of tiers
must be linked to
the cost of meeting
additional demands.**

CONSERVATION-BASED RATES: ENSURING LEGAL DEFENSIBILITY

The legality of conservation-based rates has been top of mind since the City of San Juan Capistrano's rate structure was ruled unconstitutional. The case highlighted the need to tie rates to the cost of service.

THE SAN JUAN CAPISTRANO CHALLENGE

In *Capistrano Taxpayers Association v. City of San Juan Capistrano*, the 4th District Court of Appeal struck down the City's rates in 2015. The case centered on several issues:

- » The City did not calculate the actual cost of service for its four price tiers.
- » Instead of justifying the price points for its tiers, the City assigned arbitrary percent increases over the first tier.
- » The relative cost of four of San Juan Capistrano's five sources of water was not itemized.

What was Learned: Keeping it Legal

The San Juan Capistrano case made one thing clear: Water providers must show their work when setting rates.

The court ruling applied to punitive tiered pricing, but not tiered rates in general. Conservation-based rates (also known as budget-based rates) built around the cost of providing water are legal. Providers must be able to show that pricing is based on costs of meeting the needs of a specific customer.

If a water provider must tap in to more expensive supplies, that cost can be reflected in the tiers. Costs may also include conservation, required peaking capacity and the cost of investigating new supplies, but the allocation of such costs must be well documented.

Proposition 218

Proposition 218, passed in 1996, requires government agencies to charge only the cost of a service and no more.

To avoid challenges under Proposition 218, agencies should have a rate study to:



IDENTIFY COSTS AND REVENUE REQUIREMENTS

Determine the income necessary to recover costs for such things as operations and maintenance, capital expenses and debt service obligations.



ALLOCATE COSTS TO CUSTOMER CLASSES

Consider varying costs of existing sources of supply, the costs of developing alternative supplies and water conservation programs, and the costs of increasing storage and delivery capacity.



DESIGN RATES

The structure should be equitable to customers, achieve revenue stability for the agency and send an effective conservation signal.



A study with conservation-based rates is no different. Items such as landscape measurements and weather data are factors that help a water agency better forecast demand (i.e. costs).

To hear a discussion about conservation-based rates, visit: https://youtu.be/mZdoL_5qdac

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