



BOARD POLICY

**Approved by the CAWCD Board
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CENTRAL ARIZONA PROJECT RATE SETTING POLICY

1. Goals of Rate Setting

- 1.1. Cost Recovery. CAP is a governmental entity that manages a water resource for the benefit of its rate and tax payers. Water rates are set in order to recover costs, on a long-term basis, net of other revenue sources.
- 1.2. Encourage Use. The policy of the state is to encourage use of renewable water supplies such as CAP water. The adoption of rates which facilitate use of CAP water by those who need and are entitled to CAP water furthers this state policy.
- 1.3. Financial Stability. To reliably perform its services, CAP must maintain a strong financial position and long-term balanced cash flows. Setting rates at levels which, on a long-term stabilized basis, are above cost is inconsistent with CAP's service responsibility. However, setting rates which on an overall basis are below cost would jeopardize the financial stability of the project. Measurement of cost is subject to uncertainty and relies on estimates. CAP will endeavor to accurately measure its cost and charge this amount to its users. CAP must also maintain reasonable levels of cash reserves as a financial buffer to avoid undue fluctuations in rates and to ensure its ability to meet its financial obligations in the event of higher than expected costs.
- 1.4. Price Stability and Predictability. Though the long run benefits of using renewable water supplies are self evident, in the short run switching from non-renewable supplies involves risks and sacrifices. CAP can mitigate those impacts by making an effort to maintain relatively stable and predictable rates. If changes are required, the changes should be announced well in advance and, if possible, phased in over a period of time.
- 1.5. Operational Efficiency. CAP owes a duty to its tax and rate payers to operate its facilities efficiently, maintaining rates as low as possible without compromising service reliability. CAP is not subject to competition or regulation which in other forms of enterprise would provide an independently imposed constraint or discipline for cost containment. CAP nevertheless commits itself to a goal of operating its facilities at the lowest possible cost consistent with maintaining a highly reliable service capability.

- 1.6. Accountability. CAP is responsible for the subcontracting and delivery of an average of 1.5 million acre-feet per year of water, the state's largest single source of renewable water, and therefore controls an asset of enormous importance to the state. The establishment of policies concerning availability and rates for this water is perhaps the most important responsibility of the CAP Board of Directors. Since rates charged to one user group indirectly affect rates charged to other users, rates should be considered as a package, and not in a piecemeal fashion. Water delivery policies and rates should be established in a highly public process only after due consideration and analysis of economic and financial impacts, and inviting comment from all affected parties.
- 1.7. Maximize Economic Benefit. In years when CAP subcontractors accept delivery of less than their full contract entitlement at the contract price and after statutory replenishment obligations for the CAGR have been met, the remaining water ("excess water") may be delivered to the subcontractors or other parties at rates established by the Board for such deliveries. CAP seeks to maximize the economic benefit from the use of water it supplies by making excess water available for delivery to direct uses and storage activities within the district. To that end, the Board may establish rates which differentiate among various user categories, taking into account the demand characteristics of such user categories and incremental costs of delivering water to them.
- 1.8. Legal Compliance. Any rate making processes and policies must be accomplished in accordance with statutory and contractual requirements.

2. Cost Measurement

- 2.1. CAP will periodically conduct cost of service studies to determine long-term cost structure of the operation and maintenance of its facilities.
- 2.2. Such studies will analyze the operating components of the system and estimate annual costs in the future for operations, repair and replacement, and convert those costs to an "equivalent annual" amount. This amount will be calculated so as to be sufficient to cover the estimated annual costs taking into account time value of money and the establishment and maintenance of reasonable financial reserves for operational contingencies and self insurance. Such studies may also consider energy costs associated with certain deliveries.
- 2.3. Cost of service studies will be conducted as needed, not less often than once every five years.
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3. Subcontract Water Delivery Charges

- 3.1. Water deliveries pursuant to subcontracts will be charged in accordance with subcontract requirements.

4. Capital Charges

- 4.1. Capital charges under the long term M&I subcontracts will be set in accordance with contract requirements taking into account additional revenue sources for repayment. Agricultural deliveries are assessed a \$1/af capital charge.
- 4.2. Additional sources of revenue for repayment include ad valorem taxes, electric revenue from CAP's power resources, "4.5 mil" surcharges on Hoover and Parker-Davis power sold in Arizona, capital charges on other water deliveries, and other miscellaneous revenues.

5. Excess Water

- 5.1. Water delivery charges for excess water will be established. CAP may establish a separate capital charge for excess water deliveries.
- 5.2. Differential rates for multiple user categories may be established by the excess water rate setting process. The goal of establishing a differential rate is to induce utilization of CAP water that would not exist otherwise. The formulation of prices for agricultural pools, water bank water, and other customer groups is an example of this approach.
- 5.3. In general, preference will be given to customers within the district that are willing to pay more for water, limited to full cost recovery. This approach may be modified by the establishment of pre-determined delivery amounts in certain price categories ("pools") to provide greater certainty for planning purposes by customer groups in lower price categories.
- 5.4. Water delivery charges for excess water may be priced below the M&I water delivery price, provided that the reduced price covers the incremental costs of such excess water deliveries, and the establishment of a reduced price does not result in an increase in the amount that would otherwise have been charged as the M&I water delivery charge, taking into account incremental costs of the increased deliveries, the benefit of spreading fixed costs over increased delivery amounts, and interest savings which result from increased deliveries, to agricultural uses which qualify for capital repayment without interest under the master repayment contract.

6. Forward announcement of prices, pools and price stability

- 6.1. CAP will announce prices biennially, providing prices for the next two years in accordance with contract requirements, and providing non-binding estimates of prices for the succeeding four years.
- 6.2. The first year of the rate schedule will be considered "firm" pricing, subject to change only in emergency circumstances and if a change would be permitted under the water delivery contract. The succeeding years in the price schedule are advisory for customer planning purposes, but subject to change.

price categories, then the size of the pools will also be forecast, on a 10 year rolling basis with the first 5 years of the forecast being firm, subject to change only in emergency circumstances and if a change would be permitted under applicable contract requirements.

- 6.4. CAP will endeavor to avoid “rate shock.” If financially feasible, it will phase in required rate increases over a reasonable period of time.

7. Rate Setting Process

- 7.1. A public rate setting process will be conducted biennially. This process will define customer groups and rates to be charged to each group. If then applicable, the size of “pools” of water available to each group will also be established.

- 7.2. Rates will be set only after being publicly announced and providing adequate time for public comment. The suggested calendar for the biennial rate setting process is as follows:

7.2.1. March – staff delivers proposed rate schedule and analysis to Board and customers for study; interested parties are invited to submit written comments;

7.2.2. April – Staff holds customer workshop;

7.2.3. April - public comments are analyzed and reviewed by staff and preliminary rate schedule is sent to the Finance and Audit Committee for a recommendation to the Board;

7.2.4. May – Board adopts preliminary rate schedule;

7.2.5. June – Board adopts final rate schedule.

- 7.3. Following adoption of rates, the following procedure will be followed:

7.3.1. June 1 – expected receipt of notice from Bureau of Reclamation of water availability for following year;

7.3.2. July 1 – CAP notifies customers of availability and price for following year;

7.3.3. October 1 – Customers submit in writing a schedule showing desired monthly deliveries for following year and preliminary estimates for succeeding two years;

7.3.4. November 15 – CAP furnishes customers a monthly delivery schedule for following year;

7.3.5. November 20 – first billing for following year’s deliveries is sent to customers.

7.4. In general, rates will be considered as a package, and not individually. In an exceptional circumstance (such as a “declaration of surplus” by the Secretary of the Interior), the Board may establish a new rate or user category in an interim rate action. In any such action, the Board shall consider the financial impacts to the project and effects on other customers.

7.5. The Board retains its authority permitted under water delivery contracts to adjust rates during the year if rates prove inadequate to cover cost, and the Board determines that an interim adjustment of rates is in the best interest of the project.

8. Implementation

8.1. Staff will conduct analysis and obtain studies necessary for the implementation of this rate setting process.

8.2. The first rate setting in accordance with this process will be constructed in calendar year 1998, to the extent feasible, and cost studies will be completed and full implementation of this policy will be accomplished by 1999.

8.3. The Board retains the right to establish and modify rates during this implementation phase.