

Utility Rate Studies

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Overview

- Establishing cost-based rates, fees, and charges is an important component in a well-managed and operated utility
- Cost-based rates provide sufficient funding to allow communities to build, operate, maintain, and re-invest in their utilities
- Properly and adequately funded utilities also allow for the economic development and sustainability of the local community



What do rate studies accomplish?

- Helps to maintain the long-term health and integrity of the utility system
- Quantifies policies, priorities, and initiatives
- Tells the “true” cost of providing the service
- Tracks cost information
- Evaluates equity between customer groups
- Communicates financial decisions and their impacts
- Provide a management decision tool



A successful rate study blends

- Finance
- Engineering
- Customer Service
- Administration



Rate Study Steps

- Determine Sensitivities and Priorities
- Review / Revise Fiscal Policies
- Revenue Requirement Analysis
- Cost of Service Analysis
- Rate Structure Design
- Public Education – ongoing PPU effort



Establishing Sensitivities and Priorities

- What is Important?
 - Growth pays for growth?
 - Renewal and replacement funding?
 - Discount programs?
 - Smooth rate impacts over time?
 - Phase in cost-of-service impacts?
 - Level of debt funding?
 - Promote conservation, sustainability, equity?



Fiscal Policies provide...

- A basis for financial performance and budgeting
- A plan for weathering financial disruptions and downturns
- A foundation for consistent rate decisions
- A documentation of management philosophy

- Target Reserves are an example of Fiscal Policies that help determine rates.



Revenue Requirements Analysis

Revenue Requirements are the summation of the operation, maintenance, and capital costs that a utility must recover during the time period for which the rates will be in place

- Determines the adequate and appropriate funding of the utility
- Develops a multi-year financial plan to support the utility
- Evaluates the sufficiency of current rates on a stand-alone basis
- Develops an annual rate implementation strategy



Revenue Requirement Analysis (cont.)

Forecast of Revenue at existing rates

+

Forecast of O&M costs

+

Planned Capital costs

+

Existing & new debt service

=

ANNUAL REVENUE REQUIREMENT



Operating Cost Considerations

- Inflation factors, CPI, local economic conditions
- Strategic program initiatives
- Additional needs (staffing, regulatory requirements)
- Increasing costs (purchases, materials, supplies, wholesale power)
- Indirect costs (allocation rates)



Capital Cost Considerations

- Cash?
 - Pay as you go -> higher near term rates
Existing customers pay 100% of initial costs
- Debt?
 - Mitigates immediate rate impacts
 - More closely matches costs to useful life
 - Spreads costs between existing and future rate payers
 - Debt capacity can be an issue
- Hybrid?
 - Evaluate the need for debt (large, long life projects)
 - Align funding with nature of project



Cost of Service Analysis

- Determines what cost differences, if any, exist between serving the various customer classes of service.
- Equitably distributes the revenue requirements between the various customer classes of service served by the utility
 - Cost allocations are based on
 - Industry standard methodologies
 - Unique usage characteristics of our customers (energy and demand)
 - Unique facility requirements (planning and design criteria, decommissioning)



Rate Design

- Determines how to recover the appropriate level of costs from each customer class of service
- Different rate structures may be used to collect the appropriate level of revenues from each customer class of service
- Composed of fixed and variable charges



Rate Design Considerations

- Equity of Rates
- Complexity of Rates
- Rate Impacts
- Revenue stability and predictability
- Social objectives (affordability, economic development, reliability, sustainability)



What happens if no rate study is conducted?

- Perhaps nothing – if nothing changes
- However, a rate study can be extremely valuable if
 - Customer load shapes change
 - A particular customer, or class of customer believes that rates are too high or that another class is paying too little
 - There is a desire for new rate structures due to regulatory changes, wholesale power changes, and/or changes in management philosophy
 - New debt service is added
 - The utility grows through service territory annexations and/or significant economic development
- Ultimately, PPU must be able to defend why it charges as it does



What are the benefits of a Rate Study

- Defensible basis for rates
- Ensure best practices
- Fair and equitable rate charges to customers
- Bond markets favor a multi-year schedule to support fiscal sustainability
- Outside perspective lends credibility and objectivity to rates



Questions?



