

Are Tiered Conservation Rates Valid?



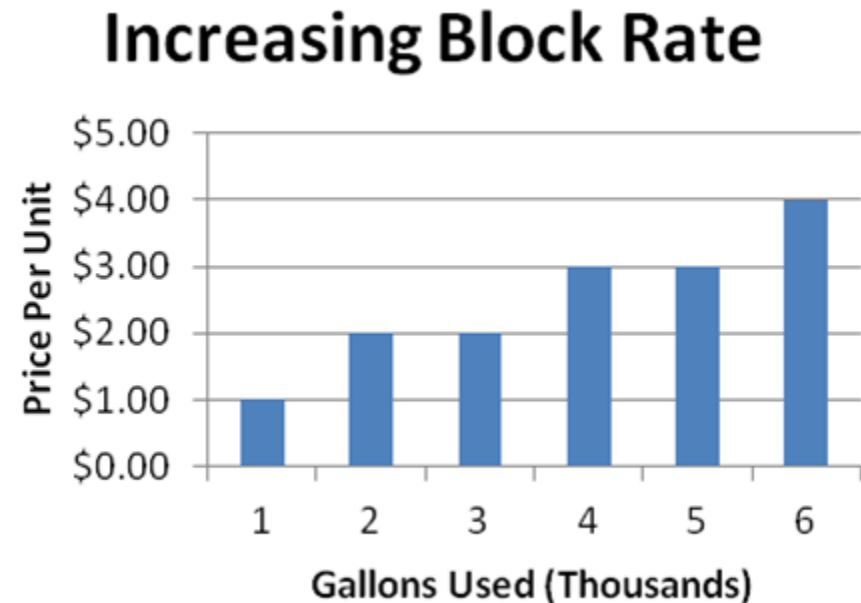
Implications of California's *San Juan Capistrano* Case for Florida Water Utilities

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Water Conserving Rate Structures in Florida

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- **§ 373.227(3) Fla. Stat.** – Public supply CUPs are conditioned on adoption of a rate structure that encourages conservation
- Public supply utilities have wide latitude in selecting appropriate rate structure
- Most Florida public supply utilities have adopted inclining block tiered water rates to comply with the CUP conservation requirements



CHALLENGE TO CALIFORNIA TIERED CONSERVATION RATES

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Tiered prices

The city of San Juan Capistrano's 2010 water rate schedule

(Cost per 748 gallons)

Tier 1

\$2.47

Tier 2

\$3.29

Tier 3

\$4.94

Tier 4

\$9.05



- As in Florida, California public suppliers commonly adopt tiered rates, explicitly for the purpose of encouraging water conservation
- California Constitution requires conservation and efficient water use
- A taxpayers association challenged the validity of the tiered rates adopted by the City of San Juan Capistrano on the basis that tiered conservation rates violate Proposition 218 of the California Constitution

PROPOSITION 218

- Amendment to California Constitution approved by voters in 1996
- Places limitations on local government finance and governance
- Limits ability of local governments to impose assessments and property-related fees
- Any “fee or charge imposed upon any parcel or person as an incident of property ownership shall not exceed the proportional cost of the service attributable to the parcel.”
- Significant limitation on how fees are assessed and justified

Capistrano Taxpayers Ass'n, Inc. v. City of San Juan Capistrano

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California's Fourth Appellate District April 2015 decision:

- Higher consumption users can be charged higher rates, *if* it can be shown by the utility that the need for development of expensive facilities such as a water recycling plant or desalination facility is attributable to users in the higher rate tier
- Engineering Report San Juan Capistrano relied on to support tiered rates did not establish a nexus between the cost of the service provided and the price charged at each tier.

Capistrano Taxpayers Ass'n, Inc. v. City of San Juan Capistrano

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California's Fourth Appellate District April 2015 decision:

- Tiered water rates do not automatically violate requirements of Proposition 218
- Rates charged to customers must correspond to actual cost of providing water to the customers in each tier – **basing tiers on amounts needed to encourage conservation alone is invalid**
- Utility must show that the cost of providing water to higher consumption users is proportional to their water use
- Limitations of Proposition 218 also apply to reclaimed water rates

City of San Juan Capistrano

Decision Aftermath



- Governor Jerry Brown: ruling “put a straightjacket on local government at a time when maximum flexibility is needed” due to drought conditions
- City of San Juan Capistrano required to refund customers charged at higher tiered rates
- Cal. Atty General and State Water Resources Control Board request that Cal. Supreme Court “depublish” 4th District’s opinion – would mean case has no precedential value
 - **Request for depublication denied by Cal. Supreme Ct in July**
- May 2015 class action lawsuit filed against Marin Municipal Water District seeking to recover excess fees charged under tiered rates

City of San Juan Capistrano Decision Aftermath

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California water utilities are already amending rates to comply by eliminating multiple tiers:

*Excerpt from Tuolumne Utilities District
November 2015 Draft Rate Study:*

In addition to state law regarding the rate setting process, certain case law also applies. On April 20, 2015, a California appellate court determined that the tiered water rate structure used by the City of San Juan Capistrano violated the provisions of Proposition 218 relating to the proportional cost of the service (Capistrano Taxpayers Association Inc. v. City of San Juan Capistrano). The court stated the City failed to provide sufficient proof that their tiered pricing for water service reflected actual costs of service to high water use customers. Tiered rates can comply with Proposition 218 as long as the rates reflect the additional marginal cost to provide the service including necessary capital improvements. The agency has the burden of proof to substantiate that the property-related fee or charge does not exceed the cost to provide the service, as well as the proportional cost of service. As a result of this case the District is proposing to eliminate its 6-tier rate structure and replacing it with one fixed rate and one tier.



Revised 10/26/15

Tuolumne
Utilities
District

FINAL DRAFT
RATE STUDY
FYE16-FYE20



NOVEMBER
2015



City of San Juan Capistrano

Decision Aftermath

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Measures Considered in Response to *San Juan Capistrano* Decision:

- New Constitutional amendment
- Statutory limitations on class action lawsuits against utilities
- Statutory affirmation that tiered rates can comply with Prop 218
- 2/3 voter approval of rates under Prop 218
- Statutory validation of existing rate structures
- Fines instead of fees for excessive use
- Divestment of government utilities to private investor owned utilities

Implications for Florida Public Suppliers



Florida's Constitution does not have a direct constitutional or statutory limitation on rates like Proposition 218, **however:**

- *Contractors and Builders Ass'n of Pinellas County v. City of Dunedin* (Fla. 1976) regarding validity of utility impact fees:
 - Differential rates and charges must be “just and equitable”
 - Utility rates classes cannot be unreasonable or “discriminatory”
 - Total fee charged must be justified by the costs incurred for service
 - Fee charged to a particular class of users has to be proportional to the impact of the class on the need for the facilities required
 - Class cannot be arbitrarily established in a way that is not related to the services to be provided
- For water utilities, proportional impact is directly related to the amount of water the customer will use
- No reason the same proportionality rationale could not be applied to customers subject to tiered rates

Implications for Florida Public Suppliers



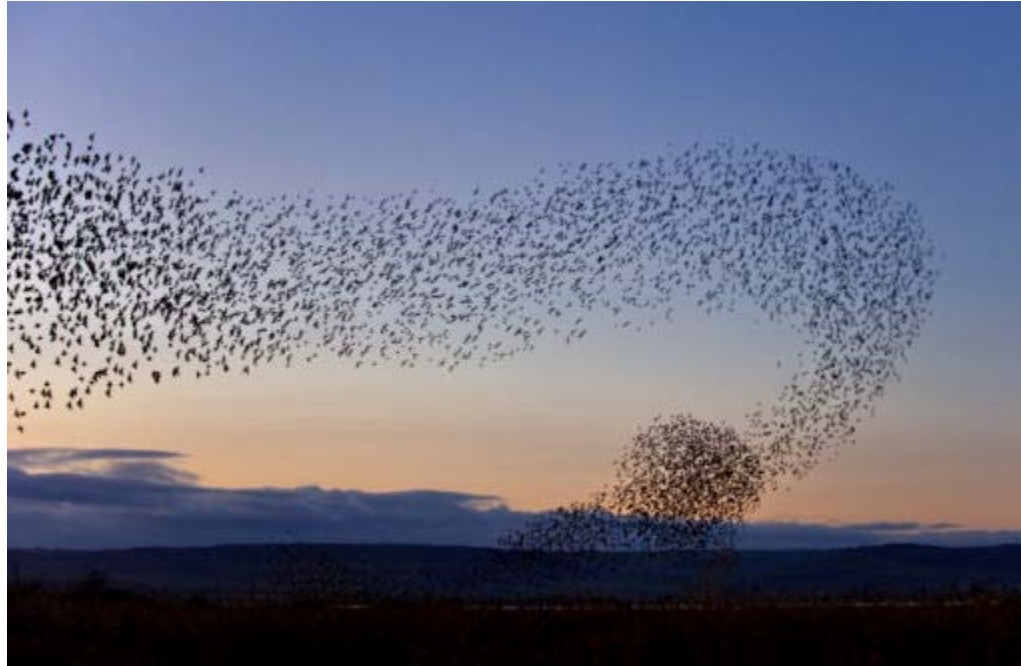
U.S. Supreme Court - *Koontz v. St. Johns River Water Management Dist.*

- Like *Dunedin* proportionality test, 5th Amendment “takings clause” requires nexus and proportionality in relation to imposition of fees and financial assessments concerning taking of property
- Double nexus analysis extends to requiring property owners to pay fee amount in return for permit authorizing particular land use
- Potential argument that residential property ownership is conditioned on obtaining certificate of occupancy, which requires subjecting the property to water and sewer rates established by the utility

Florida water utilities should proactively address justification for tiered conservation by tying rate decisions to costs associated with users in each tier

Conclusion

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Questions and Discussion