February 22, 2021

Citizens’ Water Advisory Committee
C/o Tucson Water Intergovernmental Coordination
Delivered via Email to: Jessica.Rodriguez@tucsonaz.gov

Re: Pre-Annexation Development Agreements and Differential Rates Presentation

I have had an opportunity to review the February 3, 2021 presentation by Interim Assistant City Manager Timothy Thomure and Assistant City Attorney Christopher Avery entitled Pre-Annexation Development Agreements and Differential Rates. (Attachment 1)

First, I would like to preface my remarks with some history associated with regional water and sewer service. Before the Intergovernmental Agreement (IGA) referenced in the document, the City and the County agreed to form an entity called the Metropolitan Utilities Management Agency for the purpose of regionalizing and consolidating water and sewer service for all citizens of Pima County, whether they live in cities, towns or the unincorporated area of Pima County. Unfortunately, that entity did not last and the outgrowth was the 1979 City/County IGA dividing water and sewer service. The original concept was that the City of Tucson would be the regional water provider and Pima County would be the regional sewer provider. Only the latter is viable to date.

Given the presentation and the history of Tucson Water providing what was originally deemed to be a regional service, it is not surprising that 34 percent of Tucson Water customers live outside the City limits. While the decision on differential water rates will rest with the Mayor and Council, I suggest that Article III Paragraph A of the 1979 IGA regarding water service reflects equal footing for both the City and the County when it comes to cost. The phrase, “…minimize costs to water rate payers in City and County,” underpins the concept of water service in equal cost as well as benefits to both City and County residents. This concept was the sole basis for allocating County-generated effluent to the City at no cost to “…maintain management of the total water resources of the Santa Cruz and adjacent water basins.” This clearly implies a regional benefit, not a city-centric benefit.

Additionally, the cited memorandum on Page 7 of the presentation incorrectly “cherry picks” data from my June 17, 2016 memorandum to the Board of Supervisors; it only quotes the first page. The full version of this memorandum clearly indicates that, while counties are
left out of the distribution of state-shared income taxes, incorporating or annexing is not the financial boon they are purported to be in this slide. In fact, my memorandum goes on to say that this additional revenue would be consumed in one line of business for newly incorporated residents in the form of simply police protection. (Attachment 2)

Justifying differential rates through financial backing of the City’s General Fund is no different than the County’s General Fund backing the wastewater enterprise. Under no circumstances would we consider differential sewer rates to City customers. Our customers are regional, in fact, in my memorandum that was cited by the City, I conclude that this strategy will lead to increased local taxes, instead of being a tax reduction strategy.

Thank you for allowing me to clarify the recent presentation on this matter before your Committee. Please share this information with all committee members.

Sincerely,

C.H. Huckelberry
County Administrator

Attachments

c: The Honorable Chair and Members, Pima County Board of Supervisors
Pima County Wastewater Reclamation Advisory Committee
Jan Lesher, Chief Deputy County Administrator
Carmine DeBonis, Jr., Deputy County Administrator for Public Works
Yves Khawam, PhD, Assistant County Administrator for Public Works
Jackson Jenkins, Director, Regional Wastewater Reclamation
Pre-Annexation Development Agreements and Differential Rates

Citizens’ Water Advisory Committee
February 3, 2021

Timothy Thomure, Interim Asst. City Manager
Christopher Avery, Asst. City Attorney
• About 34% of Tucson Water customers are located outside of the city limits
• About 28% are located in unincorporated Pima County
• About 6% are in another jurisdiction: Marana, Oro Valley, South Tucson
CITIZENS’ WATER ADVISORY COMMITTEE
Pre-Annexation Development Agreements and Differential Rates

• **Differential Rates are allowed.** Requires a rational relationship to services provided. This has been tested in Court in AZ

• Legal Context of ARS 9-511

  If a municipality provides water to another municipality, the rates it charges for the water to the public in the other municipality shall be one of the following:

  1. The same or less than the rates it charges its own residents for water.

  2. The same or less than the rates the other municipality charges its residents for water.

  3. If the other municipality does not provide water, the average rates charged for water to the residents in the other municipality by private water companies.

  4. Rates determined by a contract which is approved by both municipalities and in which such rates are justified by a cost-of-service study or by any other method agreed to by both municipalities.
## Differential Rates are commonplace

<table>
<thead>
<tr>
<th>City</th>
<th>Inside</th>
<th>Outside</th>
<th>Inside (1st tier use)</th>
<th>Outside (1st tier use)</th>
<th>Inside/Outside Adjuster</th>
<th>Notes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chandler</td>
<td>$9.07/mo</td>
<td>$12.70/mo</td>
<td>$1.60 per 1,000 gal</td>
<td>$2.24 per 1,000 gal</td>
<td>+40%</td>
<td>volume rate is for first 10,000 gal</td>
</tr>
<tr>
<td>Flagstaff</td>
<td>$15.27/mo</td>
<td>$16.80/mo</td>
<td>$3.98 per 1,000 gal</td>
<td>$4.38 per 1,000 gal</td>
<td>+10%</td>
<td>volume rate is for first 3,500 gal</td>
</tr>
<tr>
<td>Flowing Wells</td>
<td>$12.00/mo</td>
<td>$16.00/mo</td>
<td>$2.45 per 1,000 gal</td>
<td>$2.52 per 1,000 gal</td>
<td>n/a</td>
<td>volume rate is per 1,000 gal</td>
</tr>
<tr>
<td>Glendale</td>
<td>$10.20/mo</td>
<td>$13.26/mo</td>
<td>$2.26 per 1,000 gal</td>
<td>$2.94 per 1,000 gal</td>
<td>+30%</td>
<td>volume rate is for first 6,000 gal</td>
</tr>
<tr>
<td>Metro Water</td>
<td>$29.50/mo</td>
<td>$31.00/mo</td>
<td>$2.75 per 1,000 gal</td>
<td>$3.00 per 1,000 gal</td>
<td>n/a</td>
<td>Metro’s differential rate applies only to its Metro SW-Diablo Village Service Area; up to 3,000 gal included in base rate; volume charge is for 3,001 – 10,000 gal</td>
</tr>
<tr>
<td>Phoenix</td>
<td>$5.50/mo</td>
<td>$8.25/mo</td>
<td>$4.08 flat</td>
<td>$6.12 flat</td>
<td>+50%</td>
<td>the volume rate is a flat fee for any use over the 10 ccf summer allowance; 6 ccf winter / 10 ccf summer allowance is included in base rate</td>
</tr>
<tr>
<td>Scottsdale</td>
<td>$11.90/mo</td>
<td>$13.69/mo</td>
<td>$1.65 per 1,000 gal</td>
<td>$1.90 per 1,000 gal</td>
<td>+15% *</td>
<td>volume rate is per 1,000 gal for first 5,000 gal; *also, a 25% surcharge on new meter fees outside of City limits</td>
</tr>
<tr>
<td>Tempe</td>
<td>$11.50/mo</td>
<td>$14.95/mo</td>
<td>$1.80 per 1,000 gal</td>
<td>$2.34 per 1,000 gal</td>
<td>+30%</td>
<td>volume rate is for first 6,000 gal</td>
</tr>
<tr>
<td>Yuma</td>
<td>$17.47/mo</td>
<td>$23.24/mo</td>
<td>$1.53/ccf</td>
<td>$2.03/ccf</td>
<td>+30%</td>
<td></td>
</tr>
</tbody>
</table>

Differential Rates are commonplace.
Updated survey is being conducted:

1. Do you serve any water customers outside of your jurisdiction? If so, what percentage is that of total customer base?

2. Do you charge a differential rates to customers outside your municipality?

3. If you charge a differential rate, what year was it established?

4. If you charge a differential rate, how much is it?

5. If you do charge a differential rate, what is the basis? (e.g. Revenue generation, cost-of-service, or support policy outcomes such as annexation)

6. Where does the revenue from differential rates go? (e.g. Stay in the utility or other city fund?)
CITIZENS’ WATER ADVISORY COMMITTEE
Pre-Annexation Development Agreements and Differential Rates

- 1979 City and County IGA
- 1970’s Lift Charges
CITIZENS’ WATER ADVISORY COMMITTEE
Pre-Annexation Development Agreements and Differential Rates

• Policy objectives (“why differential rates?”)

• Unincorporated areas receive lower State Shared Revenues (SSR)

• For Pima County, this impact to SSR is $42.6M (2016 Memorandum Chuck Huckleberry)

• Annexation / incorporation is the prime policy objective
Industry policy norms

- Inside City customer-ownership ROI
- Revenue risk of outside customers
- Financial backing of General Fund

Under this proposal, rates in unincorporated areas would approximately match prior financial plan
CITIZENS’ WATER ADVISORY COMMITTEE
Pre-Annexation Development Agreements and Differential Rates

• Utilization of funds
  • Use in General Fund is legal
  • Use within TW is legal and could offset general rate increases
  • Use within TW is legal and could be directed to assistance programs, etc that benefits all customers
CITIZENS’ WATER ADVISORY COMMITTEE
Pre-Annexation Development Agreements and Differential Rates

Next Steps

• Stakeholder Outreach now through April 6, 2021
• Return to Mayor and Council with summary of public outreach and Notice of Intent (NOI) for consideration on April 6, 2021
• Public Hearing June 8, 2021
• Effective Date July 5, 2021
CITIZENS’ WATER ADVISORY COMMITTEE
Pre-Annexation Development Agreements and Differential Rates

Stakeholders

- Community Water Coalition
- Watershed Management Group
- Tucson Metro Chamber of Commerce
- Southern Arizona Housing Builder Association
- Metropolitan Pima Alliance
- Tucson Real Estate Advisory Council
- Tucson Association Realtors
- SERI
- Coalition for Sonoran Desert Protection
- Sierra Club
- LUCHA
- CHiSPA
Questions?
MEMORANDUM

Date: June 17, 2016

To: The Honorable Chair and Members
Pima County Board of Supervisors

From: C.H. Huckelberry
County Administrator

Re: State Shared Revenue Increase Based on Annexation or Incorporation

Every few years, discussion occurs regarding Pima County’s unincorporated population, which is the largest of any county in Arizona, and whether this population should either become a city or be annexed into adjacent cities or towns. This discussion centers around the increased State Shared Revenues (SSRs) that theoretically would allow taxes to be decreased. This premise is significantly flawed, and the more likely result from our unincorporated population becoming a city or town or being annexed by other jurisdictions would be an actual tax increase.

Consideration of the following factors must be included in any discussion of this issue:

- SSRs are distributed to cities and towns, as well as counties. Any new city or town or annexation of the 362,082 persons living in our unincorporated area would increase SSRs for that new town or the annexed jurisdiction, including Vehicle License Tax (VLT), Highway User Revenue Funds (HURF), State Shared sales tax and State income tax. Based on the population and existing revenue distribution, this newly incorporated city or town or annexed population would receive an additional $103.7 million in SSRs. This appears significant.

- The first problem with such an assumption is that, overall, statewide tax revenues from these categories do not increase; they are shared. Hence, any increase for a new city or town or annexed community will result in decreases for all other existing cities and towns. In this case, the total decrease in revenue for existing cities and towns within Pima County would be $29.1 million. Therefore, the net new regional additional tax revenues from SSRs would be $74.6 million, which still appears to be a significant amount.

- In addition to the existing cities and towns losing SSRs, the County would also see losses in SSRs in those revenue categories that rely on unincorporated population as a distribution factor. The County would lose its VLT revenues for transportation and see a significant reduction in County HURF revenues. These losses would equal $32 million. Therefore, the net increase in revenues to the region would be further reduced from $74.6 million to $42.6 million.
The next significant questions are whether the region would be better off with this new or annexed community with a net increase of $42.6 million, and could this increase in revenue offset expected service costs for a new city, town, or annexed community? To answer this question, the best model would be to examine aggregate budgets of cities and towns in Arizona where the population ranges from as high 261,000 to as low as 171,000. The table below shows a list of the six Arizona communities that fall within this population threshold, as well as their respective annual and per capita budgets for last year. As can be seen, the annual budgets of even the least populated community of Peoria has an annual budget that exceeds by a factor of 12 the additional regional revenues that would be derived from such a strategy. Even with discounting the water and wastewater enterprise funds run by the community of Peoria, this factor would still exceed the additional revenue by 9.5 times. Clearly, a new community would need to rely on increased taxes. Hence, rather than being a tax reduction strategy, it is a strategy that will actually lead to increased local taxes.

<table>
<thead>
<tr>
<th>City/Town</th>
<th>Population</th>
<th>FY2015/16 General Fund Expenditures</th>
<th>FY2015/16 Total Funds Expenditures</th>
<th>Total Budget, Net of Enterprise Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chandler</td>
<td>260,828</td>
<td>$244,595,922</td>
<td>$910,614,017</td>
<td>$810,734,843</td>
</tr>
<tr>
<td>Gilbert</td>
<td>247,542</td>
<td>169,904,050</td>
<td>615,009,220</td>
<td>518,437,420</td>
</tr>
<tr>
<td>Glendale</td>
<td>240,126</td>
<td>206,154,495</td>
<td>632,000,000</td>
<td>535,418,169</td>
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<tr>
<td>Peoria</td>
<td>171,237</td>
<td>168,566,321</td>
<td>511,000,000</td>
<td>403,422,981</td>
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<tr>
<td>Scottsdale</td>
<td>236,839</td>
<td>273,234,364</td>
<td>1,201,690,332</td>
<td>1,016,311,698</td>
</tr>
<tr>
<td>Tempe</td>
<td>175,826</td>
<td>187,647,884</td>
<td>607,527,884</td>
<td>516,329,698</td>
</tr>
</tbody>
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<th>Total Budget, Net of Enterprise Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chandler</td>
<td>260,828</td>
<td>$937.77</td>
<td>3,491.24</td>
<td>3,108.31</td>
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<tr>
<td>Gilbert</td>
<td>247,542</td>
<td>686.36</td>
<td>2,484.46</td>
<td>2,094.34</td>
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<td>Glendale</td>
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<td>858.53</td>
<td>2,631.95</td>
<td>2,229.74</td>
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<tr>
<td>Peoria</td>
<td>171,237</td>
<td>984.40</td>
<td>2,984.17</td>
<td>2,355.93</td>
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<td>Scottsdale</td>
<td>236,839</td>
<td>1,153.67</td>
<td>5,073.87</td>
<td>4,291.15</td>
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<tr>
<td>Tempe</td>
<td>175,826</td>
<td>1,067.24</td>
<td>3,455.28</td>
<td>2,936.59</td>
</tr>
</tbody>
</table>

\(^1\text{US Census Bureau population estimate for July 1, 2015 }\text{https://www.census.gov/popest/data/}\)
Assuming the highest annual per capita budget expenditure of the City of Scottsdale for our unincorporated population, the new community would result in a budget expenditure of $1.55 billion. Utilizing even the lowest per capita annual budget expenditure, the Town of Gilbert at $2,094.34, still results in an annual expenditure of $758.3 million.

Believing that incorporating our unincorporated population in either a new city or annexing it into existing cities and towns will result in a tax decrease is a fallacy. The exact opposite would occur.

CHH/mjk