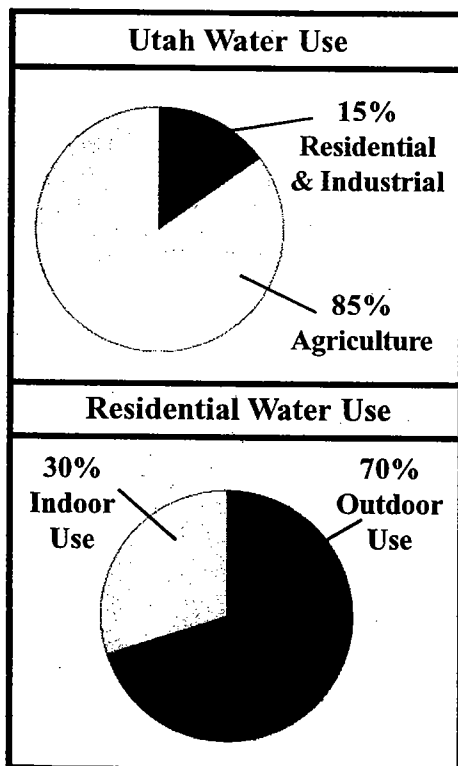


Utah Rivers Council

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“It is hard to justify the extent we subsidize municipal and industrial water rates with tax dollars, given that Utah has among the lowest rates and the highest per-person use in America.”
-Governor Leavitt

Figure 1. Only 3 percent of Utah’s water is for urban use – most of which is used on lawns. Claims the Salt Lake Valley is running out of water are greatly exaggerated.



Mirage in the Desert: Property Tax Subsidies for Water

Property tax collection by Utah water conservancy districts has been a matter of discussion and criticism among the public and elected officials. Several times over the last five years legislation has been introduced to lower or remove the property tax levy but has been met by stringent opposition from collectors of the tax.

Critics contend property tax collections subsidize water rates and encourage people to overuse water. Collectors of the tax argue property taxes are essential to gaining competitive bond ratings for water development and provide a stable revenue source.

To help aid this discussion, the Utah Rivers Council launched a research project in 2001 to determine the prevalence of property tax collections among water suppliers across the West. It should be noted there are different challenges in water finance between rural and urban areas. Since rural suppliers deliver water to a small population with little rate revenue to pay for capital projects, property taxes are appealing for financing water delivery. But urban suppliers can collect a large revenue stream from water rates because of the large population consuming water. Not all Utah urban water suppliers have taken advantage of this stable revenue source by shifting the costs of water supply onto water rates.

Water Use & Pricing

Utah’s urban water use is one of the highest in the Nation, according to the U.S.G.S. (Figure 2).¹ Conversely, Utah’s water rates are among the lowest in the country (Appendix B).² Utahns pay for water not only in their water bill but in their tax base. Salt Lake County residents pay only 49 percent of the cost of supplying water in their water bill with the remaining costs paid for in property, sales and income taxes (Figure 3).³ These taxes mask the true cost of water delivery and keep water rates artificially low.

As with any commodity, low prices encourage consumers to purchase more product. If the full cost of water were placed in rates consumers would be more conscientious about how much water they pay for and use. In turn, water use would go down. This effect of *price* upon *use* is called *elasticity* and is in the range of 50 to 70 percent. That is, a 20 percent price increase will lead to a decrease in water use in the range of 10 to 14 percent.

Though there have been some hasty predictions about the rate increases that would occur if property taxes were removed, these claims ignore elasticity and have not been presented for public discussion. It appears to be more than coincidence these claims originate from the suppliers collecting property taxes who seek to keep collections in place.

Further, these claims ignore rate structures which could offset price increases. Most Utah water suppliers charge one water rate regardless of the amount of water used. But other western cities charge several rates to discourage waste and minimize capital spending. A low rate is charged until a certain volume of water is used when a higher rate is charged to discourage over-watering. The revenue lost by removing property taxes could thus be generated from large volume users who create the largest burden on the system by using this inclining rate structure.

Many western communities have found success in using market-based water pricing. For example, Irvine Ranch Water District used water pricing to reward efficient water use resulting in a nearly 20 percent reduction in outdoor water use. Marin Municipal Water District avoided expenditures for a new water pipeline by implementing a rate increase which reduced water demand 15 percent in 5 years despite an 8 percent population increase. Through water pricing and other programs Los Angeles reported in 1997 it had reduced its water use back to 1970 levels even amidst a 25 percent population increase to 3.7 million people.

Study Methodology

Because each state creates its own laws governing the operation of water supply, a wide variety of public entities deliver water to the West's metropolitan areas. Some suppliers have been absorbed into city or county governments, some are private companies, some deliver additional commodities like electricity, some manage sewer facilities, and some are limited to specific watersheds.

Fifty-four water suppliers were selected from 11 Western States. These suppliers were mailed a survey and respondents were later contacted by phone to confirm statements. Since the purpose of this study was to take a broad look at financing urban water delivery, this research focused on metropolitan water suppliers instead of titles given to specific agencies. For the most part, rural water supply financing was not evaluated. Had water suppliers been selected based solely on their title, entire states would be ignored thus limiting the scope of evaluation.

Arguments Against Property Tax Collections by Urban Water Suppliers

A. Property taxes encourage water waste & create inequity between use & payment

Most urban water suppliers surveyed do not collect property taxes (Figure 4). Property taxes lower the retail price of water since part of the delivery cost is hidden in property, sales, and income taxes. This subsidy discourages consumers from saving water. Since property taxes remain steady regardless of water use, low water users—such as those who have small lot sizes or are conscientious about their use—often pay for wasteful users in their taxes, particularly during the summer.

Figure 2. Culinary Water Use in Gallons Per Day

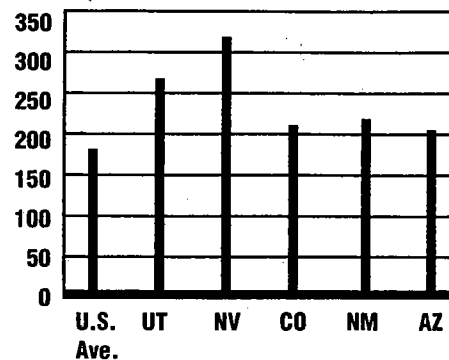


Figure 3. Revenue Sources for Salt Lake County Water Supply

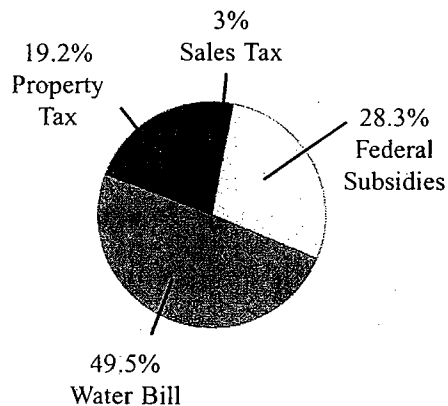
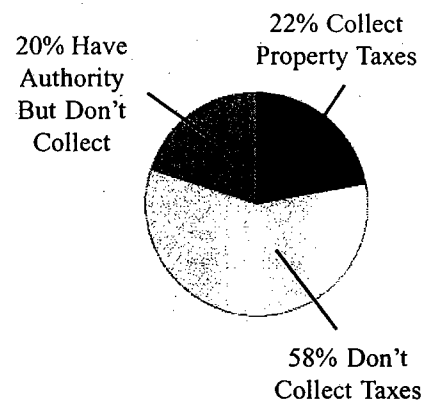


Figure 4. Proportion of Western Water Suppliers Collecting Property Taxes



Property tax subsidies discourage consumers from saving water since tax payments remain steady regardless of water use.

For example, consider a university with high water usage for summer irrigation. Because the university is exempt from paying property taxes, part of its water use is paid for by homeowners and businesses in their property taxes. This mechanism provides no incentive for the university or the homeowner to save water.

B. Subsidized water rates lead to over-spending on capital projects

Because low water rates encourage over-consumption, much of the Salt Lake Valley's peak summer water usage is simply waste. Yet demand projections that are used to justify capital expenditures are based on this waste. If water use was reduced, capital spending for new projects could be avoided or delayed (Figure 5). In other words, reducing demand through appropriate water pricing is a substitute to increasing supply.

Although some demand reduction goals have been put forth in Utah, the timeline for these goals is 30-50 years away, after new capital expenditures have been made (Plans A and B in Figure 5). If property tax subsidies were removed, water demand would drop and negate the need for capital expenditures (Plan C in Figure 5).

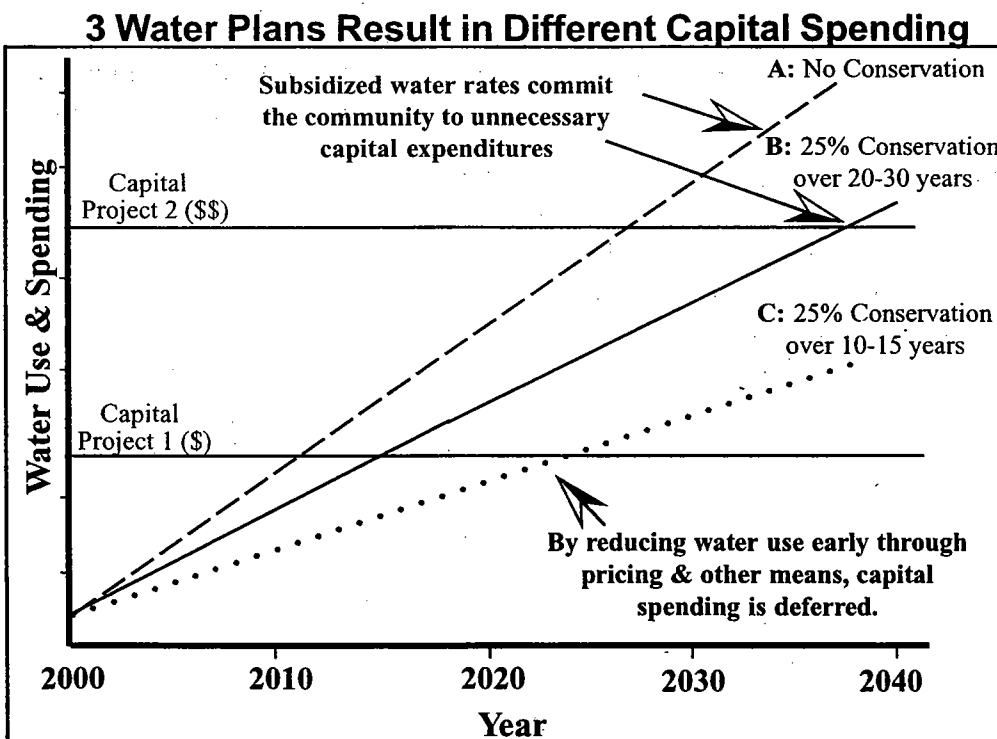
Figure 5. The graph illustrates 3 water plans over time. Removing water subsidies (lower plan C) reduces demand and delays or negates capital spending whereas plans B and C continue subsidies and require greater capital spending.

For example, property tax collectors claim the Salt Lake Valley is running out of water requiring the expenditure of tax funds on Bear River development. Yet this argument presumes water demand is fixed. In other words, supply-side investments are presented without giving equal consideration to demand-side investments. In fact, conservation is rarely viewed as a potential water supply in Utah.

C. Competitive bond ratings can be achieved without property taxes

Scores of waters suppliers inside and outside Utah have received highly competitive bond ratings yet levy no taxes. According to this survey, there is only a 3 percent grade difference for ratings received on bonds issued by suppliers collecting property taxes with those ratings given to water suppliers not collecting property taxes.

Of those districts not collecting property taxes, 72 percent had ratings in the "highest" and "high" grade categories while those using the property tax had, on average, 75 percent of their ratings in these two categories.



The rating process for revenue bonds is based on a variety of performance criteria and high ratings cannot be attained simply by collecting property taxes. There are many other ways to improve bond ratings such as through purchasing bond insurance as practiced by many Utah water conservancy districts.

Furthermore, this argument's importance has been exaggerated. There are a number of city, county, and state agencies issuing bonds without collecting property taxes. Shouldn't all Utah agencies issuing bonds be given taxing authority if it would improve their bond ratings?

D. Capital projects can easily be paid for in water rates, as they frequently are among water suppliers inside & outside Utah

Some urban Utah water suppliers allege property taxes are needed to raise capital. This argument is without merit since this tax revenue is often used for purposes unrelated to capital projects. An examination of urban Utah water conservancy districts demonstrates property taxes are used for administrative costs such as lobbying fees, operation, maintenance, and only occasionally for debt service on capital projects.

Urban water suppliers from inside and outside Utah have been borrowing money to make capital investments for decades without the use of property taxes. The majority of water suppliers surveyed use rate revenue to repay debt issued for capital projects. Although raising capital may be challenging in rural communities, metropolitan areas have little difficulty raising revenue from water sales when rates are priced appropriately.

E. Tax subsidies discourage the use of alternative water sources

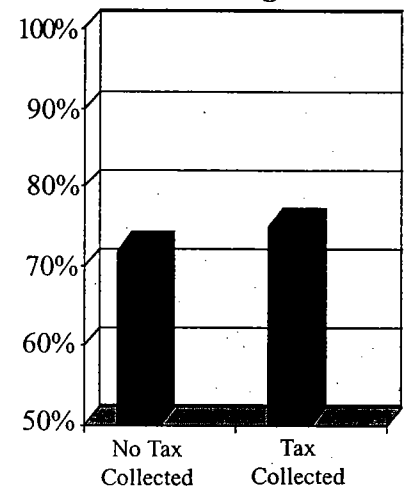
Like other commodities, water is bought and sold on a commercial market. Since Utah's urban water rates are subsidized by property taxes the price of water is lower than its cost of delivery. If property taxes were removed, water rates could approach the cost of delivery and make alternative water sources competitive in their price.

Though there has been some exploration of other water sources, the price of developing them is higher than the subsidized price of water. Surplus agricultural water, water reuse, secondary water, gray water, reclaimed water, and other water sources are frequently used in communities outside Utah. These kinds of water sources have not been implemented in the Salt Lake Valley because the price of these sources is greater than subsidized water rates.

For example, the Utah State Water Plan acknowledges there is 160,000 acre-feet of water in the Salt Lake Valley remaining from Utah's past agricultural era. Although this is enough water for a city of 600,000 people's annual use, most of this water is not being transferred to new uses partly because many owners of this water are attempting to sell this water at prices higher than subsidized water rates.

Scores of waters suppliers inside and outside Utah have received highly competitive bond ratings yet levy no taxes.

Figure 6. Comparison of Bond Ratings Within "High & Highest" Grade Categories



Only a 3 percent grade difference was found for bond ratings received by suppliers collecting property taxes compared with suppliers not collecting property taxes.

If property taxes were removed water rates could approach the cost of delivery. This change could make alternative water sources competitive with water rates.

F. Appointed boards collecting property taxes constitutes taxation without representation and leads to less public oversight

Most water suppliers levying property taxes outside Utah have elected boards of directors while all Utah water conservancy district boards are appointed.

Many believe property tax collections by agencies appointed to office constitutes taxation without representation and leads to less public oversight. Over the years, several observations by various agencies and elected officials have provided support for these claims. A 1989 audit of the Salt Lake County Water Conservancy District conducted by the Legislative Auditor General found:

“Since the district wholesales most water directly to cities, it does not receive the public attention and scrutiny directed at other organizations.”

“The district consistently budgets more than necessary for its operations, leading it to collect more revenue than needed. ... Over budgeting, because it is not a true representation of needs, discourages accountability.”

“Standard budget procedures require that revenues be planned to equal expenditures, not exceed them. The district, however, continues to collect excess revenue. For example, although 14 percent of planned O&M expenditures were not made the last four years, revenue collections were based on the assumption that they would be.”⁵

“District [CUWCD] records indicate they have collected at least \$7.2 million more in property taxes and water sales than necessary. If this trend continues, the district will have unnecessarily collected \$81 million by the year 2011.”

-Legislative Auditor

The total over budgeted by this agency in 1986-1989 equaled over \$4.2 million. But over-collections of property taxes were not only confined to this agency. In 1998, the Utah Legislature considered lowering the property tax levy of water conservancy districts by 25 percent. Representatives from the Central Utah Water Conservancy District (CUWCD) testified that such a lowering of their property tax levy would “jeopardize Utah’s portion of Colorado River water.” After the bill was defeated, the Legislature initiated an audit by the Legislative Auditor General of the CUWCD. The 1999 Legislative Auditor report made several findings related to property tax collections:

“District [CUWCD] records indicate they have collected at least \$7.2 million more in property taxes and water sales than necessary. If this trend continues, the district will have unnecessarily collected \$81 million by the year 2011.”

“District can reduce its tax rate 17.5 percent to .00033 and still meet its obligations, resulting in a gross tax savings of \$81 million by 2011.”⁶

Utah water conservancy districts rely more heavily on property tax revenue to pay administrative costs than water suppliers outside Utah.

The auditors also found violations of the Utah Water Conservancy District Act since several board members were found to be inappropriately receiving \$110,000 from district contracts. These observations support criticism that property tax collections by water suppliers appointed into office leads to less public oversight.

Study Results

Of the 54 water suppliers surveyed outside Utah, all but one has developed its own water supply similar to Utah water conservancy districts.

The results from Utah water conservancy districts are separated from suppliers outside Utah under the heading 'Utah Results.' Only half of Utah water conservancy districts responded so the remaining data was collected from other sources.⁴

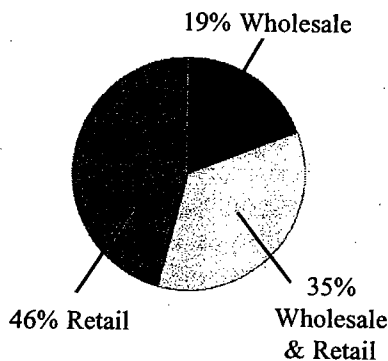
1) Does your agency sell water by wholesale, retail, or both?

- 10 respondents supply water exclusively on a wholesale basis.
- 25 supply water only on a retail basis.
- 19 both wholesale and retail water.

Utah Results: Of the 8 Utah water conservancy districts surveyed:

- 4 Utah suppliers are both wholesalers and retailers of water.
- 4 Utah suppliers only wholesale water.

Figure 7. Type of Water Sales



2) As a water supplier do you have the authority to levy property taxes? If so, is the tax currently levied?

- 31 (57%) have no authority to levy property taxes.
- 11 (21%) have the authority to levy a property tax but are not collecting it.
- 12 (22%) are using their ability to levy a property tax. Six of these wholesale water and 6 are water retailers.

Utah Results: All 8 Utah water conservancy districts surveyed collect property taxes.

3) If property taxes are collected is this revenue placed in an unrestricted general fund (for administrative costs) or is it earmarked for a special purpose such as a state or federal water project?

- Of the 12 suppliers levying property taxes only 3 have the ability to use the revenue for administrative costs.
- The other 9 respondents are restricted to using the revenue for: 1) Purchasing water; 2) Flood control; 3) Bond payments for capital projects.

Utah Results: Of the 8 water conservancy districts surveyed:

- 5 use property tax revenues for administrative purposes.
- 3 use property tax revenue for both administrative purposes and for bond payments on capital projects.

4) If property taxes are levied what percentage of your total revenue did these taxes represent in your most recent fiscal year?

- Of the 12 respondents levying property taxes:
- 8 receive less than 16 percent of their total budget from property taxes.
- 4 receive 28-55 percent of their total budget from property taxes.

Utah Results: Out of the 8 water conservancy districts surveyed:

- 4 receive 17-20 percent of their total budget from property taxes.
- 4 receive 32-67 percent of their total budget from property taxes.

5) If property taxes are levied is your board of directors elected or appointed into office?

- 9 of the 12 water suppliers collecting property taxes have elected boards.
- 3 have boards appointed by member cities or agencies.

Utah Results: All Utah water conservancy districts surveyed have appointed boards of directors.

6) What type of bonds do you have outstanding: revenue bonds, general obligation bonds, or some other finance source?

- 9 suppliers (17%) have no debt;
- 23 suppliers (43%) use only revenue bonds;
- 3 suppliers (6%) use only general obligation bonds;
- 19 suppliers (34%) use both revenue and general obligation bonds and/or receive funds from state revolving loan funds, private general mortgage bonds, or certificates of participation.

Utah Results: Of the 8 Utah water conservancy districts surveyed:

- 5 issued revenue bonds;
- 1 has issued a general obligation bond;
- 1 has issued both revenue and general obligation bonds;
- 1 has no outstanding debt.

7) What bond ratings have you received?

Survey respondents were divided into two categories: 1) Those not collecting property taxes; 2) Those collecting property taxes.

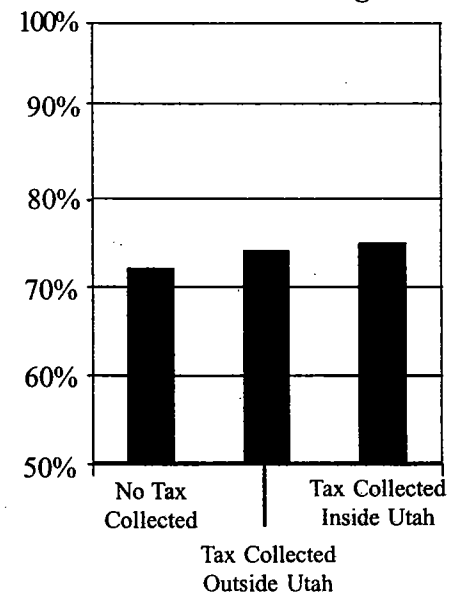
- For the 42 agencies NOT collecting property taxes, 8 suppliers have no bonds issued and 34 suppliers reported a total of 57 ratings.
- Of these 57 ratings: 41 have the highest (insured to that level) and high grade ratings.
- 16 reported an upper medium rating.
- For the 12 agencies collecting property taxes, 19 ratings were reported.
- Of these 19 ratings: 14 reported receiving the highest (insured to that level) and high grade ratings;
- 3 received an upper medium grade rating;
- 1 respondent received a medium grade rating;
- 1 was unrated at the time of survey.

Utah Results: The 8 water conservancy districts surveyed reported 8 ratings.

- Of these: 6 received the highest (insured to that level) and high grade ratings;
- 1 has an upper medium grade rating;
- 1 received an unrated State loan.

Of those districts outside Utah not collecting property taxes, 72 percent had ratings in the categories of “highest” and “high” grade while 74 percent of those collecting property taxes outside Utah had their ratings in these two categories. In Utah, 75 percent received ratings in these two categories.

Figure 8. Comparison of Water Suppliers Receiving “High & Highest” Grade Bond Ratings



Appendix A:

Water Supplier	Collect Property Tax?	Bond Ratings
Nevada		
Las Vegas Valley WD	NO; Authority but No Collection*	AA
Southern Nevada Water Authority	NO	AA, AA-
Truckee Meadows Water Authority	NO	AA
Carson City Water	NO	A1, A+, AAA (insured rating)
Boulder City Water	NO	No Bonds
Henderson City Water	NO	Aa3, AA-
Arizona		
Tucson WD	NO	Aa3, A+
Metro WD	NO ANC	A+, A2, A3, AAA (insured)
Phoenix Water	NO	AA (insured to AAA)
Arizona Water Co.	NO	Private bonds, no rating
Colorado		
Denver Water	NO ANC	AA+, Aa1, AA+
Elco WD	NO ANC	AAA, Aaa (insured)
Left Hand WD	NO ANC	AAA (insured)
Parkville WD	NO ANC	No bonds
Washington		
Woodinville WD	NO	A2 (insured to Aaa)
Highline WD	NO	A+
Seattle Public Utilities	NO	AA, AA2
Tacoma Water	NO	Aa3, AA-
Spokane Water	NO	No bonds
Oregon		
Tualatin Valley WD	NO ANC	Aa-, A1 (insured to Aaa)
Portland Water Bureau	NO ANC	Aa1 (insured to AAA)
Eugene Water & Electric	NO	AA3, AA, AA
Corvallis Public Works	NO	Aa3, A2, A1 (insured to AAA)
Montana		
Mountain Water Co.	NO	No bonds
Helena Public Works	NO	A, AAA (insured)
Billings Public Utilities	NO	No bonds
Idaho		
Pocatello Water Dept.	NO	No bonds
Cour d'Alene Water Dept.	NO	Not rated
Wyoming		
Cheyenne Utilities Board	NO	AA, AA
Central Wyoming Water	NO	AAA (insured)
New Mexico		
Albuquerque Public Utilities	NO	AA, Aa3, AA
Roswell Utilities Dept.	NO	No bonds
Rio Rancho Water Utility	NO ANC	A-
Los Alamos County Water	NO	No bonds
Santa Fe Public Utilities	NO	AAA, Aaa (insured)
Texas		
Brazos River Authority	NO	A, A2
Trinity River Authority	NO ANC	Aaa (insured)
California		
LADWP	NO	AA, AA+, Aa3
Pasadena Water	NO	AA-, A+ (insured to AAA)
Santa Barbara Public Utility	NO	A2
Orange County WD	NO	AA, AA2
Santa Monica Public Utility	NO ANC	No bonds

Most western water suppliers surveyed from both wholesale and retail agencies do not collect property taxes. Only 22 percent of water suppliers surveyed were found to collect property taxes.

Appendix B

Residential Water Rates in Western Cities	
City	Estimated Cost per 1,000 gallons
Reno, NV	\$3.39
Seattle, WA	2.30
Los Angeles, CA	2.22
Park City, UT	2.20
Tucson, AZ	1.81
Boise, ID	1.68
Las Vegas, NV	1.65
Albuquerque, NM	1.41
Salt Lake City, UT	1.04
Provo, UT	0.75
Utah Average	\$1.15
National Average	\$1.96

Water Supplier	Collect Property Tax?	Bond Ratings
*** "Yes" Respondents		
California		
San Juan WD	YES - debt service; some VAB** EB- Elected Board	AAA, AAA (insured)
Irvine Ranch WD	YES - VAB; EB	AA Backed by letter of credit
Alameda County WD	YES; to purchase state water; EB	AA-, A1
Eastern Municipal WD	YES - debt service; some VAB; EB	A1, A+ (insured to AAA)
Metro WD of Southern CA	YES VAB; Appointed by member cities	Aa2, AA
San Diego Water Authority	YES - debt service; Appointed by member cities	AA, Aa3, AA-
Texas		
Kleinwood MUD	YES; VAB and some O&M; EB	Aaa (insured)
Kings Manor MUD	YES; VAB and some O&M; EB	Not rated
Tarrant Regional WD	YES; only for flood control; EB	AAA, Aaa (insured)
New Mexico		
Ruidoso Water Dept.	YES VAB; EB	Baa1 (insured to Aaa)
Oregon		
Sunrise Water Authority	YES VAB and other debt service; EB	AAA (insured)
Colorado		
Northern Colorado WCD	YES - capital projects and O&M Board appointed	AA
Utah		
Jordan Valley WCD	YES - general fund Board appointed	A1, AA-
Central Utah WCD	YES - general fund and bonds Board appointed	Aa3, AA
Metropolitan WD	YES - general fund Board appointed	AA- (insured to AAA)
Bear River WCD	YES - general fund Board appointed	Not rated
Washington County WCD	YES - general fund and bonds Board appointed	Aaa (insured)
Weber Basin WCD	YES - general fund and VAB Board appointed	AA (insured to Aaa)
Kane County WCD	YES - general fund Board appointed	Aaa (insured)
Uintah WCD	YES - general fund Board appointed	No bonds

*ANC - Have authority to tax but are not collecting the tax.

**VAB - Property tax revenues are used on voter-approved bonds for capital projects.

Investment Grade

Moody's

S&P

Highest Grade:

Aaa

AAA

High Grade:

Aa1, Aa2,
Aa3

AA+, AA, AA-

Upper Medium Grade:

A1, A2, A3

A+, A,
A-

Recommendations

- Property tax collections by rural water suppliers should be left in place and studied to consider possible alternate revenue sources.
- Property tax collections by urban water suppliers in metropolitan areas should be phased out over time.
- Property tax collections should be lowered to meet current contract obligations for bond payments — if individual water suppliers have pledged tax revenue before this time — until the bonds are paid off. Once these bonds have expired such tax collections should be phased out.
- Loss of property tax revenue from water suppliers should be made up among large volume, municipal users by employing increasing block rate structures as used in other parts of the West including Park City, Utah.

References:

- ¹ U.S. Geological Survey, 1995 Culinary Water Use Per Capita, *2000 Economic Report to the Governor*.
- ² Out-of-state values adapted from "Western States Water Newsletter," December 31, 1998. In-state values taken from Utah Division of Drinking Water, *1999 Survey of Community Drinking Water Systems*.
- ³ Blattenberger, Gail, *The Price of Water in Salt Lake County*, April 2001.
- ⁴ Property tax collection information was obtained from the State Auditor. Bond rating information for non-respondents was obtained from Moody's Investor Services.
- ⁵ Office of the Legislative Auditor General, State of Utah, *A Performance Audit of the Salt Lake County Water Conservancy District*, August 1989.
- ⁶ Office of the Legislative Auditor General, State of Utah, *A Performance Audit of the Central Utah Water Conservancy District*, July 1999.

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