

What Should Water Rates Be?

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There has been much discussion about water rates in the town of Liberty during the past two weeks. Some customers, particularly those living outside the town, have complained about the price charged for water. This dissatisfaction brings up an interesting question: "What should water rates be?" What price is equitable to all customers and, at the same time, provides financial stability for the water utility.

An economist would say, obviously the easiest way to determine a "fair" price is to have water sold in a competitive market. In that case, most would accept the market price as a "fair" price. After all, potable water is a commodity, i.e., there is no product differential — one vendor's water is just like any other vendor's water. A rational consumer would select the lowest priced water, given that all suppliers meet certain cleanliness and purity standards.

There have been great price reductions in other services that once were government-sanctioned monopolies. For example, long-distance telephone rates have been reduced dramatically by breakup of the telephone monopoly and the introduction of competition. Electric rates will probably be reduced greatly with the soon-to-be introduction of competition in the production of electricity. In both of these cases, the industry was (will be) divided vertically, i.e., the production and supply was separated from the local distribution of the product.

The problem of water rates arises because we do not have competition, but rather, a government-sanctioned monopoly. The monopoly can be a part of local government, a special-purpose district, or a franchised-company. Most localities make the water monopoly a part of local government and set rates by legislation. Others may grant a franchise and, in effect, set rates by legislation of the Public Service Commission.

Given that we have water monopolies, the question becomes, "What price should the monopoly charge?" In setting rates, monopolies usually want to at least appear, if not actually be fair in their rates. In this quest for fairness, most people relate a fair price as to the actual cost of the good or service. So it is with water rates, most people agree that if one customer causes cost to increase, that particular customer should bear the weight of that cost. Therefore, most would agree that water rates should have some relation to costs.

Most water suppliers charge more for the first few thousand gallons (usually 2,000 gallons) because there are certain costs that are the same for each customer. For example, the cost of reading the meter and sending a bill is the same for each customer. One customer may use 3,000 gallons of water and another 30,000 gallons yet the cost of sending the bill is the same in both cases. Hence, most water suppliers charge more for the first two thousand gallons of water. Usually, one person living alone will use about 2,000 gallons per month. Yes, that includes a shower every day!

A quick survey of six upstate water monopolies indicates that the average cost for a residence is \$5.60 for a base rate or the first two thousand gallons per month plus \$1.75 for each additional thousand gallons. Rates for the six water systems ranged from a high of \$9.74 for the first two thousand gallons to a low of \$2.40. For the additional thousand gallons, the high was \$2.00 and the low was \$1.20. In both cases, the city of Greenville had the lowest rate.

Water Rates for Selected Upstate Cities

Monthly Amt .	City of Pickens	City of Clemson	City of Greenville	Water Dist Easley-Central	City of Liberty	City of Anderson	Average
\$/ base of 2000 gallons	3.66	6.50	2.40	4.60	9.76	6.68	5.60
Additional \$/ thous. gal	2.00	1.86	1.20	1.96	1.92	1.58	1.75

The low rates of the city of Greenville could be attributed to many things; however, economies of scale probably have more effect than anything. In a 1985 report for the South Carolina Water Commission, the Strom Thurmond Institute of Clemson University indicated that there was considerable advantage to supplying water in large quantities, particularly in high-density population areas. That study also acknowledged that in the future [1999?], "the issue of water rate schedules likely will be of critical importance."

The higher base rate shown for the Town of Liberty is probably attributable to new system components, which expand system capacity. The general feeling is that base rates should pay for administrative costs and the cost of providing capacity. By increasing capacity, any system will probably increase base rates. Hence, expanding capacity will usually require increases in base rates.

Most cities that have a water monopoly sell water to their citizens and to individuals living near but not within the city. These rates are usually set greater than the insider rates in order to give incentive for annexation. Municipalities in South Carolina need this tool since it is about the only incentive to encourage annexation and viability of the municipalities.

To enjoy low water rates, customers should consider combining of the many small water utilities into fewer, larger utilities.

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