



# Power User's Guide

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## How Systems Should Arrive at New Rates Every Year

As is true for many things, rate setting is a balancing act. When big issues or events are in play, how you go about calculating rates and how you present them must be done accurately and convincingly. On the other hand, if the system is operating at “steady state”<sup>1</sup> your calculation methods and presentation can be basic and laidback. Then there are all those shades of gray.

Before you propose new rates you should assess the financial and rate setting situation of the system:

- Steady state – use SimpleRates©. This will be the case for most systems during most years.
- Shades of gray but with the help of SimpleRates© it's doable – again, use SimpleRates©. This will be the case for most systems for one to three years or so.

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<sup>1</sup> “Steady state” describes the condition of a utility where the operating and ownership costs are relatively stable and only rising slowly, mainly due to inflation, there are no large financial upsets (such as a capital improvement) on the near horizon, user rates are demonstrably adequate and fair right now and ratepayers will not revolt over incremental increases that will keep the system on track financially and operationally.

Getting rates adopted, even in steady state, can be problematic. Learn about these issues in the "Ratepayer's Survival Guide" and "How to Get Great Rates."

**Power thought:** *Systems should raise rates every year there is inflation in the costs to own and operate the system, which is nearly every year. Such inflationary increases will prevent almost all wrenching rate adjustments, the ones that really get people angry. Angry people find it hard to remain reasonable so you want to avoid that.*

Now, let's work through the SimpleRates© tabs.

### **My Account Tab**

SimpleRates© and other information and tools you have downloaded are stored in the on-line toolbox called "My Account." You can login to My Account from the top right corner of our homepage.

At the top of the My Account tab screen be sure to enter the name of the person and the company/organization affiliation you want to get credit for doing this rate calculation (you?). These names will show up in the report that SimpleRates© will generate.

To open SimpleRates© (or another tool in your toolbox) scroll down the My Account tab and click on the item you want.

On the line called, "Entity This Rate Calculation is for," you will enter a name like, the "City of My Town, State" or "Rural Water District #3, My County, State."

You can run the rates for multiple scenarios or multiple systems by running the calculations for one, printing out the report and then starting the next one. But you can't save scenarios so be sure you are done with one before starting the next.

### **Basic Info Tab**

- "Start Date" – this is the first day of the "test year" you will use as your cost data source. Don't just plug dollar amounts from the system's projected budget into SimpleRates©. Definitely don't use the current year or last year's budget unless you want to show decision-makers the rates they should have been charging during those years. The upcoming fiscal year is a good year to choose. If that is still a long ways off, start with the current year's costs and estimate from there.

**Power thought:** *You are setting rates for the future, not the past, so use future costs – more on this later.*

- "Measurement" – the distribution of users is based upon measurement in thousands of gallons, zero to 20, on a monthly use basis. However, if you select cubic feet as the unit of measure, the cubic foot equivalents of these volumes will appear in later tabs and in the report. There are 7.4805 gallons per cubic foot so the cubic foot volumes that will appear will be very uneven looking numbers. Volume in thousands of gallons will be in small, whole numbers; 0, 1, 2, 3, etc. That is, if you select "monthly" as the billing frequency.

*When you enter revenues in the Cost Calculations tab they will skew the resulting user rates unless you set the “% Fixed” value for them properly. Do that this way. Enter all system costs first, no revenues yet. Note the “% Fixed” at the bottom of the “Cost Calculations” table. This is the weighted average of all costs entered so far. Now, enter the revenue and this weighted average “% Fixed” value beside it. Doing this will make these revenues rate structure neutral.*

2. Make sure the “% Fixed” percentages are appropriate for all costs. (Actually, there are costs other than “fixed” and “variable.” If a system has a significant portion of its costs in these other types the system needs a comprehensive rate analysis to get all user rates and special rates and fees set appropriately.)
  - Before tackling number 2 above you need to get some working definitions in mind:
    - “Fixed” and “variable” costs are not so because they either do not change or they do. Costs are fixed or variable in relation to other things.
      - Fixed costs are those that are related to the FACT that someone is a customer. Fixed costs don't stay the same. No cost does that, at least over time. Fixed costs are related to customers – think postage, paper, envelopes or postcards for bills, the computer and software for generating bills, staff time to do billing, the building and its heat, air, etc. in which staff and their equipment reside to do billing and administration, general administration time to manage the overall operation and the like.
      - Variable costs are related to the VOLUME of service each customer receives. (It's actually deeper and more complex than that. Some of these issues are covered in the “Articles Collection.”) Clear examples of variable costs are chemicals for treatment of water, electricity to treat and pump the water, staff time needed to manage the operation of the system and the like.
      - Many costs are a blend of fixed and variable. You will need to decide what those percentages are. The default values in SimpleRates© are a good starting place.
    - Based upon these definitions you will probably end up calling a lower percentage of the system's costs fixed than you would have otherwise. That means the minimum charge will end up being lower and the unit charge higher than you would have intuitively set them.
    - We cannot over-stress the importance of assigning these percentages appropriately and consistently. You will need to strike a good balance between fixed and variable costs that are close to mathematically correct but are also payable by the vast majority of ratepayers. It's bad business to focus too narrowly on getting mathematically correct rates if you create lots of “bad” customers in the process. See “How to Get Great Rates” for more on this.