

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2022-001141

09/11/2023

HONORABLE RANDALL H. WARNER

CLERK OF THE COURT
T. Aird
Deputy

PIMA COUNTY

JEFFREY WILLIS

v.

CITY OF TUCSON, et al.

CHARLES W WIRKEN

MICHAEL G RANKIN
CHRISTOPHER E AVERY
BRETT W JOHNSON
IAN R JOYCE
COLIN PATRICK AHLER
COURTNEY L. HENSON
JUDGE WARNER

UNDER ADVISEMENT RULING

Two summary judgment motions are under advisement following argument: (1) Pima County's June 20, 2023 Motion for Summary Judgment on Count 1 of Complaint, and (2) City of Tucson's June 29, 2023 Motion for Summary Judgment for Lack of Standing. The main issue in this case is whether Tucson's water rates for unincorporated areas are just and reasonable as required by A.R.S. § 9-511.01. As a matter of law, they are not because Tucson set the rates without basing them on any cost study, supply data, or cash flow projections. Summary judgment is therefore granted for Pima County.

1. Facts.

The City of Tucson provides water service to users outside city limits, including Pima County. Although many municipalities do this to some extent, Tucson is unique in that around a third of its customers are outside city limits.

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2022-001141

09/11/2023

In 2021, Tucson decided to charge users in unincorporated Pima County more for water service than those in the City. The City Council adopted Ordinance No. 11846 on June 22, 2021, which raised water rates effective December 1, 2021 for customers in unincorporated areas. The rates specified in Ordinance No. 11846 are different for different classes of users, but are generally 10% higher than rates for similar customers within city limits.

Upon adopting Ordinance No. 11846, the City Council directed staff “to complete a broad cost of service analysis” based on the rates adopted.

Tucson hired Raftelis Financial Consultants, Inc. to conduct the cost-of-service study. Raftelis completed a Phase 1 and then a Phase 2 study. The Phase 2 study begins by recognizing that its purpose was to provide support for already-determined rates:

On June 22, 2021, the City of Tucson (City) Mayor and Council approved a rate differential for Tucson Water customers located within unincorporated Pima County (Outside City Customers). This differential will be in addition to the rates assessed to all other customers (Inside City Customers). This decision was policy based and goes into effect on December 1, 2021. Mayor and Council further directed Tucson Water to conduct a cost-of service analysis using standard industry practices to determine a potential cost basis for differential rates.

The study concludes that a 9% to 26% differential would be justified based mainly on different risks borne by customers within and outside the City, and around a 5% differential would be justified by cost differences between customers within and outside the City.

After receiving the study, the City Council adopted Ordinance No. 11881 on October 19, 2021. The October ordinance implements the same rate increase that was adopted in June. It states that the rates are supported by the Raftelis studies, and advance “critical policy considerations” including:

1. the rate structure supports and rewards annexation and incorporation, providing economic benefit and increased state shared revenues for the City and the region;
2. the rate structure recognizes that the City, as owner of Tucson Water, bears financial risks and liabilities that are not

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2022-001141

09/11/2023

shared by the unincorporated county, including the City's financial backstopping of the utility; and

3. the rate structure promotes environmental sustainability and water conservation, particularly in areas outside the city limits where the City has limited powers to promote those interests.

The Ordinance further notes that the rate structure is common among other Arizona municipal water providers, and results in reasonable differential rates.

Pima County filed this lawsuit in December 2021. In March 2023, while the litigation was pending, the City Council adopted Ordinance 11993 to exempt Pima County and other governmental customers from the differential rates.

2. Standing.

Tucson argues that Pima County lacks standing to challenge the differential rate, which no longer applies to it by virtue of Ordinance 11993. This is a corollary to Pima County's mootness argument, which the Court already rejected based on the Supreme Court's holding in *Pointe Resorts, Inc. v. Culbertson*, 158 Ariz. 137, 141 (1988), that "usually a defendant cannot by its own voluntary conduct 'moot' a case and deprive a court of jurisdiction." When it filed this lawsuit, Pima County had standing to seek declaratory relief on its own behalf, though not on behalf of others. Tucson cannot voluntarily deprive it of that standing in the middle of litigation for the same reason it cannot voluntarily moot this case in the middle of litigation.

Tucson argues that Pima County lacks standing to claim race-based discrimination. According to its Response, Pima County does not make that claim.

3. Violation of A.R.S. § 9-511.01.

Pima County argues that Tucson's water rates for users in unincorporated areas are not "just and reasonable" as required by A.R.S. § 9-511.01. That statute governs municipal water rates and ratemaking. Subsections A through C prescribe the process municipalities must follow to raise water rates. Subsections D and E require that rates and rate increases be "just and reasonable." Subsection E further states: "Every unjust or unreasonable rate or charge demanded or received by a municipality is prohibited and unlawful." A.R.S. § 9-511.01(E).

What does "just and reasonable mean"? At the very least it means rates must be grounded in cost of service. The Court reaches this conclusion for three reasons.

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2022-001141

09/11/2023

First, the term “just and reasonable” comes from public utility law, which requires cost-based ratemaking. For example, Arizona’s Constitution empowers and requires the Corporation Commission to prescribe “just and reasonable rates” for public service corporations. Ariz. Const. Art. XV, §§ 3, 12. When setting just and reasonable rates, the Corporation Commission is instructed to “focus on the principle that ‘total revenue, including income from rates and charges, should be sufficient to meet a utility’s operating costs and to give the utility and its stockholders a reasonable rate of return on the utility’s investment’” *RUCO v. Arizona Corporation Comm’n*, 199 Ariz. 588, 591 (App. 2001), quoting *Scates v. Arizona Corporation Comm’n*, 118 Ariz. 531, 533-34 (App. 1978). That the Legislature used the same standard for municipal ratemaking as for public utility ratemaking suggests an intent that rates would be determined in a similar manner.

Second, A.R.S. § 9-511.01 requires a municipality raising water rates to prepare and publish “a written report or supply data supporting the increased rate” which includes “cash flow projections” showing anticipated revenues and expenses. A.R.S. § 9-511.01(A)(1). The Legislature would not have required that data if it did not intend rates would be tied to it.

Third, persuasive cases from other jurisdictions support an interpretation that “just and reasonable” rates must be tied to cost. *See, e.g., Atlas Valley Golf & Country Club, Inc. v. Village of Goodrich*, 575 N.W.2d 56, 61 (Mich. App. 1997) (municipality could charge higher rate to nonresidents if justified by costs); *Bobrowicz v. City of Chicago*, 522 N.E.2d 663, 668-669 (Ill. App. 1988) (differential rates are reasonable if justified by a difference in cost).

Having concluded that A.R.S. § 9-511.01 requires water rates to be grounded in cost, the next question is whether Tucson’s differential rates satisfy that requirement. They do not. When Tucson set the rates, it did not base them on costs or other financial data.

The fact that Tucson obtained a cost-of-service study after it set the rates does not cure the problem. The record shows the study was done for the purpose of justifying already-set rates, which Tucson then re-approved. And the rates were not based on the Raftelis study. Rather than calculating rates, the Raftelis study found that rates already set for policy reasons fall within a reasonable range. The text and structure of A.R.S. § 9-511.01 make clear that the required written report, data, and cash flow projections are to provide the basis for rates, and the rates here were set before any of the information required by A.R.S. § 9-511.01(A) was generated.

Tucson argues that it is a fact question whether water rates are unjust or unreasonable. It is not clear whether, as a general proposition, a superior court’s decision about the reasonableness of municipal water rates would be deemed legal and reviewed de novo, or factual and reviewed deferentially. But the decision here turns on a legal issue. The challenged rates are unreasonable as a matter of law because, on the undisputed facts, Tucson did not set them based on cost data.

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2022-001141

09/11/2023

For these reasons, Pima County is entitled to summary judgment and it is not necessary to decide other issues raised in the parties' briefs.

4. Orders.

IT IS ORDERED granting Pima County's June 20, 2023 Motion for Summary Judgment on Count 1 of Complaint.

IT IS FURTHER ORDERED denying the City of Tucson's June 29, 2023 Motion for Summary Judgment for Lack of Standing.

IT IS FURTHER ORDERED that Pima County lodge a form of judgment, and that any request for costs or attorneys' fees be filed, within 30 days.