Allocation of Demand Management Costs

Finance and Insurance Committee
Item 6a
November 4, 2019
In 2018, Board approved Demand Management cost allocation study to incorporate into 2020 rate cycle.

Costs are currently collected through Water Stewardship Rate.

Reasons now is appropriate time for Board to decide Demand Management cost recovery method for 2020 rate cycle forward:

- Evidentiary foundation for current method ends in 2020.
  - Allocation of Water Stewardship Rate 100% to transportation through 2020 has been based on 25-year capital planning period from 1996 to 2020.

- Consultants recommend change for 2020 forward.
  - Do not recommend retaining status quo after 2020.
  - Recommend new functionalization or non-functionalized charge.
Why Review Demand Management Cost Allocation Now? (cont.)

SDCWA full exchange agreement payments resume in 2021

- In 2018, Board approved suspending billing/collecting Water Stewardship Rate on exchange deliveries 2018 to 2020 during Demand Management cost allocation study period; total uncollected to date ~ $46 million.
- Absent change, exchange agreement calls for billing/collection of Water Stewardship Rate to resume in 2021.

Litigation

- In 2017, Court of Appeal held administrative record for 2011-2014 did not support Water Stewardship Rate allocation to transportation.
- Administrative records for 2015 forward provide additional support; those rates have been challenged but not yet litigated.
Why Does Metropolitan Invest in Demand Management?

An essential component of reliable water service

A legislatively-directed activity for the provision of water service throughout the region (SB60)

Demand Management investments:

- Increase reliability of water service to the service area population and properties
- Reduce and avoid future capital and other costs
- Decrease the burden on various types of infrastructure
- Free up system capacity
- Reduce the region’s reliance on importing water, freeing up scarce resources
- Increase Metropolitan’s ability to store scarce resources for emergencies
- Ensure Metropolitan’s services meet member agencies’ demands
Demand Management investments provide regional benefits to all existing and potential system users

- By developing and conserving locally, these actions improve reliability even for water systems without a physical connection to Metropolitan
- Reliability measured in many ways: point in time, over time, over hydrologic cycles
- Benefits realized by all member agencies

Member agencies rely on Metropolitan even when not currently using Metropolitan services

- The benefits of managing demand on Metropolitan improves system reliability for member agencies’ potential use
### Metropolitan’s Demand Management Costs, $ in millions

<table>
<thead>
<tr>
<th>Program</th>
<th>FY 2018/19 Budget</th>
<th>FY 2019/20 Budget</th>
</tr>
</thead>
<tbody>
<tr>
<td>Conservation Program</td>
<td>$43.0</td>
<td>$43.0</td>
</tr>
<tr>
<td>Local Resources Program</td>
<td>$44.1</td>
<td>$40.8</td>
</tr>
<tr>
<td>Future Supply Actions</td>
<td>$2.0</td>
<td>$2.0</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$89.1</strong></td>
<td><strong>$85.8</strong></td>
</tr>
</tbody>
</table>

- Metropolitan’s LRP costs are long-term fixed costs
- LRP agreements are 15 to 25 year commitments
Current Demand Management Cost Recovery

Water Stewardship Rate

- 100% Volumetric
- Assigned to transportation, which is applicable to all Metropolitan transactions (sales, wheeling, and exchanges)
- Collected on all transactions (except SDCWA exchange deliveries 2018 to 2020)

Current assignment based on 25-year planning period

- 1996 IRP: "The Preferred Resource Mix of the regional reliability plan forms the basis for determining Metropolitan's facility requirements and capital expenditures from fiscal year 1995-96 through 2019-20...."

Planned Transportation Infrastructure Investments

- ~ $ 3 billion in avoided transportation infrastructure investments
Demand Management Cost Allocation Study

- Demand Management Budget
  - Costs of board-approved budget must be recovered
  - Demand Management budget must recognize the obligation to continue to pay contractual LRP and other incentives

- Updated functionalization is forward looking
  - Provided by Peter Mayer, WaterDM principle
  - May be applied to rate-design alternatives

- Rate design alternatives
  - Provided by Rick Giardina, Raftelis Financial Consultants, Inc.
  - Variable and fixed alternatives
  - Functionalized and non-functionalized alternatives
Proposed process

- **May 2019**: Overview of Demand Management Cost Functionalization
- **July 2019**: Demand Management Cost Functionalization for Metropolitan
- **Fall 2019**: Incorporating Demand Management Cost Functionalization recommendations into the Cost of Service process
- **December 2019**: Budget process
- **February 2020**: Proposed water rates and charges for calendar years 2021 and 2022
Board to approve the most appropriate method to recover Demand Management costs

Upcoming process to establish rates and charges for Calendar Years 2021 and 2022 is the appropriate time, and will establish replacement cost recovery options will be presented by Rick Giardina, Raftelis

Link to all material is available at www.mwdh2o.com, Financial Information Home page