

By the Board of Directors of
The Metropolitan Water District
of Southern California
at its meeting held

MAY 10 1994

8-1

**MWD**

[Signature]
METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA
EXECUTIVE SECRETARY

April 20, 1994

To: Board of Directors (Finance and Insurance Committee--Action)
(Water Problems Committee--Action)
From: General Manager (Executive Committee--Action)
Subject: Interim Agricultural Water Program

The Ad Hoc Committee on Agricultural Water Policy was formed to review and recommend Board policy changes regarding agricultural water deliveries. The Committee decided to address agricultural issues in two phases: a short-term phase to deal with agriculture price issues and a long-term phase to fully consider the reliability aspects. With this in mind, the Committee considered twelve alternative agricultural water pricing policies, short-listed to six alternatives, and recommends a consensus alternative entitled the Interim Agricultural Water Program (Program). The Program represents a short-term solution for agriculture's issues regarding price, and will be evaluated as an ongoing Program as described more fully in this letter. Staff will continue to evaluate potential long-term solutions.

This Board letter describes recent issues, agricultural water policy principles, the Program, financial implications associated with the Program, legal ramifications, environmental considerations, steps required to implement the Program, and a long-term strategy. The modifications to this Board letter from the pending letter you received last month are indicated by strikeouts and underlines.

Recent Issues

Recently, two issues have been raised regarding the rate and term of the Program. The rationale for the \$137/\$113 per acre-foot (AF) discount is not fully developed. Also, the four-year demonstration program is felt by some to be longer than needed to develop the

appropriate "long-term" program. Staff recommends two measures to bridge the issues. First, a consultant study evaluating the benefit of interruptibility to Metropolitan will be conducted and reported to your Board within one year. This will help Metropolitan refine the discount. Second, a two-year complete review by the Board is recommended. Based upon staff analysis, the results of the above-mentioned consultant's report, and the review, the Board will reaffirm, discontinue or otherwise modify the Interim Agricultural Water Program as described in this letter as well as adopt a long-term strategy for providing reliability for agricultural water users in the Metropolitan service area.

Agricultural Policy Principles

The recommended Program is based on three major principles as follows:

- 1) Any agricultural discount should be set in a manner that does not encourage agricultural demands on Metropolitan to increase.
- 2) Metropolitan must be fully committed to interrupting service delivery to agricultural water users that receive agricultural water discounts.
- 3) The agricultural water discount should be passed through in its entirety to the agricultural customer.

Interim Agricultural Water Program Summary

The major terms and conditions of the Interim Agricultural Water Program are summarized in Attachment A. The Program would be a four-year demonstration program with a detailed evaluation after ~~four~~ two years to determine whether the Program should continue. At two years, the Board would determine whether to reaffirm, discontinue or otherwise modify the Program. Participating Member Agencies would provide monthly agricultural water certifications in conformance with the Administrative Code, which would be subject to audit at the end of the ~~third~~ second year

of the Program. Audits would be conducted more frequently if requested by the Member Agency. The maximum annual amount of water delivered under this Program would be limited to ~~116,545~~ 155,034 acre-feet. This is equal to the past four-year average of agricultural deliveries as shown in Table 1. Table 1A shows the past four-year average of agricultural deliveries as presented in last month's pending Board letter.

Should a supply shortage occur, Metropolitan could reduce agricultural deliveries up to 30 percent prior to imposing mandatory reduction targets for firm deliveries. Agriculture would not suffer greater cutbacks until Stage IV of the Incremental Interruption and Conservation Plan (IICP) is reached, when firm deliveries are facing a 15 percent reduction in their target quantity. It should be noted that the IICP will be undergoing extensive review in fiscal year 1994-95 and may be modified.

Should agriculture experience a decrease in deliveries, Metropolitan would use its "best efforts" to procure sufficient supplies of transfer water to meet the demands of agriculture on a take-or-pay basis. The cost to the Member Agency for this additional water would likely be higher than the noninterruptible rate, reflecting the added cost of transfer water. It should be noted that the demand of firm users for the transfer water would be satisfied before making it available to agricultural users.

The agricultural discount would be established as a water rate rather than as a contractual program. If the Program is adopted, the recommended effective date would be May 1, 1994. The agricultural discount would be ~~\$137 per-acre-foot-(AF)~~/AF for treated water and \$113/AF for untreated water, and it is proposed that the discount remain at that level for the duration of the four-year Program, unless revised by subsequent action of your Board. The Member Agency and subagency should pass the entire discount through to the agricultural user.

Agricultural Water Discount

The Program and Seasonal Storage Service (SSS) are two major water management programs that have a similar feature of reducing demand during water shortages. While it is difficult to make a precise determination of benefits

TABLE 1

MAXIMUM AMOUNT OF AGRICULTURAL DISCOUNT WATER
MEMBER AGENCIES MAY PURCHASE

Member Agency	1989-90 Agricultural Water Deliveries (acre-feet)	1990-91 Agricultural Water Deliveries (acre-feet)	1991-92 Agricultural Water Deliveries (acre-feet)	1992-93 Agricultural Water Deliveries (acre-feet)	4-Year Average Agricultural Water Deliveries (acre-feet)
Anaheim	131	109	88	132	115
Calleguas MWD	10,728	9,403	5,077	3,447	7,164
Chino Basin MWD	118	107	152	110	122
Coastal MWD	440	490	0	0	233
Eastern MWD	9,618	9,903	4,194	3,328	6,761
Fullerton	77	75	55	35	60
Las Virgenes MWD	56	66	38	43	51
MWD of Orange County	13,441	8,870	3,426	3,962	7,425
San Diego CWA	118,315	114,918	86,515	82,088	100,459
Three Valleys MWD	115	109	102	97	106
Torrance	0	89	0	0	22
West Basin MWD	473	206	0	0	170
Western MWD	45,461	37,751	22,053	24,124	32,347
Total	198,973	182,096	121,700	117,366	155,034

TABLE 1A

MAXIMUM AMOUNT OF AGRICULTURAL DISCOUNT WATER
MEMBER AGENCIES MAY PURCHASE

Member Agency	1989-90 Agricultural Water Deliveries (acre-feet)	1990-91 Agricultural Water Deliveries (acre-feet)	1991-92 Agricultural Water Deliveries (acre-feet)	1992-93 Agricultural Water Deliveries (acre-feet)	4-Year Average Agricultural Water Deliveries (acre-feet)
Anaheim	132	108	80	132	113
Calleguas MWD	10,728	9,403	5,077	3,447	7,164
Chino Basin MWD	118	26	152	94	98
Coastal MWD	382	411	0	0	198
Eastern MWD	9,618	9,903	3,223	0	5,686
Fullerton	77	75	48	35	59
MWD of Orange County	13,441	8,870	3,426	3,962	7,425
San Diego CWA	118,315	111,811	22,505	0	63,158
Three Valleys MWD	115	109	102	97	106
Torrance	0	89	0	0	22
West Basin MWD	473	206	0	0	170
Western MWD	45,461	37,751	22,053	24,124	32,347
Total	198,860	178,762	56,666	31,891	116,545

and corresponding discounts for each, it is possible to make some general comparisons.

In accordance with the Metropolitan Water District Act, agricultural water may be fully interrupted in a shortage. Shedding agricultural demand makes water available for municipal and industrial (M&I) uses. Similarly, SSS may be suspended in a shortage. Therefore, the Program and long-term SSS provide similar potential benefits and similar discounts would be justifiable.

It is possible to view agricultural water as providing greater benefits than SSS. Metropolitan does not require Member Agencies to produce water from seasonal storage, so they could replace suspended SSS deliveries with firm purchases. Considering this aspect of SSS, the Program provides greater benefits and hence should receive a larger discount than SSS.

In contrast, there is an argument that SSS provides greater benefits than agricultural water. Agricultural water use occurs in the summer when there are no SSS deliveries. During summer months agricultural water use could contribute to peaking and premature facility expansion, while SSS would help reduce peaking and premature facility expansion. Thus, SSS would provide greater benefits than the Program and should receive a greater discount.

Considering these benefit comparisons, the Ad Hoc Committee on Agricultural Water Policy recommended agricultural discounts for treated and untreated water of \$137/AF and \$113/AF, respectively.

An outside consultant will be retained to conduct an assessment of the value of agricultural interruptibility. Further development and quantification of water management benefits will help justify the level of agricultural water discount. This study will be completed and reported to the Board within one year, and will be used in the detailed evaluation of the Program at the end of the second year.

Financial Implications

If the agricultural water discount is set at \$137/AF for treated and \$113/AF for untreated water, it is recommended that any shortfall in revenues due to the discount be funded from the Water Rate Stabilization Fund, rather than increasing base water rates in 1994-95.

If ~~116,545~~ 155,034 acre-feet of agricultural water is sold, approximately ~~\$16~~ \$20.3 million would be drawn from the Water Rate Stabilization Fund (WRSF) to fund the Program. If the shortfall is not funded with the WRSF, base water rates would have to be increased by ~~\$10~~ \$13/AF on July 1, 1994 to make up the shortfall.

Table 2 shows the projected rate increases and/or reserve draws required over the next four years to provide the agricultural discount assuming a constant discount of \$137/AF for treated water and \$113/AF for untreated water. The Program would provide about ~~\$67~~ \$81.2 million in cumulative savings to the agricultural community over four years. Table 2A shows the projected rate increase and/or reserve draws required over the next four years as presented in last month's pending Board letter.

The revenue and rate impacts shown in Table 2 assume that all of the water currently delivered for agricultural use would continue to pay the noninterruptible rate over the four-year period, if the Program is not adopted. As such, the financial impacts reflected in Table 2 represent the extreme case regarding the cost of the Program and its effects on noninterruptible rates. In fact, the actual impact on the WRSF and/or rates will be dependent on the actual deliveries of water to both ~~municipal-and-industrial-(M&I)~~ M&I users and agricultural users.

Legal Considerations

The cutbacks of agricultural deliveries up to 30 percent prior to imposition of mandatory reduction targets for firm deliveries provides is a water management benefit resulting-in that was considered in setting the proposed discount. General Counsel has advised that these features of the Program present two issues. The first issue is whether Metropolitan may legally cut back agricultural water deliveries without providing notice of partial discontinuance of deliveries of surplus water under Section 132 of the MWD Act. The second issue is that an agreed-upon schedule for cutbacks may imply firmer status for the remaining deliveries of agricultural water than is permitted under Section 132.

Both of these issues may be resolved, however, if the cutback schedule is issued by Metropolitan as a partial discontinuance of surplus water deliveries, in compliance with the notice requirements of Section 132 of the MWD Act. Therefore, it is recommended that your Board determine

TABLE 2

**PROJECTED BASE RATES PER ACRE-FOOT
WITH \$137/AF TREATED AND \$113/AF UNTREATED
AG DISCOUNT**

<u>FY ENDING</u>	<u>PROJECTED RATES WITHOUT AG DISCOUNT</u>	<u>INCREASED BASE RATE WITH AG DISCOUNT (1)</u>	<u>DIFFERENCE</u>	<u>REDUCTION IN WATER RATE STABILIZATION FUND REQUIRED TO AVOID RATE INCREASE (2)</u>
1995	\$335	\$348	\$13	\$20.3 M
1996	335	348	13	20.3 M
1997	344	356	12	20.3 M
1998	368	380	12	20.3 M
				<u>\$81.2 M</u>

(1) Discount effective May 1, 1994.

(2) Additional reserves required or cost reductions needed to have base rate projections equal to current projections.

(3) Assumes delivery of 155,034 acre-feet of agricultural water each year.

25-Apr-94

P:\FINSERV\RATEAG-R.WQ1-BP435

40830

and declare that surplus water is needed or required for domestic or municipal uses within the District, under the one year's notice to agricultural water users of a potential service interruption during 1994 which was provided by your Board in its Resolution No. 8394 of March 9, 1993. Such declaration would permit Metropolitan to agree in advance to the specified levels of cutbacks described above as part of the Interim Agricultural Water Program. The Board would further delegate to the General Manager the power to determine the amount of actual cutbacks, based on the requirements of the Program.

It is proposed that the Program be a four-year program. To allow Metropolitan to retain the flexibility to adopt changes to the cutback schedule as the Program evolves, your Board should additionally adopt by a two-thirds vote a Resolution under Section 132 of the MWD Act providing notice of a potential whole or partial discontinuance of surplus water deliveries in 1995. A similar Resolution should be adopted every year thereafter while the Interim Agricultural Water Program is in effect.

Environmental Considerations

This action is not subject to the California Environmental Quality Act because: (i) the provisions with respect to rates are exempted by Public Resources Code Section 21080(b)(8) since it recommends restructuring of rates and other charges which are for the purposes of meeting operating expenses, purchasing or leasing supplies, equipment or materials, meeting financial needs and requirements, and obtaining funds for capital projects necessary to maintain service within existing service areas; (ii) the provisions with respect to reduced deliveries of agricultural water cannot have an effect on the environment without future additional action by Metropolitan's General Manager, which action may not be subject to the California Environmental Quality Act if a water shortage emergency exists at the time such action is taken; and (iii) the remaining provisions can have no effect on the environment.

Next-Steps Steps for Implementation

To establish an agricultural water rate, ~~it is recommended that~~ the Water Problems Committee ~~set~~ will ~~hold~~ a public hearing ~~to be held at its May meeting on~~ will be held on the proposed agricultural water rate and on the proposed notice of discontinuance (whole or in part) of surplus

TABLE 2A

**PROJECTED BASE RATES PER ACRE-FOOT
WITH \$137/AF TREATED AND \$113/AF UNTREATED
AG DISCOUNT**

<u>FY ENDING</u>	<u>PROJECTED RATES WITHOUT AG DISCOUNT</u>	<u>INCREASED BASE RATE WITH AG DISCOUNT (1)</u>	<u>DIFFERENCE</u>	<u>REDUCTION IN WATER RATE STABILIZATION FUND REQUIRED TO AVOID RATE INCREASE (2)</u>
1995	\$335	\$345	\$10	\$16 M
1996	335	344	9	17 M
1997	344	353	9	17 M
1998	368	376	8	17 M
				<u>\$67 M</u>

(1) Discount effective May 1, 1994.

(2) Additional reserves required or cost reductions needed to have base rate projections equal to current projections.

(3) Assumes delivery of 116,545 acre-feet of agricultural water each year.

31-Mar-94

P:\FINSERV\RATEAG\$R.WQ1-BP435

water deliveries in 1995. The new rates ~~could~~ would be ~~approved~~ considered at the May Committee and Board meetings and, if approved, become effective May 1, 1994. The notice of discontinuance would be effective one year after adoption of a resolution giving such notice.

Long-Term Strategy

Staff will continue to evaluate potential long-term strategies for agricultural water policy. These strategies would include resolving reliability issues by possible modifications to the Metropolitan's Administrative Code and/or Act and evaluating alternative water sources for supplying agricultural water users. At the end of the second year of the Program, it is recommended that your Board adopt a strategy for addressing reliability issues. At that time, the Program would be evaluated and the Board could reaffirm or otherwise modify the Program to reflect the long-term strategy.

Board Committee Assignments

FINANCE AND INSURANCE, WATER PROBLEMS, AND EXECUTIVE COMMITTEES

This letter is referred for action to:

The Finance and Insurance Committee because of its authority to determine revenues to be obtained through sales of water, water standby, or availability of service charges, and the levying of taxes, pursuant to Administrative Code Section 2441(e);

The Water Problems Committee because of its authority to study, revise, and make recommendations with regard to the selling prices of water and conditions governing sales and exchanges of water, and the policies regarding the sale and delivery of water for various uses; and

The Executive Committee because of its authority to study, advise, and make recommendations on policies and procedures to be considered by the Board, pursuant to Administrative Code Sections 2417(e).

Recommendation**Water Problems Committee, Finance and Insurance Committee,
and Executive Committee for Action**

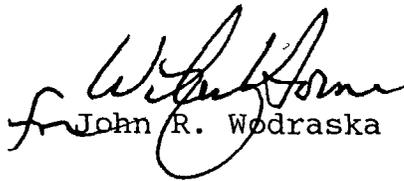
It is recommended that the following actions be approved by your Board:

- ~~That the Water Problems Committee at its regular meeting to be convened on April 10, 1994, set a public hearing on the Interim Agricultural Water Program and the agricultural water rate proposed as part of the Program, and on the proposed notice of whole or partial discontinuance of surplus water deliveries in 1995 pursuant to Section 132 of the MWD Act. The hearing would take place prior to the regular meeting of the Water Problems Committee on May 9, 1994.~~
- That your Board adopt the principles for the Interim Agricultural Water Program set forth in this Board letter.
- That your Board declare and determine that a partial discontinuance of surplus water shall be implemented under Section 132 of the MWD Act and pursuant to the notice of a potential interruption in 1994 which was provided by your Board on March 9, 1993.
- That your Board delegate to the General Manager the authority to implement partial discontinuance of surplus water deliveries, at the levels shown in Item 7 of Attachment A.
- That, subject to a public hearing on the water rates, your Board set the discounts for agricultural water deliveries at \$137/AF and \$113/AF for treated and untreated water, respectively, for the term of the Program.
- That the additional features of the Program be as set forth in Attachment A.
- That your Board find that such rates are exempt from the California Environmental Quality Act by Public Resources Code Section 21080(b)(8) since it recommends restructuring of rates and other charges which are for the purposes of meeting operating expenses, purchasing or leasing supplies,

April 20, 1994

equipment or materials, meeting financial needs and requirements, and obtaining funds for capital projects necessary to maintain service within existing service areas.

- That your Board, following a public hearing, additionally adopt by a two-thirds vote the Resolution under Section 132 of the MWD Act providing notice of a potential whole or partial discontinuance of surplus water deliveries in 1995 pursuant to the Program.
- That your Board authorize the General Counsel to amend the Administrative Code consistent with the Program description in this letter.
- That your Board direct staff to retain a consultant to assess the value of agricultural interruptibility to Metropolitan. The results shall be reported to the Board at the end of the first year of the Program.
- That your Board direct staff to develop a long-term strategy to resolve reliability issues for agricultural water in Metropolitan's service area. At the end of the second year of the Program, a long-term strategy will be proposed for adoption and the Program will be reviewed by the Board in light of the recommended strategy.


John R. Wodraska

JMB:as

Attachment

ATTACHMENT A

INTERIM AGRICULTURAL WATER PROGRAM

Terms and conditions of an Interim Agricultural Water Program would include the following:

- 1) The Interim Agricultural Water Program would be a demonstration program with a sunset/renewal in 4 years. At the end of the second year, the Program will be evaluated in light of the consultant's assessment of the water management benefit of interrupting agriculture, the long-term strategy adopted by the Board, and the audit of certifications.
- 2) The maximum amount of water delivered annually under this Program would be limited to the average agricultural water deliveries for the past four years beginning in fiscal year 1989-90.
- 3) The Member Agency would provide monthly agricultural water certifications in conformance with the Administrative Code and prepare an annual report.
- 4) The Program would be audited at the end of ~~three~~ two years (end of fiscal year ~~1996-97~~ 1995-96), or more frequently if requested by the Member Agency or Metropolitan.
- 5) If the audit reveals certifications greater than actual use, then the Member Agency must pay the amount of discount received for the volume in question, plus interest and late payment penalties.
- 6) The Member Agency must submit a plan to meet the mandatory cuts to agriculture.
- 7) Should a supply shortage occur, Metropolitan could reduce agricultural deliveries up to 30 percent prior to imposing Incremental Interruption and Conservation Plan (IICP) mandatory reduction targets for firm deliveries, as follows:

<u>IICP Stage</u>	<u>Existing-IIEP Target Reduction in Firm Deliveries</u>	<u>IIEP-Target Reduction in Non-Firm Agricultural Deliveries</u>
I	Voluntary	Up to 30%
II	5%	30%
III	10%	30%
IV	15%	40%
V	20%	50%
VI	30%	90%

The required reduction would be measured against the specified target reduction in the Member Agency's ~~Incremental-Interruption-and-Conservation-Plan~~ (IIEP) IICP base-year usage. This current base year of 1989-90 is subject to change, since the IICP will be reviewed in fiscal year 1994-95.

- 8) Member Agencies would be allowed flexibility in meeting Metropolitan's requirements for a reduction by using local resources.
- 9) Metropolitan would commit to use "best efforts" to procure sufficient supplies of transfer water to meet the demands of agriculture on a take-or-pay basis. The acre-foot cost to the Member Agency during such a shortage could be higher than the noninterruptible rate, reflecting the added cost of transfer water.
- 10) The agricultural water discount would be set at \$137/AF and \$113/AF for treated and untreated water, respectively, for the four-year term of the program.
- 11) The Member Agency and subagency should pass the complete agricultural discount through to the agricultural water users.