

- **Board of Directors**  
**Water Planning and Stewardship Committee**

June 10, 2008 Board Meeting

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8-7

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**Subject**

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Consider Options for the Interim Agricultural Water Program

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**Description**

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In May 2008, an information letter was provided to the Board on the status of options identified through the Long Range Finance Plan (LRFP) Update process for Replenishment Service (Replenishment) and the Interim Agricultural Water Program (IAWP). The Board requested that the IAWP be brought back for discussion and action at the June 2008 Board Meeting.

***Background***

Water delivered under the IAWP is provided at a discount. This program has a lower level of reliability than water provided at full service rates (often described as Tier 1 and Tier 2 water). Deliveries for the IAWP may be curtailed before interrupting or otherwise affecting full service deliveries. IAWP water may be reduced up to 30 percent, prior to reductions to municipal and industrial deliveries, upon a one-year notice.

Metropolitan's authority to provide water for agricultural uses is governed by the Metropolitan Water District Act, Section 132, Sale of Surplus Water:

(a) A district may provide, sell and deliver surplus water not needed or required for domestic or municipal uses within the district for beneficial purposes, but shall give preference to uses within the district. The supplying of surplus water shall be subject to the paramount right of the district to discontinue that supply in whole or in part, and to take and hold, or to provide, sell and deliver, that water for domestic or municipal uses within the district, upon one year's written notice to the purchaser or user of that surplus water. The notice shall be given by the board whenever the board determines and declares, by resolution adopted by a two-thirds vote, that the water is needed or required for domestic or municipal uses within the district.

(b) For the purposes of this act, any water purchased at the uniform rate or rates established by the district for domestic or municipal uses and used for beneficial purposes with that district shall be deemed to be water for domestic or municipal uses and not surplus water.

The IAWP regulations are included in Division IV, Chapter 9 of the Metropolitan Administrative Code. Additional information on the IAWP is provided in [Attachment 1](#), Background on the Interim Agricultural Water Program.

***IAWP Discussion***

The LRFP Update workgroup, consisting of member agencies, subagencies and Metropolitan staff, discussed the IAWP at several meetings. IAWP participants believe that providing a discount for IAWP water (1) creates additional sales of surplus water that result in lower overall rates to firm water users, (2) provides a regional water management benefit as IAWP users agree to reduce use up to 30 percent prior to any reductions by firm water users, and (3) sustains an important segment of the Southern California economy.

Some agencies that do not receive IAWP water expressed concerns about Metropolitan securing water transfers while simultaneously selling water for agricultural use at a discount. Some agencies the decision to provide a discount to agricultural water users to promote local benefits of economic and environmental betterment should be made at the member agency level and not by Metropolitan.

Other agencies stated the program and its pricing should have a sound economic basis grounded in water management principles, and should therefore be reviewed in the IRP Update process.

### ***IAWP Recommendation***

The LRFP Update workgroup discussed a number of options for the future of the IAWP. These options are detailed in **Attachment 2**, and include:

1. Status Quo
2. Review the Water Management Benefits in the Integrated Water Resources Plan Update to Determine Required Changes
3. Elimination
4. Phase Out
5. Flexible Pricing
6. Contracts

The LRFP Update workgroup met on April 17, 2008 and recommended that a six-month process involving Metropolitan staff, member agencies, agricultural water retailers, and grower representatives evaluating these options and others would be an appropriate way to proceed. Staff would continue to update the committee and board on progress, with a recommendation for continuation or changes to the IAWP to be presented for consideration at the December 2008 board and committee meetings. On May 12, 2008, the Water Planning and Stewardship Committee agreed to consider action of this matter at their June 2008 meeting.

### **Policy**

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Metropolitan Water District Administrative Code Section 4106: Interim Agricultural Water Program Purposes

Metropolitan Water District Administrative Code Section 4401: Rates

Metropolitan Water District Administrative Code Section 4507: Billing and Payment for Water Deliveries

Metropolitan Water District Administrative Code Division IV, Chapter 9: Interim Agricultural Water Program Service Regulations

Metropolitan Water District Act Section 132: Sale of Surplus Water

### **California Environmental Quality Act (CEQA)**

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CEQA determination for Options #1 and #2:

The proposed action is not defined as a project under CEQA because it involves continuing administrative activities, such as general policy and procedure making (Section 15378(b)(2) of the State CEQA Guidelines). In addition, where it can be seen with certainty that there is no possibility that the proposed action in question may have a significant effect on the environment, the proposed action is not subject to CEQA (Section 15061(b)(3) of the State CEQA Guidelines).

The CEQA determination is: Determine that the proposed action is not subject to CEQA pursuant to Sections 15378(b)(2) and 15061(b)(3) of the State CEQA Guidelines.

### **Board Options**

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#### **Option #1**

Adopt the CEQA determination and

- a. Adopt the LRFP Update workgroup recommendation to undertake a six-month process involving Metropolitan staff, member agencies, agricultural water retailers, and grower representatives to evaluate the options discussed in Attachment 2 and others; and
- b. Return to the Board with recommendations for consideration at the December 2008 board and committee meetings.

**Fiscal Impact:** None

**Option #2**

Adopt the CEQA determination and direct staff to return with a proposal to implement an alternative option.

**Fiscal Impact:** Unknown

**Staff Recommendation**

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Option #1



Brian G. Thomas  
Chief Financial Officer

5/27/2008

Date



Jeffrey Kightlinger  
General Manager

5/27/2008

Date

**Attachment 1 – Background on the Interim Agricultural Water Program**

**Attachment 2 – Options for the Interim Agricultural Water Program**

BLA #6193

## **Background on the Interim Agricultural Water Program**

The potential water management benefits of interrupting agricultural water deliveries prior to urban deliveries was recognized in the “Interruptible Program” established by Metropolitan in 1981. On the heels of the 1992 drought, Metropolitan converted the “Interruptible Program” into a more rigorous Interim Agricultural Water Program (IAWP) in May 1994. The IAWP provides for the delivery of surplus water for agricultural purposes at a discounted rate. Under the IAWP, water is delivered at a discounted rate in exchange for up to a 30 percent reduction in demand by participating agricultural water users at Metropolitan’s call during periods of shortage. This reduction enables Metropolitan to better conserve limited supplies during such shortages.

The IAWP was initially set up as a demonstration program with a sunset/renewal period of three years. In exchange for the IAWP water discount, Metropolitan can reduce IAWP water deliveries up to 30 percent prior to implementing any mandatory allocations under its drought management plan. The three-year demonstration period ended June 1997, after which time Metropolitan continued the IAWP for an additional five years. A bundled rate for treated and untreated agricultural water was incorporated into Metropolitan’s rate structure in January 2003. IAWP parameters set forth in Section 4106 and Chapter 9 of Metropolitan’s Administrative Code, and administrative procedures developed under the program’s demonstration period and refined under the five-year extension, now continue.

### *Program Features*

Metropolitan’s Administrative Code generally defines agricultural purposes under the IAWP as water used for growing or raising agricultural, horticultural or floricultural products for the purposes of commerce, trade, or industry, or for use by educational or correctional institutions, on parcels where greater than one acre is used exclusively for the aforementioned purposes. It applies to both the growing of crops and raising of livestock and fowl for human consumption or market. It also applies to the feeding of fowl or livestock for the purpose of obtaining their products for human consumption or market.

The IAWP limits the maximum amount of discounted agricultural water available to a member agency on an annual basis each fiscal year. These limits, based on the agency’s average annual agricultural water use for the four-year period preceding the program’s 1994 implementation, are still in place, and are shown in Table 1, Member Agency FY IAWP Maximum Amounts.

In order to receive the IAWP discount, member agencies must certify to Metropolitan the amount of agricultural water used within their service area on a monthly basis. Such use is actually determined through certifications provided by the retail agency supplying agricultural water to the end user. Metropolitan, in turn, issues a discount for the amount of water certified to the member agency. Member agencies are required to pass the discount on to the retail agency, which then transfers the discount to the end user.

**Table 1. Member Agency FY IAWP Maximum Amounts**

<b>Agency</b>	<b>Maximum Annual IAWP (AF)</b>
Anaheim	115
Calleguas MWD	7,164
Inland Empire Utilities Agency	122
Eastern MWD	6,761
Fullerton	60
Las Virgenes MWD	207
MWDOC	7,657
SDCWA	100,459
Three Valleys MWD	106
Torrance	22
West Basin MWD	170
Western MWD	32,347
<b>Total</b>	<b>155,190</b>

Metropolitan reviews IAWP performance on an annual basis. This review includes verifying water usage on a retail agency basis to ensure that IAWP certifications submitted during the year preceding the review are accurate, verifying that the IAWP discount is being transferred to end-users, and spot-checking agricultural parcels to ensure participation according to Metropolitan's agricultural purposes definition. Based on this review, Metropolitan may adjust IAWP credits issued to an agency during the previous year.

The Metropolitan Water District Act allows Metropolitan to deliver or sell surplus water for any beneficial use that is not needed for domestic or municipal uses. Metropolitan has the right to discontinue surplus water service, in whole or in part, upon one year's written notice to the purchasers or users of the water. Following such notification, Metropolitan's General Manager has the discretion to reduce IAWP deliveries up to 30 percent prior to imposing any mandatory urban water allocation under the Water Surplus and Drought Management (WSDM) Plan during the year for which notification is given. Metropolitan's Administrative Code requires the General Manager to give written notice of Metropolitan's intent to reduce or interrupt IAWP delivery as soon as practicable after such determination is made.

As part of the demonstration program, member agencies were required to submit a plan indicating how a 30 percent reduction would be met in their service areas. Metropolitan was to have received these plans by November 1994. In June 2007, Metropolitan requested that these member agency reduction plans be revised or updated to reflect conditions and current IAWP participation. These member agency reduction plans were used to formulate methodologies and procedures for initiating, implementing and validating IAWP reductions.

### Options for the Interim Agricultural Water Program

The following options for the future of the Interim Agricultural Water Program (IAWP) were identified by the Long Range Finance Plan workgroup and Metropolitan staff, although no consensus has been reached by the Long Range Finance Plan workgroup on the best option.

#### *Status Quo*

The Status Quo option has been suggested by some IAWP participants. They would request that the Board retain the IAWP at its current discount levels with current interruptibility, as recommended by the Board in its October 2001 rates action. IAWP participants will have the opportunity to show the value of their ability to interrupt in calendar year 2008, as Metropolitan implemented a 30 percent reduction in IAWP water use effective January 1, 2008. Many IAWP participants have taken actions that are irrevocable in the near-term<sup>1</sup> in order to meet their commitments to reduce usage. For purposes of illustration, the following schedule of reductions in firm and IAWP deliveries was adopted by Metropolitan’s Board as part of the Shortage Allocation Plan.

<b>Regional Shortage Level</b>	<b>Regional Shortage Percentage</b>	<b>IAWP Reduction Percentage</b>
	Voluntary	Up to 30%
1	5%	30%
2	10%	30%
3	15%	40%
4	20%	50%
5	25%	75%
6	30%	90%
7	35%	100%
8	40%	100%
9	45%	100%
10	50%	100%

Retaining the IAWP as currently implemented has the added feature of not disrupting Metropolitan’s rate structure, which has been crafted by the member agencies, Metropolitan and the Board to balance payment for services with the type of services received. For example, IAWP deliveries are not included in deliveries for purposes of calculating the Readiness-to-Serve (RTS) shares because of the IAWP’s lower service level and interruptible nature. Likewise, IAWP deliveries were not included in developing each member agency’s base firm demand for setting the cap on the amount of Tier 1 water each agency may purchase because IAWP deliveries are not considered firm water.

#### *Review the Water Management Benefits in the Integrated Water Resources Plan Update to Determine Required Changes*

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<sup>1</sup> These actions are primarily the “stumping” of trees, which inhibits growth and fruit production.

Proposed by some IAWP proponents, this option would retain the Status Quo as described above while providing an opportunity to review and examine the water management benefits of the IAWP through the IRP Update process. Metropolitan's supply conditions have changed significantly since the IAWP was established in 1994, and the program should be reviewed in light of changing water supply conditions. The IRP Update could be used as the forum to determine what type of water management programs and objectives are most appropriate for Metropolitan and how agricultural water use could fit into those programs.

The IRP Update would evaluate whether the IAWP provides a water management benefit, and if so, define what it is. For some LRFP workgroup participants, it is unclear to which of Metropolitan's resource targets of conservation, local resources, storage and transfers the IAWP belongs.

### *Elimination*

The option to eliminate the IAWP discount was suggested by several member agencies. Metropolitan was established to provide municipal and industrial water to urban areas of Southern California. Agricultural water sales are provided under Metropolitan's authority to sell surplus water. Given Metropolitan's water supply situation on the State Water Project, water is projected to be available for storage or other purposes on average in only three out of ten years. A significant portion of agricultural water sales are made to high value crop growers who value reliability and may be willing to pay full service prices in exchange for higher reliability. These IAWP participants are able to switch to full service rates and under the Act, their water usage would be considered a municipal and domestic water use.

Under this option, the Board would take action to eliminate the discount and requirement to reduce prior to M&I reductions at some future effective date. Upon that date, no further sales of agricultural water at a discount to full service rates would occur. The IAWP participants' obligation to curtail water use prior to M&I reductions would simultaneously end<sup>2</sup>. However, their obligation to curtail use would still exist under a Shortage Allocation Plan. Member agencies and program participants would either have to find alternative water sources, pay Metropolitan's full service rates, or provide agricultural water users discounted water, with the discount funded locally.

If the IAWP were eliminated, member agency RTS shares would shift over time, if some portion of the existing IAWP sales converted to full service. As the RTS shares are based on a ten-fiscal-year rolling average of firm sales, the change to member agencies currently participating in the IAWP would gradually phase in and could be planned. With regard to the Tier 1 caps established as part of the 2001 rate proposal, at least two options are available. One option is to recalculate the Tier 1 caps of member agencies who have participated in the IAWP such that the shift of agricultural water to full service would not trigger Tier 2 sales. Other LRFP Update workgroup participants noted that the Tier 1 limits should not be changed as it was anticipated that sales under the IAWP program would be reduced over time anyway.

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<sup>2</sup> This is a distinction from the current program as IAWP participants cannot opt in to the program when Metropolitan has adequate supplies and opt out of the program when curtailments of deliveries occur. As Metropolitan has implemented a 30% reduction in Calendar Year 2008, IAWP participants cannot currently convert to full service.

### *Phase Out*

The option to phase out the IAWP over some period of time was suggested by some member agencies. While acknowledging the arguments favoring outright elimination of the program, they also recognize that eliminating the program too quickly may not provide adequate time for IAWP participants to transition both financially and physically from the IAWP program. The LRF Update workgroup did not reach consensus on the appropriate time frame for phasing out the IAWP program, but suggestions of 3, 5 and 10 years were made.

Phasing out the IAWP would result in the program and its associated discount and curtailment commitments diminishing over time. For example, if the phase out period was three years, then the following discount and reduction schedule could be implemented.

<b>Year</b>	<b>Discount from Untreated Full Service Tier 1 Rate</b>	<b>Discount from Treated Full Service Tier 1 Rate</b>	<b>IAWP Reduction Percentage at Regional Shortage Level 1</b>
0	\$90 per AF	\$114 per AF	30%
1	\$67 per AF	\$86 per AF	22%
2	\$45 per AF	\$57 per AF	15%
3	\$22 per AF	\$28 per AF	7%
4	\$0 per AF	\$0 per AF	0%

The issues associated with the RTS and Tier 1 caps that were identified in the Elimination option would also be applicable to the Phase Out option. During the phase out period, certification of agricultural sales would need to continue in order for the member agency to receive the discount.

### *The Flexible Pricing Option*

The IAWP focuses on selling surplus water not needed for municipal and domestic uses to agricultural users at a discount in exchange for the ability to interrupt deliveries to IAWP participants up to 30 percent prior to imposing mandatory reductions to firm deliveries. This program as currently constructed may not be feasible, given Metropolitan's water supply situation on the SWP.

In years when surplus water is available, water could be sold to agricultural users at a discount, as these sales would result in revenues over incremental costs and would contribute to the fixed costs of the system. In shortage years, deliveries would be cut following the reduction schedule currently in place and remaining deliveries billed at the Tier 1 full service rate. Shortage years would be defined as years when the IAWP program deliveries are curtailed. In order to accurately assess the benefits of this option, it could be included in the IRP Update process.

In this manner, agricultural users would have access to Metropolitan water with the same reliability they have now, and other firm water users would not feel that they were subsidizing discounted water deliveries in shortage years.

Restructuring the IAWP in this manner would require member agencies to use the certification process to identify qualifying sales transactions. Because the sales would not be firm, they would not be included in calculating a member agency's RTS Charge shares. As the sales are not fully interruptible, they would continue to be included for purposes of calculating the Capacity Charge.

#### *Contracts*

A September 1996 Board letter extending the program allowed 5 years to establish contracts or other arrangements to provide incentives reflecting the benefits of agricultural water deliveries. This option was presented by Metropolitan staff but not supported by the LRFP Update workgroup.

Contracts could be performance based. As an example, Metropolitan could develop contracts with certain landowners or lessees modeled after the Land Agreements that are part of the Land Management Agreement with the Palo Verde Irrigation District. During periods of adequate supply, Metropolitan would charge something less than the full service rate. During shortages, Metropolitan would call on those participating landowners or lessees to reduce water usage. In exchange for not irrigating contract lands for an agreed time period, Metropolitan could provide structured payments based on the amount of land and water used to irrigate that land.

According to member agencies and industry representatives, most IAWP water is used on trees and vines, not row crops. High value row crops, such as strawberries, have already converted to full service water; lower value row crops are either not grown in Metropolitan's service area or use local supplies. As such, programs similar to the land following program would not be practical in Metropolitan's service area.