



● **Board of Directors**  
***Finance and Insurance Committee***

4/11/2017 Board Meeting

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**8-1**

**Subject**

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Adopt CEQA determination and adopt resolution approving Treatment Charge Workgroup's proposed policy principles, recommended treatment capacity charge, and treatment capacity charge implementation

**Executive Summary**

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In February 2017, a report was presented to the Finance and Insurance (F&I) Committee providing an overview of the work of the Treatment Charge Workgroup (Workgroup). The Workgroup met from September 2016 through February 2017. The culmination of this effort is the "Proposed Policy Principles, Recommendations, and Implementation Considerations" (Proposal) for a treatment fixed charge beginning no sooner than January 1, 2021, with the remaining treatment revenue requirement to continue to be recovered through a uniform, volumetric rate. The Proposal, included as [Attachment 1](#), was presented to and discussed by the F&I Committee at its February 2017 and March 2017 regular meetings. Pursuant to the Committee's consensus that the Proposal be presented as an action item at the April meetings of the F&I Committee and the Board, this letter recommends approval of the Proposal. Specifically, it recommends adoption of the Resolution approving the Treatment Charge Workgroup's proposed policy principles, recommendations for a treatment capacity charge, and implementation of a treatment capacity charge, provided as [Attachment 2](#).

**Details**

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On April 12, 2016, Metropolitan's Board of Directors adopted the biennial budget for fiscal years (FY) 2016/17 and 2017/18, water rates for calendar years (CY) 2017 and 2018, and charges for CY 2017. Pursuant to requests for staff to review and present alternatives to the 100% volumetric treatment surcharge, which recovers all revenue requirements allocable to Metropolitan's treatment function, staff, with consultation provided by Raftelis Financial Consultants, Inc., proposed the Board adopt a two-part Treated Water Fixed Charge based upon the cost of service report which was included in Board Letter 8-1 dated April 12, 2016. The first component of the proposed charge would have recovered the Fixed Standby costs of the treatment function and would have been apportioned to member agencies based on the average treated water sales by member agency for the most recent ten fiscal years (ten-year rolling average). The second component would have recovered the Fixed Demand costs and would have been apportioned to member agencies based on each agency's peak treated water demand for the last three summer seasons, defined as the highest daily treated water demand for May through September.

The Board voted instead to continue the 100% volumetric Treatment Surcharge and to: (1) define objectives of a new treated water charge, (2) further analyze alternatives to bring back to the Board for further discussion in fall 2016, and (3) bring a possible recommendation to the Board for a new treated water charge effective January 1, 2018. Staff proposed the following process to the Executive Committee to achieve those objectives:

- Staff would chair a Workgroup of member agencies to work on the issues;
- The Workgroup would use the monthly Member Agency Managers meeting to receive input and information;
- The Workgroup would provide analyses for the Board and develop options and approaches; and
- The F&I Committee would receive regular updates, review proposals and provide direction to the Workgroup.

On June 28, 2016, the Executive Committee formed the Workgroup, which was open to representatives of all of Metropolitan's member agencies, and directed the Workgroup participants to address the following policy issues:

- Define objectives of a fixed treated water charge;
- Determine costs to be included in a fixed charge;
- Determine allocation methodology;
- Address issues related to the implementation of a new charge; and
- Consider implementation in January 2018 or as part of the next biennial budget.

The Executive Committee also established a timeline pursuant to which the Workgroup would be formed in July/August 2016, the F&I Committee would receive a recommendation from the Workgroup in March 2017, and the F&I Committee would make a recommendation to the Board in July 2017 for potential implementation in CY 2018 or CY 2019.

Metropolitan retained Dr. Tom Chesnutt of A&N Technical Services, Inc. to facilitate the process for the participating member agencies. Sixteen member agencies participated in the process (List of Workgroup Participants, Attachment 5). On August 15, 2016, staff provided an update to the F&I Committee regarding the formation of the Workgroup, the Executive Committee's directions to the Workgroup on policy, and the intended process for the Workgroup.

The Workgroup met six times from September 2016 to February 2017. During the process, staff presented information to the Workgroup and Member Agency Managers, including information regarding water treatment plant flows, financial statement and rate impacts of write-down of treatment plants, review of the Metropolitan budget, review of the functionalization and allocation of Metropolitan's treatment costs, and a long-term Treatment Surcharge forecast. The Member Agency Managers were also provided with updates from September 2016 to November 2016 (there was no Member Agency Managers meeting in December 2016) and January 2017.

In February 2017, the Workgroup voted to present the "Proposed Policy Principles, Recommendations, and Implementation Considerations" included as [Attachment 1](#). Updates were provided to the F&I Committee from September 2016 to February 2017, with discussions of the Workgroup's Proposal at the February 2017 and March 2017 F&I Committee meetings.

### **Workgroup Proposal**

The Proposal consists of:

- Policy Principles for Treatment Rates and Charges;
- Recommendations for Treatment Rates and Charges; and
- An implementation consideration for Treated Water Charges.

#### Policy Principles for Treatment Rates and Charges

The Workgroup proposes that the Board adopt the following Policy Principles quoted in full below, which would provide a guidance framework for changes Metropolitan may wish to make to any treatment rate or charge now or in the future:

1. Treatment rates and charges shall align treatment costs with treatment services and benefits received consistent with cost of service principles.
2. Treatment services shall be recognized to include physical water treatment, as well as operational benefits such as available treatment capacity used by member agencies.
3. In an effort to contain overall treatment costs on an on-going basis, MWD shall programmatically identify opportunities to partially or fully decommission unneeded treatment infrastructure and minimize future O&M and capital expenditures. MWD should obtain member agency commitment to utilize new or expanded future treatment capacity.

#### Recommendations for Treatment Rates and Charges

The Workgroup further recommends the adoption of a Treatment Capacity Charge that mirrors the existing Metropolitan Capacity Charge. The Treatment Capacity Charge would recover the capital financing costs

functionalized to the Treatment function that are allocated to the Fixed Demand category. Fixed Demand costs are those capital costs incurred to meet maximum summer treatment capacity. These Treatment Fixed Demand costs would be recovered from member agencies based on their three-year trailing maximum summer peak day demand through treated water connections. The summer demand period is defined as May 1 through September 30. All other Treatment function costs would continue to be recovered through a uniform, volumetric rate per acre-foot of treated water sales. The Workgroup's recommended Treatment Capacity Charge reflects the second component of the two-part Treated Water Fixed Charge proposed by staff to the Board on April 12, 2016, which also proposed to recover Fixed Demand costs based on three-year trailing maximum summer peak day demand.

#### An implementation consideration for Treated Water Charges

To provide member agencies with sufficient time to plan for operational and financial impacts, the Workgroup proposes to incorporate the Treatment Capacity Charge into Metropolitan's biennial cost of service process and implement it no sooner than January 1, 2021. If implemented for CY 2021, the Treatment Capacity Charge for each agency would be determined based on the three-year trailing maximum summer peak day demand through treated water connections for CYs 2017 through 2019.

A resolution approving the Treatment Charge Workgroup's Policies, Recommendations, and Implementation, which includes the Treatment Capacity Charge, is provided as **Attachment 2**. If the resolution approving all of the Workgroup's recommendations is approved, staff will include a Treatment Capacity Charge in the proposed rates and charges effective January 1, 2021 and January 1, 2022, developed in the manner described above. A resolution approving only the Workgroup's proposed Policy Principles is provided as **Attachment 4**. If the resolution approving only the Workgroup's Policy Principles is approved, the principles would provide a guidance framework for changes Metropolitan may consider regarding treatment rates or charges in the future.

#### **Requests from the March 13, 2017 F&I Committee Meeting**

Members of the F&I Committee, at its March 13, 2017 meeting, requested that staff provide additional information regarding two topics.

##### 1. Resiliency

One of the attributes of effective treated water cost recovery identified by the Workgroup was the structuring of Metropolitan's treatment revenues with low variability and appropriate levels of resiliency. The request was made for information about the need for financial resiliency through a treatment fixed charge, if financial resiliency is going to be part of the principles recommended by the Workgroup

The Workgroup provided background statements in their written communication to the F&I Committee, concluding "structuring MWD's treatment revenues with low variability and appropriate levels of resiliency" is one of "several important attributes of effective treated water cost recovery." (Page 1 of **Attachment 1**.) Thus, the Workgroup is not proposing that the Board adopt financial resiliency as a policy principle, but the Workgroup does conclude that financial resiliency is an important attribute of the recovery of Metropolitan's treatment costs.

Financial resiliency has been in the forefront of recent water utility research. Financial resiliency is defined as "the ability to thrive in the presence of fiscal stresses that threaten to temporarily or systematically move an organization or industry off-balance or out of fiscal equilibrium."<sup>1</sup> Key to financial resiliency is the robustness of the utility business model in generating stable and adequate revenue streams. Fixed charges, when replacing revenues generated by volumetric rates, contribute to stable revenue streams and enhance financial resiliency.

The proposed Treatment Capacity Charge would generate a fixed revenue stream to replace a portion of the current treatment revenue requirement that is 100 percent dependent on sales volumes. By definition, the Treatment Capacity Charge would improve the stability of treatment cost recovery, of which 91 percent are fixed

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<sup>1</sup> Water Research Foundation, "Defining a Resilient Business Model for Water Utilities", prepared by: Jeff Hughes, Mary Tiger, Shadi Eskaf, Stacey Isaac Berahzer, Sarah Royster, Christine Boyle, and Dayne Batten, Environmental Finance Center at the University of North Carolina at Chapel Hill, Chapel Hill, NC 27599-3330; and Peiffer Brandt and Catherine Noyes, Raftelis Financial Consultants, Inc., 1031 South Caldwell St., Suite 100, Charlotte, NC 28203; ©2014, page 2.

costs. This would result in less revenue dependent on sales volumes, a more stable revenue stream, and improved financial resilience across a range of hydrologic variability.

## 2. Background Information Regarding Treatment Costs

At the March 13, 2017 F&I Committee meeting, staff presented a summary slide (slide 6 of the PowerPoint presentation) containing the costs, by category, that make up Metropolitan's 2017/18 Treatment Revenue Requirement, which are functionalized as treatment costs pursuant to Metropolitan's cost of service process. A request was made for background information that makes up each of the categories of treatment costs summarized in slide 6. Staff made a detailed presentation to Workgroup participants on October 20, 2016, which contains the background information requested, and is included herein as **Attachment 3**. The presentation referenced cost data shown in the current biennial budget document; it also referenced the relevant schedules in the cost of service study, which was included in Board Letter 8-1 dated April 12, 2016. This information was also provided as part of Attachment 4 in Board Letter 8a to the F&I Committee, dated February 14, 2017.

The budget is the foundation of the cost of service report. There is much detail in the budget document on Metropolitan's website regarding departmental operating and capital financing expenditures. Budgets are developed in detail by line item (labor, chemicals, materials, professional services, travel, etc.) for each team. The budgeted dollars by team roll up to units, units roll to sections, sections roll to groups. The largest portions of the budget for the Water System Operations (WSO) group are the Water Treatment and Conveyance and Distribution section budgets, which together make up 59 percent of WSO's budget. The other six WSO sections (Office of the General Manager, Operations Support Services, Water Quality, Water Operations and Planning, Safety and Environmental Services, Power Operations and Planning) serve a support function within the group. The Water Treatment section of the WSO budget of \$74.5 million includes the budget for the five treatment plants. (Page 63 of the budget, and slide 5 in **Attachment 3**.) The Water Treatment Section budget includes the salaries and benefits, professional services, materials and supplies, outside services, and variable treatment costs for chemicals, power, and solids. Accordingly, a large portion of the Treatment Revenue Requirement is contained in the WSO Budget.

Treatment revenue requirements are made up of the following items: WSO direct departmental O&M costs at the five treatment plants; WSO support O&M costs; Support O&M costs from Other Groups; Capital Financing costs; Revenue Offsets; Administrative & General costs. (Schedules 8 and 9 in the cost of service report, and slide 10 in **Attachment 3**.)

- WSO Direct O&M costs come from the budget and are functionalized to treatment by location and by activity so that they include only costs pertaining to treatment; thus, a portion of the Electrical and Control Teams O&M at the five treatment plants is subtracted because they perform Distribution functions. (Slide 9 in **Attachment 3**.)
- WSO support O&M costs includes a portion of Operations Support, Operations Planning, Water Quality, Safety & Environmental, and Power Operations. These are functionalized to treatment by time keeping and team function.
- Support O&M costs from Other Groups includes Engineering, functionalized to treatment by Net Book Value (NBV) shares; it also includes Information Technology, Human Resources, and Office of the General Manager, and these costs are functionalized prorata by labor costs.
- Capital financing costs includes debt service and Pay-As-You-Go funding of the Capital Investment Plan. Capital costs are functionalized to treatment by NBV shares. Treatment NBV includes all Metropolitan facilities which perform treatment functions. Treatment NBV is around 31% in FY 2017/18. (Schedule 4 in the cost of service report, and slide 11 in **Attachment 3**.)
- Revenue Offsets includes interest income and property tax revenues. These are functionalized prorata by total costs and by NBV shares, respectively.
- Administrative & General includes departmental O&M for Administrative Services, General Counsel, General Auditor, Ethics, and Office of the CFO. These costs are functionalized prorata by total costs.

The supporting treatment cost details can be found in the budget documents pages 36, 62, and 63; the cost of service report, pages 63 to 72; and the Workgroup October 20, 2016 presentation.

## Policy

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Metropolitan Water District Act Section 133: Fixing of Water Rates

Metropolitan Water District Act Section 134: Adequacy of Water Rates; Uniformity of Rates

Metropolitan Water District Act Section 134.5: Water Standby or Availability of Service Charge

Metropolitan Water District Administrative Code Section 4301(a): Cost of Service and Revenue Requirement

By Minute Item 50438, the Board, at its April 12, 2016 meeting, approved a motion that the Board (1) define objectives of a new treated water charge, (2) further analyze alternatives to bring back to the Board for further discussion in fall 2016, and (3) bring a possible recommendation for a new treated water charge effective January 1, 2018.

## California Environmental Quality Act (CEQA)

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### CEQA determination for Options #1, #2, and #3:

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, the proposed action is not subject to CEQA because it involves other government fiscal activities, which do not involve any commitment to any specific project which may result in a potentially significant physical impact on the environment (Section 15378(b)(4) of the State CEQA Guidelines). Finally, where it can be seen with certainty that there is no possibility that the proposed actions may have a significant impact on the environment, those actions are not subject to CEQA pursuant to Section 15061(b)(3) of the State CEQA Guidelines.

The CEQA determination for Options #1, #2, and #3 is: Determine that the proposed action is not defined as a project and is not subject to CEQA pursuant to Sections 15378(b)(2), 15378(b)(4), and 15061(b)(3) of the State CEQA Guidelines.

## Board Options

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### Option #1

Adopt the CEQA determination that the proposed action is not defined as a project under CEQA and is not subject to CEQA, and

Adopt the Resolution Approving the Treatment Charge Workgroup's Policy Principles, Recommendation for a Treatment Capacity Charge, and Implementation of a Treatment Capacity Charge.

**Fiscal Impact:** None

### Option #2

Adopt the CEQA determination that the proposed action is not defined as a project under CEQA and is not subject to CEQA, and

Adopt the Resolution Approving the Treatment Charge Workgroup's Proposed Policy Principles and take no further action at this time.

**Fiscal Impact:** None

### Option #3

Adopt the CEQA determination that the proposed action is not defined as a project under CEQA and is not subject to CEQA, and

Take no action at this time and maintain Metropolitan's current 100% volumetric Treatment Surcharge.

**Fiscal Impact:** None

**Staff Recommendation**

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Option #1

  
\_\_\_\_\_  
Gary Breaux  
Chief Financial Officer/  
Assistant General Manager

4/4/2017  
Date

  
\_\_\_\_\_  
Jeffrey Kightlinger  
General Manager

4/4/2017  
Date

**Attachment 1 – Proposed Policy Principles, Recommendations, and Implementation Considerations**

**Attachment 2 – Resolution Approving the Treatment Charge Workgroup’s Proposed Policy Principles, Recommendations for a Treatment Capacity Charge, and Implementation of a Treatment Capacity Charge**

**Attachment 3 – October 20, 2016 Presentation to the Treatment Charge Workgroup, containing background material on treatment costs**

**Attachment 4 – Resolution Approving the Treatment Charge Workgroup’s Proposed Policy Principles**

**Attachment 5 – List of Workgroup Participants**

Ref# cfo12650105

**TREATMENT CHARGE WORKGROUP**  
**PROPOSED POLICY PRINCIPLES, RECOMMENDATIONS, AND**  
**IMPLEMENTATION CONSIDERATIONS**

**February 2, 2017**

The Treatment Charge Workgroup (“Workgroup”) was initially established by the MWD Board of Directors to develop recommendations for a fixed treatment surcharge for subsequent consideration by the Board. The constraints placed on the Workgroup were simply that any recommendations had to be based on the existing Cost of Service Study. Several meetings of the Workgroup have been utilized to discuss the attributes of successful treatment cost recovery, and the methods of accounting for assets, revenues and costs.

The Workgroup concluded there are several important attributes of effective treated water cost recovery. These include, but are not limited to, providing a clear nexus between member agency treatment service costs and the benefits received, and structuring MWD’s treatment revenues with low variability and appropriate levels of resiliency.

Prior to establishing a specific rate-related proposal, the Workgroup recommends the Board’s consideration and potential adoption of Policy Principles. These principles would provide a guidance framework for changes MWD may wish to make to the treated water portion of its rate structure in the future.

Potential imposition of a new treated water charge would more ideally be done in the context of a full rate refinement review. This would ensure the components of the resultant rate structure are fully harmonized. However, absent a full rate refinement review, modifications to MWD’s existing charges may be implemented to incorporate policy changes regarding the recovery of treatment component costs. This document presents Proposed Policy Principles, Recommendations, and an implementation consideration.

**Policy Principles for Treatment Rates and Charges:**

1. Treatment rates and charges shall align treatment costs with treatment services and benefits received consistent with cost of service principles.
2. Treatment services shall be recognized to include physical water treatment, as well as operational benefits such as available treatment capacity used by member agencies.
3. In an effort to contain overall treatment costs on an on-going basis, MWD shall programmatically identify opportunities to partially or fully decommission unneeded treatment infrastructure and minimize future O&M and capital expenditures. MWD

should obtain member agency commitment to utilize new or expanded future treatment capacity.

**Recommendations for Treatment Rates and Charges:**

1. Adopt a Treatment Capacity Charge that mirrors the existing Capacity Charge in a manner consistent with cost of service principles.
2. This Treatment Capacity Charge should be implemented based upon a three-year trailing maximum peak day flow through treated water service connections during the May 1 through September 30 peak summer demand period.

**An Implementation Consideration for Treated Water Charges:**

1. To provide member agencies with sufficient time to plan for operational and financial impacts to their agencies and sub-agencies, this Treatment Capacity Charge should be integrated into MWD's biennial cost of service process and considered for implementation at the Board's discretion with rates and charges effective no sooner than January 1, 2021 (thus, inclusive only of the summer peaks of 2017-2019.)

THE METROPOLITAN WATER DISTRICT  
OF SOUTHERN CALIFORNIA

RESOLUTION \_\_\_\_

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**RESOLUTION OF THE BOARD OF DIRECTORS  
OF THE METROPOLITAN WATER DISTRICT OF  
SOUTHERN CALIFORNIA  
APPROVING  
THE TREATMENT CHARGE WORKGROUP'S PROPOSED POLICY PRINCIPLES,  
RECOMMENDATIONS FOR A TREATMENT CAPACITY CHARGE, AND  
IMPLEMENTATION OF A TREATMENT CAPACITY CHARGE**

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WHEREAS, the Board of Directors ("Board") of The Metropolitan Water District of Southern California ("Metropolitan"), pursuant to Sections 133, 134 and 134.5 of the Metropolitan Water District Act (the "Act"), is authorized to fix such rate or rates for water as will result in revenue which, together with revenue from any water standby or availability of service charge or assessment, will pay the operating expenses of Metropolitan, provide for repairs and maintenance, provide for payment of the purchase price or other charges for property or services or other rights acquired by Metropolitan, and provide for the payment of the interest and principal of its bonded debt, including payment of the interest and principal of Metropolitan's non-tax funded debt; and

WHEREAS, on April 12, 2016, the Board voted to (1) define objectives of a new treated water charge, (2) further analyze alternatives to bring back to the Board for discussion in fall 2016, and (3) bring a possible recommendation to the Board for a new treated water charge effective January 1, 2018; and

WHEREAS, on June 28, 2016, the Executive Committee of the Board approved the formation of a Workgroup to achieve its objectives, with participation made open to all member agencies; and

WHEREAS, the Executive Committee established a timeline for the Workgroup to provide recommendations to Metropolitan's Finance and Insurance (F&I) Committee, and directed the Workgroup to:

- Define objectives of a fixed treated water charge;
- Determine costs to be included in a fixed charge;
- Determine allocation methodology;
- Address issues related to the implementation of a new charge; and
- Consider implementation in January 2018 or as part of the next biennial budget.

WHEREAS, Metropolitan retained Dr. Tom Chesnutt of A&N Technical Services, Inc. to facilitate the process, which took place from September 2016 through February 2017; and

WHEREAS, at the February meeting of the F&I Committee, the Workgroup presented its Proposal in a document titled, "Treatment Charge Workgroup Proposed Policy Principles, Recommendations, and Implementation Considerations" (Proposal), dated February 2, 2017; and

WHEREAS, the Proposal recommends that the Board adopt three policy principles, as follows:

1. Treatment rates and charges shall align treatment costs with treatment services and benefits received consistent with cost of service principles.
2. Treatment services shall be recognized to include physical water treatment, as well as operational benefits such as available treatment capacity used by member agencies.
3. In an effort to contain overall treatment costs on an on-going basis, MWD shall programmatically identify opportunities to partially or fully decommission unneeded treatment infrastructure and minimize future O&M and capital expenditures. MWD should obtain member agency commitment to utilize new or expanded future treatment capacity.

WHEREAS, the Proposal recommends a Treatment Capacity Charge that mirrors the existing Metropolitan Capacity Charge, to be allocated to member agencies based upon a three-year trailing maximum peak day flow through treated water service connections during the May 1 through September 30 peak summer demand period; and

WHEREAS, the recommended Treatment Capacity Charge would recover the capital financing costs incurred to meet maximum summer treatment capacity, also referred to as "fixed demand costs"; and

WHEREAS, to provide member agencies with sufficient time to plan for operational and financial impacts to their agencies and sub-agencies, the Proposal recommends the Treatment Capacity Charge be integrated into Metropolitan's biennial cost of service process and considered for implementation at the Board's discretion with rates and charges effective no sooner than January 1, 2021; and

WHEREAS, the F&I Committee considered the Proposal at its regular February 2017 and March 2017 meetings, pursuant to informational presentations, review, and deliberation; and

WHEREAS, on April 10, 2017, the Proposal, together with a staff review thereof, was further discussed and reviewed by the F&I Committee and by the Board on April 11, 2017; and

WHEREAS, each of said meetings of the Board were conducted in accordance with the Brown Act (commencing at 54950 of the Government Code), at which due notice was provided and quorums were present and acting throughout; and

NOW, THEREFORE, the Board of Directors of The Metropolitan Water District of Southern California does hereby resolve, determine and order as follows:

**Section 1.** That the Board of Directors of Metropolitan hereby adopts the following policy principles for the recovery of treatment costs:

1. Treatment rates and charges shall align treatment costs with treatment services and benefits received consistent with cost of service principles.
2. Treatment services shall be recognized to include physical water treatment, as well as operational benefits such as available treatment capacity used by member agencies.
3. In an effort to contain overall treatment costs on an on-going basis, MWD shall programmatically identify opportunities to partially or fully decommission unneeded treatment infrastructure and minimize future O&M and capital expenditures. MWD should obtain member agency commitment to utilize new or expanded future treatment capacity.

**Section 2.** That the Board hereby directs the General Manager to integrate into Metropolitan's biennial cost of service process for the proposal of rates and charges a Treatment Capacity Charge effective January 1, 2021.

**Section 3.** That such Treatment Capacity Charge shall mirror the existing Capacity Charge in a manner consistent with cost of service principles.

**Section 4.** That such Treatment Capacity Charge for each member public agency ("member agency") be based upon a three-year trailing maximum peak day flow through treated water service connections during the May 1 through September 30 peak summer demand period.

**Section 5.** That this Board finds that the adoption of the policy principles and Treatment Capacity Charge 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, the proposed action is not subject to CEQA because it involves other government fiscal activities, which do not involve any commitment to any specific project which may result in a potentially significant physical impact on the environment (Section 15378(b)(4) of the State CEQA Guidelines). Finally, where it can be seen with certainty that there is no possibility that the proposed actions may have a significant impact on the environment, those actions are not subject to CEQA pursuant to Section 15061(b)(3) of the State CEQA Guidelines.

**Section 6.** That the General Manager and the General Counsel are hereby authorized to do all things necessary and desirable to accomplish the purposes of this Resolution, including, without limitation, the commencement or defense of litigation.

**Section 7.** That the General Manager is hereby authorized and directed to take all necessary action to satisfy relevant statutes requiring notice by publication.

**Section 8.** That the Board Executive Secretary is hereby directed to transmit a certified copy of this Resolution to the presiding officer of the governing body of each member agency.

I HEREBY CERTIFY that the foregoing is a full, true and correct copy of a Resolution adopted by the Board of Directors of The Metropolitan Water District of Southern California, at its meeting held on April 11, 2017.

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Board Executive Secretary  
The Metropolitan Water District  
of Southern California

# Treatment Fixed Charge Workgroup

## Meeting #3

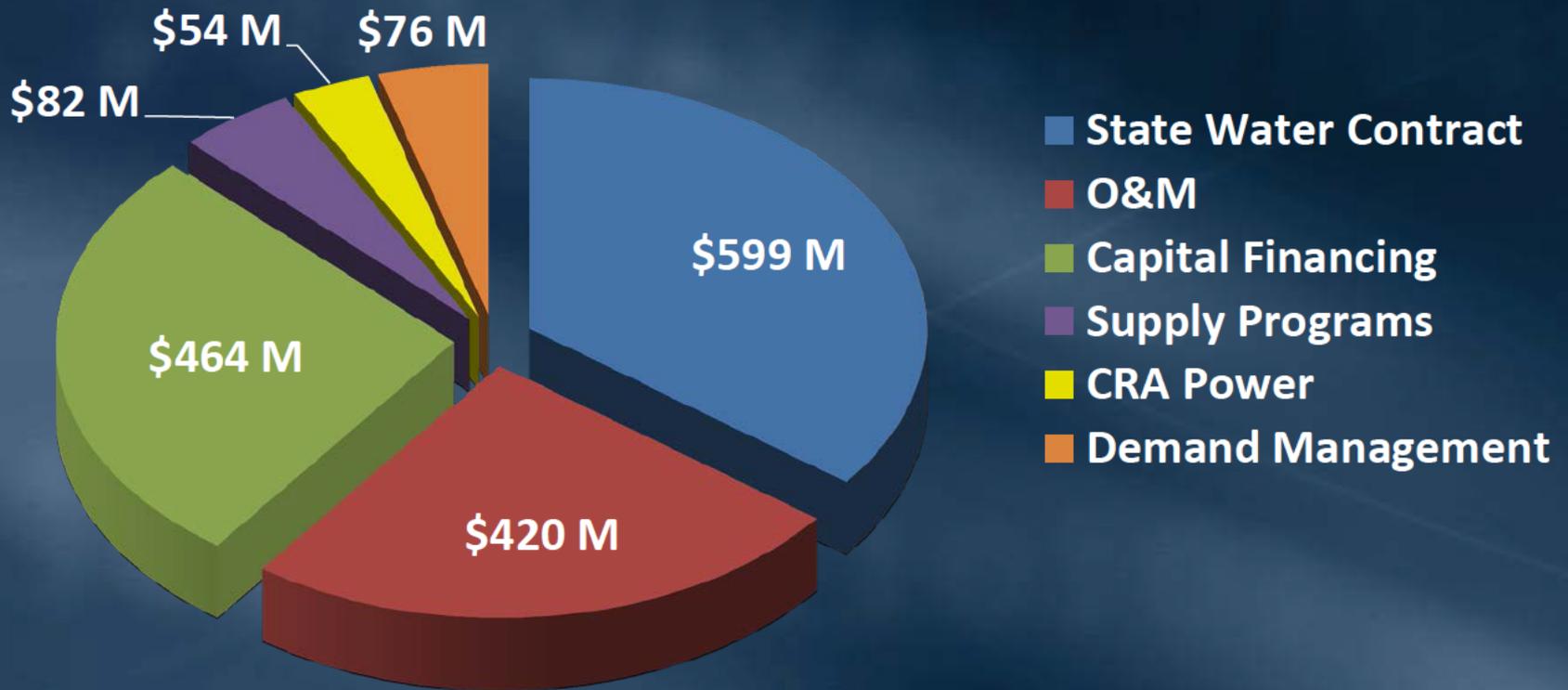


# Review of Budget

- Budget is foundation of Treatment Cost of Service
- Treatment Cost of Service analysis involves the functionalization of costs within the budget
  - Treatment O&M, WSO support costs, O&M from other groups, capital financing, and A&G costs
- Overview of components of fiscal year expenditure budget and departmental O&M budget

# Expenditures

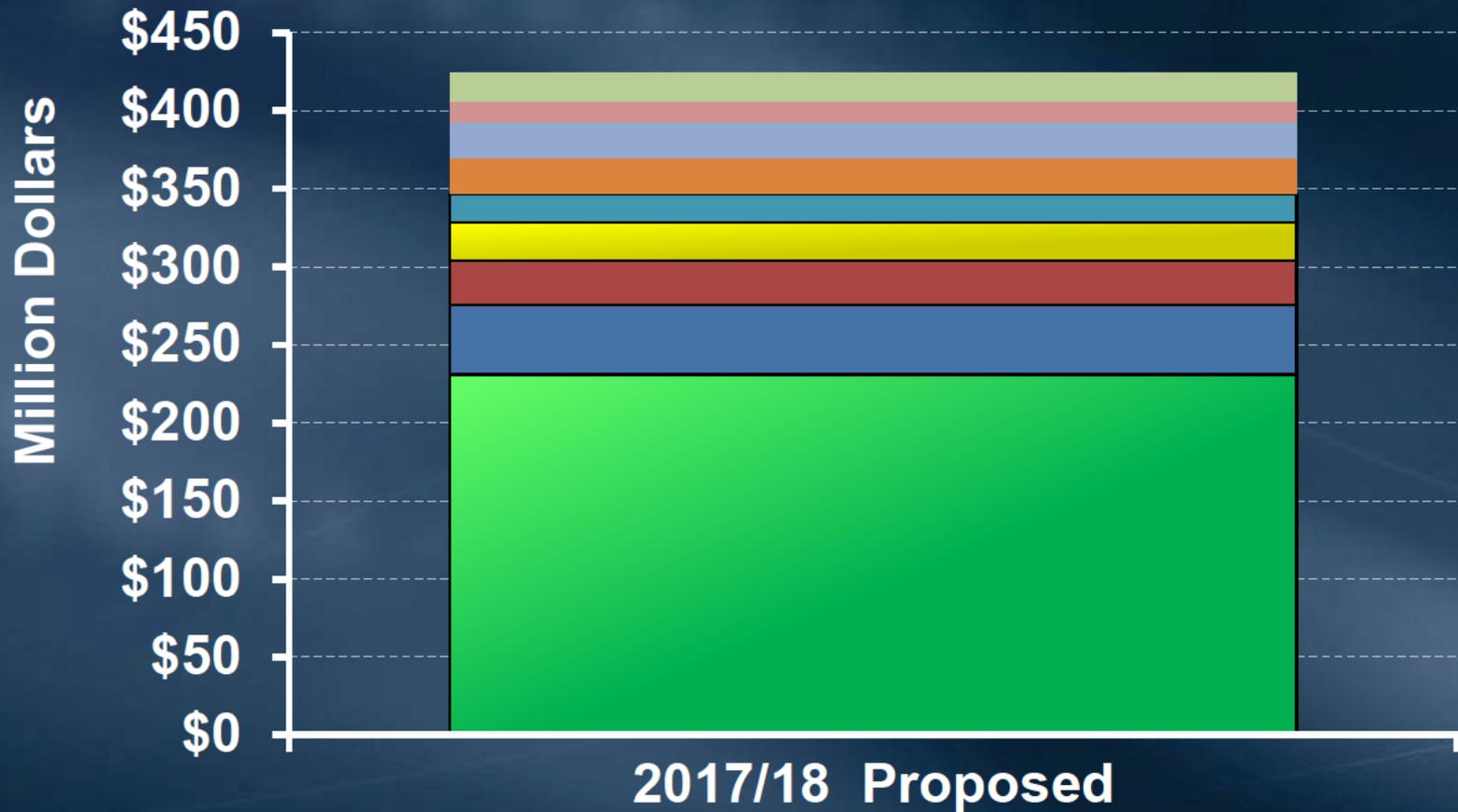
FY 2017/18 Budget - \$1.7 B



Without Revenue Offsets, Increase in Required Reserves

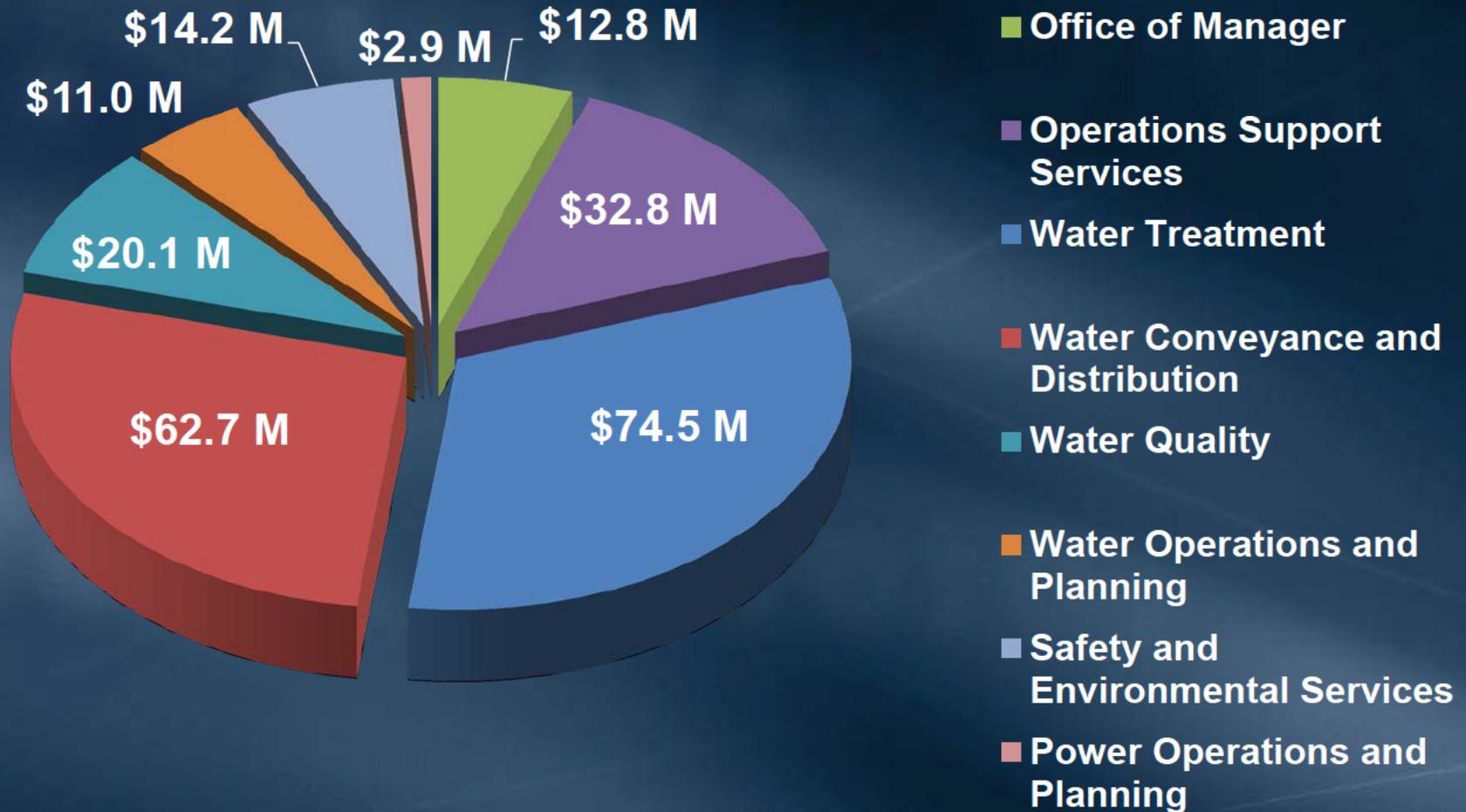
# O&M Expenditure Budget

- Real Property Development & Mgmt
- Human Resources
- Legal, Audit, & Ethics
- Engineering Services
- Water System Operations
- GM & Board of Directors
- Chief Financial Officer
- External Affairs
- Business Technology



# Water System Operations Budget

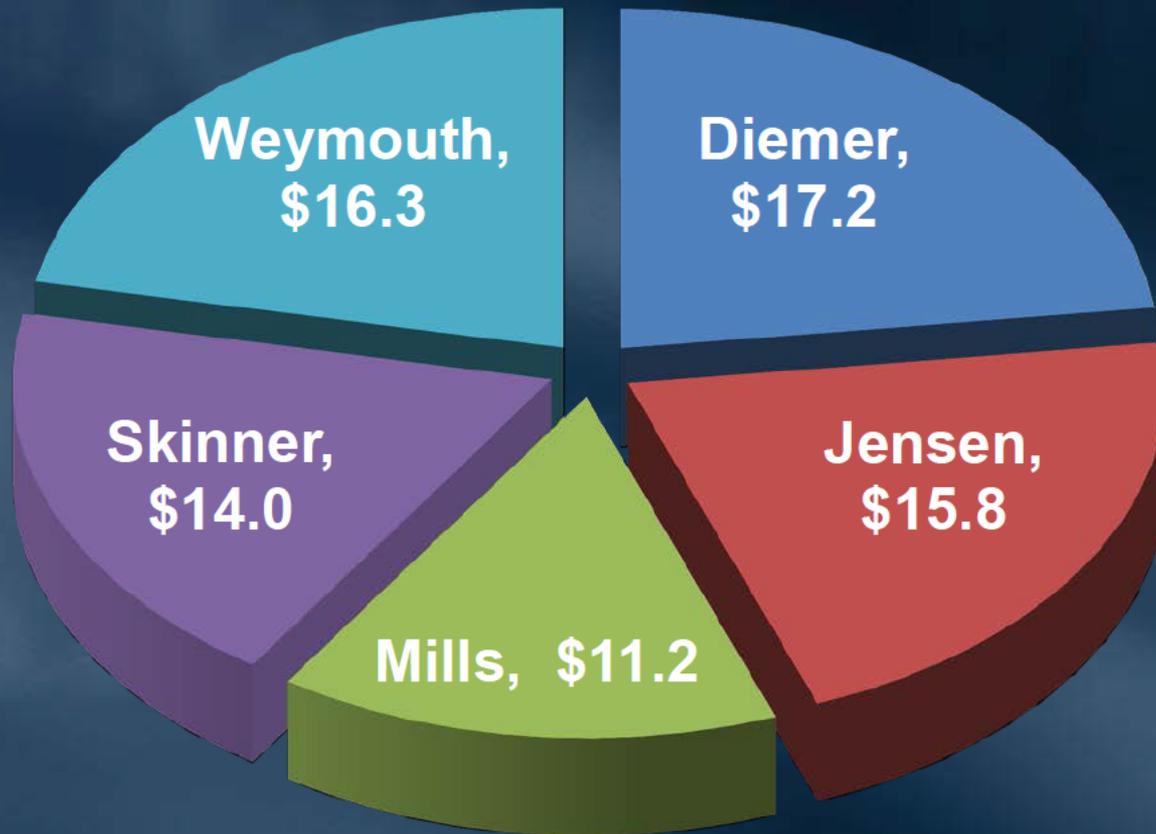
## FY 2017/18 - \$231 M\*



\* Includes variable treatment (chemicals, solids, power)

# Water Treatment Section Budget

FY 2017/18 - \$74.5 M\*



\* Includes variable treatment at each plant (chemicals, solids, power)

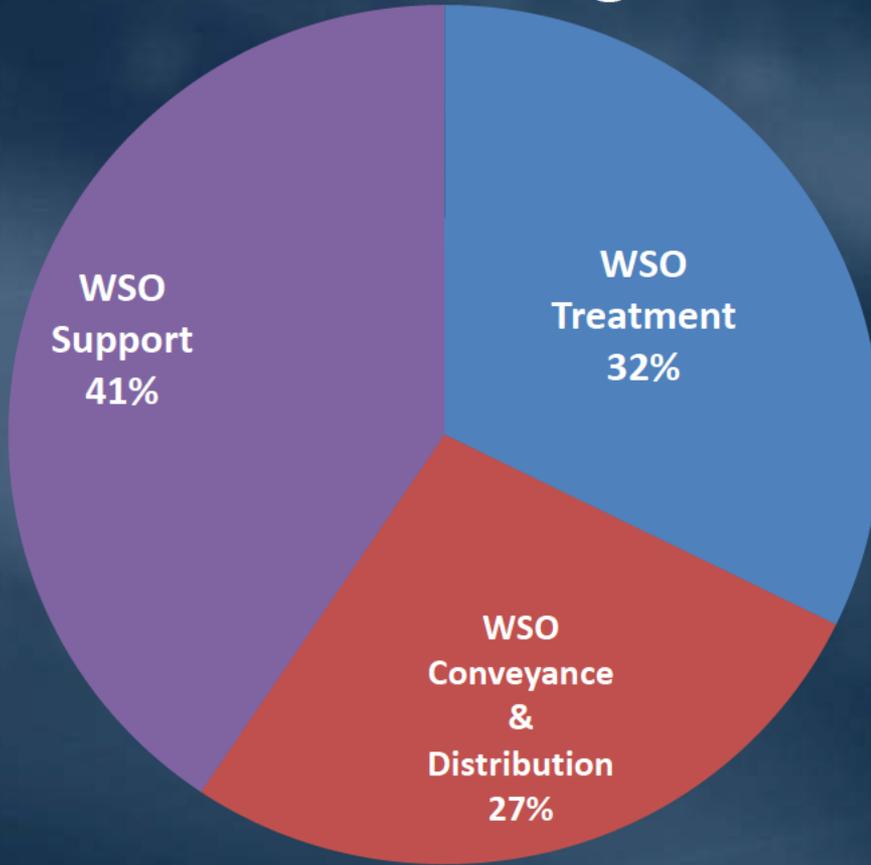
# Treatment Cost of Service analysis:

## Functionalization of costs

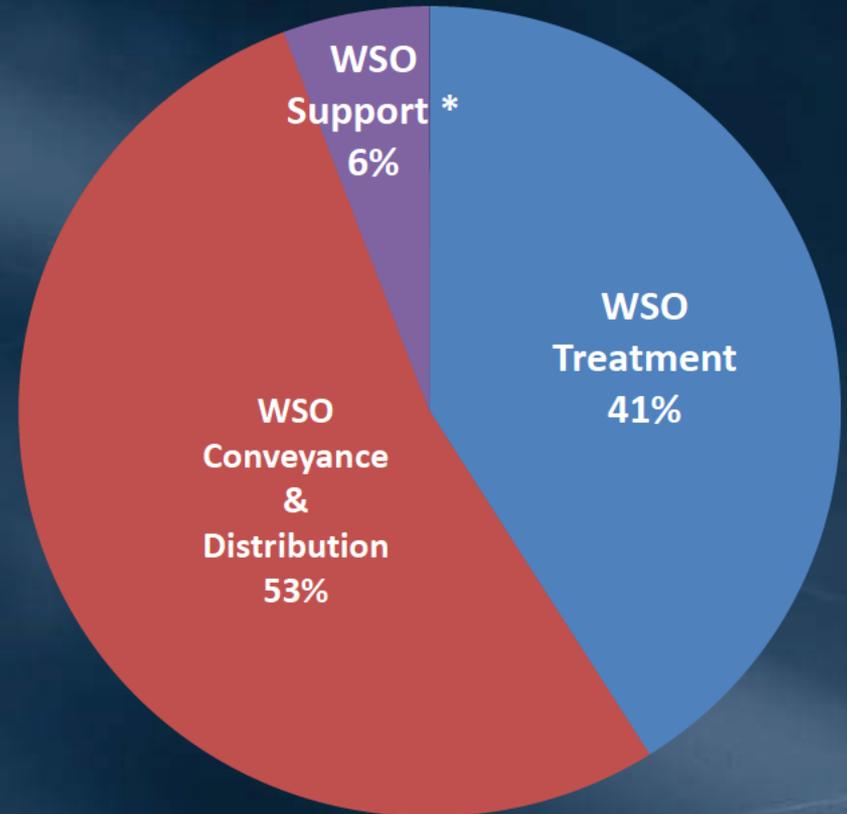
- Start with direct Departmental O&M at the five treatment plants from Budget
- Add WSO support O&M
  - Oper. Support, Oper. Planning, Water Quality, Safety & Environmental, Power Operations
- Add support O&M from other groups
  - Human Resources, IT, Engineering, GM
- Add capital financing costs
- Subtract Revenue Offsets
- Add A&G

# FY17/18 WSO O&M Budget functionalized

## Budget



## Revenue Requirement



\* Functionalized as Supply, Storage, A&G Sched. 8 in COS

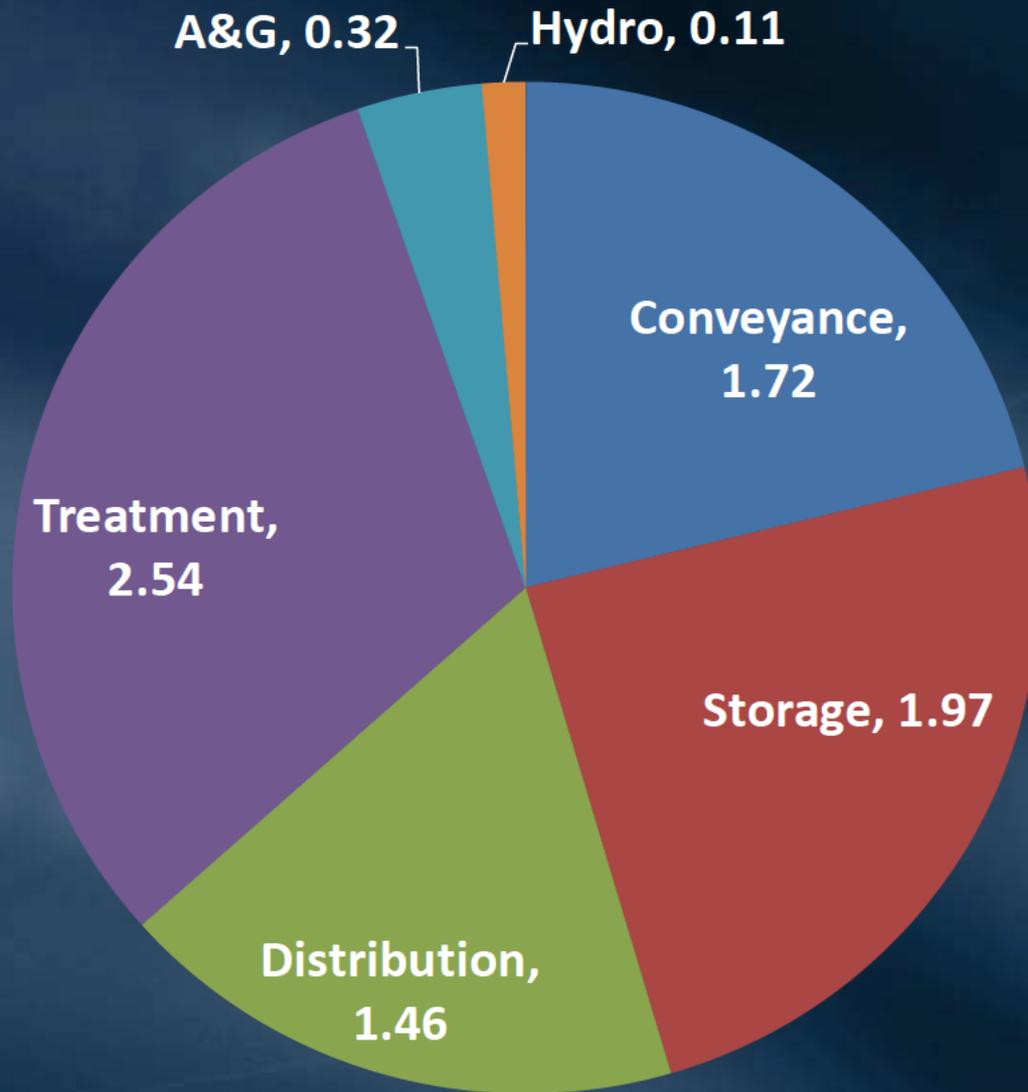
# FY17/18 Treatment Direct O&M calculation

	\$million	Functionalized by
Water Treatment Section	74.5	location
Overhead Credit from Construction	(3.5)	Prorated by O&M (17%)
Electrical & Control Teams	<u>(9.0)</u>	Activity (50%)
Water Treatment Direct O&M	62.1	

# FY17/18 Treatment costs functionalization

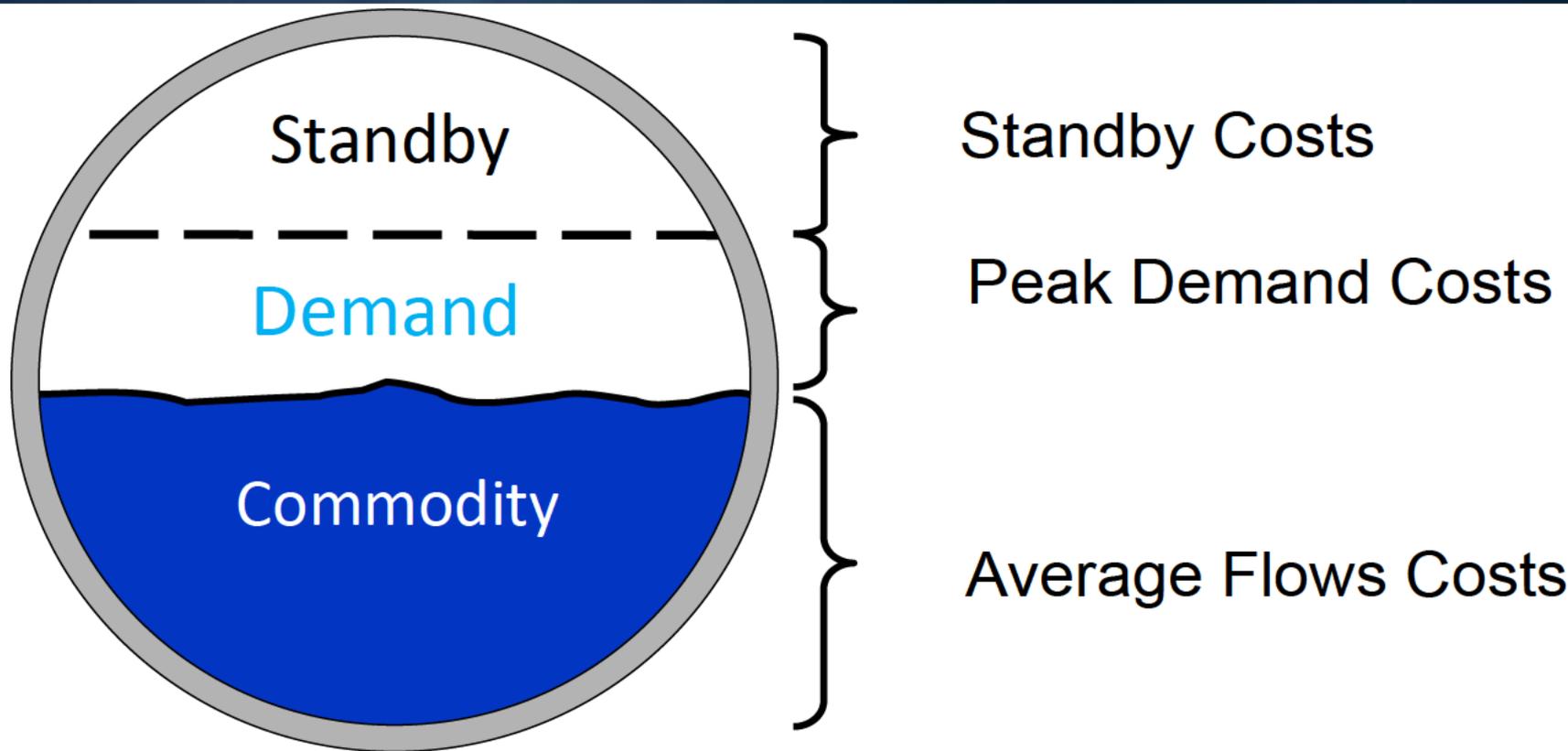
Dept. O&M	\$million	Functionalized by
Water Treatment Direct O&M	62.1	Location / activity
WSO support	23.7	Time keeping; Team function
Engineering & IT	15.7	NBV; Prorated by Labor \$
GM & HR	3.9	Prorated by Labor \$ (26%)
Capital financing costs	144.4	NBV (31%)
Revenue Offsets	(7.6)	Pro rata share of Taxes & Interest
A&G	<u>22.3</u>	Prorated by Rev. Req. (17%)
Revenue Requirement	264.5	

# FY17/18 Net Book Value (\$billion)



Sched. 4 in COS

# Cost of Service: Allocation of costs



# FY17/18 Treatment Cost of Service: Allocation of costs

- Fixed Commodity factor = Treated Sales / Treatment Design Capacity
  - Design capacity = 3,947 cfs = 2.86 MAF
  - 0.83 MAF / 2.86 MAF = 29%
- Demand factor = Treated Sales \* Non-coincident Peak Factor / Design Capacity
  - Treated non-coincident peak factor = 1.96  
= 3-year non-coincident peak day/average flows
  - 0.83 MAF \* (1.96-1) / 2.86 MAF = 28%
- Standby factor = residual = 43%

# FY17/18 Treatment Cost of Service: Allocation of costs (\$million)

	Capital	O&M + A&G - Offsets	Total
Fixed Commodity	41.8	96.6	138.4
Variable Commodity	0	24.5	24.5
Demand	40.1	2.0	42.1
<u>Standby</u>	<u>62.6</u>	<u>(3.0)</u>	<u>59.6</u>
total	144.4	120.0	264.5

Sched. 14 in COS

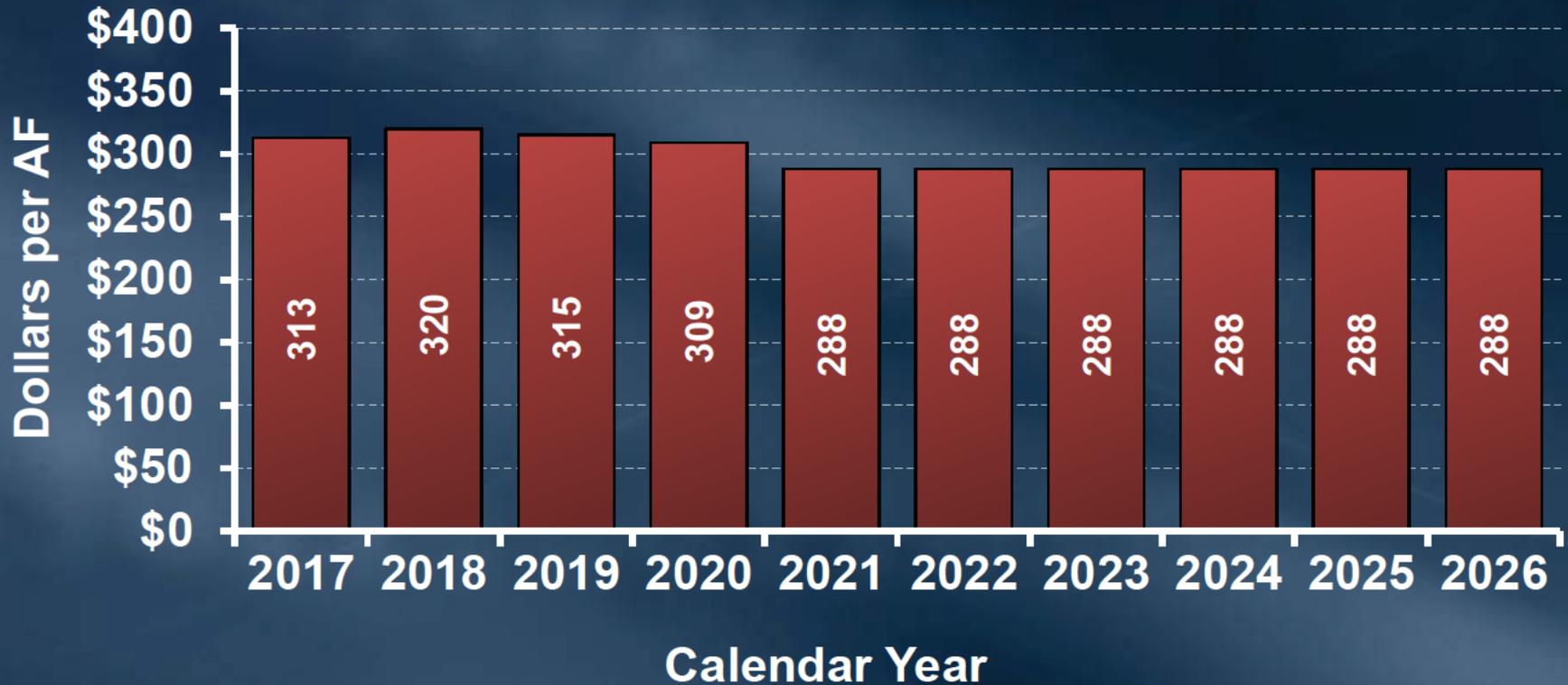
# FY17/18 Treatment Cost of Service: Distribution to Rate Elements

Revenue Requirement	Costs (\$million)	Rate
Fixed Commodity	138.4	
Variable Commodity	24.5	
Demand	42.1	
Standby	<u>59.6</u>	
Total	264.5	\$320/AF

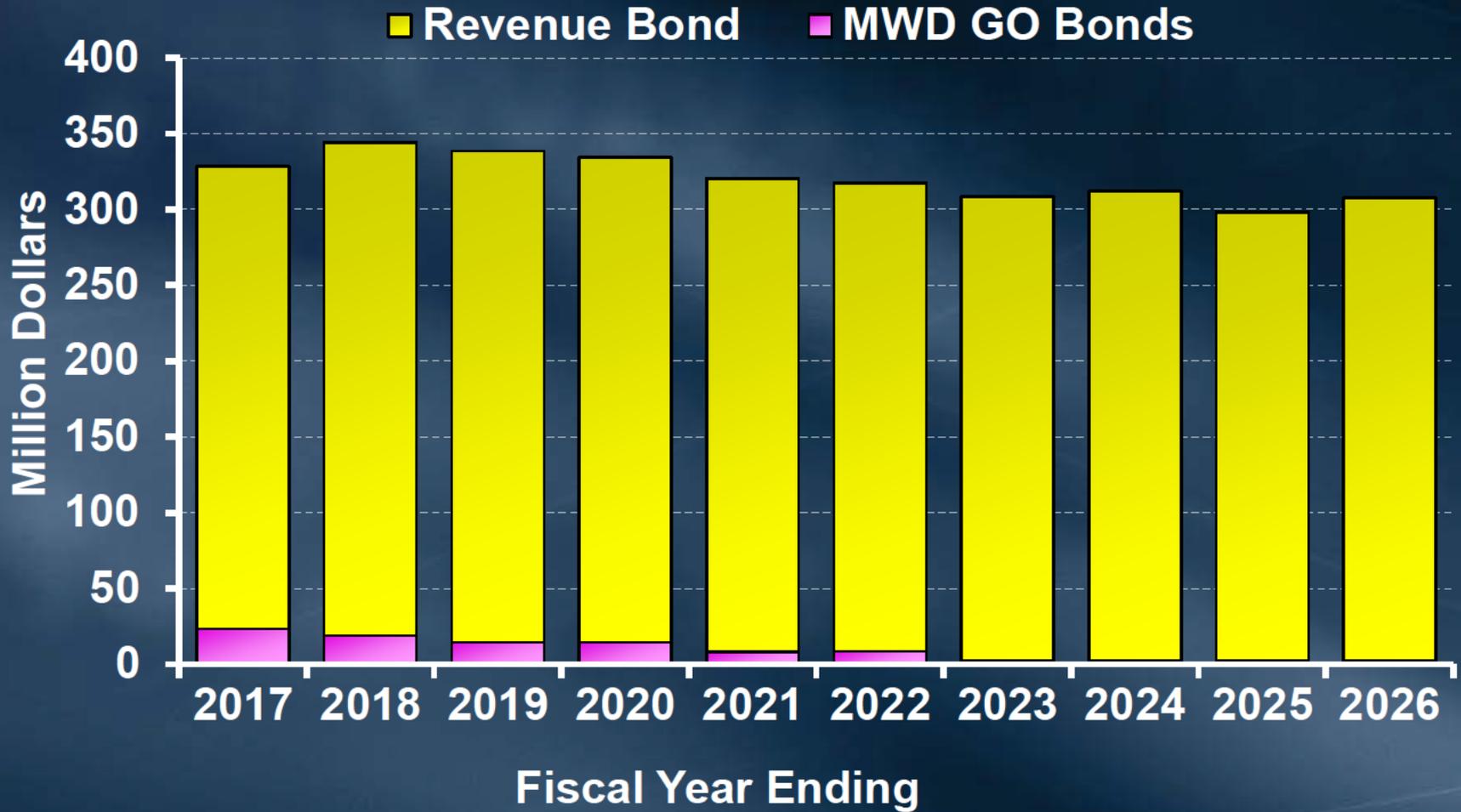
Sched. 15 in COS

# Long-Term Treatment Surcharge Forecast

# Projected Treatment Surcharge

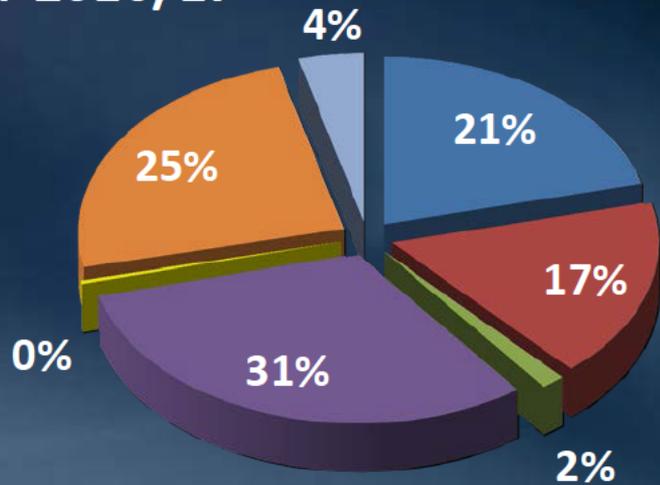


# Debt Service

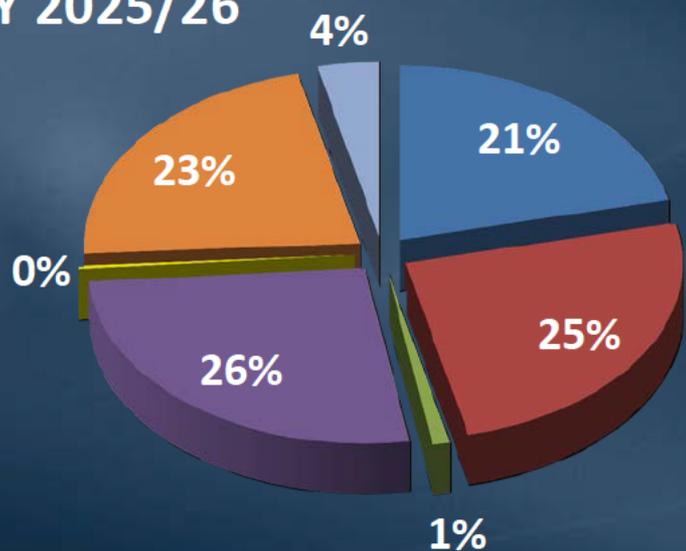


# Net Book Value

**FY 2016/17**



**FY 2025/26**



- Conveyance & Aqueduct
- Distribution
- Hydroelectric
- Treatment
- Source of Supply
- Storage
- Administrative & General





THE METROPOLITAN WATER DISTRICT  
OF SOUTHERN CALIFORNIA

RESOLUTION \_\_\_\_

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**RESOLUTION OF THE BOARD OF DIRECTORS  
OF THE METROPOLITAN WATER DISTRICT OF  
SOUTHERN CALIFORNIA  
APPROVING  
THE TREATMENT CHARGE WORKGROUP'S PROPOSED POLICY PRINCIPLES**

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WHEREAS, the Board of Directors (“Board”) of The Metropolitan Water District of Southern California (“Metropolitan”), pursuant to Sections 133, 134 and 134.5 of the Metropolitan Water District Act (the “Act”), is authorized to fix such rate or rates for water as will result in revenue which, together with revenue from any water standby or availability of service charge or assessment, will pay the operating expenses of Metropolitan, provide for repairs and maintenance, provide for payment of the purchase price or other charges for property or services or other rights acquired by Metropolitan, and provide for the payment of the interest and principal of its bonded debt, including payment of the interest and principal of Metropolitan’s non-tax funded debt; and

WHEREAS, on April 12, 2016, the Board voted to (1) define objectives of a new treated water charge, (2) further analyze alternatives to bring back to the Board for discussion in fall 2016, and (3) bring a possible recommendation to the Board for a new treated water charge effective January 1, 2018; and

WHEREAS, on June 28, 2016, the Executive Committee of the Board approved the formation of a Workgroup to achieve its objectives, with participation made open to all member agencies; and

WHEREAS, the Executive Committee established a timeline for the Workgroup to provide recommendations to Metropolitan’s Finance and Insurance (F&I) Committee, and directed the Workgroup to:

- Define objectives of a fixed treated water charge;
- Determine costs to be included in a fixed charge;
- Determine allocation methodology;
- Address issues related to the implementation of a new charge; and
- Consider implementation in January 2018 or as part of the next biennial budget.

WHEREAS, Metropolitan retained Dr. Tom Chesnutt of A&N Technical Services, Inc. to facilitate the process, which took place from September 2016 through February 2017; and

WHEREAS, at the February meeting of the F&I Committee, the Workgroup presented its Proposal in a document titled, “Treatment Charge Workgroup Proposed Policy Principles, Recommendations, and Implementation Considerations” (Proposal), dated February 2, 2017; and

WHEREAS, the Proposal recommends that the Board adopt three policy principles, which would provide a guidance framework for changes Metropolitan may wish to make to any treatment rate or charge now or in the future, as follows:

1. Treatment rates and charges shall align treatment costs with treatment services and benefits received consistent with cost of service principles.
2. Treatment services shall be recognized to include physical water treatment, as well as operational benefits such as available treatment capacity used by member agencies.
3. In an effort to contain overall treatment costs on an on-going basis, MWD shall programmatically identify opportunities to partially or fully decommission unneeded treatment infrastructure and minimize future O&M and capital expenditures. MWD should obtain member agency commitment to utilize new or expanded future treatment capacity.

WHEREAS, the Proposal recommends a Treatment Capacity Charge that mirrors the existing Metropolitan Capacity Charge, to be allocated to member agencies based upon a three-year trailing maximum peak day flow through treated water service connections during the May 1 through September 30 peak summer demand period; and

WHEREAS, the recommended Treatment Capacity Charge would recover the capital financing costs incurred to meet maximum summer treatment capacity, also referred to as “fixed demand costs”; and

WHEREAS, to provide member agencies with sufficient time to plan for operational and financial impacts to their agencies and sub-agencies, the Proposal recommends the Treatment Capacity Charge be integrated into Metropolitan’s biennial cost of service process and considered for implementation at the Board’s discretion with rates and charges effective no sooner than January 1, 2021; and

WHEREAS, the F&I Committee considered the Proposal at its regular February 2017 and March 2017 meetings, pursuant to informational presentations, review, and deliberation; and

WHEREAS, on April 10, 2017, the Proposal, together with a staff review thereof, was further discussed and reviewed by the F&I Committee and by the Board on April 11, 2017; and

WHEREAS, each of said meetings of the Board were conducted in accordance with the Brown Act (commencing at 54950 of the Government Code), at which due notice was provided and quorums were present and acting throughout; and

NOW, THEREFORE, the Board of Directors of The Metropolitan Water District of Southern California does hereby resolve, determine and order as follows:

**Section 1.** That the Board of Directors of Metropolitan hereby adopts the following policy principles for the recovery of treatment costs, which would provide a guidance framework for changes Metropolitan may wish to make to any treatment rate or charge now or in the future:

1. Treatment rates and charges shall align treatment costs with treatment services and benefits received consistent with cost of service principles.

2. Treatment services shall be recognized to include physical water treatment, as well as operational benefits such as available treatment capacity used by member agencies.
3. In an effort to contain overall treatment costs on an on-going basis, MWD shall programmatically identify opportunities to partially or fully decommission unneeded treatment infrastructure and minimize future O&M and capital expenditures. MWD should obtain member agency commitment to utilize new or expanded future treatment capacity.

**Section 2.** That this Board finds that the adoption of the policy 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, the proposed action is not subject to CEQA because it involves other government fiscal activities, which do not involve any commitment to any specific project which may result in a potentially significant physical impact on the environment (Section 15378(b)(4) of the State CEQA Guidelines). Finally, where it can be seen with certainty that there is no possibility that the proposed actions may have a significant impact on the environment, those actions are not subject to CEQA pursuant to Section 15061(b)(3) of the State CEQA Guidelines.

**Section 3.** That the General Manager and the General Counsel are hereby authorized to do all things necessary and desirable to accomplish the purposes of this Resolution, including, without limitation, the commencement or defense of litigation.

**Section 4.** That the Board Executive Secretary is hereby directed to transmit a certified copy of this Resolution to the presiding officer of the governing body of each member agency.

I HEREBY CERTIFY that the foregoing is a full, true and correct copy of a Resolution adopted by the Board of Directors of The Metropolitan Water District of Southern California, at its meeting held on April 11, 2017.

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Secretary of the Board of Directors  
of The Metropolitan Water District  
of Southern California

## **List of Treatment Charge Workgroup Participants**

1. City of Anaheim
2. Calleguas Municipal Water District
3. Inland Empire Utilities Agency
4. Central Basin Municipal Water District
5. Eastern Municipal Water District
6. Foothill Municipal Water District
7. City of Glendale
8. City of Los Angeles
9. Las Virgenes Municipal Water District
10. Municipal Water District of Orange County
11. City of Pasadena
12. Three Valleys Municipal Water District
13. San Diego County Water Authority
14. Upper San Gabriel Valley Municipal Water District
15. West Basin Municipal Water District
16. Western Municipal Water District of Riverside County