THE METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA

BOARD ACTION

- Board of Directors
  Water Planning and Stewardship Committee

5/11/2021 Board Meeting

7-7

Subject

Authorize the General Manager to enter into agreement with participating member agencies to provide a credit to offset the increased costs and impacts incurred by a member agency associated with shifting deliveries to different service connections at the request of Metropolitan during calendar years 2021 and 2022; the General Manager has determined that the proposed action is exempt or otherwise not subject to CEQA

Executive Summary

Calendar year (CY) 2021 is the second year of drought in the State Water Project (SWP) watershed. Following a 20 percent allocation on the SWP in CY 2020, CY 2021 is now tied for the lowest SWP allocation in history at 5 percent. These low allocations come on the heels of Metropolitan accumulating high regional storage reserves, which help buffer the region from direct impacts of these extremely dry conditions.

The extreme dry conditions on the SWP system result in operational challenges that affect contractors throughout the SWP system. The Department of Water Resources has very little operational flexibility to assist contractors in meeting their delivery needs in the northern portions of the SWP system due to these conditions. Metropolitan is fortunate to have invested in storage programs both within the SWP system and along the Central Valley that can be used in these dry conditions to provide reliable supplies to our member agencies.

However, even with these storage assets, Metropolitan is taking prudent actions to preserve the supplies that are available on the SWP system, in case the drought continues beyond 2021. These actions focus on preserving storage that is available to the portions of Metropolitan's system that are more reliant on SWP deliveries. Operational steps are being taken to expand deliveries of Colorado River supplies and water stored in Diamond Valley Lake into portions of the service area that would normally only receive SWP supplies. These actions reduce the withdrawals from Metropolitan's surface storage on the SWP system, which can be preserved for use in the portions of the service area that are more reliant on SWP deliveries, should the drought continue into a third year.

In previous years, Metropolitan has also worked with the city of Los Angeles (LADWP) to utilize flexibility within their distribution system to exchange delivery of Metropolitan's treated Colorado River supplies for Los Angeles Aqueduct supplies delivered by LADWP to Calleguas Municipal Water District and Las Virgenes Municipal Water District instead of Metropolitan's untreated SWP supplies. This further helps to preserve Metropolitan's storage reserves on the SWP; however, this activity comes at a cost and risk to LADWP. LADWP incurs the cost of Metropolitan's Treatment Surcharge by helping with this operational shift in addition to other water quality impacts. Under an existing agreement, Metropolitan has been able to credit LADWP for the costs of this operational shift, but it took years for the appropriate cost adjustments to be reconciled.

Given a desire to utilize this operational shift in years with extremely low SWP allocations, staff recommends adoption of a voluntary program that allows Metropolitan to directly offset the increased costs and impacts an agency may incur when complying with Metropolitan's request to shift delivery locations in order to achieve regional reliability benefits. This program would be effective for CY 2021 and CY 2022, allowing Metropolitan to offset increased costs and impacts a member agency may incur up to an amount per acre-foot (AF) $5/AF above Metropolitan's Treatment Surcharge for an operational shift at Metropolitan's request. The CY 2021 Treatment Surcharge is $327/AF, and CY 2022 is $344/AF. The credit would be net of the member agency's own treatment costs. The amount above the Treatment Surcharge helps offset additional costs or impacts incurred by

the member agency due to impacts to their system resulting from shifts in their operations. The anticipated operational shifts are shifts from untreated deliveries to treated deliveries, and that is the reason for using the Treatment Surcharge as a guideline. The program would be reassessed after CY 2022 based on operational experience, observed costs, and other lessons learned.

Details

Background

Metropolitan's continued system and supply investments and robust Water Surplus and Drought Management (WSDM) portfolio help manage supplies to meet the region's demands. Through Metropolitan's WSDM strategy, supplies are stored when conditions are wet to help meet demands during dry years. In 2019, Metropolitan implemented the Cyclic Cost-Offset Program (CCOP), which helped increase the capture of supplies that would have otherwise been lost to the region. The CCOP resulted in pre-delivering surplus supplies when available and decreasing replenishment demands in the subsequent dry and limited supply years (2020 and 2021), thus bolstering drought reliability for the region. In 2020, Metropolitan ended the year with its highest storage on record.

Now, in 2021, the region enters a second year of a drought and faces a SWP allocation that is tied for the lowest in history. With consecutive years of very low SWP allocations, Metropolitan could be required to withdraw a significant amount of storage reserves that normally augment its SWP supplies. Last year, while the watersheds that support the SWP were entering this period of severe drought, storage on the SWP declined. At the same time, Metropolitan's continued investments in supply programs, low demands from its member agencies, and favorable supply conditions at the Colorado River and along the Colorado River Aqueduct, allowed Metropolitan to increase its storage on the Colorado side of its system. For example, Metropolitan's Lake Mead Intentionally Created Surplus at the end of 2020 was at its highest in history at about 1.3 million AF.

In order to maximize available Colorado River supplies and to save the limited SWP storage for potential future drought years, Metropolitan is maximizing use of its integrated and flexible system. Metropolitan is working with the member agencies to shift the points of delivery to meet demands wherever possible to preserve SWP storage. Additionally, some shifts in delivery locations can be done by member agencies, but these shifts may result in additional operational costs. For example, under a new distribution system configuration, and particularly at lower flows, the member agencies may need to take additional actions to maintain adequate disinfectant levels. Accordingly, staff recommends that the Board approve a cost-offset program, authorizing the General Manager to pay a credit of up to $5/AF above Metropolitan's Treatment Surcharge per AF of water delivered under qualifying operational changes. The Treatment Surcharge for CY 2021 is $327/AF and in CY 2022 is $344/AF. The Treatment Surcharge is used as the marker, as the operational shifts anticipated will require a shift from untreated to treated water, but final credit will be net of the member agency's own treatment costs.

Staff recommends the Board authorize the General Manager to provide a credit, to offset the costs member agencies incur to shift their operations in order to allow Metropolitan to maximize delivery of Colorado River water supplies.

Proposed Authorization for the General Manager

This action seeks authority for the General Manager to issue cost-offset credits for member agency actions related to operational changes to their system that provide a regional benefit. Cost-offset credits would only be given to a member agency in the following conditions:

- The member agency takes an action to make changes to its operations to accommodate Metropolitan's operational request.
- The member agency incurs costs due to these actions that are above the normal costs to operate their system.

The conditions above ensure that Metropolitan only pays cost-offset credits for deliveries that are necessary for Metropolitan to implement its own operational changes. It also clarifies that credits are only made available to offset the increased operational costs to a member agency above the normal cost they would incur to receive Metropolitan water deliveries. General terms for the cost-offset credits are included in **Attachment 1.**

Under current circumstances, the General Manager would work with participating member agencies and enter into agreements pursuant to this action to address the current need to shift deliveries sourced from SWP storage to deliveries from the Colorado River. For example, the General Manager, with the agreement of LADWP, would implement the proposed program to shift deliveries to LADWP from untreated water at LA-35 to treated water deliveries at LA-17. The operational shift increases LADWP's costs by the difference between Metropolitan's Treatment Surcharge and LADWP's own cost of treating SWP supplies and other operational costs. Therefore, these costs would be considered in calculating a credit for LADWP.

Operational Shift Cost-Offset Program (OSCOP)

General terms for the Operational Shift Cost-Offset Program are described in Attachment 1. If made available, OSCOP would be limited to up to $332/AF in CY 2021 and $349/AF in CY 2022. The OSCOP would be offered in CYs 2021 and 2022. Once this period ends, the OSCOP would be evaluated, and adjustments to the program would be considered as needed. Certification and reconciliation procedures would be put in place to allow staff to review the potential costs a given agency may incur (considering also potential avoided costs) in order to calculate whether the change in operations leads to net additional costs. This would form the basis for whether an agency can receive any credit. All water delivered under the OSCOP would be billed at Metropolitan's applicable full-service rate. If cost-offset credits are issued in a given year, Metropolitan would account for the costs as other supply programs. The Chief Financial Officer would account for the costs in the quarterly financial report as budgeted supply program costs.

Initiating Cost-Offset Credits and Reporting

Metropolitan regularly reports to the Board on developing supply and demand conditions through WSDM Plan reports. These monthly reports are provided through the winter and spring. Staff keeps the Board apprised of developing conditions, including the potential use of storage assets and the likelihood of storing or withdrawing supplies. The implementation of the OSCOP in order to reduce deliveries using SWP storage and increase deliveries using the Colorado River storage would be part of this regular reporting process.

To calculate the credit, staff would look at the net additional costs an agency incurs in taking the above actions beyond their normal cost for making operational changes to their system to accommodate Metropolitan's operational changes. The increased costs would be eligible for the credit, up to $5/AF above the Treatment Surcharge.

Summary

The proposed OSCOP would help Metropolitan maximize the current resources available from Colorado River and SWP storage. Offsetting costs for agencies to shift deliveries helps fully utilize our diverse portfolio and increases reliability for the entire region. OSCOP will allow for improved availability of storage reserves to supplement supplies during dry years. This program helps reduce the need for purchasing more expensive transfer supplies. With this delegation of authority to the General Manager, Metropolitan would have additional operational flexibility to decrease deliveries from the SWP side of its system and increase deliveries from the Colorado River part of its system in the current year to increase storage supplies on the SWP for the future.

Policy

Metropolitan Water District Administrative Code Section 11104: Delegation of Responsibilities

Metropolitan Water District Administrative Code Section 4209: Contracts

California Environmental Quality Act (CEQA)

CEQA determination for Option #1:

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 of 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.

CEQA determination for Option #2:

None required

Board Options

Option #1

Authorize the General Manager to enter into agreements to provide a cost-offset credit of up to $332 per AF in CY 2021 and $349 per AF in CY 2022 for net increased costs incurred by a member agency from shifting operations to improve regional reliability, consistent with the terms in **Attachment 1**.

Fiscal Impact: Up to $332 per AF credit to the member agency in CY 2021 and $349/AF in CY 2022. Depending on the operational shifts required, the immediate costs to Metropolitan result in a cost per AF delivered, using Metropolitan's supply programs budget.
Business Analysis: Metropolitan would improve regional reliability by shifting operations to deliver more Colorado River water and reserving its supplies on the SWP. The additional cost to manage such water at an amount not to exceed $332 per AF in CY 2021 and $349 in CY 2022 is reasonable in light of Metropolitan's past average cost of $300 per AF to recover water in its SWP storage programs, north-of-Delta transfers (with costs in the range of $625/AF), and the anticipated unavailability of that water in the near future.

Option #2

Do not authorize the General Manager to enter into agreements to provide a credit for operational shifts.
Fiscal Impact: None
Business Analysis: Not implementing the credit decreases Metropolitan's flexibility in managing supplies for the region and reduces overall regional reliability.

Staff Recommendation

Option #1

Brad Coffey 5/4/2021

Brad Coffey *Date*
Manager, Water Resource Management

5/5/2021

Jeffrey Kightlinger *Date*
General Manager

Attachment 1 –Term Sheet Member Agency Cost-Offset Credits

Ref# wrm12678676

Term Sheet

Operational Shift Cost-Offset Program (OSCOP)

Cost-Offset Credit

- Credit of up to $332 per acre-foot (AF) in calendar year (CY) 2021 and up to $349 per AF in CY 2022 to help offset the estimated additional costs and risks incurred by the agency as a result of voluntary operational changes requested by Metropolitan for the purpose of maximizing Metropolitan's water resources.
- Metropolitan would have sole discretion in determining the eligible costs that would be credited.
- Credit would be based on Metropolitan's requested operation compared to the agency's normal operation. For example, if a member agency shifted deliveries from untreated to treated service connections per Metropolitan's request, the agency's increased cost would be the difference between Metropolitan's Treatment Surcharge and the agency's own cost to treat water. The agency may also incur other costs to implement the change in operation, which could include power or disinfection costs within their distribution system. In this case, Metropolitan would reimburse the agency for these cost increases on a per acre-foot basis, up to the maximum amount described above.
- All components of Metropolitan's full-service water rate, including the Readiness-to-Serve Charge, would be charged at the time the water is delivered. The Capacity Charge will apply, as OSCOP is not intended to change the amount of overall deliveries or the timing of the deliveries, rather just shift location of deliveries. Any operational changes that do affect the Capacity Charge determination, based solely on Metropolitan's request, will be evaluated for the applicability of the Capacity Charge.
- Member agency will be invoiced for water delivered.
- Transactions would be accounted for at the meter level.
- The credit would be applied to the member agency meter invoiced amount and would be subject to reconciliation of the credit amount and the delivery amount. Adjustments to credits could result from reconciliations.

Term

- Metropolitan would enter OSCOP agreements with the member agencies interested in participating in the Program.
    - 2-year program agreement; and
    - The credit would apply only to deliveries made pursuant to the Program.