The workgroup was tasked with and attempted to answer the following:

1. **What are the cost impacts to Poway, Valley Center, and City of San Diego of detachment based on the Hanemann report?**
2. **Do detachment and roll-off have the same impacts?**
3. **Are there any offsets to the cost impacts?**

Baseline reasonable assumptions need to be formulated in order to move forward with an estimate of impacts on the three agencies identified (City of San Diego, Valley Center, and Poway).

The assumptions are:

1. That there is no increase in water sales by the remaining water agencies after a deannaxation to offset any of the lost revenue. This is a reasonable assumption because of recent flat and/or decreasing water sales and the mandatory implementation of new conservation measures required by the state in the next 5 years.

2. That rates will be allocated in the same manner that they are currently allocated by SDCWA. This is a reasonable assumption as it is impossible to predict how future Boards will vote to allocate rates and the current SDCWA Board recently voted to postpone any changes to fixed and variable rate allocation until at least 2024. *(*One subcommittee member noted that SDCWA would likely change its rates if there were a detachment. This is also a reasonable assumption as the SDCWA has a responsibility to ensure its sustainability for the entire region and adequate revenues to protect its financial viability is paramount. This subcommittee does not know what those changes might be and as a future SDCWA board holds rate autonomy, we did not venture to make a guess.)*

3. The Hanemann report is being used as the basis for the numbers and costs.

Estimate of impacts on Poway, Valley Center, and City of San Diego

The best predictor of future cost allocations amongst water agencies from SDCWA is to look at past rolling averages of cost allocations and contributions. Each member agency of SDCWA has a different mix of fixed versus variable rates based on past purchases and also has different customer bases that purchase differing amounts of agricultural or Municipal & Industrial water.

SDCWA's fixed costs vary in allocation time periods from 3 to 10 year rolling averages. A 5 year time period takes into account both high water and low water demand years. (IE, rainy and dry years)

Based on information received from SDCWA in the chart below, Poway has a 5 year contributed asset share of 2.2%, City of San Diego has 37.2% and Valley Center has 4.2%. If none of those agencies significantly roll off of SDCWA in the near future, their cost allocation percentages from SDCWA for the next five years should be similar to the past five years.

	5-year Contributions ($)	% Share (1yr)	% Share (5yr)	% Share (10yr)	% Share (Lifetime)
Carlsbad	$166,400,036	4.9%	4.8%	4.5%	3.7%
Del Mar	$10,665,817	0.3%	0.3%	0.3%	0.3%
Escondido	$101,156,513	3.1%	2.9%	3.3%	3.5%
Fallbrook	$71,558,859	2.1%	2.1%	2.2%	2.2%
Helix	$194,382,714	5.7%	5.6%	5.6%	6.7%
Lakeside	$27,119,110	0.9%	0.8%	0.8%	0.7%
National City (SWA)	$18,966,416	0.5%	0.5%	0.7%	0.7%
Oceanside	$185,318,306	5.3%	5.4%	5.3%	5.2%
Olivenhain	$144,513,295	4.5%	4.2%	4.1%	3.4%
Otay	$275,733,880	8.2%	8.0%	7.7%	6.0%
Padre Dam	$98,251,567	2.9%	2.8%	2.8%	2.7%
Pendleton	$508,056	0.0%	0.0%	0.0%	0.1%
Poway	**$74,690,419**	**2.3%**	**2.2%**	**2.2%**	**2.1%**
Rainbow	$133,246,992	3.9%	3.9%	4.0%	3.9%
Ramona	$44,190,254	1.2%	1.3%	1.3%	1.5%
Rincon	$52,328,006	1.6%	1.5%	1.6%	1.4%
San Diego	**$1,285,972,646**	**35.9%**	**37.2%**	**37.0%**	**39.7%**
San Dieguito	$35,493,779	1.1%	1.0%	1.0%	1.1%
Santa Fe	$58,041,000	1.7%	1.7%	1.6%	1.6%
South Bay (SWA)	$49,983,992	1.4%	1.4%	1.4%	1.9%
Vallecitos	$157,741,869	4.5%	4.6%	4.2%	3.0%
Valley Center	**$146,368,851**	**4.2%**	**4.2%**	**4.6%**	**5.0%**
Vista	$92,909,811	2.7%	2.7%	3.0%	3.0%
Yuima	$33,945,773	1.1%	1.0%	0.8%	0.5%

Of note: Poway's lifetime contributed assets equate to 2.1%, which is only .1% off of its last 5 year average. Valley Center has been purchasing significantly less water over the past 5 years based on its water use profile (heavy agriculture), therefore its 5 year average is .8% less than its lifetime average.)

Dr. Hanemann produced a report that stated that *"The* ***purpose of imposing some financial obligation*** *on FPUD or RMWD if they are permitted to detach from SDCWA is to provide a level of* ***financial protection for SDCWA and the remaining member agencies in the short run while*** *they adjust to the changed financial situation of a detachment." Specifically, Dr. Hanemann included the following calculations in his report for a detachment exit fee with a suggestion of 10 years as a reasonable planning timeline:*

Annual Financial impact of detachment (CY 2022)

Item	FPUD	RMWD	FPUD + RMWD
REDUCTION IN REVENUE			
Without property tax loss	$8,590,141	$24,329,127	$32,919,268
With property tax loss	$8,750,141	$24,519,127	$33,269,268
REDUCTION IN EXPENDITURE			
Short-run	$4,686,300	$16,002,000	$20,688,300
Long-run	$5,047,100	$17,234,000	$22,281,100
CHANGE IN NET REVENUE			
SHORT-RUN			
Without property tax loss	$3,903,841	$8,327,127	$12,230,968
With property tax loss	$4,063,841	$8,517,127	$12,580,968
LONG-RUN			
Without property tax loss	$3,543,041	$7,095,127	$10,638,168
With property tax loss	$3,703,041	$7,285,127	$10,988,168

8

Based on the numbers provided by Dr. Hanemann, a change in net revenue of $12.58 million would happen in the short run if there were no detachment exit fee and both Fallbrook and Rainbow detached. Based on the assumptions above, and assuming SDCWA collected the reduction in revenue from all remaining agencies and water purchases remained somewhat consistent with the past 5 year rolling average, Poway would see an increase of $276,781 per year in the short term; City of San Diego would see $4,654,958; and Valley Center would see $528,400 as its annual increase. All of these are estimates, as no one can predict the exact volume of water each agency will purchase in any given year.

The committee did not delve into what the rates impacts would be for each of the retail ratepayers at the three identified agencies, as every member agency has different cost of service studies based on their customer base (agricultural, industrial, commercial, residential, etc.), meter sizes and different cost tiers for water use. Each retail member agency would need to determine for themselves how they would allocate their annual respective cost impacts noted above to their ratepayers.

The elephant in the room – Are the impacts of detachment and roll off the same?

It is important to note that there is no obligation for any member agency to take any amount of supply from SDCWA. However, a member agency that remains as a member of the SDCWA will still have to pay fixed costs to SDCWA, even if they do not take a drop of water. The elephant in the room is <u>not</u> if detachment and roll off are the same. They are not. The impacts of detachment and roll off are different in that an agency that rolls off will still be a member agency of the SDCWA and will be contributing to future cost increases and rates set by the SDCWA board. A detachment, once completed, means that a member agency is no longer a member agency of SDCWA and will not be contributing to future costs – unless an exit fee is conditioned by LAFCO for a certain time period.

The true elephant in the room is that unless SDCWA reduces (or leverages to others) its fixed take or pay supplies; it will have more fixed take or pay supplies than it will have demand in the next ten years if its member agencies fully develop all of their local supply projects. Dr. Hanemann also noted in his presentation to the LAFCO Detachment Workgroup that there is a "*Financial exposure to reduction in water sales. With current rates, I estimate that for every 1,000 AF less that SDCWA delivers to member agencies, its net revenue falls on average by almost $1M. This is of some concern given that SDCWA is projected to experience a reduction of about 60,000 AF in deliveries to member agencies by around 2030.*" If member agencies roll off to the tune of 60,000 acre feet by 2030 through the development of local supplies, (according to Dr. Hanemann) this will reduce the SDCWA net revenue by $60,000,000. By way of comparison, FY 2022 Net Water Sales Revenue by SDCWA (in its annual budget) is $108,586,236. A loss of $60 million in net revenue is more than half of SDCWA's total current annual net revenue. This is not a sustainable future and does not bode well for future rate affordability. This topic should be explored in depth via the upcoming SDCWA MSR. Any MSR review of SDCWA should also include a review of MWD and its operations and agreements within the SDCWA region.

Is there an offset to Fallbrook and Rainbow for ESP North County Pump Station that was never built? (Need more information.)

Fallbrook and Rainbow assert that there is a cost savings to the remaining member agencies if they detach as the ESP North County Pump Station does not need to be built if they detach. SDCWA asserts that there is no cost savings, as construction of the ESP North County Pump Station is not included in their current budget. Both of these statements are true. However, almost $21 million was identified in the SDCWA 2010/2011 Budget for the ESP North County Pump Station. According to a mid-term budget review, this project was deferred in 2011, however bond documents appear to show inclusion of this project in 2008. If debt was already issued to pay for this project and rates were set accordingly, there should be some costs that are avoided by not having to build this pump station. SDCWA should look at its older documents to identify and address this issue. This was a project included in the CIP (and some funds were spent on design) that set rates and debt issuance over a decade ago to pay for construction this project. Further information is needed to answer this question.