

EXHIBIT “B”

West Basin Municipal Water District  
Water Shortage Allocation Plan  
Outline of Penalty Options

**In order to minimize financial risk, West Basin will collect any over-allocation penalty due to Metropolitan from those customer agencies that collectively contributed to West Basin exceeding its allocation.**

Staff has prepared the following options for the board’s consideration regarding the assessment of customer agency penalties beyond what is owed to Metropolitan, and the potential use of penalty net revenue.

- 1. Assess the same penalty structure and penalty rates employed in Metropolitan’s Water Supply Allocation Plan, to every unit of customer agency usage above individual allocations\*, as follows:**

<b>Usage Above Allocation</b>	<b>Penalty Rate</b>
100% - 115%	1 x Tier 2 (or \$528/AF as of 1/1/09)
Above 115%	3 x Tier 2 (or \$1,584/AF as of 1/1/09)

\* *allocation* is the pre-determined amount of water that a customer agency can use without penalty over a 12-month allocation period for each Stage of the Water Shortage Allocation Plan.

- a. Arguments for:
  - Consistent with Metropolitan penalty structure used to enforce the Allocation Plan throughout southern California
  - Sends strong economic signal to use water more efficiently
  - Net revenue to West Basin can be appropriately applied to revenue shortfalls due to conservation and reliability programs to reduce dependence on imported supplies.
  - Higher penalties will encourage customer agencies to implement tiered retail rate structures to target highest water users
- b. Arguments against:
  - Penalty rates could be considered excessive in addition to already increasing base water rates
  - Potential for economic signal to be less effective if penalty is not understood beforehand, and because penalty will be assessed after the allocation period

- 2. Assess no more than Tier 2 rate to every unit of customer agency usage above individual allocations, unless it is required to meet West Basin’s penalty obligation to Metropolitan.**

## EXHIBIT “B”

Usage Above Allocation	Penalty Rate
Above 100%	Tier 2 (or \$528/AF as of 1/1/09)

- a. Arguments for:
  - Less financial burden on customer agencies and/or consumers while still maintaining an enforcement penalty
  - Higher probability of acceptance among customer agencies
- b. Arguments against:
  - Penalty might not be sufficient to encourage desired behavior in those areas of West Basin most likely to exceed allocation

### **3. Assess no penalty above what is owed Metropolitan.**

- a. Arguments for:
  - No additional financial burden to customer agencies/consumers beyond the rising cost of base water rates
- b. Arguments against:
  - No enforcement mechanism for shortage allocations
  - Not equitable to those customer agencies that are successful in staying within allocations
  - No precedent established for potential future shortage allocations beyond 2009
  - Any unbudgeted financial impact to West Basin of lower sales will be borne solely by base water rates and could potentially impact West Basin’s net revenues and the resulting debt coverage

### Options for Use of Net Penalty Revenue Collected from Customer Agencies

#### **1. Apply towards investments in conservation/education and water reliability projects and programs that benefit the service area as a whole (e.g. recycling, desalination, storage, conservation, etc)**

- At board’s discretion, funds can be used to first cover any West Basin water sales revenue shortfall (less than budget forecast) due to extraordinary conservation efforts.

- a. Arguments for:
  - Entire West Basin service area enjoys a water reliability benefit from recycled water and future desalination, even if physical facilities are not located within customer agency boundaries
  - Relative ease of administration for West Basin; board is sole decision making body
  - West Basin is protected financially from low sales

## EXHIBIT “B”

b. Arguments against:

- Potential perception of penalty structure as revenue-generation mechanism for West Basin programs

**2. To the greatest extent practicable, apply towards investments in conservation/education and water reliability projects and programs within the customer agency (ies) where the penalty is incurred.**

- At board’s discretion, funds can be used to first cover any West Basin water sales revenue shortfall (less than budget forecast) due to extraordinary conservation efforts.

a. Arguments for:

- Penalties may be more readily accepted if funds are applied towards projects that provide a direct benefit to the consumers within that customer agency
- Consistent with Metropolitan’s policy for use of penalty funds, as adopted by their board in February 2008
- Funds to be concentrated where most needed to reduce future demand on imported water
- Increases follow-up outreach opportunities in areas where conservation should be enhanced

b. Arguments against:

- Potential for the economic signal to conserve to be less effective because penalties paid by an agency would in effect be returned to the agency
- More difficult for West Basin to administer/implement
- Conservation/education only option in many parts of service area; West Basin may not have sufficient staff resources to implement
- Customers may not appreciate that their penalty may far exceed the costs necessary to support the customer agency program costs which could result in West Basin recognizing the balance into net revenues.

**3. Apply 25% of net revenues to conservation programs within the customer agency (ies) of origin, and the balance towards investments in water reliability projects and programs that have a regional benefit.**

- At board’s discretion, funds can be used to first cover any West Basin water sales revenue shortfall (less than budget forecast) due to extraordinary conservation efforts

a. Arguments for:

## EXHIBIT “B”

- Provides a compromise and dual benefit to areas where no physical recycled water infrastructure is located
- Reduces potential objections by customer agencies

b. Arguments against:

- More difficult for West Basin to administer/implement

### **Preferred Penalty Option**

#### Options for Use of Net Penalty Revenue Collected from Customer Agencies

- 1. Apply towards investments in conservation/education and water reliability projects and programs that benefit the service area as a whole (e.g. recycling, desalination, storage, conservation, etc)**
  - At board’s discretion, funds can be used to first cover any West Basin water sales revenue shortfall (less than budget forecast) due to extraordinary conservation efforts.