

Agenda Item: 10
Meeting Date: May 13, 2004

California Bay-Delta Public Advisory Committee

Draft Finance Options Report

Summary: Authority staff will provide a review of the Draft Finance Options Report, summarizing some of the key findings.

Recommended Action: This is an informational item only. No action will be taken.

Background

BDPAC and the Authority have directed staff to develop a comprehensive Long-Term Finance Options Report. A technical team of consultants working with Authority staff is responsible for drafting the Finance Options Report which is the culmination of a year-long effort. As part of this effort, Authority staff has established an eight-member Independent Review Panel with broad expertise in public financing. An Ad Hoc Work Group consisting of stakeholders and implementing agency staff is reviewing and providing input to the Authority staff and the Technical Team on the approach and analysis of finance issues and options. The Ad Hoc Work Group was formed by nominations from the BDPAC Steering Committee. A list of all participants is attached (Attachment 1).

The Technical Team has undertaken an analysis that focused on development of the following key materials:

- **Summary of CALFED Finance Planning Efforts and Next Steps.** This document, produced in March 2003, provides an overview of past financing efforts related to the CALFED Bay-Delta Program and suggests likely next steps in developing a Program-wide finance plan.
- **Framework and Issues Report.** This document, finalized in October 2003, provides both a preliminary outline of the proposed general framework to be used to develop finance options and a summary of overarching finance issues identified by program managers, stakeholders and others. It also identifies several guiding principles for allocating CALFED Program costs among the public, water users, and other Program beneficiaries.

- **Finance Options Report.** The Finance Options Report provides the results of the Technical Team's analysis of each Program element's finance options, presents cross-cutting findings and suggests next steps for moving forward. This report is intended to serve as the foundation for ongoing Authority discussions related to long-term finance.

Schedule

A Draft Finance Options Report is scheduled to be available on May 10. Copies of the report will be on the CALFED Program website and hard copies will be provided at the May BDPAC meeting. At the May meeting, the Authority staff will provide an overview of the Draft Report and summarize some of the key findings. Additional public comment on the Draft Report is expected at the BDPAC subcommittee meetings throughout June. The final Independent Review Panel meeting is scheduled for May 18. The Panel's primary deliverable is a final written report, which is to include a critique of the staff analysis of the report. As feasible and appropriate, a final written Panel report may also include specific Panel recommendations regarding a preferred approach and/or next steps for structuring and implementing a finance plan. The Authority staff intends to use the Panel's report to inform its development of a final Finance Options Report for subsequent consideration by the appropriate advisory and decision-making authorities. The Finance Options Report is scheduled to be finalized at the August Authority meeting.

Draft Findings

The Draft Finance Options Report offers an element-by-element analysis of the possible options for financing the CALFED Program. The Draft Report:

- Provides a description of the long-term costs and describes the benefits and likely beneficiaries for each program element
- Explores new revenue sources and finance approaches as well as identifying potential funding constraints
- Develops information on public and water user benefits of the program to better guide priorities for limited public/private funds

Some of the Draft Report findings include:

- ***Wide range in potential cost of CALFED Program.*** The Draft Report identifies CALFED Program average costs at between \$500 million and \$1 billion per year. The wide cost range reflects substantial uncertainty over individual Program elements and total CALFED Program costs. Some of the uncertainties will be resolved once engineering feasibility studies are completed; and some will be resolved once questions about Program scale and scope are addressed. Overall cost accounting for the CALFED Program is greatly complicated by the substantial amount of local investments that potentially contribute to CALFED objectives. Program cost estimates will need to be continually updated as better data becomes available.

- ***Benefits-based analysis offers mixed potential.*** The Draft Report suggests that a benefits-based analysis offers mixed potential for crafting a stable funding picture. While the beneficiary pays principle seems intuitive and attractive, it is not currently possible to implement a purely benefits-based cost allocation in some areas, and may be cost prohibitive for several programs into the foreseeable future. There are simply too many unknowns. Still, this shortage of quantitative economic data does not mean that the Program must be implemented solely with public funds. In fact, the analysis was able to characterize, and in many cases quantify, benefits for a broad range of identifiable beneficiary groups beyond the general public. Not surprisingly, most of the benefits that are measurable now, or could be measured in the near-term, are associated with water supply, water quality, and flood control. The benefit categories that are more problematic primarily involve those produced from ecosystem improvements.
- ***Divergent views about environmental mitigation responsibilities.*** The analysis crystallized the many perspectives stakeholders have regarding the accounting of environmental mitigation responsibilities. For example, there are differing views surrounding the Ecosystem Restoration Program (ERP) and the baseline (point in time) by which to measure the benefits the ERP generates. Some stakeholders view the ERP as producing current and future benefits that accrue to both the general public and water users. Others view the ERP as mitigation for past infringement of rights (pre-CALFED's Record of Decision) that should be paid by those that caused the impacts. There is no economic test to resolve this disagreement. The Draft Report's approach is to characterize Program benefits according to these different views and to illustrate their implications for allocating Program costs. This approach results in two different allocations: one that shifts greater responsibility to the public ("public emphasis"); and a second that places a greater burden on water users ("user emphasis").
- ***Significant potential to broaden funding sources.*** While there is not sufficient quantitative economic data to develop purely benefits-based cost allocations, there is convincing evidence to begin framing options for broadening the revenue sources for many program elements. Regardless of whether the analysis emphasizes public or user funding, there appears to be a sound rationale for considering shifting and expanding the funding base for CALFED Program activities.
- ***Variety of finance tools available.*** The analysis suggests the Authority can and likely would need to draw on a combination of finance tools to fund the Program's many activities. This could include a blend of annual appropriations from State and Federal governments, debt financing, increased charges for CVP/SWP charges, new State-administered fees, and ongoing local contributions. Each tool offers advantages and drawbacks, and policymakers would need to work with affected stakeholder communities to find a combination that offers a supportable and stable source of funding.

- ***Strategies for prioritizing public funds.*** It is clear from the analysis that the public--and the California public in particular--is likely to continue playing a major role in financing the CALFED Program. Given the likelihood of ongoing budget constraints, the State needs pragmatic and sound strategies for prioritizing competing funding demands. In reviewing the full complement of Program elements and components, the Draft Report suggests that public dollars may be most wisely invested in the following areas: (1) program actions with highly uncertain or very diffuse benefits to specific user groups; (2) program actions generating broad public goods such as environmental restoration; and (3) program actions that catalyze local investment in new water management approaches and technology.

List of Attachments

Attachment 1 – List of Finance Plan Participants

Attachment 2 – Independent Review Panel Biographical Sketches

Contact

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Agenda Item: 10
Meeting Date: May 13, 2004

KEY FINANCE PLAN PARTICIPANTS

Independent Review Panel

David Abel, President, Abel & Associates
David Dowall, Professor, U.C. Berkeley (Chair)
Frederick Furlong, Federal Reserve Bank
Michael Hanemann, Professor, U.C. Berkeley
Wendy Illingworth, Consultant, Economic Insights
Dean Mischynski, Director, California Research Bureau
Daniel Sumner, Professor, U.C. Davis
Dennis Wichelns, Professor, C.S.U. Fresno

Ad Hoc Stakeholder and Implementing Agency Work Group

Don Bransford, GCID
Tina Cannon, Department of Fish and Game
Mark Cowin, Department of Water Resources
Greg Gartrell, Contra Costa Water Agency
Joe Grindstaff, Santa Ana Watershed Project Authority
David Guy, Northern California Water Association
Steve Hall, Association of CA Water Agencies
Ann Hayden, Environmental Defense
Robert Meacher, Plumas County Supervisor, RCRC
Jerry Meral, Planning and Conservation League Foundation
Barry Nelson, Natural Resources Defense Council
Dan Nelson, SLDMWA
Mark Newton, Legislative Analyst's Office
Lowell Ploss, SJR Group Authority
Tim Quinn, MWD
Frances Spivy-Weber, Mono Lake Committee
Jerry Toenyes, Northern California Power Agency
Doug Wallace, East Bay MUD
Brent Walthall, Kern County Water Agency
Tom Zuckerman, Delta landowner

Technical Team – California Bay-Delta Authority Staff and Consultants

Kate Hansel, Assistant Director, California Bay-Delta Authority
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David Mitchell, M-Cubed
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Roger Mann, RMEcon
Ken Kirby, Indep. Consultant
David Kracman, Schlumberger
Loren Botoroff, Independent. Consultant
Bennett Brooks, CONCUR

Agenda Item: 10
Meeting Date: May 13, 2004

INDEPENDENT REVIEW PANEL

Biographical Sketches

David Dowall (Panel Chair) is a Professor of City and Regional Planning at the University of California, Berkeley. He is a Visiting Fellow of the Public Policy Institute of California. Dowall is a leading expert in urban economics and infrastructure policy and frequently consults for the World Bank, Asian Development Bank, United Nations Development Programme, and U.S. Agency for International Development. He has served as policy advisor to local and central governments and businesses in over 40 countries. He has authored several books including his more recent book Making Room for the Future: Rebuilding California's Infrastructure. He holds a B.S. in economics from University of Maryland and both a master's degree in urban and regional planning and a Ph.D in economics from University of Colorado.

David Abel is President and CEO of a California-based Public Affairs Consulting Firm, ABL, Incorporated, engaged in public policy, affordable housing development, transportation, and civic affairs. The firm also publishes two widely respected newsletters: "*The Planning Report*" which covers land-use and the "*Metro Investment Report*" which covers public infrastructure investment. Mr. Abel is also Chair of the LA Area Chamber Transportation, Water and Infrastructure Committee, and is a Lecturer in UCSD's Urban Studies Department, as well as both a Senior Fellow at Occidental College's International & Public Affairs Center and the Chair of USC's School of Public Policy's Overseers Board. In addition to his law & education degrees, his educational background includes an undergraduate degree in economics at the London School of Economics, and a master's degree in Urban Studies.

Frederick T. Furlong is vice president in charge of the Financial and Regional Research Studies Section of the Economic Research Department at the Federal Reserve Bank of San Francisco. Furlong came to the Reserve Bank in 1983 after serving five years as an economist at the Board of Governors of the Federal Reserve System in Washington, D.C. While at the Bank, Furlong has written extensively in the areas of banking, financial markets and monetary policy. He currently serves as a member of the Bay Area Council and Bay Area Economic Forum. After earning a bachelor's degree in science at St. Mary's College of California, Furlong received master's and Ph.D. degrees in economics at the University of California at Los Angeles.

W. Michael Hanemann serves as the Chancellor's Professor in the Department of Agricultural and Resource Economics and in the Goldman School of Public Policy at the University of California, Berkeley. Hanemann's research interests include non-market valuation, environmental economics and policy, water pricing and management, demand modeling for market research and policy design, the economics of irreversibility and adaptive management, and welfare economics. Hanemann is a member of the Environmental Economics Advisory Committee of USEPA's Science Advisory Board, and a member of the BDPAC Drinking Water Quality Subcommittee. He is the author of

Urban Water Demand Management and Planning and other publications on urban water financing. His work has appeared in *AER*, *Econometrica*, *JEEM*, *AJAE*, and elsewhere. Hanemann holds a master's degree from the London School of Economics, and both a masters in Public Finance and Decision Theory and Ph.D in economics from Harvard University.

Wendy Illingworth is founder and principal of Economic Insights, an economic consulting firm. She specializes in resource and regional economics, with expertise in the economic and financial aspects of water supply and pricing issues. She has had approximately twenty-five years' experience in resource planning, rate and economic impact issues for water and electric utilities. The last fifteen years of her experience has concentrated on issues related to California water supplies. Her work has focused on areas of economic and financial impacts of alternative supply strategies, economic impacts of proposed projects or regulations, rate design. Illingworth received her undergraduate and graduate degrees in economics from the University of Arizona.

Dean Misczynski is founding director of the California Research Bureau in the California State Library. The Bureau, begun 1991 and modeled on the Library of Congress' Congressional Research Service, provides policy research services to both houses of the California Legislature and the Governor's Office. Misczynski worked for California's Senate for several years, where he drafted the Mello-Roos Act, the Infrastructure Financing District Act (which allows limited tax increment financing for infrastructure to serve new development) and other local financing legislation. He also served as deputy director of the state's Office of Planning and Research. Misczynski's graduate and undergraduate education were at Stanford in economics.

Daniel A. Sumner is Director of the University of California Agricultural Issues Center and the Frank H. Buck, Jr., Professor, Department of Agriculture and Resource Economics, University of California, Davis. Sumner spent several years as a senior economist at the President's Council of Economics Advisers and at the United States Department of Agriculture, where he served as Assistant Secretary for Economics in 1992 and early 1993. Sumner is the author of numerous professional articles, chapters and reports and the author, coauthor or editor of 10 books. Sumner is a graduate of California State Polytechnic University in agricultural management. He has a master's degree from Michigan State and a Ph.D. in economics from the University of Chicago.

Dennis Wichelns is Chief Economist with the California Water Institute and Professor of Agricultural Economics, at the California State University, Fresno. Since 1985, Wichelns has maintained an active program of research and consulting activities in California, with particular emphasis on irrigation and drainage issues in the San Joaquin Valley. His current research includes analysis of water supply and demand issues in California, transboundary competition for water resources, and the special role that improvements in water management can play in reducing poverty, improving environmental quality, and enhancing food security. He has degrees in Agricultural Economics from the Univ. of Maryland and the University of California, Davis.