

Chapter VII

CONCLUSIONS AND RECOMMENDATIONS

This study was undertaken to comply with the requirements of P.L. 99-546 and to respond to a recommendation by the GAO to consider a more streamlined method to allocate joint costs of the CVP. It reviewed a number of alternative allocation methods; developed, analyzed and compared in detail the allocation of CVP plant-in-service costs for two alternative methods to the existing allocation; and selected a recommended alternative. Early in the study, the existing allocation was reviewed and revised to assure consistency and compliance with legislation, policies, and agreements. In addition, a new spreadsheet was developed to streamline the annual update of the allocation of CVP plant-in-service costs. Subsequently, two alternative allocation methods were developed – a Proportional Alternative and Contractors’ Proposal. For each alternative, costs were allocated to project purposes and repayment responsibilities for irrigation water users, M&I water users, and commercial power customers were calculated.

To date, the total cost of CVP plant-in-service facilities is approximately \$3,290 million (1999 CVP interim cost allocation annual update). This amount represents total non-indexed costs incurred since construction of CVP facilities began. As noted in Chapter I, since costs specific to one project purpose, such as irrigation, are allocated to the purpose served, the central challenge of the allocation process is the allocation of joint costs – the costs of facilities serving more than one purpose; these amount to a total of about \$623 million (about 19 percent of total CVP plant-in-service costs). With the exception of the Tehama-Colusa Canal and associated fish facilities, the joint costs of the CVP are associated principally with storage facilities that were authorized and constructed from the late 1930s through the mid-1960s. Since that time, facilities constructed by Reclamation have been either single purpose with their costs allocated to the purpose for which the facilities were constructed or the facilities have had the allocation of their costs established by

authorizing legislation. Facilities constructed by the COE and integrated into the CVP have had their costs allocated by the COE. As the total plant-in-service investment has continued to rise with the addition of new features, the joint costs subject to allocation by Reclamation have become a smaller proportion of total project costs. Consequently, the effect of a change in the allocation of these joint costs, regardless of the percentages used, is lessened by both the magnitude of specific costs and the many repayment requirements that are not subject to change.

Evaluation and comparison of the alternatives required development of study-specific evaluation criteria because the circumstances involved in this cost allocation study differ from those typically encountered in cost allocation studies conducted during project planning and development. In planning studies, no allocation exists, and the problem is that of developing one, including choice of the appropriate allocation method. For this study, an allocation does exist so that the relevant question is whether one or both of the additional alternative allocation methods considered have characteristics that provide a compelling reason to change the existing method.

Evaluation criteria were formulated to address that question. Application of the criteria determined which alternatives met the basic requirements for an interim cost allocation and highlighted differences between the existing allocation method and the alternatives.

CONCLUSIONS

As described in detail in Chapter VI, the conclusion of this evaluation process is that neither the Proportional Alternative nor the Contractors' Proposal contains characteristics that support their selection as an interim cost allocation. The principal reasons supporting this selection are summarized below (for more detail, refer to Chapter VI).

Proportional Alternative

The Proportional Alternative would allocate joint costs in proportion to specific costs incurred for each project purpose in a manner similar to the distribution of joint, or overhead, costs by a private firm producing multiple products. This approach would not allocate joint costs in relation to benefits provided by the project. Another serious shortcoming of the Proportional Alternative is that future additions of single-purpose facilities, the costs of which are specific, would alter the allocation of costs for all existing facilities with joint costs even if the benefits derived from the facilities with joint costs did not change.

Contractors' Proposal

The Contractors' Proposal would allocate joint costs based on a determination of project benefits, but would utilize an older estimate of benefits than the Existing Allocation and would introduce the environment as a new water use. This alternative would replace the 1975 joint cost allocation factors used in the Existing Allocation with factors calculated in 1970. This change would be based primarily on the claims that the cost of the single-purpose power alternative in 1975 was biased by high energy costs at the time and that flood control benefits were understated because previous COE flood control benefit estimates were not indexed to then-current levels in the 1975 study. High energy costs were symptomatic of the period, and short of a new study, it is not clear there is a compelling reason for change. The COE flood control benefits were not indexed as a result of the recommendation by the COE, which appears, in this evaluation, to have been reasonable (for more detail, refer to Chapter VI).

In addition, the Contractors' Proposal would add the environment as a water use for the purpose

of calculating repayment responsibilities for costs allocated to the water supply purpose. The amount of environmental water would be based on the amount of water dedicated annually by section 3406(b)(2) of the CVPIA to restore fish and wildlife habitats and would be treated as an additional CVP water supply. Ultimately, according to the proposal, the amount of environmental water would build to 800,000 acre-feet per year. The Contractors' Proposal assumes that some of the costs associated with this water would be reimbursable, representing environmental mitigation, while the remainder, representing enhancement, would be non-reimbursable. As discussed in Chapter VI, the CVPIA does not indicate that any CVP costs are to be reallocated as a result this dedication of water and does not state that any of the dedicated water is for habitat enhancement purposes. In fact, the CVPIA includes provisions to acquire water through water purchases using the Restoration Fund in addition to the 800,000 acre-feet to help fulfill remaining mitigation, protection, and restoration needs and to enhance aquatic and wetland habitats. Furthermore, environmental water released from CVP reservoirs for instream environmental benefits could also be used downstream for other beneficial purposes, including irrigation or M&I uses, farther downstream. In such cases, the Contractors' Proposal could double count the use of water. Finally, the history of Federal legislation and SWRCB decisions clearly shows that maintaining environmental conditions is a requirement of the project and that water rights, including CVP water rights, are contingent upon meeting certain environmental priorities. Consequently, the Contractors' Proposal is not consistent with existing Reclamation guidance on allocating costs, nor with provisions of Federal Reclamation law and State water rights decisions.

RECOMMENDATIONS

Neither the Proportional Alternative nor the Contractors' Proposal includes characteristics that provide compelling reasons to change the existing allocation method. Accordingly, the Existing Allocation is selected as the recommended allocation alternative.

In the course of this study, alternatives to the

Existing Allocation were considered through detailed analysis of the two allocation methods and initial consideration of other potential allocation methods. These evaluations have led to the following two additional recommendations. First, joint costs should continue to be allocated using a benefits-based method. Since 1956, the joint costs of the CVP have been allocated using the SCRIB method, which is a benefits-based method. This method is the established method for Federal water resources agencies to allocate costs and is incorporated in Reclamation directives. For the CVP, the SCRIB method has been accepted as the basis for setting water rates for many decades, and the procedure for allocating the costs of existing and new project features has been incorporated into the expectations of water users. The SCRIB method

should continue to be employed as annual and other adjustments are made to the CVP cost allocation and should be the method used if any major new cost allocation study is performed.

Second, Reclamation should consider the requirements to complete a new cost reallocation study using the SCRIB method and an interim allocation of CVP costs based on new estimates of project accomplishments – including water supply, flood control, power, and fish and wildlife – benefits, and costs. It is expected that such a study would be time consuming and potentially costly. Therefore, before such a study were undertaken, an evaluation should be completed to identify what existing data are available for use, what new data would be required, and the levels of effort needed to develop new data and perform the analyses required for a new cost allocation study and how present benefits and costs would be integrated with former estimates of benefits and costs and contractor repayment. This evaluation would include coordination with other agencies that would be expected to provide input to a new allocation study – such as the COE and Service – to determine their ability and willingness to participate in it.