NCPA Power Management and Administrative Cost Allocation Review Group – Issue 7: Revenue Allocation

NCPA Facilities Committee

November 2, 2016

Purpose

- Update the Facilities Committee on the Review Group’s recommendations and discussions related to its Issue #7—Revenue Allocation

Content

- Introduction
- Broad recommendations
  - Use the Nexant model to allocate revenues
  - Use 2 threshold tests to determine eligibility for revenues
  - Address transition issues with new Members
- Specific Applications
  - Toward unfunded personnel-related costs
  - Toward Agency Administrative & General Expenses
  - Toward Facilities that have non-Member Participants
- Summary and Conclusion
- Supporting Materials

Introduction

- In May 2015, the NCPA Commission
  - Referred the review of the Power Management and Administrative Services cost allocation methodologies and principles to the Facilities Committee; and
  - Directed the FC to coordinate a review Group to carry out these actions
- The Review Group identified 7 issues to analyze
- Issue #7 explores a number of factors to consider when NCPA allocates revenue
- The Review Group met 4 times on this topic
- White Paper captures detailed discussion

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The Review Group recommends using the Nexant model to allocate revenues

- Most accurate way to map revenues to specific services and functions that produce the revenue (*causation, and comparable treatment*)
- Reflects existing Members' investments in those same services and functions (*equitable allocation of costs and revenues*)
- It is objective and auditable (*transparency*)
- There is little to no additional work to implement use of the Nexant model for this purpose (*simplicity*)
- The model is flexible enough to deal with significant changes in industry and the organization (*durability*)

Membership status should be the first threshold test

- Recommendation: Membership required to be eligible for allocation of revenue
  - Some possible exceptions discussed later

- Rationale:
  - Membership should have its privileges
  - Creates clear threshold test
  - Value proposition for prospective and existing Membership
  - Reflects Members' long-standing commitments and investments in NCPA

Pricing structure under which services are provided should be a second threshold test

- Recommendation: Allocate revenues to those Members that take service under a variable-rate structure, or portion thereof.

- Rationale:
  - Today's Members face full price risk under the existing variable-rate pricing structure
  - Some Members have sought fixed-rate pricing structures avoiding this same risk
  - Revenues should be used as a means of affecting price reductions, but only to those who face price risk

The Review Group recommends a transitional treatment for New Members

- Recommendation: Use historic (lagged) data when allocating new revenue (e.g. previous year's Nexant model)

- Rationale:
  - Some recognition toward legacy Members' past investments in NCPA

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Review Group supports using revenues for unfunded liabilities, at Members' direction

- NCPA Commission approved a long-term funding plan to address unfunded personnel costs
- A component of the plan was to explore using new revenues toward those costs

- The Review Group supports this general notion, with the following additional considerations:
  - Separately allocate revenues/obligations to Members
  - Allow Members to direct the use of allocated revenues toward the respective Members' allocated share of obligations

Review Group supports using revenues for Agency A&G if the policy is applied broadly

- Concept: allocate a portion of new revenue to Agency Administrative & General expenses
- Review Group supports this concept if both:
  - The policy is applied consistently to any new revenues produced by NCPA programs (*comparable treatment)*
  - The proportion that is allocated toward Agency A&G is representative of the time and duration that effort is expended by the A&G functions in producing the new revenue (*causation*)

Review Group did not unanimously agree on non-Member Project Participants

- Review Group favors (4:1) a position that would allow revenue allocation to the entire Project, including non-Member Participants
  - Recall, overarching recommendation is to use the Nexant Model to allocate revenue
  - In favor: Alameda, Plumas, Roseville, SVP
- Alternate position would allow revenue allocation to the portion of the Project with Member interest and exclude the portion of non-Member interest
  - In favor: Palo Alto

This component of the policy decision will affect LEC and Geothermal Participants

- NCPA General counsel opines that NCPA is not contractually obligated to allocate revenues to projects
- LEC
  - 13 Participants in total
  - 4 non-Member Participants
  - Non-Member represent approximately 50% of total
- Geothermal
  - 11 Participants in total
  - 1 non-Member Participant
  - Non-Member represent approximately 6% of total

The Review Group offers its best points for each position for your consideration

Members-only

- Clear benefit to Membership
- No contractual obligation
- No expectation of revenue allocation at the time of contract execution
- Slippery slope: future projects?
- Better reflects Members' historic investments

Project-wide

- Non-member Participants accepted substantial risks/liabilities for the life of the project
- Commensurate with Members' risks
- Variable-rate pricing structure
- Needed non-Member participation to reach scale

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The Review Group offers the following recommendations to the FC

- Use the Nexant model to allocate revenues
- Use threshold tests to determine eligibility for revenues:
  - Membership Status
  - Pricing structure (i.e. variable vs. fixed)
- Address transition issues with new Membership
- Use revenues toward unfunded personnel-related costs, under Members’ individual direction
- Allocation a portion of revenue toward Agency A&G costs, provided that the policy is applied broadly and represents work & effort in business development

The Review Group offers the following discussion item to the FC

- The group did not reach a unanimous position on allocations of revenue to NCPA Projects that includes non-Member participants.
- Key question: should NCPA allocate revenues, via the Nexant model, to the entire Facility, which by extension allocates revenues to non-Members?
- The Review Group offers its main arguments to two positions.

DISCUSSION

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Representative Example: Nexant Model

	Baseline [2]	Allocation of Costs & Revenues [3]					Totals	
	FY 2017 Power Mgmt Total Pwr Mgmt Base Line	PCWA	Merced Irrigation District	City of Shasta Lake [4]	Marin Clean Energy [5]	City of Roseville [5]	Total Share of Revenues	Net Allocated Costs
Alameda	$930,043	($31,088)	($30,818)	($17,222)	($30,087)	($84,719)	($193,934)	$736,109
BART	$733,786	($5,956)	($18,094)	$19,397	($39,245)	($75,500)	($119,399)	$614,387
Biggs	$51,828	($885)	($1,248)	($1,462)	($17,236)	($5,338)	($26,168)	$25,660
Gridley	$84,433	($1,581)	($2,393)	($1,906)	($15,688)	($6,490)	($28,058)	$56,375
Healdsburg	$178,545	($5,189)	($5,517)	($3,657)	($11,586)	($16,905)	($42,854)	$135,691
Lodi	$1,014,445	($25,949)	($30,148)	($20,864)	($105,290)	($87,458)	($269,710)	$744,735
Lompoc	$278,132	($7,187)	($8,170)	($6,329)	($26,739)	($25,441)	($73,865)	$204,266
Palo Alto	$1,638,424	($35,865)	($51,299)	($34,026)	($226,128)	($131,422)	($478,740)	$1,159,684
Plumas Sierra	$325,799	($8,244)	($9,628)	($7,258)	($50,603)	($33,766)	($109,500)	$216,299
Port of Oakland	$324,169	($4,202)	($7,303)	($11,550)	($36,223)	($27,340)	($86,618)	$237,551
Roseville	$455,313	($22,271)	($21,657)	($16,720)	($38,257)	$0	($98,904)	$356,409
Santa Clara	$3,178,163	($174,038)	($132,945)	($111,132)	($472,026)	($286,683)	($1,176,824)	$2,001,340
Truckee-Donner	$0	$0	($0)	($0)	($0)	($0)	($0)	($0)
TID	$147,523	($6,874)	($6,972)	($7,099)	($7,588)	($11,296)	($39,829)	$107,694
Ukiah	$380,550	($9,317)	($11,108)	($8,042)	($87,261)	($29,543)	($145,271)	$235,279
LEC	$1,203,438	($68,534)	($52,564)	($114,668)	($111,953)	($128,099)	($475,817)	$727,621
Totals	$0	$407,181	$389,864	$342,538	$1,275,910	$950,000	($3,365,493)	$7,559,100

Representative Example: metrics & footnotes

	Totals		Metrics	
	Total Share of Revenues	Net Allocated Costs	Member Proportion of Baseline Cost	Member Proportion of Revenues
Alameda	($193,934)	$736,109	8.51%	5.76%
BART	($119,399)	$614,387	6.72%	3.55%
Biggs	($26,168)	$25,660	0.47%	0.78%
Gridley	($28,058)	$56,375	0.77%	0.83%
Healdsburg	($42,854)	$135,691	1.63%	1.27%
Lodi	($269,710)	$744,735	9.29%	8.01%
Lompoc	($73,865)	$204,266	2.55%	2.19%
Palo Alto	($478,740)	$1,159,684	15.00%	14.22%
Plumas Sierra	($109,500)	$216,299	2.98%	3.25%
Port of Oakland	($86,618)	$237,551	2.97%	2.57%
Roseville	($98,904)	$356,409	4.17%	2.94%
Santa Clara	($1,176,824)	$2,001,340	29.09%	34.97%
Truckee-Donner	($0)	($0)	0.00%	0.00%
TID	($39,829)	$107,694	1.35%	1.18%
Ukiah	($145,271)	$235,279	3.48%	4.32%
LEC	($475,817)	$727,621	11.02%	14.14%
Totals	($3,365,493)	$7,559,100	100.00%	100.00%

Footnotes:

1. Total gross value of the Power Management service contract in its first year.
2. Price quotes and subsequent allocation of service contract revenues were prepared in separate iterations of the Nexant cost allocation model.
3. As calculated in the specific price quote.
4. The price quote for the City of Shasta Lake does not incorporate any revenues CSL may be entitled to as a Member of NCPA (i.e. from expansion of PM services).
5. Marin and Roseville figures are provided to illustrate how the allocation of revenue can change depending on the services provided.

List of Methods Considered by the Review Group

- Existing Nexant model
- Uniform allocation (i.e. 1/n)
- JPA percentages (i.e. load)
- Peak demand (MW) for a defined period of time
- Contribution to NCPA budgeted costs
- Hybrid 1:
  - Portion via uniform allocation
  - Balance via Nexant model
- Hybrid 2:
  - Portion to a business development fund
  - Balance via Nexant model