

Financial Capability for the Cost of Clean: A Call for Portfolio Management



**Eric Rothstein, CPA
Vice President
CH2M HILL**

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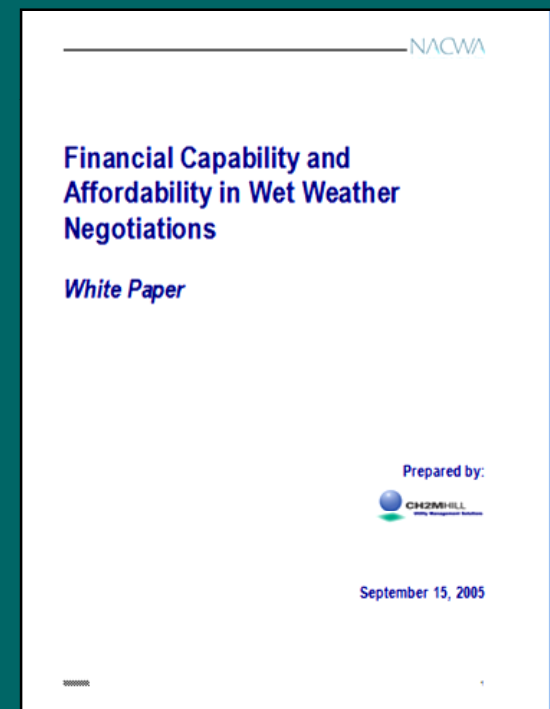


Presentation Outline

- Status of Financial Capability Assessment in Clean Water Act enforcement
 - ⊙ Problems with FCA methodology
 - ⊙ Problems with enforcement practices and permittee responses
- NACWA Guiding Principles
- Portfolio management framework

Status of Financial Capability Assessments in CWA Enforcement

- Financial capability being placed as a central consideration (by permittees) in negotiations
- Inadequacies of current FCA methodology and regulatory response are recognized
- Opportunity to broaden consideration of issues consistent with evolution of EPA's regulatory framework



Problems with consideration of financial impacts in enforcement

- Absence of financial planning and appropriate provision for capital financing
- Focus on Median Household Income (MHI)
- Exclusion of other “water” and asset management costs
- No framework for consideration of additional, site specific, factors’

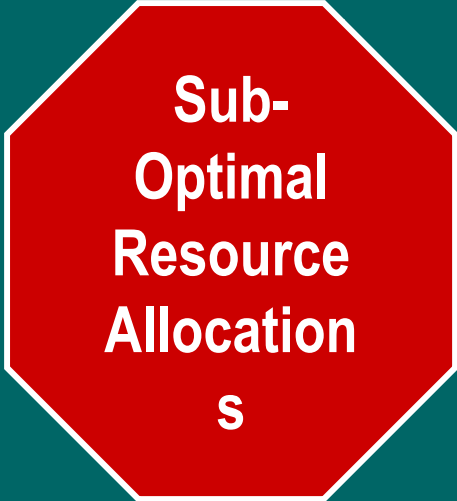
No major metropolitan permittee has a ‘high burden’ per EPA

Ineffective regulation

Several permittees have developed CIPs with schedules > 20 years

Problems with enforcement practices and permittee responses

- Enforcement practices
 - ⊙ Myopic allegiance to prescriptive formulas of FCA guidance
 - ⊙ Pursuit of implementation commitments without assessment of costs or financial capabilities
 - ⊙ Separate, uncoordinated actions on individual provisions of CWA
- Permittee responses
 - ⊙ Deferred implementation of high return projects to obtain regulator consensus
 - Protracted negotiations
 - Scheduling based on focus of regulators' actions
 - ⊙ Inadequate asset management based reinvestment to manage risks
 - ⊙ Limited independent redress of local conditions (e.g. affordability programs)



Sub-
Optimal
Resource
Allocation
S

NACWA Guiding Principles

- **Economic Capability**
 - ⊙ First consideration must be the community's economic situation
 - ⊙ Economic capability must be assessed in light of other investments and potential environmental benefit.
 - ⊙ Improvements should mitigate potential adverse impact of their cost on distressed populations.
- **Program Scope and Timetable**
 - ⊙ Scope and implementation schedule must be tailored to community's unique financial condition.
 - ⊙ Considering financial capability in light of other investment demands and potential benefits ensures greatest water quality improvement at the earliest possible time.

NACWA Guiding Principles – Highlights

- **Economic Capability**
 - ⊙ Prescriptive formulas alone don't work
 - ⊙ Local conditions are the primary factors in determining economic capability.
 - ⊙ Holistic view of environmental investment
 - ⊙ Fiduciary obligations to maximize benefit
- **Program Scope and Timetable**
 - ⊙ Maximize water quality benefit while maintaining a healthy economic balance for the community.
 - ⊙ Appropriate pace of environmental investments cannot be prescribed (e.g., 20 years)
 - There is no legislative limitation on extended implementation schedules.

Implications of NACWA Guiding Principles

- Negotiation Implications
 - ⊙ Program schedules cannot be prescribed (e.g., 20 years)
 - Must reflect community capabilities & investment alternatives.
 - ⊙ No legislative limitation on schedules
- Policy Implications
 - ⊙ Consideration of financial capability given other investment demands and potential environmental benefits requires a new analytical framework



Portfolio Management

DRAFT

Portfolio Management Framework

Optimize Community Water Quality Investments

Household Financial Impacts

Wt

Median Household Income

Shelter Costs

Water, Wastewater, Stormwater Rates

State / Local Tax Structure

Community Financial Impacts

Wt

Historical Water Quality Investment

Non W.Q. Environmental Investments

Economic / Population Trends

Financial Health Indicators

Environmental Justice Impact

Wt

Low Income Ratepayer %

Localized Construction Disruptions

Specific Community Impacts

Rental / Tenant Impacts

Program Delivery Impact

Wt

WQ Infrastructure Market Saturation

Program Management

Attributes of **draft** portfolio management framework

- Recognizes local factors using disciplined (conceptually simple) scoring and ranking
 - Explicit recognition of environmental justice and program delivery issues
 - Structured framework consistent with NACWA guiding principles
- Weighting factors & performance scales may be used by negotiating parties to tailor approach
- Supports prioritization of water quality investments based on net benefits





Conclusions

- Current financial capability assessment methodology is **fundamentally** flawed
 - ⊙ Enforcement of sub-optimality
 - ⊙ Incremental adjustments insufficient
- NACWA guiding principles highlight:
 - ⊙ primacy of local factors in determining financial capabilities
 - ⊙ call for holistic perspective consistent with EPA's evolving regulatory approach
- Portfolio management framework offered to advance discussion

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