

**EEP / DWQ Nutrient Offset Payment Program
Transitioning to an Actual Cost-Based Pricing Method**

**Meeting Summary
April 8, 2009
Yates Mill Historic County Park
Raleigh, NC**

- I. Handouts Distributed at the Meeting
- II. Welcome & Orientation
- III. Requests for Information from EEP (Since March 25th meeting)
- IV. Continuation of Presentation: Transitioning the EEP Nutrient Offset Program to Actual Cost Method
 1. Transitioning the EEP Nutrient Offset Program to an Actual Cost Method - Actual Cost Method Scenarios (Powerpoint Presentation by Jim Stanfill)
 2. EEP Nutrient Offset Program Forecasts by CU and Basin (Powerpoint Presentation by David Robinson)
 3. Debrief Actual Cost Method Scenarios
- V. Group Discussions
 - a. Revisit the Issues, Identify new Issues as needed
 - b. Joint Criteria
 - c. Identification of Stakeholder Interests (what's important)
- VI. Proposed Recommendations
- VII. Closing Summary and Next Steps

Reports and presentations are accessible via the NRLI website at:
<http://www.ncsu.edu/nrli/decision-making/projects/index.php>

I. Meeting Handouts

1. Participants were provided with the following handouts:
 - a. April 8 Agenda
 - b. March 25 Meeting Summary
 - c. Issues and Options

- d. Transitioning the EEP Nutrient Offset Program to an Actual Cost Method: Actual Method Scenarios (Powerpoint Presentation by Stanfill)
- e. Actual Cost Data: Program Level Nitrogen, Program Level Phosphorus, River Basin Level Nitrogen-Neuse, River Basin Level Nitrogen Tar-Pam (Table Presentation by Stanfill)
- f. EEP Nutrient Offset Program Forecasts by CU and Basin (Powerpoint Presentation by David Robinson)

All handouts are available under the section labeled: April 8, 2009 at:
www.ncsu.edu/nrli/decision-making/projects/NOPPStakeholderPage.php

2. Participants who attended the April 8, 2009 meeting.

April 8, 2009 Participants	
Name	Affiliation
Bill Diuguid	NC Division of Water Quality
Rich Gannon	NC Division of Water Quality
John Huisman	NC Division of Water Quality
Kristin Miguez	NC Ecosystem Enhancement Program
David Robinson	NC Ecosystem Enhancement Program
Suzanne Klimek	NC Ecosystem Enhancement Program
Kelly Williams	NC Ecosystem Enhancement Program
Jim Stanfill	NC Ecosystem Enhancement Program
Robert Brown	NC Ecosystem Enhancement Program
Eric Ellis	NC Ecosystem Enhancement Program
Bill Gilmore	NC Ecosystem Enhancement Program
Susan Lodwood	NC Ecosystem Enhancement Program
Erin Wynia	NC League of Municipalities
Charles Brown	Town of Cary
Haywood Phthisic	LNBA/NRCA & Johnston County
Jonas Hill	Pitt County
Sandi Wilbur	City of Durham
Anne Coan	NC Farm Bureau Federation
Mike Schlegel	Triangle-J Council of Government
Adam Rigsbee	Restoration Systems, Inc.
Heather Jacobs Deck	Pamlico-Tar River Foundation
Alissa Bierman	Neuse River Keeper Foundation
Katherine Locbaum	Neuse River Keeper Foundation
Mary Lou Addor	NCSU Natural Resources Leadership Institute
Steve Smutko	NCSU Natural Resources Leadership Institute

II. Welcome and Orientation

Mary Lou Addor, NRLI, opened the meeting with introductions, provided an overview the agenda and meeting process.

Agenda Review

The agenda items included:

1. Welcome & Introductions
 - a. Review the purpose and scope of the stakeholder process
2. Review March 25th Meeting Summary for additional changes and comments
3. Agenda Review for April 8th
 - a. Presentation & Discussion: Actual Cost Method Scenarios
 - b. Discussion of Issues/Recommendations
 - c. (Lunch Break)
 - d. Contd. Discussion of Issues/Recommendations
 - e. Closing Summary & What's Next?
4. Process Review
 - a. Roles and responsibilities (facilitators, stakeholders, EEP, DWQ)
 - b. Decision rule
 - c. Ground rules
 - d. Parking lot
5. Inform stakeholders of information requests to EEP
6. Wayne Community College BMP Visit (See Kristin Miguez for additional information).

Review of Purpose and Scope

The purpose and scope of the stakeholder meetings are to:

- **Purpose:** *Provide guidance to the Ecosystem Enhancement Program in transitioning from a fee-based system to an actual cost system as required by the General Assembly.*
- **Scope:** The focus of the stakeholder recommendations will be on the pricing methodology.

Process Review

1. Roles

- a. Stakeholders: responsible for disclosing interests, needs, actions, and issues in a timely manner and committing to the purpose of the stakeholder process. Stakeholders will be expected to represent the

- interests of (1) themselves, (2) organizations which they have the authority to represent, or (3) groups of constituents with similar interests.
- b. Facilitators: responsible for helping the group stays on process and on topic, promoting open and balanced discussion, and organizing information for effective use.
 - c. EEP: responsible for convening the group, providing basic information about the cost-based pricing method and the nutrient offset payment program generally.
 - d. DWQ: responsible for assisting with understanding content and any agency policies that pertain to the formula.

2. Decision Rule

When the group presents proposals for consideration, each stakeholder (1 representative per organization) will designate his or her level of agreement using the following scale:

Level 1: Endorsement (I like it)

Level 2: Endorsement with a minor point of contention (basically I like it)

Level 3: Agreement with reservations (I can live with it)

Level 4: Stand Aside (I don't like it but I don't want to hold up the group)

Level 5: Block (I will not support the proposal and will act outside the group to meet my interests)

The final report will show at which level individuals or groups supported the final product. The focus for each stakeholder should be on making good decisions for his or her constituency, not simply to reach agreement.

3. Ground Rules

- a. Work the problem, not the person.
- b. Make space for others to contribute
- c. Follow the process
- d. One speaker at a time
- e. Park-off agenda items
- f. Rolling breaks
- g. Cell phones on vibrate
- h. Test assumptions/Ask Questions

4. Parking Lot

Topics not considered by the group to be germane to the day's agenda will be listed on a separate flip chart under the heading "Parking Lot." Prior to adjourning each meeting, the facilitators will review parking lot items, and the group will determine how (and possibly when) each item will be handled.

5. Debrief Format

In order to help the stakeholders create a shared understanding of the questions and responses that follow a presentation, the following debrief format was introduced.

- a. Questions of Clarification
- b. Reactions to what you just heard
- c. Implications for purpose of the stakeholder group
- d. Actions (recommendations)

III. Requests for Information from EEP (Since March 25th meeting)

1. **Request #1** Provide at the next Stakeholder's Meeting, two fee rates based on geographic application of the Actual Cost Method. The first rate involves using Neuse 01 actual cost data to produce a nitrogen fee, and the second scenario involves using historical cost data excluding Neuse 01 for a programmatic fee for the remaining geographic areas.
2. **Request#2:** Stakeholder requested information about the change in property values over time to be used as an inflation index for property acquisition cost related to future contracts.
3. **Request #3:** Stakeholders requested information about the effect when there is a change in advance mitigation, both on price stability and environmental impact.

IV. PRESENTATIONS - Continuation of Presentation: Transitioning the EEP Nutrient Offset Program to Actual Cost Method

All handouts are available under the section labeled: April 8, 2009 at:
www.ncsu.edu/nrli/decision-making/projects/NOPPPStakeholderPage.php

1. Transitioning the EEP Nutrient Offset Program to an Actual Cost Method

The continuation of the "[Transitioning the EEP Nutrient Offset Program to an Actual Cost Method](#)" presentation, Jim Stanfill presented several alternatives scenarios. During the presentation, Jim described the results of conducting the Actual Cost Method at a program level, river basin level and a cataloging unit level (at three geographic application levels).

Issues and Choices of the ACM

Jim began by reviewing the **four broad issues and choices** of the actual cost method.

1. **Geographic Application** (Application of Rate NOT Location of Mitigation)
 - a. Program Level
 - b. Basin Level
 - c. Cataloging Unit Level
2. **Frequency of Adjustment**
3. **Length of Adjustment Period**
4. **Should Costs be Adjusted below Actual Costs**

Projects Costs

Jim provided an overview of the actual cost method formula, and reminded the participants that all of the variables of actual costs (administrative and project costs) are known with the exception of the "**project costs in process.**"

The NC Legislature is requiring the use of actual costs to generate nutrient reduction credits. **There are nine objectives to the actual cost method.** (information brought forward from the March 25 presentation).

1. Must use actual costs of generating nutrient reduction credits.
2. All costs must be accounted for in the ACM.
3. Must be a self-sustaining financial model.
4. Rates must change (upwards or downwards) as actual costs change.
5. Method must be applicable at a Cataloging Unit (CU), Basin or Program Level.
6. Must be applicable to either nitrogen or phosphorus offsets.
7. Must be understandable and easy to use
8. Must be predictable and equitable
9. Transition plan by September 2009.

Question: Stakeholder: How are past costs projected into the future?

Response: Jim Stanfill: We are not basing cost data on any theoretical cost of the EEP program. We will include actual cost of:

- Acquisition
- Design
- Construction
- Monitoring Costs
- Stewardship

These are specific projects that have a specific number of contracts. Some are complete and some are future contracts that need to be completed.

Adjustment Factor

Jim **reintroduced the Adjustment Factor** (reference handout d, p. 4 and summary of annual forecasts). This section outlines the Questions, Responses, and Comments provided during this presentation.

Comment: Concerns were expressed about the rate change and adjustment factor. Jim offered a hypothetical to address these concerns: if the base rate is \$20, and the adjustment factor is \$10, then the new fee is \$30 for that year. When you run the model again the following year, the actual costs minus actual receipts are expected to generate a smaller gap. Following the adjustment each year, the actual costs should do down.

Question: Is it the adjustment factor that will be adjusted by 25% each year?

Response: Let us hold that question for later in the presentation.

ACM Assumptions

Jim identified **several assumptions about the actual cost method scenarios** which are:

1. Adjustment Frequency: annually
2. Use 3 year running average to calculate average pounds expected to be paid per year
3. Adjustment Period - four years
4. Inflation Index: USACE Civil Works Construction Cost Index
5. Admin Costs Per Payment limited to 8 years

Jim elaborated about several aspects of the ACM assumptions: with respect to the admin costs per payment limited to 8 years, historically 8 years is the life of the project where 90% of the project costs occur.

Comment: A stakeholder expressed the concern about the 4 year adjustment period - suggesting the program will not be able to recover costs to a balance of zero (assumption that everything remains constant).

Response: Yes, that is understood, and you are correct if you assume that everything else remains constant. However, in reality, the annual difference is a moving target anyway.

Actual cost method scenario for Neuse Nitrogen at the Program Level

Jim highlighted the following key points:

1. Some of the future project costs are associated with full delivery projects and EEP cannot discuss those projects.
2. Future project costs and administration costs are adjusted for inflation.
3. With respect to actual cost of program, there are no completed projects since the oldest project is about 4 years old.
4. It is important to note that we have been estimating our costs at the program level, so the adjustments are minimal at that level. However, when you apply the cost method at smaller geographic levels, you see significant adjustments are required to make it balance from year to year.

Comment: One stakeholder commented regarding the ACM program-level results, that a bigger drop in the adjustment factor would have been expected given the initial \$11/lb and then the increase to \$28/lb.

Question: How is it that you've managed to get your costs so closely aligned to the \$11 figure for nitrogen?

Response: (Stanfill) Because during most of the time we have been running our program, we were focused on coming in at the \$11 target for the Neuse, and most of our payments were generated from that basin.

Actual cost method scenario for Neuse Nitrogen at the Basin Level

Jim pointed out that the Neuse Nitrogen Program dominates the state's nutrient program; 97% of payments are made in Neuse 01 - if you include all payments from the Basin (including the Tar-Pam nitrogen).

Actual cost method scenario for Tar-Pam Nitrogen at the Basin Level

Jim pointed out that the administration costs are proportionate to lbs.

Question: What are your base administrative costs? Do you adjust them up or down based on annual program activity, especially in zero payment years?

Response: (Stanfill) Administrative costs are adjusted for inflation (and go up or down in proportion to real costs). Staff costs remain stable over time so that the actual cost is the base cost.

Question: How do you divide administrative costs geographically (between basins or at the CU level) particularly if you don't have projects in a particular CU?

Response: (Stanfill) If there are no costs in that CU, then there is nothing to recoup, therefore, we have no administrative costs associated with that CU.

Question: Personnel costs seem low. Does that account for everything?

Response: (Stanfill) Yes. We do not have many staff assigned to the nutrient offset program. We have several other programs that we run. Almost all of our projects have been full delivery or full purchase, that's why we show so few personnel costs in this particular program.

Comment: Concern raised by one of the stakeholders that the adjustment factor is very difficult to explain and as a result, does not meet one of the objectives of the actual cost method (i.e., easy to explain).

Actual cost method scenario for Tar-Pam Phosphorus at the Basin Level

Comment: It is anticipated that the development community will be concerned with the basin level Tar-Pam phosphorus

Actual cost method scenario for the CU level

Jim identified the problems running the actual cost method at the CU level. This would require increased management and additional programming. There is also a concern that there would be limited data at the CU level

Additional Questions of Clarification

Question: Based on the 2009 data that you're showing, can we expect that the average for the Neuse and Tar-Pamlico to be accurate?

Response: (Stanfill) We feel comfortable with the 3-year moving average. If we attempted to look at the data monthly, the data would show some months having more payments than others. Payments seem to be cyclical for economic reasons as well as business budgeting reasons inclusive of the construction season. Overall, a 3-year moving average reflects both suggestions from this stakeholder group as well as what we feel is most realistic.

Comment: There seems to be a discrepancy between the credits (denominator) in the main Actual Cost calculation and the Adjustment Factor calculation. Can you help clarify?

Response: (Stanfill) The credit component (denominator) in the Adjustment Factor calculation is dependent on the Future Expected Pounds, which differs due to time intervals. The credit component (denominator) in the Actual Cost calculation is based on the actual credits that nutrient projects produced.

Comment: Suggests keeping the Actual Cost Method Adjustment and the Adjustment Factor Denominator at a yearly interval to avoid possible confusion by stakeholders and Legislators.

Response: (Stanfill) Based on stakeholder comments thus far I feel comfortable looking at running the Actual Costs once a year with some safeguards.

Question: Are the future projects the RFP projects?

Response: (Stanfill) EEP is not allowed to discuss these projects at this time. According to the ACM, future projects consist of a projected cost based on actual cost data. There is no arbitrary data cost regarding any project data.

Question: Is there a base level that would have to be maintained for administrative costs and are those costs inflated?

Response: (Stanfill) There are fixed costs for utility rate, rent, and staff that are adjusted for the future. The ACM rate incorporates administrative costs. If the program grows (need to add 1 or more employees), then the rate will reflect the increased costs. As administrative cost increases or decreases, the ACM will capture those changes. Administration is an allocated portion of specific positions that help manage the Nutrient Offset Program.

Question: Looking at the example in your power point presentation which the Actual Cost Rate is \$34.49 for Nitrogen in the Tar-Pamlico, if you're searching for the lowest cost project, do you use the current Actual Cost Rate to determine if a project is low or high?

Response: (Stanfill) No. Legislation says we must implement the lowest cost project. The \$34.49 is the rate that we charge to offset nutrients based on the actual cost at a given point in time.

Question: Why are there more asset costs than payments?

Response: (Stanfill) There are several reasons:

1. Some payments were made at a low rate (\$11/lbs N).
2. Specific to the Cataloging Unit (CU), a cost discrepancy exists due to the low volume of payments versus project costs in that CU. That project supports mitigation for both the current payments as well as future expected payments. This is the normal expectation in low-volume payment CUs because there is a minimum projects size that must be implemented.
3. In the Tar-Pam when you implements a buffer srest., the projects yield nitrogen and phosphorus credits. However, Nitrogen and Phosphorus requirements are not being paid into the program at the same rate as the projects yield. Therefore as a consequence of meeting the mitigation

requirements, there are some unused credits that are paid for by future requirements.

- Comment:** Considers that a higher Actual Cost Rate is not necessarily bad, but actually good for the municipality and environment. The stakeholder states that developers basically have two options. One option is to pay a third party provider to offset its nutrient reductions or conduct an on-site mitigation themselves. The municipalities would prefer that developers conduct on-site mitigation as opposed to paying a third party provider for nutrient reduction in order to achieve greater environmental benefits of having the mitigation physically closer to the impacts.
- Question:** Given that the adjustment period is 4 years for nitrogen at the Tar-Pamlico River Basin Level, what is the basis of the 22,984 lbs nitrogen?
- Response:** (Stanfill) The pounds of nitrogen (22,984 lbs N) are based on a 3 year running average used to calculate the average pounds expected to be paid each year.
- Comment:** Suggests using the term "Rate Review Frequency" instead of "Adjustment Factor" and "Actual Cost Method" instead of "ACM" in order to be less confusing for everyone.
- Response:** (Stanfill) Defines that the Rate Review Frequency will represent the interval of time in which rates will be reviewed or examine to determine if the Actual Cost Rate needs adjusting.
- Comment:** Expresses concern over the inability to completely recover over a long adjustment period.
- Response:** (Stanfill) If you're assuming pounds are constant, you will never recoup your cost. However, the dollar amount that I am recouping each year is getting less.
- Comment:** Why would EEP need assets in each Cataloguing Unit?
- Response:** (Stanfill) Because Legislation requires assets in each CU.
- Question:** Does the calculation count both phosphorus and corresponding nitrogen needs?
- Response:** (Stanfill) Yes, the number is added to the ledger.
- Comment:** (Stanfill) There is a discrepancy between the cost of projects and payments received within CUs and the Tar Pam RB. This is explained by the requirement to build projects within a CU even when there are a small volume of payments. Hence there is a carrying cost to build projects in low volume receipt CUs. EEP sites are appropriately sized for cost efficiency.

Question: Currently, in the Tar-Pamlico, one pays for whichever nutrient (nitrogen or phosphorus) is greater of the two and offsets for both. Can we have one rate for both nutrients in the Tar-Pamlico and not split up for nitrogen and phosphorus?

Comment: (Stanfill) If you need 150 lbs of phosphorus and 0lbs of nitrogen, what is the buffer equivalent? Basically, you would need just over an acre of buffer to offset 150 lbs of phosphorus. Technically, you're still paying and offsetting for both phosphorus and nitrogen. Downside of paying for only one nutrient is that customers would be paying a huge rate than before. Historically speaking, approximately 58% of customers require both nitrogen and phosphorus. By paying for only for what you need

2. EEP Nutrient Offset Program Forecasts by CU and Basin

David Robison presented information on [nutrient offset trends and forecasts by cataloguing unit and basin](#). David illustrated how the annual payment forecasts were derived for both the Neuse and Tar-Pam at the CU and Basin level. He presented information in terms of trends, both linear and 3-year average. For instance, David forecasted levels of nitrogen in the Neuse based on an average of three years from 2006-2008. He explained that the 2007 data (Neuse Basin: Annual Pounds of N) may be higher and the 2008 lower in comparison because the fee was expected to go up in 2008. Hence, more payments were received in 2007.

3. Debrief of Actual Cost Method Scenarios

Mary Lou worked with the group to debrief Stanfill's morning presentation. The following debrief format was used.

1. Questions of clarification
2. Reactions
3. Implications for decision-making
4. Actions for consideration

Questions of Clarification

Question: Will EEP change its rates once the Jordan Lake and Falls Lake rules are approved?

Response: (Stanfill) Based on the Actual Cost Method, it's possible that a different rate will be offered in those particular watersheds due to the unusually high costs and specific watershed requirements imposed by regulations. Costs will certainly be affected in these watersheds comparative to other areas due to the physical and BMP constraints common in an urban

environment. The rate could be geographically specific at a particular watershed level:

1. Upper Cape Fear River Basin Rate
2. Sub-basin Area Rate.

Reactions to what you just heard

The Summary of stakeholder reactions is presented followed by individual comments.

Summary:

1. ACM may have limited use in the Tar-Pamlico River Basin; may want to use as a working model for a 5-year period and then reevaluate.
2. Jordan, Falls, and High Rock: take into consideration increased land prices (much higher costs).
3. Uncomfortable with program level rate because of various situations (stakeholder did not elaborate on the various situations).
4. Tar- Pam Basin Level Nitrogen Rate of \$5.09 is very low, especially in comparison to providing costs in other locations. Could force mitigation into rural areas and away from urban.
5. Charge on CU basis could raise concerns for some given the unpredictable pricing nature. Could give rise to a number of rates and this may not be manageable.
6. Need to consider how to protect the estuary in whatever the pricing method.
7. Would like one cost at the program level.
 - a. For example, future projects at the CU level, may involve more expensive areas due to land costs and other factors. It may be more difficult adjusting the actual cost method on a regular basis given the variability in costs.
 - b. One cost at the program level might be ok if the lion's share of offsets occurs in the same area (if a large portion of offsets have not been in Neuse01 nor costs accounted for-we would not support this idea). Staff member reported that about 36% of offsets have occurred in the Neuse01.
8. For inflation rate- consider change in land acquisition costs as a additional factor along with the USACE Index
9. Rate review frequency= adjustment factor frequency (interval of time between which rates are reviewed and adjusted).
10. Truing-up: Reset enough money to have costs, if going to true-up to within \$100,000.
11. Truing-up book assets. Retire any additionally lower rate concerns. No comparisons to low rates in other areas. Concern in urban areas that developers will be forced into rural over urban areas.

Individual Comments:

- Comment:** Comments that EEP should first try using the ACM at the Program Level and then at the CU Level. Perhaps future projects could be implemented in more expensive areas, etc.
- Comment:** ACM may have limited use in the Tar-Pam. As a result, may want to consider the actual cost method as a "working model" for about 5 years. Monitor and evaluate the model, determine needed improvements, and return to the EMC to make corrections on assumptions and to include more current and historical data.
- Comment:** Suggests applying ACM at the Program Level instead of basing it on geographic areas. One of the requirements of the ACM is equity across geographic areas. For example, Greenville is located in two (Neuse and Tar-Pamlico) River Basins. One recommendation is to develop the best possible methodology at the Program Level for the time being, and then come back to EMC later as more information is available.
- Comment:** Foresees a problem in the Jordan Lake, Falls Lake and High Rock Lake watersheds. Commented that if EEP does not think it will not be in a financial hole now, then if the ACM rate is \$11 or \$15 and try's to purchase land in the Upper New Hope watershed, then EEP will financially end up in the hole really fast. We know that the Jordan Rules will be approved in the near future.
- Comment:** (Klimek) Some of the areas to be regulated in the future will have much higher land costs; therefore we need to account for the higher costs so that we do not go into a financial hole at all.
- Comment:** Not comfortable moving forward with a single statewide rate because of concern over people's reactions of having one statewide rate for the first year and then different rates for subsequent years split out by geographic area.
- Comment:** (Stanfill) Programmatically, there are enough dollars to pay for all of the programs. If we reset books, we don't need any extra money to make the one-time adjustment. In the future, everything goes to \$0, or something close to \$0, with a small adjustment.
- Question:** Would that meet all of the requirements?
- Response:** (Stanfill) Within \$100,000, there is enough money to pay for all projects. Then the adjustment would be \$0. There is enough money for offsets for all projects, everything paid for, true-up on the financial side and offset.

- Comment:** Stakeholder suggests that EEP start from scratch, clear the books and eliminate the advance credits from the program. Once you clear the books, you will have to wait until you have enough dollars to build new projects.
- Response:** (Stanfill) EEP has a time requirement imposed by DWQ to comply with new requirements.
- Concerns:** Mentions if actual cost results in low rates, then developers would be discouraged from implementing on-site mitigation. In addition, there is a concern urban impacts could be mitigated in rural areas.
- Response:** (Stanfill) The rule requests that we provide a fee based on actual cost. This does not alter the requirement of mitigation at the CU level.
- Comment:** A one-time adjustment might be more simple politically.
- Response:** (Stanfill) EEP agrees that a one-time adjustment can occur due to the Nutrient Program's fund's solvency at a program level. This would also be a simpler approach.
- Comment:** Prefers that the Rate of Review and the Period for the Rate Change to both be one year rather than the one year and four years respectively.
- Comment:** From the data and number of projects, it makes sense to have one cost, statewide, even if you mitigate at a CU Level or lower level to address the issues Durham has expressed. Even if projects become more expensive, you can adjust each year to account for the rise in cost. This is okay because you're adjusting on a regular basis with yearly cost spread statewide. The real problem is the variability of cost when you get down to the Basin Level, particularly at the CU Level, when there are extreme differences in rates.
- Response:** My reaction is that one Program Level fee is okay as long as the lions' share of offsets is in one area. It's not okay to set the rate as low as ACM is calculating it to be right now. A large portion of EEP's projects are located in the Neuse 01, but in some instances in Neuse 01, the cost of land was not included since the land was donated. I would be okay with the rate provided donated land costs are accounted for. I would fight it really hard without including compensation for land costs in the future.
- Comment:** (K. Williams) The most recent trend shows that approximately 91% of the payments are in the Neuse 01; with an overall figure of 85% since the program began.
- Question:** What is a statewide rate?

Comment: (Facilitator) Instructs everyone to use the phrase, "Program Level" rather than "Statewide", since the program is administered only in two river basins.

Comment: Regarding the inflation rate: Construction cost is a large component, however I think there is a real need for an inflation rate for land in order to reflect changes in land acquisition costs.

Implications for Decision-Making- Adjustment Factor

Several members of the stakeholder committee conveyed their concerns about the adjustment factor. As a result, they began to brainstorm ideas about the appropriate use of the adjustment factor. Three proposals were developed. Two proposals excluded the use of the adjustment factor, suggesting that program costs should be covered under the current accounting method and zeroed out before the actual cost method was used.

Proposal 1: - using an adjustment factor

- First: rate adjustment using program level data
- Subsequent years use adjustment spilt out by basin
- Number of years open for discussion- may be less than four proposed in the earlier assumptions.
- 1 year/1year same with options/triggers for adjustment

Proposal 2: - not using an adjustment factor/reset

- Reset
- Cover all costs now and start with a blank slate or close to \$100k - give or take a little.

Proposal 3: - not using an adjustment factor/reset

- Reset (true up the books)
- Retire additional assets on the books

The group requested to table the brainstorm session on the adjustment factor and adjourn for lunch before resuming this and other discussions scheduled for the afternoon.

IV. Group Discussions: Issues, Criteria, Interests, & Options

Issues

Steve Smutko began the afternoon session by introducing the handout, *"EEP/DWQ Nutrient Offset Payment Program Transitioning to an Actual Cost-Based Pricing*

Method – Issues and Options” to help frame the afternoon portion of the meeting. The objective was twofold: 1) to ensure all of the issues were captured at the March 25 meeting and add any new issues from the April 8 meeting; and 2) to acquire group support on these issues.

Issues generated at the March 25 meeting:

- a. Frequency of Adjustment
 - i. Placement of a "floor" on the adjustment factor
 - ii. Percent cost increase/decrease threshold for triggering adjustment
- b. Geographic Application
- c. Inflation Method (Adjustment) for Future Costs
- d. Addressing costs of indefinite maintenance (i.e. stewardship expenses)
- e. How to evaluate the different types of projects in estimating future cost
- f. If there is a surplus, wipe slate clean and donate overage to environment
- g. Address least cost requirement (see hot spots)
- h. Accounting for lag time from action to mitigation
- i. Factor "hot spots" into geographic determination.

Issues added by stakeholders at the April 8 meeting:

- j. Least cost mitigation
- k. Generate adequate funds to do BMP projects in urban areas; move mitigation closer to source.
- l. Tax implications to counties for state purchased property.
- m. Loss of opportunity for farmers to reach reduction goals
- n. Accurately estimating reduction for given projects.

Joint Criteria

Smutko reviewed the list of joint criteria. These are criteria that everyone will use to evaluate options and proposals. Each person may weigh each criterion differently, but it is agreed by the group that all criteria are valid.

Geographic Application

- a. Reduce price volatility (over time)
- b. Enhance/maintain price predictability
- c. Keep the number of rates in use to a tolerable level
- d. Keep computation complexity to tolerable level
- e. Keep regional price differentials within tolerable levels.
- f. Reduce risk of under collection

Frequency of Adjustment

- a. Reduce Price volatility/ enhance predictability
- b. Increase and maintain price stability
- c. Reduce administrative costs
- d. Keep size of adjustment to tolerable level

- e. Reduce differences between expenses and receipts

Interval Considerations

- a. frequency of letting projects
- b. more time=better data=better accuracy
- c. use a % trigger
- d. think annually - project your costs a year in advance

Identification of Stakeholder Interests (what's important)

The stakeholders generated a list of interests at the March 25 meeting and this list was carried forward into the April 8 meeting summary. These interests will be used by individual stakeholders as criteria to evaluate options and proposals. They are not jointly agreed on by all stakeholders, and in fact, some interests are antithetical to other interests.

1. Fair and equitable system for the river basin (all jurisdictions) or statewide.
2. Clear and concise accounting.
3. ACM is clear in its functionality.
4. Predictability of rate changes in respect to cost and time
5. Notification to public regarding rate changes.
6. Use market value appropriately.
7. Costs reflect the market enabling competition
8. Minimize costs to purchases
9. Applicant gets benefit of price fluctuation
10. Get the costs right, the actual costs
11. Reflects actual costs
12. Actual costs covers all costs
13. Restoration and impact are in close proximity
14. Account for the environmental cost of creating mitigation after the impact
15. Environment benefits
16. Provide best environmental lift at lowest costs.
17. Ecological benefit of mitigation is credited (accounted for and paid one time.
18. Formula (ACM) and use of does not result in pollution or mitigation of "hot spots" due to land costs differences and how they are reflected in the formula (appropriately small geographic scope).
19. Account for the actual cost per pound of existing projects
20. Science and economics are adjusted simultaneously.
21. Actual Cost Method is in rule that allows rates to automatically adjust up and down based on actual costs.
22. Ability to adapt prices to new realities
23. Do not deviate from historical fee area is not necessary.

Potential Options for Each Issue

The stakeholders generated potential options for three of the issues.

1. Geographic Application (*items may be outside purpose of stakeholder process as identified in the purpose and scope).

- a. 8 digit HUC or service area
- b. Basin
- c. Program
- d. Mitigate a 8 digit but use a larger accountability region
- e. Use Actual Cost on basin level but adjust by land acquisition at CU level
- f. *Go to EMC to change mitigation level to smaller than 8 digit HUC
- g. *Got to EMC to change mitigation level to preclude mitigation of hot spots and/or correct for current hot spots.
- h. *Include a transport factor to address delivery reduction differences.
- i. *Price out different BMP options
- j. *Require BMP right out of the permit

2. Frequency of Adjustment

- a. Next Payment
- b. Quarterly
- c. Annually
- d. More than annually
- e. Percentage threshold
- f. Procurement quantity
- g. Combination (change in actual costs)
- h. Based on regulatory change

3. Inflation Adjustment

- a. US ACE construction cost index
- b. Property index
- c. Service index
- d. Consumer price index
- e. Composite
- f. Multiple Indices

Resume Discussion of the Adjustment Factor

Three proposals were generated for using/not using an adjustment factor in the actual cost method.

Proposal 1: - using an adjustment factor

- 1st rate adjustment using program level data
- Subsequent years use adjustment spilt out by basin
- # of years open for discussion- may be less than four proposed in the earlier assumptions.
- 1 year/1year same with options/triggers for adjustment
(True-up scenario #1: Adjust current discrepancies at the program level in year one to true up, then make annual adjustments at the basin level in subsequent years).

Proposal 2: - not using an adjustment factor/Reset

- Reset
- Cover all costs now and start with a blank slate or close to \$100k - give or take a little.
(True-up scenario #2 Do a one-time adjustment so that receipts equal the current payment deficit within year one. True all accounts one time.)

Proposal 3: - not using an adjustment factor/Reset

- Reset (true up the books)
- Retire additional assets on the books
(True-up scenario #3 Do scenario #1 or #2; clear the books and then eliminate all excess assets from this point forward).

Facilitator questioned if stakeholders clearly understood the discussion at this point. Several committee members had questions or comments:

Comment: Believes that EEP should use the Neuse 01 as the primary indicator of costs.

Question: Comments that EEP needs to be considerate of political ramifications of credit elimination, saying that some people may think eliminating assets paid for by others fees may be looked upon poorly.

Comment: Comments that if there is not a reset of credits value then there would be an unfair advantage if those credits were sold. Claims restoration will be at \$0.00/lb rate.

Comment: Attempts to find compromise by suggesting that a percentage (i.e., 50%) could be retired and 50 left as a cushion.

Note: Comments made ultimately left some questions on the table regarding advance mitigation's effect both on price stability and environmental impacts. This led to a request for a demonstration of this information.

Comment: If the data becomes available, there is some interest in having the fee at a CU level by a few stakeholders.

Response: This comment is followed by only wanting this to be done at the program level.

Comment: EEP should consider using no more than 50% of advance mitigation assets to see if there would be enough credits to keep the rate stable.

Comment: (Stanfill) We are required to start a project when the clock begins. From an ACM perspective, the first 25 – 30 payments that we get in an area, we could wait, but here is what we're getting by holding the payments: it's a real advantage to the program from a rate perspective especially in CUs that incur a low volume of payments. That problem is eliminated with advanced mitigation, that's why I said that in the first year we'd have a really low rate and then in the second year we'd have a high rate, if we get rid of advanced credits.

Comment: Doesn't believe it's politically feasible to implement multiple rates. Based on experience, you can't have one rate here and another rate some where else.

Comment: Being from Pitt County, which is located in both the Neuse and Tar Pamlico River Basins, we voluntarily applied the Tar Pamlico rules in the Neuse basin to discourage extreme growth in the southern portion of Pitt County where there are no regulations.

Comment: EEP should charge at the program level, recognizing the cost value of donated land, so there is no need to suggest eliminating advance mitigation.

Comment: One proposal is to use a basin level rate until there is enough demand in each CU for individual mitigation sites at which time you can set a rate based on the CU level.

Comment: (Stanfill) Since in many CUs, EEP collects very little if any receipts, the Program Level makes the best sense.

PROPOSAL: The stakeholders discussed the geographic application of rates.

Step 1: Reset in year one at the basin (program?) level to 0\$

Step 2: Retire assets in Tar-Pam

a. All assets? 50%?

Step 3: Recalculate

a. Use land acquisition cost data to differentiate costs at CU Level

Response: (Stanfill) If anybody believes that 14 rates are appropriate it is okay with me. There would be 9 separate nitrogen rates and 5 separate phosphorus rates at the CU Level. Eliminating assets increases rate volatility. This approach will be difficult to explain to the General Assembly. I hope that whatever

approach we take that we will be able to explain to General Assembly.

Comment: Some counties will have more than one rate. City of Greenville would have 5 rates.

Comment: Recommends dropping the third provision of retiring 50% of assets.

Comment: (Stanfill) In the interest of trying to facilitate this process and given that 84% of the payments are in Neuse 01, the Neuse 01 should have its own rate. There should be a Program Level rate for everywhere else and set an individual rates for special watersheds such as the Neuse 01, Cape Fear, Jordan Lake and Falls Lake.

Question: At the basin level, would inflation be used to derive that rate?

Response: (Stanfill) In Full Delivery, inflation rate has been included as part of the contract. In other types of procurement, the key is using one inflation index to apply to all type of indexes. We can add property inflation indexes, if valid. All costs are inflated by an index.

Comment: Write the rule to state, "..basin level or smaller."

Comment: Set CU rates using basin data until you get enough data

Revised Proposals

Part 1:

Reset to Zero

Use a CU rate using basin level data until data available at CU

Programmatic Level for everywhere but: Neuse 01, Falls Lake, Cape Fear (high costs areas)

Alternative proposals for Part 2:

Proposal #2: Straw Poll: with retirement of 50% assets:

Level 1(Like the proposal): 1

Level 2 (Proposal is OK): 4

Level 3 (Can live with it): 2

Level 4 (Object to the proposal, but won't block): 3

Level 5 (will block the proposal): 0

Proposal #3: Straw Poll: without retirement of 50% assets:

Level 1(Like the proposal): 2

Level 2 (Proposal is OK): 2

Level 3 (Can live with it): 4

Level 4 (Object to the proposal, but won't block): 4

Level 5 (will block the proposal): 0

Closing Summary and Next Steps

Jim Stanfill offered his appreciation to the committee, stating he was impressed with the energy, effort, and intellectual input of the committee. Even when there is not agreement on proposals or ideas, the end result is a better product because of the deliberations, the suggestions, and the thoughtful questions. Jim Stanfill recognized EEP staff for their extensive efforts in preparing information for this meeting.

The following action items were identified during the April 8 meeting

Actions:

1. EEP will provide fee rates per [Request 1](#).
2. EEP will provide property inflation values and their impact on the actual cost per [Request 2](#).
3. EEP will provide data regarding the impact that advanced mitigation has on the price stability and the environment in [Request 3](#).
4. The April 8th meeting summary will be distributed in advance of the June 12th meeting and presentations posted on the NRLI website.

Next Agenda:

Part of the meeting will focus on presenting additional scenarios of the actual cost method discussed at the April 8th stakeholder meeting. In addition, there will be discussions dealing with property inflation and advanced mitigation. Recommendations from the Credit Yield Subcommittee will be presented and followed with a discussion from the larger committee. The remaining issues and options will also be discussed.

Next meeting:

Scheduled for Friday, June 12th at location to be announced.