






Long Range Finance Plan Rate Refinement Discussions

Meeting #6
December 5, 2011

Agenda

- Review of feedback from November 14
- Present straw proposal for Rate Structure refinements
- Continue discussions of Purchase Order follow on
- Next Steps

Straw Man Poll:

-  • Increase RTS/Capacity Charge
-  • “Customer Charge”
-  • Water Quality/Source Protection
-  • Adjust Ad Valorem tax
-  • DHCCP

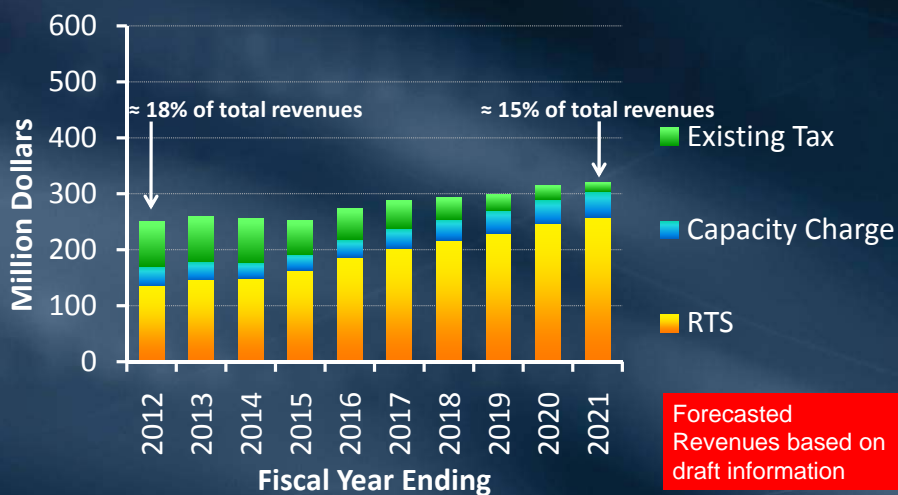
Feedback from November 14

- Support for:
 - Adjusting AV tax rate
 - Fixed charge for future DHCCP costs
- Treatment cost recovery issues need further exploration
 - Treated Water Capacity Charge and other alternatives have been explored and rejected
 - Fixed Water Quality/Source Protection Charge as alternative to recover fixed costs
- Increasing existing fixed charges not supported

Options to Address Greater Fixed Revenues

- Status quo: Fixed revenues grow in absolute terms, but proportionately, become less of the revenue structure
- SWP costs addressed through an Ad Valorem tax solution and development of a DHCCP charge
- Treatment costs addressed through a revised fixed charge proposal

Fixed Revenue Forecast, Existing Revenue Structure



Ad Valorem Tax Rate Could Generate Greater Revenues

- Status quo: tax revenues will continue to decline
- Metropolitan is authorized to use property tax revenues to fund payments under the State Water Contract
- Even holding the tax rate constant could lead to revenue benefits in the long term
 - Mitigate impacts on future water rates
 - Used to offset SWP costs, including future DHCCP costs
 - SWP reliability benefits all users in Metropolitan's service area
 - Provides a long-term revenue source that does not vary with water sales to cover fixed costs

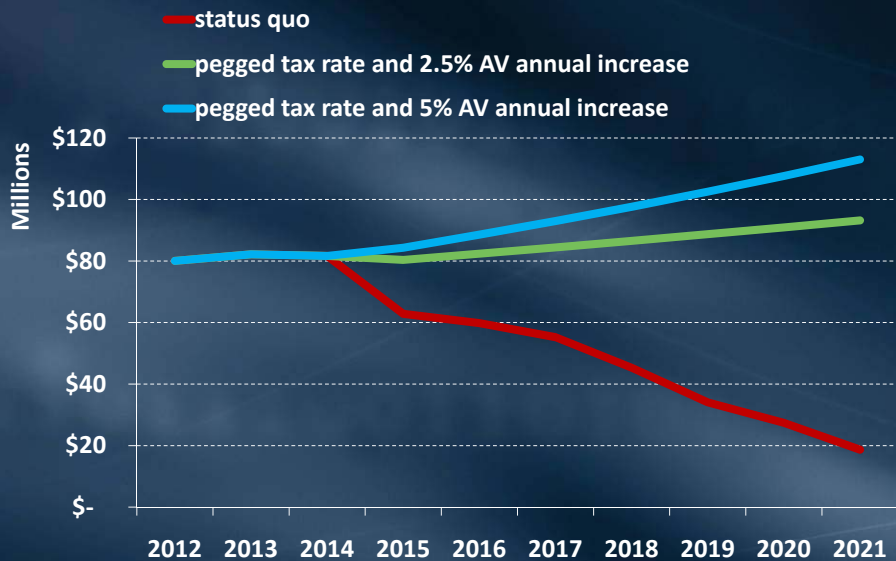
Ad Valorem Tax Solution

- Two approaches to addressing the additional use of Metropolitan's Ad Valorem tax authority
- Seek legislative change to Section 124.5 of the MWD Act
- Work within the existing limits of Section 124.5 of the MWD Act

Process to Implement an Adjustment to the Ad Valorem Tax Rate

- Send letter to both Senate and Assembly at least 10 days before public hearing
- Hold public hearing
- Board finds that a tax in excess of the MWD Act restriction is “essential to the fiscal integrity of the district”
- Annual Process
 - The process described would be performed annually

Ad Valorem Tax Rate Scenarios



Funding the DHCCP

- Adjusting the Ad Valorem tax rate could generate additional revenues, but the increment would not fully cover future DHCCP costs
- Option #1: Use adjusted AV tax revenues to offset DHCCP costs and then augment with a new fixed charge
- Use adjusted AV tax revenues to offset SWP costs and develop a stand-alone DHCCP charge to recover the DHCCP costs

New Fixed Charge Option: DHCCP Costs

- Current SWP Fixed Cost recovery:
 - Primarily recovered in the System Access Rate and Supply Rates, which are volumetric
 - Only 10% currently recovered through property taxes
- Recover future DHCCP through a fixed charge
 - Allocation basis needs to be developed
- DHCCP fixed charge produces fixed revenues in the long term

Fixed Charge Option #1: DHCCP Fixed Charge and Pegged AV tax rate

- Current estimated cost of DHCCP in FY 2014/15 of \$5 million, FY2020/21 of \$113 million
- In conjunction with pegging the AV tax rate, would produce a revenue stream to cover the costs of a Delta conveyance facility by FY 2020
 - If the AV increment is applied to the DHCCP costs, the fixed charge would generate \$39 million in FY 2020/21
- Demonstrates commitment by Metropolitan and its member agencies to funding a solution to the Delta issues

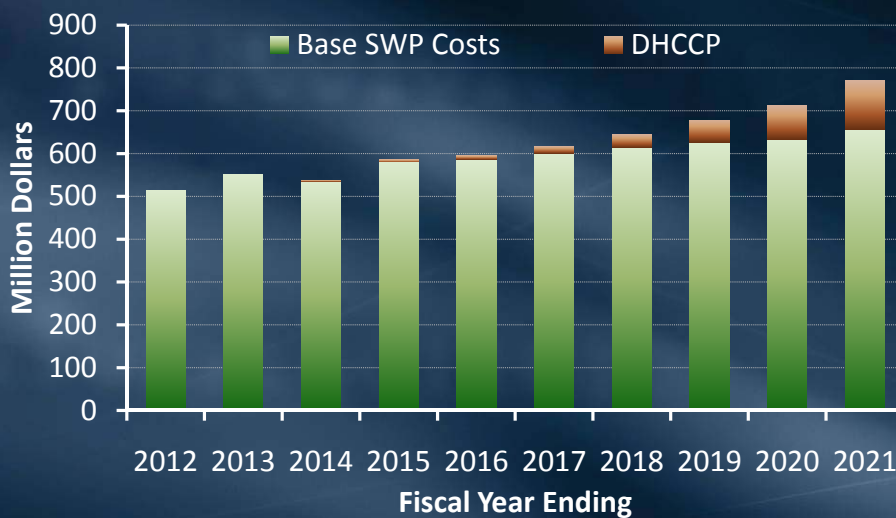
Fixed Revenue Forecast, with pegged AV and DHCCP Fixed Charge

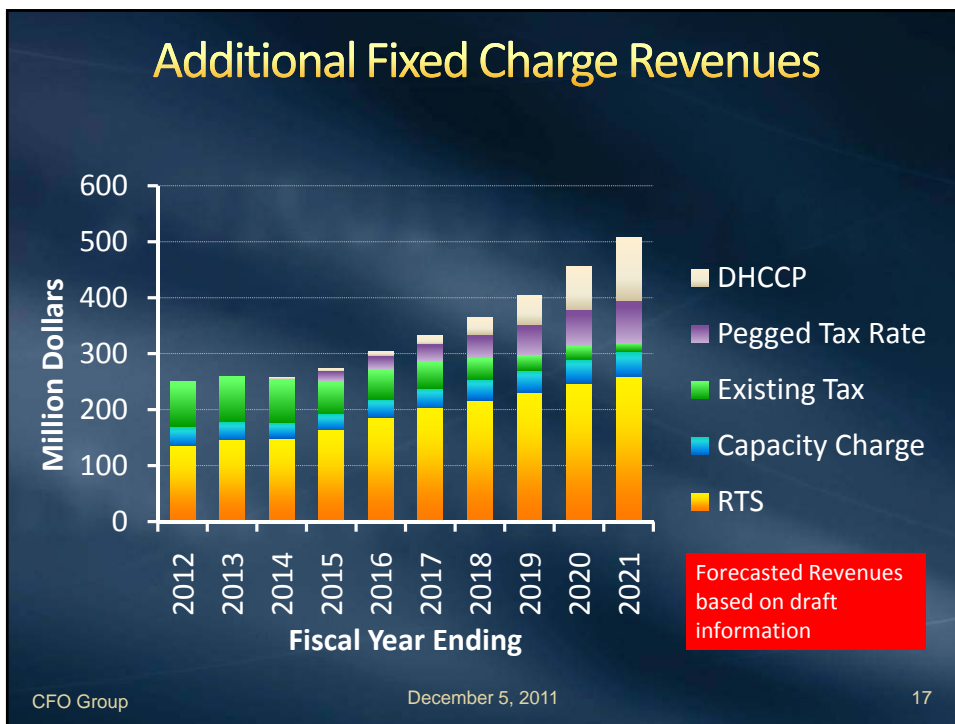


Fixed Charge Option #2: DHCCP Fixed Charge as a Stand Alone Charge

- Current estimated cost of DHCCP in FY 2014/15 of \$5 million, FY2020/21 of \$113 million
- DHCCP Fixed Charge would produce a revenue stream to cover the costs of a Delta conveyance facility by FY 2020
 - The pegged AV and a full DHCCP Charge would generate \$187 million in FY 2020/21
 - The adjusted AV could be used to offset other SWP costs, which are increasing over time

SWP Costs





MWD Treatment Plants and the Imported Water Distribution System

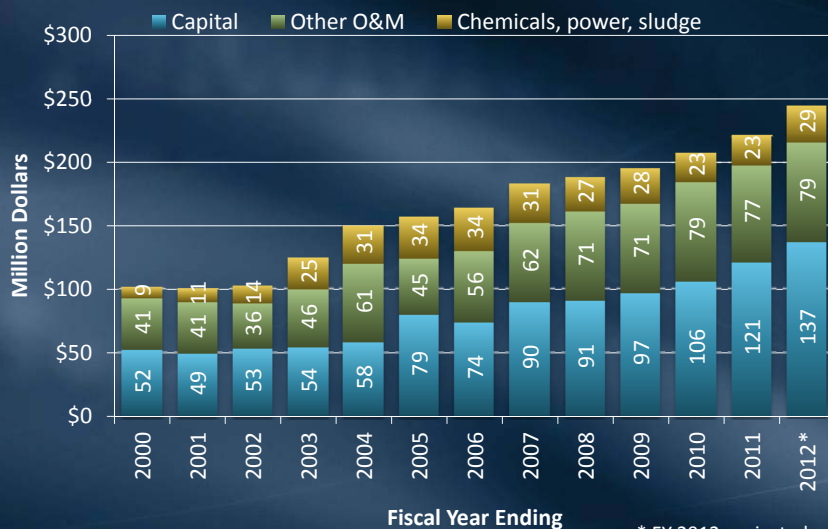


CFO Group

December 5, 2011

19

Treated Water Costs Continue to Increase Comprise ≈ 20% of Revenue Requirements

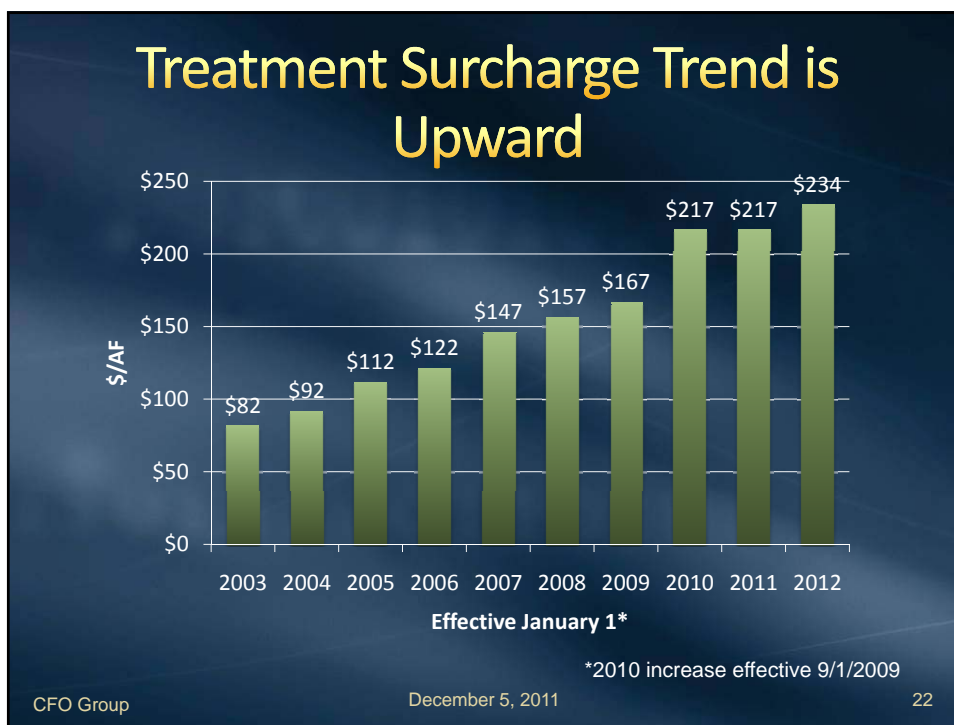
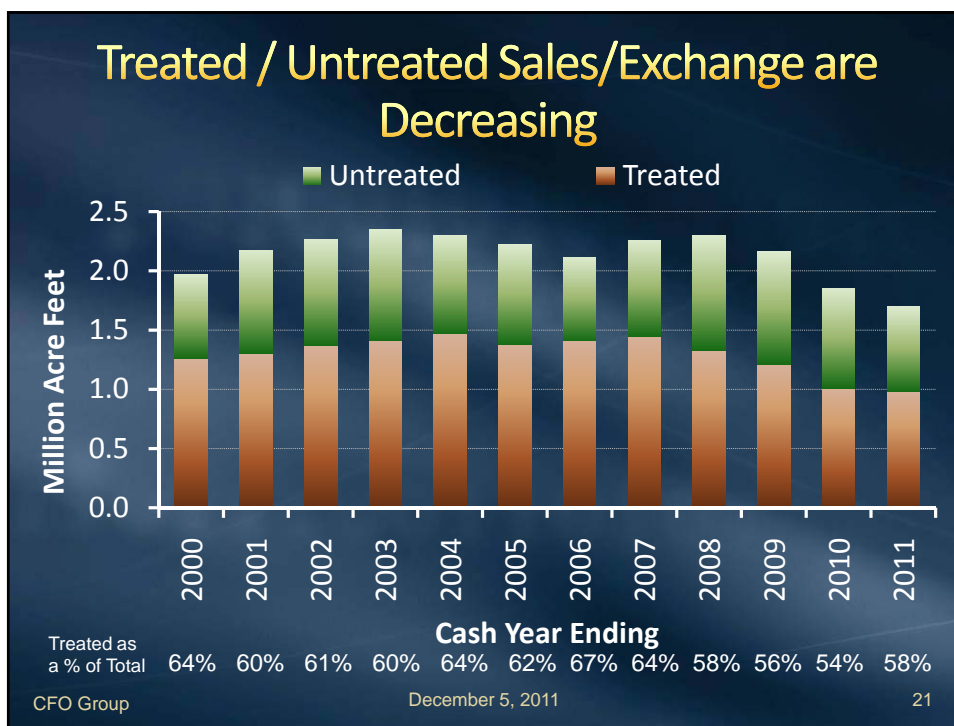


CFO Group

December 5, 2011

* FY 2012 projected

20



Treated Water Cost Recovery

- March 2005 Board Action:
 - “Work with the member agencies and Budget, Finance, Investment and Insurance Committee to evaluate a Treated Water Capacity Charge to be considered by the Board in January of 2006 to be effective January of 2007”
- November 2005 Information letter
 - No follow-on discussion
- LRF Rate Refinement Subgroup
 - October 2007, Raftelis Financial Consulting
 - April, May and June 2008
 - October 2008

Many Rate Options Have Been Considered

- Treated Water Capacity Charge (TWCC)
- Treated Water Peaking Charge (TWPC)
- Volumetric, declining block structure that ties volume to peak capacity used (TWDB)
- Seasonal Charge

Treatment Study Issues

- Previous discussions of a Treated Water Capacity Charge, or alternatives, have not generated support
- Reallocation of costs resulted in “winners” and “losers”
- Size of targeted fixed cost recovery—\$51 million in 2008 analysis—was relatively large

New Fixed Charge Option: Treated Water Costs

New Fixed Charge Option: Water Quality and Source Protection

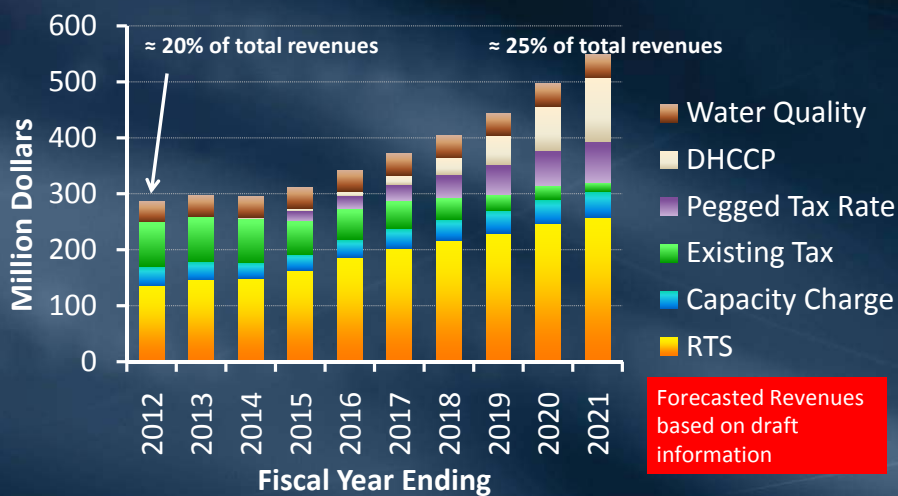
- Fixed charge to recover fixed O&M and Debt Service costs associated with Quality, Source Protection, and security activities
 - Range of \$20 to \$30 million initially
 - Reduces Treatment Surcharge
 - Allocate on a basis less likely to result in noticeable shifts
- Provides near-term benefits to revenue structure
- As costs associated with quality/source protection/security mandates increase over time, charge would recover them

CFO Group

December 5, 2011

27

Fixed Revenue Forecast, with Quality/Source Protection Fixed Charge

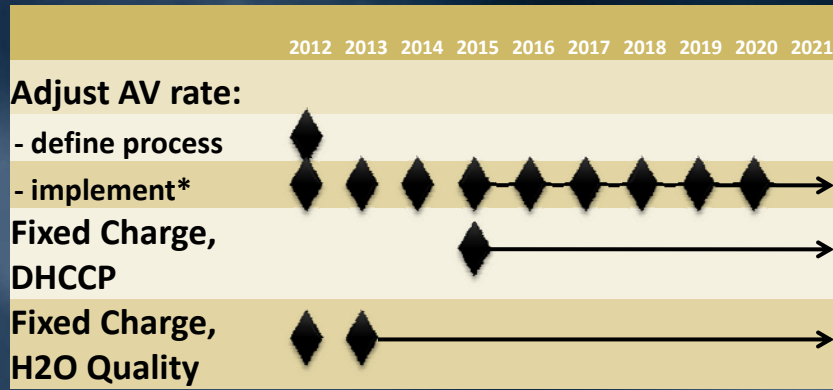


CFO Group

December 5, 2011

28

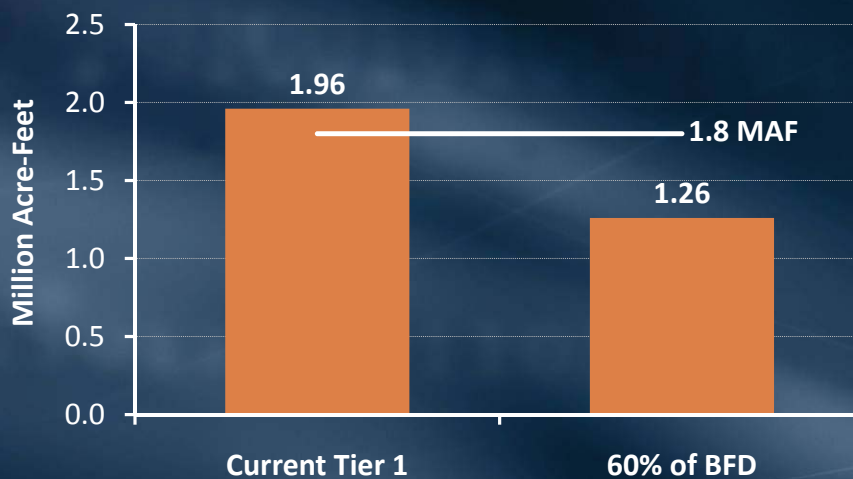
Implementation Timeline



* Board must make annual finding

Purchase Orders

Impact of No Extension of Purchase Orders, CY 2012 Tier 1 Limits



CFO Group

December 5, 2011

31

Potential Benefits of Future Purchase Orders

- Reason for POs was to provide a financial commitment to Metropolitan in exchange for greater access to Tier 1 Supply rate
 - Did POs really provide a financial commitment that was meaningful?
 - Do greater fixed revenues achieve a result equal to POs?
- Some agencies want to “trade” for Tier 1 access
 - Tier 1 is a pricing mechanism, not a right to water
 - Linked to fixed cost recovery

CFO Group

December 5, 2011

32

Observations/Lessons Learned from Existing Purchase Orders

- Was Tier 2 a disincentive to agencies to store water in wet years?
- Tier 2 as a price signal to develop local supplies
 - Does it need to be in place or applied every year?
 - Only in dry years? Only during a Supply Allocation event?
- When should agencies be exposed to Tier 2?

Tier 1 Limits

- Option #1: default, 60% of BFD, no POs
- Option #2: Roll existing calculation forward
 - See handout
- Option #3: Re-establish the Initial Base Firm Demand
 - Highest firm sales in last 10 fiscal years
 - See handout
- Option #4: Use recent base period demand from the Water Supply Allocation Plan
 - Better align with need
 - Accounts for local supply development
- Option #5: Use SAP data and reduce Tier 1 limit to long-term demands
- Others?

Next Steps

- December 12 F&I Workshop
 - Board discussion on the work of this group to date
- 2012/13 Budget and Revenue Requirements letters, January 2012
 - Finance and Insurance Committee
- Future Workgroup meeting dates to be determined