Rate Refinement Workgroup

August 13, 2012

Agenda

- Linking rate structure and water management actions: Continued discussion of dry-year Tier 1 limit
- Baseline alternatives for dry-year Tier 1 limit
- Outstanding storage issues
  - Threshold for participating in incentive storage proposals
- Fixed revenue
  - Treatment cost recovery
  - Fix Ad Valorem tax rate
- Schedule/Process to move forward

Dry-Year Tier 1 Limit Alternatives

Observations on Linking Rate Structure and Water Management Actions

- Rate structure elements unchanged
  - Unbundled, status quo
- Tier 2, storage incentives based on hydrologic/operational conditions
  - "Normal" = supply at Tier 1; storage incentives available
  - "Wet" = supply at Tier 1; storage incentives available
  - "Dry" = Tier 2 in effect

Observations on Linking Rate Structure and Water Management Actions (cont'd)

- Addresses several priorities
  - Retains Tier 2 price signal
  - Determines when Tier 2 and Storage incentives are in effect
- Improves revenue stability and certainty through conservative sales forecasting and development of additional fixed revenues
  - Use 1.7/1.75 MAF of sales/exchange to set rates

Hydrologic/Operational Conditions

- Tier 2 implementation, storage incentives availability based on hydrologic/operational conditions
- "Normal" = not in extremes for either surplus or shortages; supply at Tier 1; storage incentives available
- "Wet" = putting to SWP Groundwater Storage; spill possible; supply at Tier 1; storage incentives available
- "Dry" = pursuing transfers, exercising call options to meet demands; Tier 2 in effect

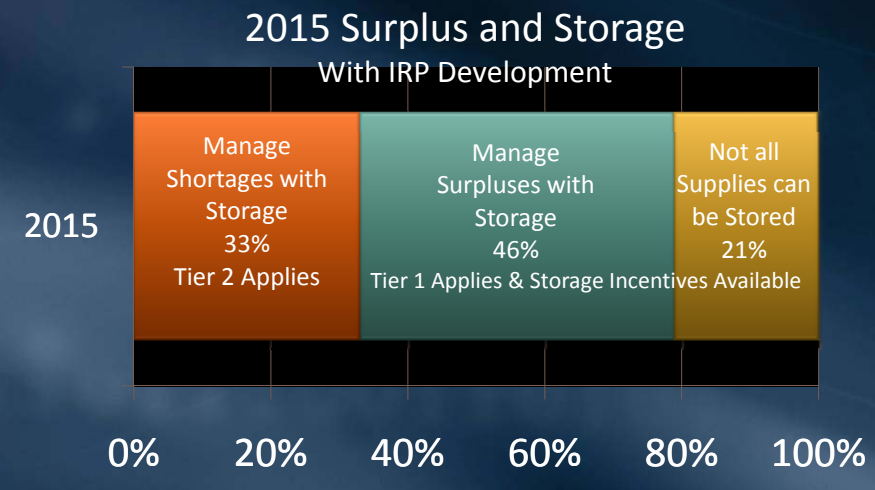
Hydrologic/Operational Conditions

- Coordination of supply rates and sales year conditions
  - Determines when Tier 2 and storage incentives are in effect
  - Retains Tier 2 price signal in all years, but only in effect in "Dry" years
  - Tier 2 continues to provide an incentive to invest in conservation and local projects
  - Tier 2 in a wet year may discourage storage activities

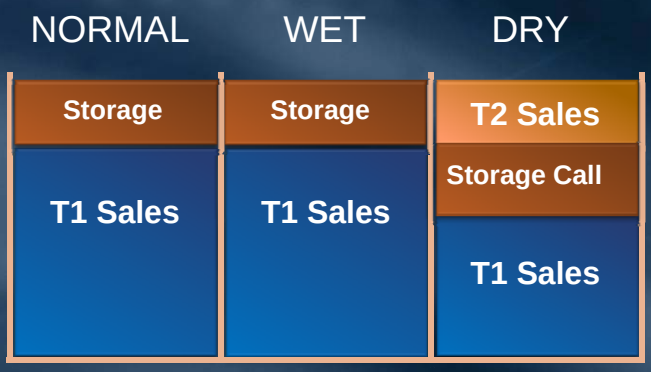
Water Supply and Drought Management Plan Stages

Surplus Stages				Actions	Shortage Stages					
4	3	2	1		1	2	3	4	5	6
				Shortage: Tier 2 Applies						
				Storage @ Tier 1 and Incentives						
				Put to SWP Groundwater Storage						
				Put to SWP Carryover						
				Put to Conjunctive Use Groundwater						
				Put to DWR Flexible Storage						
				Put to Metropolitan Surface Storage						
				Public Outreach						
				Take from Metropolitan Surface Storage						
				Take from SWP Groundwater Storage						
				Take from Conjunctive Use Storage						
				Tier 1 Reductions For Storage Incentives						
				Take from DWR Flexible Storage						
				Extraordinary Conservation						
				Call Options Contracts						
				Buy Spot Transfers						
				Implement Water Supply Allocation Plan						

How Often Would Tier 2 Apply?



Concept for Tier 2 & Storage Incentive Availability based on Hydrologic & Operational Conditions



Potential Dry-Year Tier 1 Limit Development

- Several approaches reviewed
- Resource-based approach presented and feedback received
  - Based on draft resource analysis
  - Perform without SDCWA Exchange
  - Focus on demand for imported water supply, not use of the system
    - Allocating Tier 1 water in a dry year

Tier 1 Limit - Resource Based Approach

- IRPSIM Analysis
  - 2012 starting conditions
  - 5-year simulation (2013-2017)
  - Range of historical hydrologies (1922-2004)
- What annual sales level could be supported without additional dry-year transfers?
  - Draft analysis: 1.9 MAF under IRP forecast
- Can be distributed to agencies using different patterns

Using a Resource-Based Approach to Establish the Dry-Year Tier 1 Limit

- Resource-based approach represents sustainable demand level in a dry year without necessitating transfers
  - More appropriately represents what is available versus rate setting target
  - Takes into consideration retail demands and local resources
  - Member agencies know their Tier 1 limit going into a dry fiscal year

Baseline Example

Options for Baseline to Determine Tier 1 Limit

- 10 year maximum sales
  - Total: 2.6 MAF; Firm: 2.2 MAF
- 10 year average sales
  - Total: 2.0 MAF; Firm: 1.8 MAF
- 5 year maximum sales
  - Total: 2.3 MAF; Firm: 2.1 MAF
- 5 year average sales
  - Total: 1.8 MAF; Firm: 1.7 MAF
- Total sales of supply or firm only?
- Rolling or fixed?
  - If fixed, for what period going forward?

Historical Sales Proration to 1.9 MAF

Establishing the Baseline for Tier 1 Limits: Straw Proposal

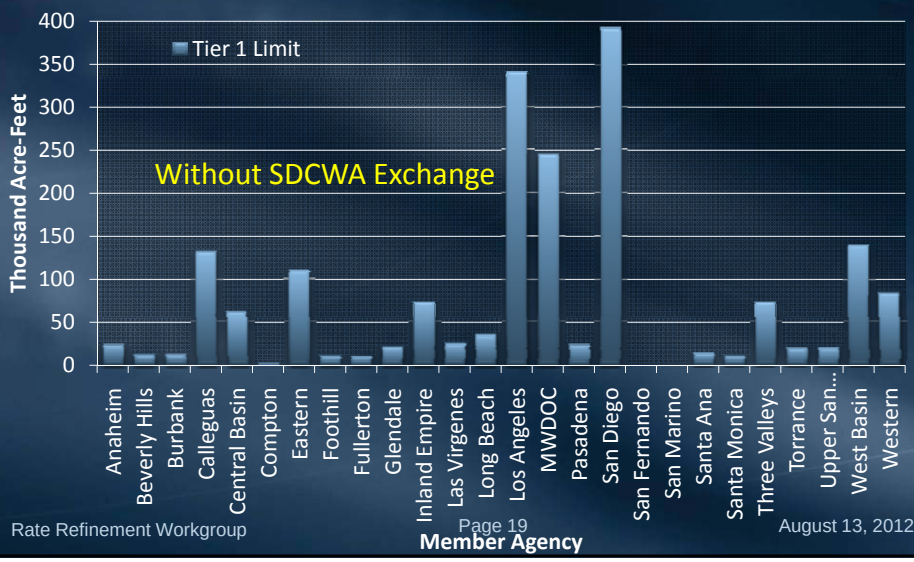
- Most recent 5 fiscal years
  - More reflective of current demands on Metropolitan
  - Incorporates shift of IAWP to firm demands, use of firm purchases for groundwater
  - Considers impacts of price-induced conservation, local resource development, and other demand management measures at the local level in more timely manner
- Firm
  - In a dry year, focus supplies on meeting firm demands
  - Going forward, interruptible programs limited to storage incentive puts

Establishing the Baseline for Tier 1 Limits: Straw Proposal (cont'd)

- Averaged
  - Spiking of demands by member agency(ies) in any one year could alter the Tier 1 allocation if using maximum sales
  - Averaging does not allow a spike in demands to carry forward and potentially result in regional demands consistently exceeding the resource-based dry-year limit
  - Likely upward adjustment to Tier 1 limit allows for dry-year variation in demands
- Rolling calculation
  - Continuously reflects the most recent demands
  - Incorporates local resource development as it occurs
- Could be provided annually with the Member Agency Managers Rates and Charges Notification Letter

1.9 MAF Resource Approach

Distribution Pattern – FY 2008-2012 Average Firm Sales by Agency



When Would Tier 2 Have Been Applied?

2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
NO	NO	NO	NO	YES	YES	YES	NO	NO	NO

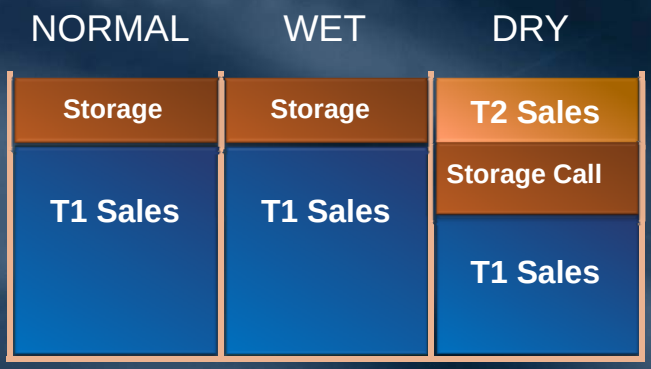
Tier 2 Sales:
89TAF 212TAF 40TAF 70TAF 291TAF 236TAF 85TAF 36TAF 1TAF

Storage Incentive Program

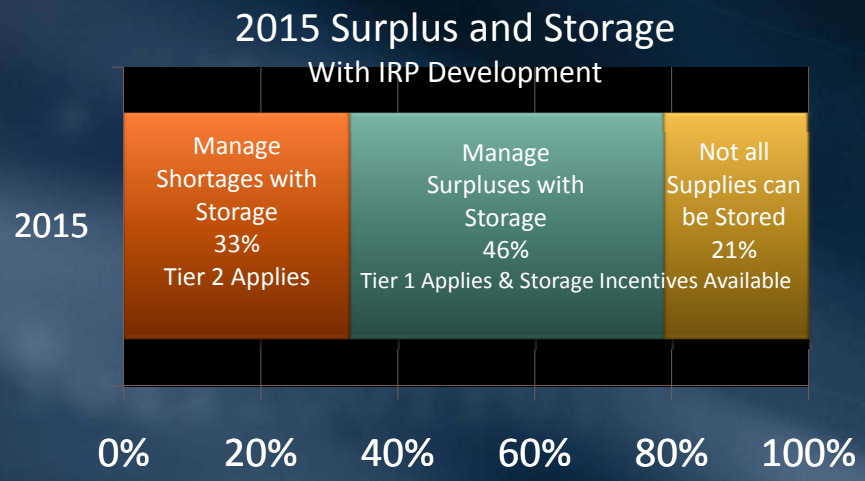
When Would Water For Storage be Available?

- It is a question of rates, not availability
- Tier 1 Full Service pricing available in "wet" and "normal" sales years without exposure to Tier 2
  - "Normal" = not in extremes for either surplus or shortages; supply at Tier 1
  - "Wet" = putting to SWP Groundwater Storage; spill possible
- Storage incentives also available in "wet" and "normal" sales year
- Implemented at General Manager's discretion

Concept for Tier 2 & Storage Incentive Availability based on Hydrologic & Operational Conditions



How Often Is Storage Available?



Outstanding Issue: Storage

- Should there be an annual full service sales minimum for an agency to participate in the incentive program?
- If consecutive wet years, member agencies could participate in the storage incentive program without ever having perform in a dry year
  - With no annual full service sales minimum, member agency could purchase only incentive water
- Straw Proposal: rate setting based on 1.5 MAF of full service sales (supply) in FY 2012/13 and 2013/14
  - As long as a member agency's full service purchases are equal to their 5-year rolling average of firm purchases, scaled to 1.5 MAF for all agencies, they can participate

Historical Sales Compared to Tier 1 Limit and Storage Threshold

Storage Issues (cont'd): Straw Proposal

- Applicability of Capacity Charge
  - Delivered only during periods when excess System Capacity exists
  - Deliveries can be interrupted
  - Not Applicable to Storage incentive program
- Applicability of Readiness to Serve Charge
  - Recovers capital costs associated with standby service and emergency storage
  - Not Applicable to Storage incentive program
- Certification
  - Excluding deliveries from CC and RTS calculations will necessitate certification process

Treatment Cost Recovery

Treated Water Cost Recovery Objectives

- Infrastructure must be designed to meet peak demands
- Current rate structure recovers peaking and standby costs uniformly through a volume charge paid by member agencies taking treated water
- Standby and peaking costs can be recovered through fixed charges
  - Board objective of increasing fixed charges and addressing peaking use
  - More equitably allocates costs of service

Treated Water Cost Recovery

- Treated water costs for FY 2012/13 from Cost of Service report
  - Fixed Demand: $48.3M assigned to peaking
  - Fixed Standby: $28.4M assigned to standby
  - Fixed and Variable Commodity: $165.6M volumetric
- Develop Treatment Cost Recovery consistent with the Conveyance and Distribution system cost recovery
  - Standby costs recovered through a Treatment RTS
    - 10-year rolling average of firm treated water sales
  - Peaking costs recovered through a Treated Water Capacity Charge
    - Three year look back of summer peak day demands; potentially phased-in
  - All other costs are recovered on a volumetric basis

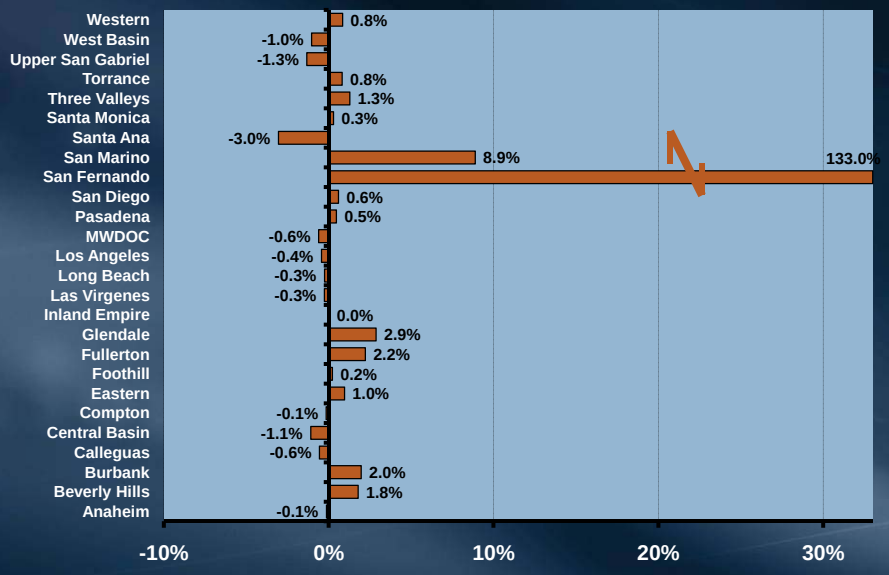
Treated Water Rate Restructuring

- For demonstration, in 2013:
  - Treatment Surcharge would be $174/AF, or $80/AF lower
  - Treatment Capacity Charge would be $21,000/cfs, charged on the peak treated demands from 2009 to 2011
  - Treatment RTS would be $29M, or $24/AF equivalent
    - Existing RTS recovered over 1.8 MAF firm demand
    - Treatment RTS recovered over 1.2 MAF treated firm demand
- Would go into effect with the 2015 rate design

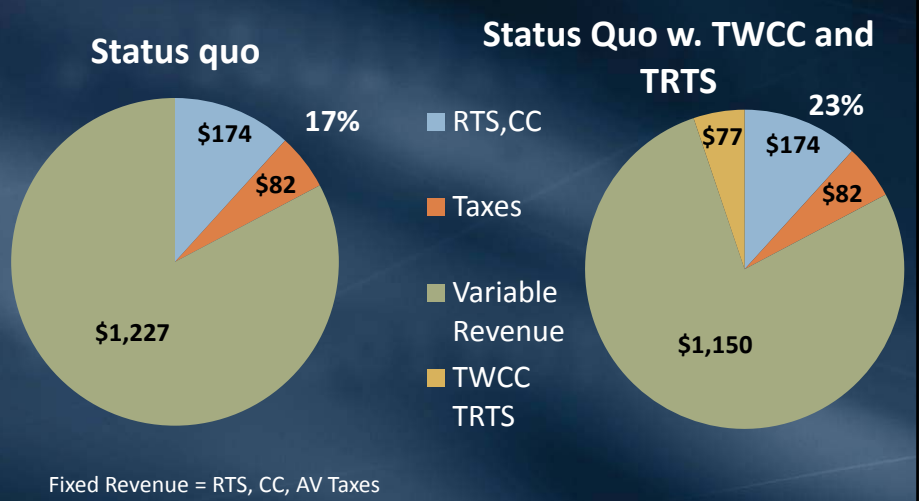
Treated Water Fixed Charges

- Historical data include exchange/wheeling, if treated
- Rate impacts highly correlated with variability of summer season treated demands
  - Reflects agencies using Metropolitan's treated water system in the summer to meet peak demand
- Two agency's impacts reflect intermittent use of treated connections

TWCC and TRTS: Rate Impacts, Full Fixed Cost Recovery



Revenues FY2012/13 ($M)



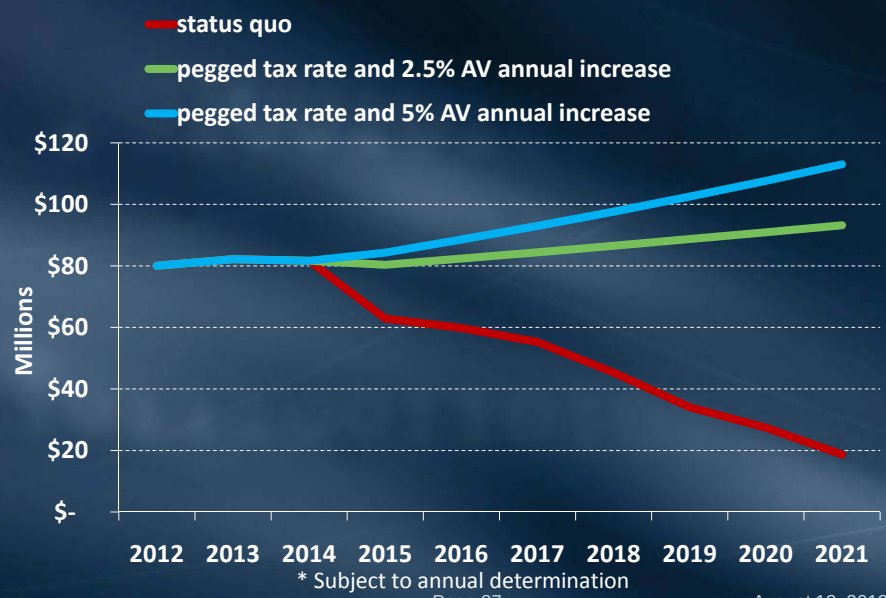
Fixed Revenue = RTS, CC, AV Taxes

Fix Ad Valorem Tax Rate

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 Rate Scenarios*



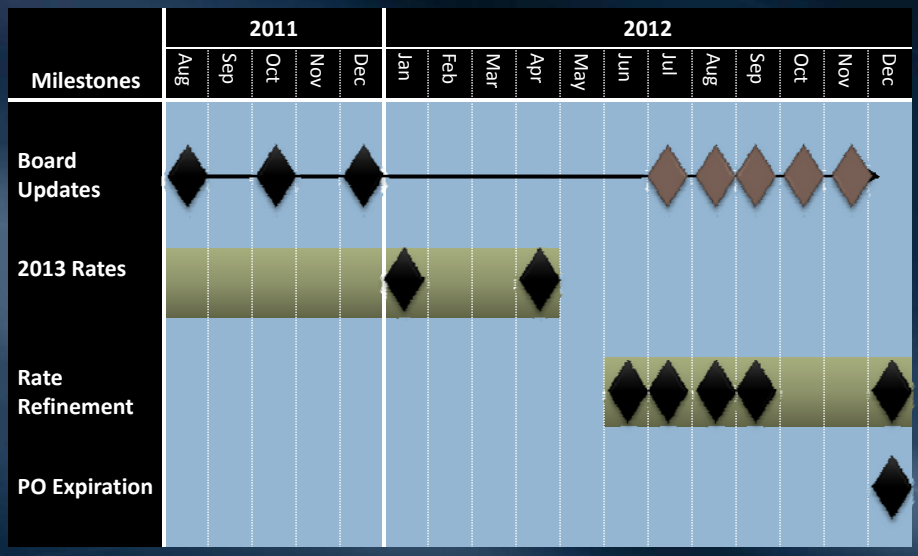
* Subject to annual determination

Discussion

Schedule/Process to Move Forward

- Member Agency Managers meetings
  - June 15, July 13, August 24, September 14
  - Managers establish priorities
- Rate Refinement Workgroup to meet between Managers meetings
  - Friday, June 29
  - Wednesday, July 25
  - Monday, August 13
  - Thursday, August 30
  - Wednesday, September 26
- Board Information letter in October 2012
- Board Action letter in November 2012
  - Administrative Code changes

Timeline : Rate Refinement

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Rate Refinement Workgroup
Page 41
August 13, 2012