



Finance & Insurance Committee

# Section 124.5 Determination Finding

Item 7-2

April 11, 2022

# Summary of Process

*Staff and the Board have engaged in a detailed, methodical and transparent process to assess the circumstances for making a finding related to the applicability of Section 124.5*

## February 2022

- Board approved a hearing date
- Board received an informational Board Letter on the proposed budget and rates, and participated in several workshops
- Staff provided notice to the CA State Legislature of the public hearing
- Staff assembled a website that contains the key supportive documents for its finding and recommendation

## March 2022

- Staff provided the Board an informational Board letter and presentation covering the substantive bases for staff's recommendation
- Board held a public hearing on this matter and the proposed budget, rates and charges

# MWD Act Section 124.5

- Metropolitan Act Section 124.5, enacted in 1984, limits ad valorem property taxes to recover:
  - Metropolitan's general obligation bond debt service
  - A portion of its State Water Contract (SWC) obligations, limited to the debt service on state general obligation bonds (Burns-Porter bonds) for facilities benefitting Metropolitan
- The restrictions of Section 124.5 do not apply if the Board finds that collecting more is "essential to the fiscal integrity of the District"
- Since FY 2013/14, the Board has determined it was essential to Metropolitan's fiscal integrity to maintain the tax rate at .0035 percent

# Essential to Fiscal Integrity

- Not defined in statute or elsewhere
- Applicability determination left to discretion of the Board
- No time period for the determination was established by the CA State Legislature
- Industry and Metropolitan metrics provide guidance

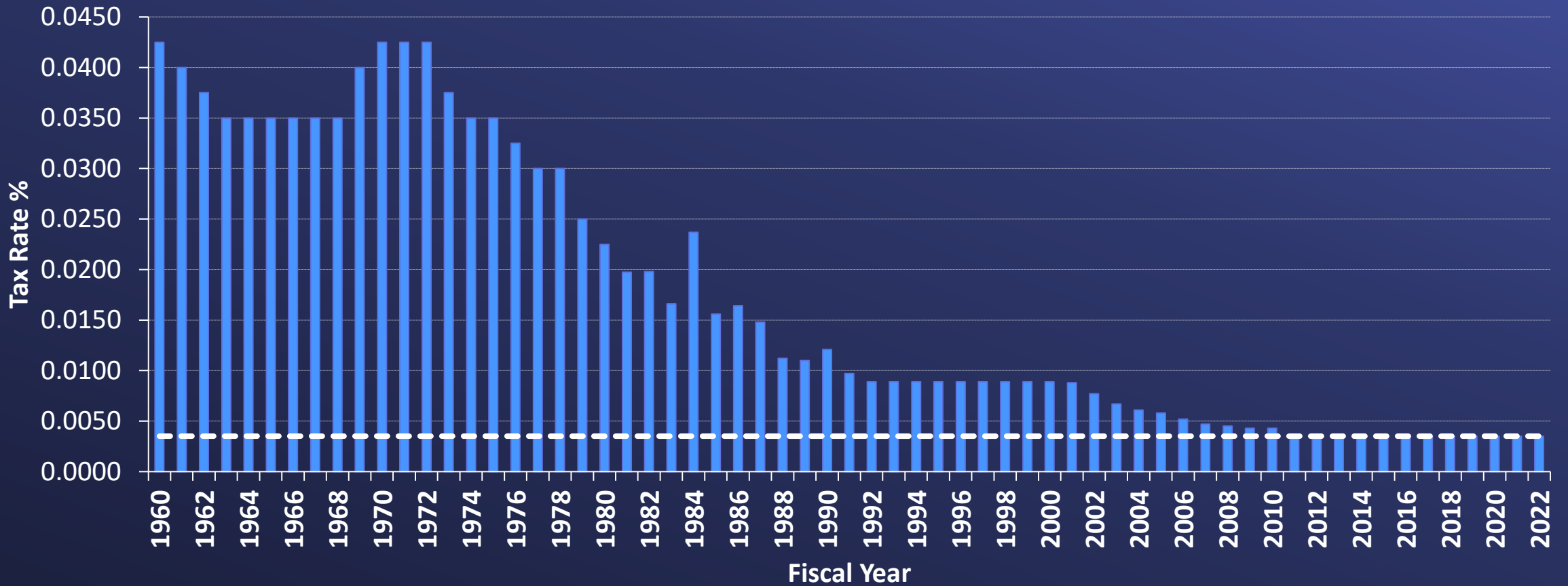
# Legal Effect of 124.5 Determination

- Section 124.5 would not apply in the relevant time period
- No specific tax rate is set with this determination; no minimum or maximum tax rate established
- Tax rates are considered and set by the Board each August

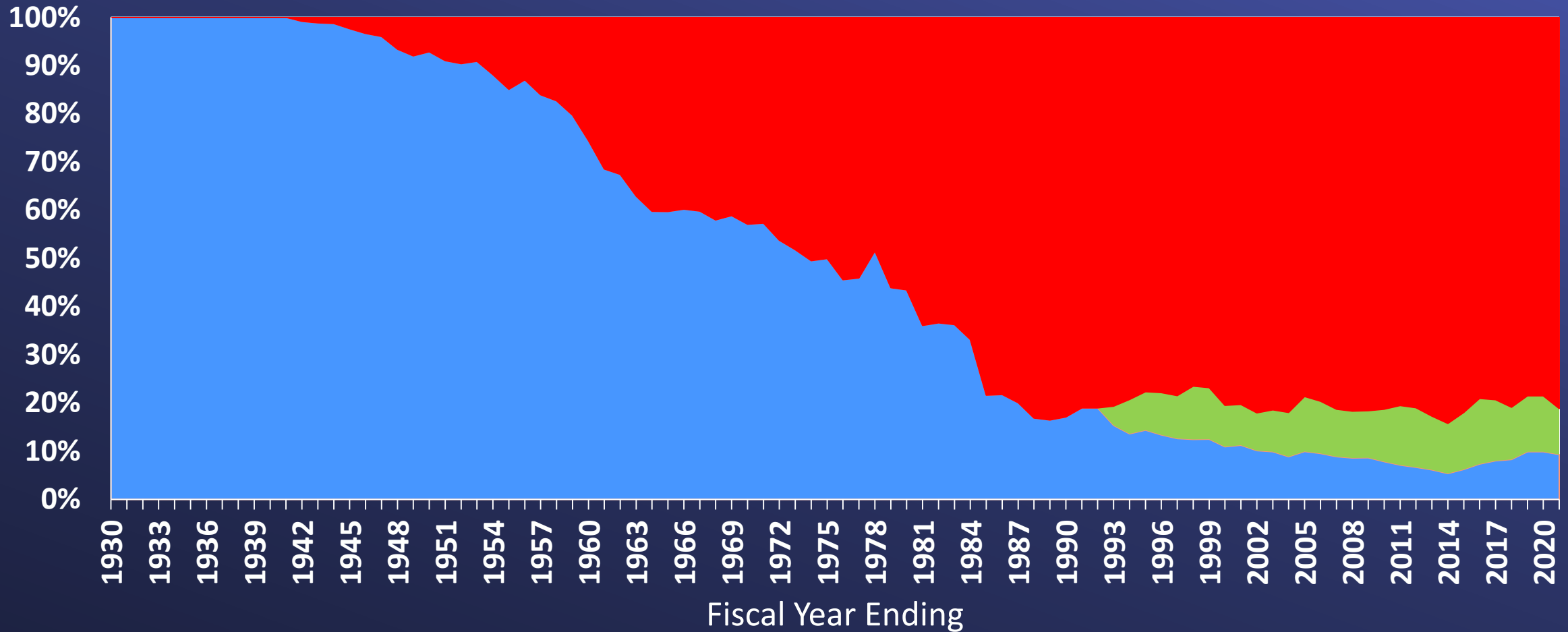
# Historical Property Tax Rates

Property Tax Rates Since 1960

Tax Rate %    - - - 0.0035%



# Historical Revenue Sources



■ Property Taxes

■ Fixed Charges

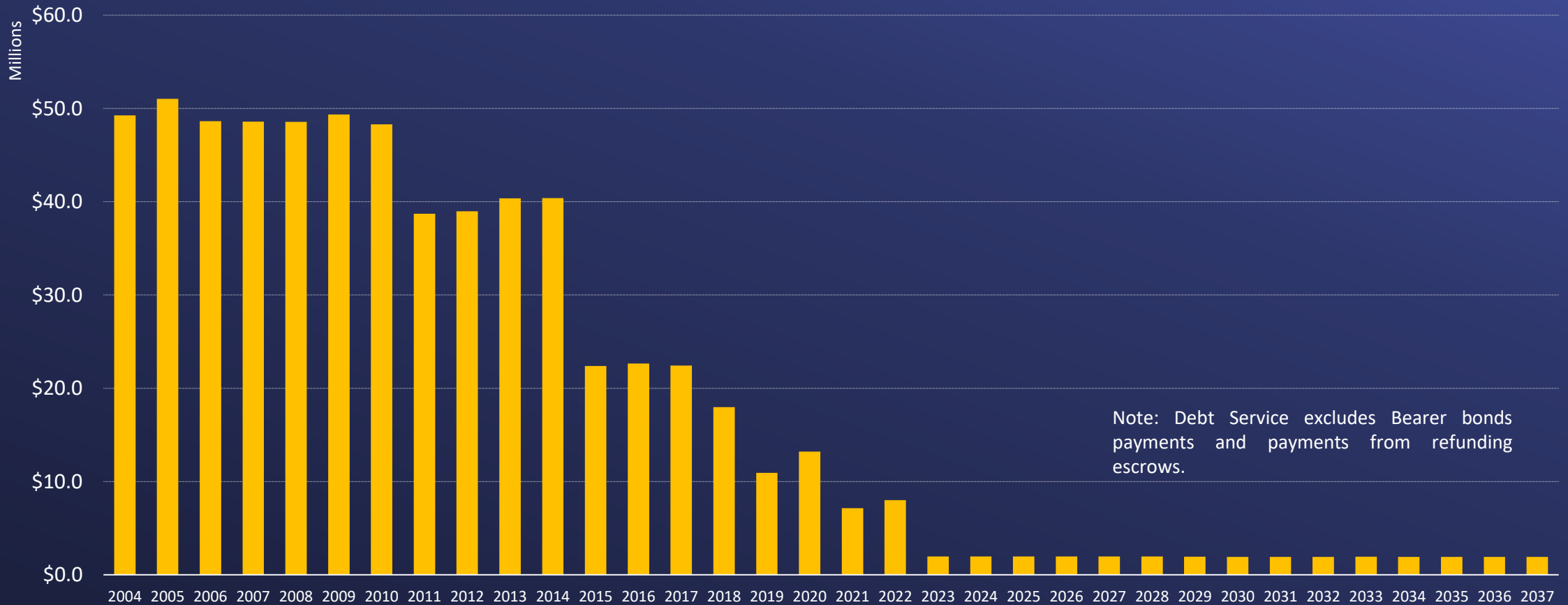
■ Volumetric Revenues\*

\* Includes water sales, exchanges and wheeling

# Outstanding Debt Service

## MWD GO Bonds

Fiscal Year Annual MWD GO Bonds Debt Service

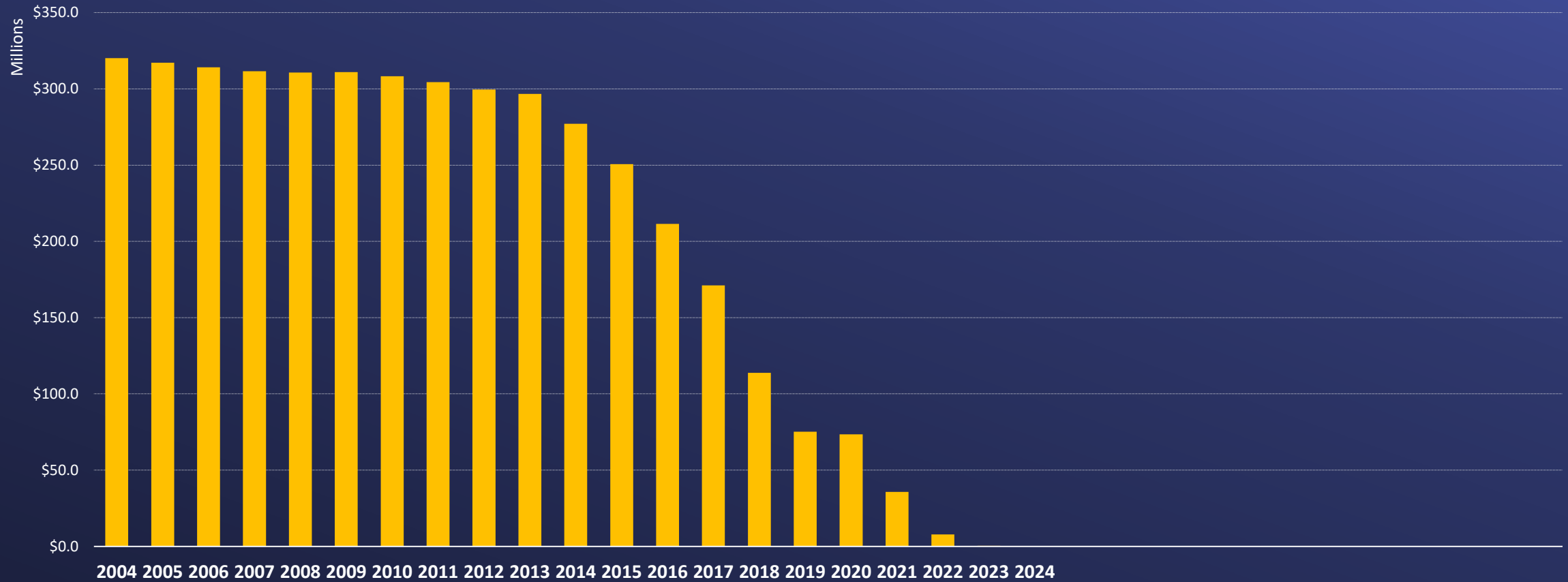




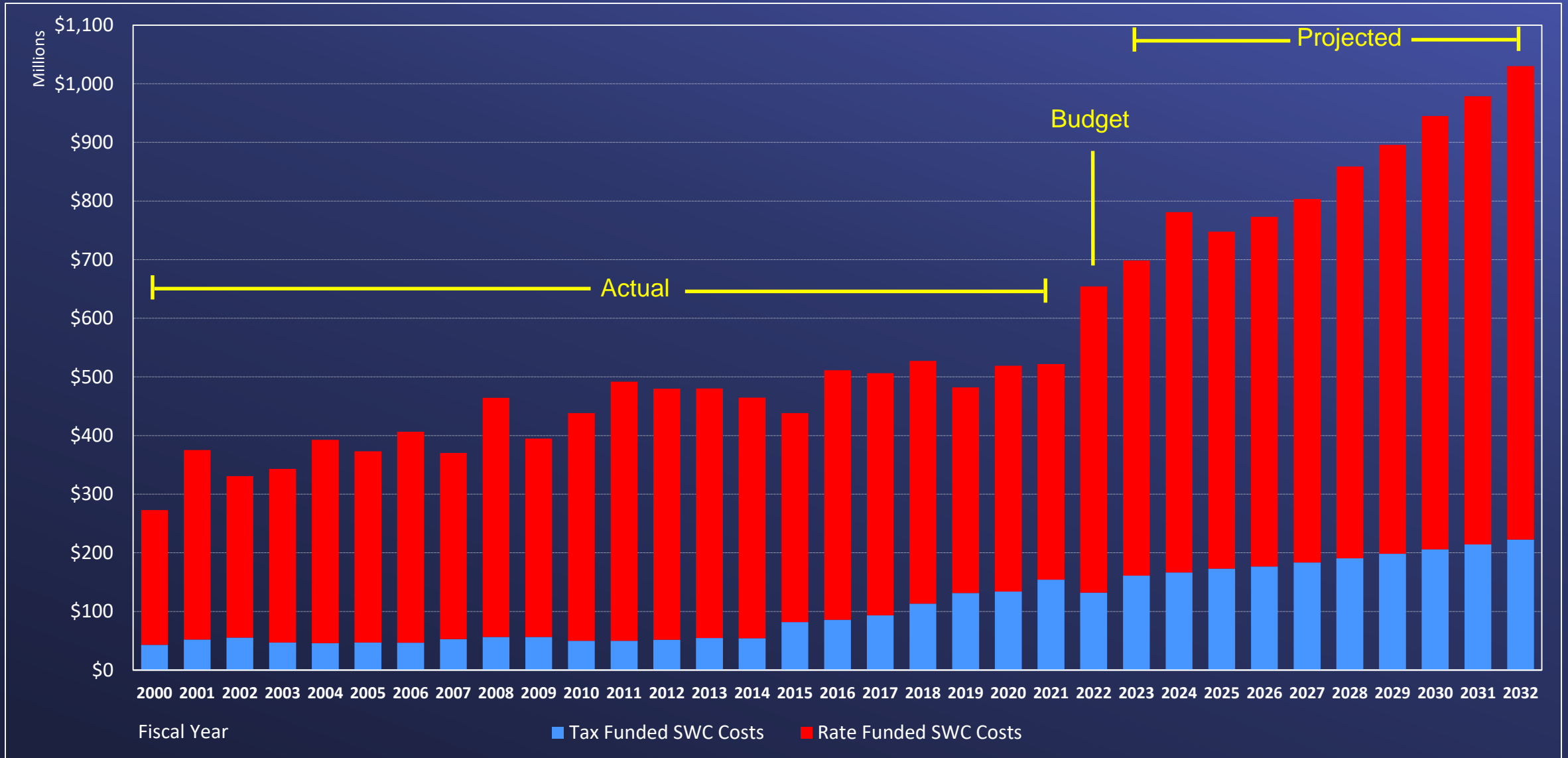
# Outstanding Debt Service

## DWR Burns-Porter Bonds

Calendar Year Annual BP Bonds Debt Service



# State Water Contract Costs



# Financial Policies and Fiscal Integrity

- The Board has adopted financial policies that provide guidance for determining its fiscal integrity.
  - Fixed-Charge Coverage Ratio of 1.20x
  - Minimum and Target Reserves
  - Revenue Bond Coverage Target of 2.00x
- A reduction in fixed charges increases dependence on variable revenue, which puts pressure on meeting the Board's financial policies during periods of higher volatility/low water transactions.

# Property taxes help address Metropolitan's inherent volatility in its financial profile

- Metropolitan's inherent volatility is tied to cycles of hydrology and long-term impacts of Climate Change.
- Fixed revenues are a key factor in managing Metropolitan's financial volatility, which is tied to these underlying determinants.
- Property taxes represent approximately 50% of fixed revenues.
- As a more stable revenue stream, property taxes offset the need to adjust volumetric rates more frequently, or in a greater magnitude.
- If a determination regarding the applicability of Section 124.5 limitation is not made, an additional 9% rate increase would be required to recover costs

# Metropolitan's fiscal integrity is supported by...

- Continuing an ad valorem property tax rate in excess of the 124.5 limit
- Maintaining a fixed revenue source in line with growing SWC costs
  - At its current rate of 0.0035 percent, property tax revenue would pay 22 percent of SWC obligations
  - If the Section 124.5 limit applies, property taxes would pay less than one-tenth of 1 percent of SWC obligations
- Providing a diversity of fixed revenue sources (Prop Tax, RTS/Standby Charge, Capacity Charge)
- Distributing the costs of Metropolitan's services more equitably (residences and businesses pay a modest share vs. Member Agencies) through property taxes

# Support for a Four-Year Determination

Making a four-year determination of the applicability of the MWD Act Section 124.5 is appropriate because...

1. Provides flexibility to manage Metropolitan's finances during current drought conditions
2. Ongoing financial and strategic planning efforts, which rely on this revenue component, won't be completed and implemented within the upcoming biennium budget period
3. The inherent volatility found in Metropolitan's financial profile has a cyclicity beyond the biennium budget period
4. Consistent with the scope of many financial planning timeframes

# Options for Consideration

Staff has presented the board with three options for the determination finding related to the applicability of the Section 124.5 limitation:

Option #1: Adopt the resolution finding that for fiscal years 2022/23 through 2025/26, the ad valorem property tax rate limitation of Metropolitan Water District Act Section 124.5 is not applicable because it is essential to Metropolitan's fiscal integrity to collect ad valorem property taxes in excess of the limitation

Option #2: Adopt the resolution finding that for fiscal years 2022/23 and 2023/24, the ad valorem property tax rate limitation of Metropolitan Water District Act Section 124.5 is not applicable because it is essential to Metropolitan's fiscal integrity to collect ad valorem property taxes in excess of the limitation

Option #3: Make no determination and allows the Section 124.5 limitation to apply

# Recommendation

## Staff recommends Option #1

Option #1: Adopt the resolution finding that for fiscal years 2022/23 through 2025/26, the ad valorem property tax rate limitation of Metropolitan Water District Act Section 124.5 is not applicable because it is essential to Metropolitan's fiscal integrity to collect ad valorem property taxes in excess of the limitation





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# Questions

