



# San Diego County Water Authority

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April 30, 2017

Mr. Randy Record and  
Members of the Board of Directors  
Metropolitan Water District of Southern California  
P.O. Box 54153  
Los Angeles, CA 90054-0153

**MEMBER AGENCIES**

Carlsbad  
Municipal Water District

City of Del Mar

City of Escondido

City of National City

City of Oceanside

City of Poway

City of San Diego

Fallbrook  
Public Utility District

Helix Water District

Lakeside Water District

Olivenhain  
Municipal Water District

Otay Water District

Padre Dam  
Municipal Water District

Camp Pendleton  
Marine Corps Base

Rainbow  
Municipal Water District

Ramona  
Municipal Water District

Rincon del Diablo  
Municipal Water District

San Dieguito Water District

Santa Fe Irrigation District

South Bay Irrigation District

Vallecitos Water District

Valley Center  
Municipal Water District

Vista Irrigation District

Yuima  
Municipal Water District

**OTHER  
REPRESENTATIVE**

County of San Diego

RE: MWD's Appendix A, Board Distribution Draft dated 04/26/17

Dear Chairman Record and Members of the Board:

On April 26, the Chief Financial Officer (CFO) provided a copy of Draft "Recent Developments for Metropolitan's Bond Disclosure" for the upcoming issuance of Subordinate Water Revenue Refunding Bonds, 2017 Series A. The draft incorporates by reference MWD's Appendix A dated February 24, 2017, which it referred to as its "2017 Appendix A," the draft of which we commented on by letters dated February 12 and February 14, 2017. Our February 12 and 14 letters and attachments were provided to all MWD board members, introduced into the record of MWD committee and board proceedings and are incorporated herein by reference. The Water Authority hereby resubmits its prior comments on the 2017 Appendix A, the vast majority of which MWD has not addressed. This letter will focus principally on the "recent developments" reported by MWD (and others not reported by MWD), beginning at page 13 of the Board Distribution Draft dated April 26, 2017.

*General and continuing objection to new process for preparation and review of Appendix A.* We have objected previously to the new process the CFO is following of having a "biannual" Appendix A, updated only in the manner used here, i.e., a statement of "recent events," without describing how those recent "events" impact disclosures and assessments by management in other parts of the Appendix A. If "recent events" are important enough to be disclosed, then they are important enough for management to address in other relevant and related sections of Appendix A.

*Oroville Dam.* The updates with regard to Oroville Dam fail to tie back to any water supply or financial impacts on MWD. This information should be provided and all related sections of Appendix A updated, accordingly.

*State Water Project (SWP) allocation.* The update reports the increase in MWD's calendar year 2017 SWP supply allocation to 85% (to 1,624,775 acre-feet), but does not

note that the increase represents a 25% increase over the 60% SWP supply allocation contained in the 2017 Appendix A. MWD does not address or describe the additional cost and operating impacts of such an increase in SWP supplies in other relevant sections of Appendix A, and we request that it do so.

*Agreement with City of Los Angeles.* MWD has failed to disclose its recent agreement with the City of Los Angeles, purportedly executed under the authority of the General Manager. Involving use of MWD's facilities, including as much as 200,000 acre-feet of its storage capacity, this transaction should be disclosed, and MWD should describe the water supply, cost and operating impacts on MWD.

*Reserves.* The brief mention of the "need" for \$50 million additional borrowing to be deposited to MWD's unrestricted cash reserves should tie back in to other relevant disclosures and updates, including discussion of the minimum cash reserve balance required to be on hand at the fiscal year end of June 30, 2017. It appears that MWD will only meet its minimum cash reserve requirement by borrowing money (either \$250 million of the \$338 million in projected reserves, or, \$300 million of the \$388 million in projected reserves). In addition, as noted earlier, MWD presumably must incur SWP power costs to store the 25 percent increase in its SWP supply allocation. Given its cash situation, MWD should disclose if additional borrowings are anticipated in order to store SWP water (the cost of which was not included in the budget), or if not, what the expected source of funds will be. We also request confirmation 1) that the Water Authority's security deposit is no longer commingled with these unrestricted cash reserves, as reported by MWD; and 2) the amount of the current balance being held in what MWD has reported as its "Exchange Agreement Set-Aside" fund.

*Failed board effort to implement a fixed charge for recovery of some portion of MWD's treatment costs.* MWD has failed to include disclosure of the board's recent action on a proposed fixed charge to recover some portion of MWD's treatment costs. MWD's water sales are declining; see Water Authority delegates' letter dated January 10, 2016 RE Memo 8-3: Adopt the 2015 Integrated Resources Plan Update – REQUEST TO DEFER BOARD ACTION ADOPTING 2015 IRP UPDATE, OR IN THE ALTERNATIVE, OPPOSE, which was previously provided to all MWD board members, introduced into the record of MWD committee and board proceedings and is incorporated herein by reference. Given the focus rating agencies place on the willingness of the MWD board to raise rates, we believe there should be disclosure that, after a year of additional effort, the MWD board of directors once again voted against implementation of even a small increment of additional fixed cost recovery. We have been told many times that the MWD member agencies and its board "like things the way they are," with 85% to 90% of revenues coming from MWD's volumetric water rates (many of which have been declared illegal). However, this approach is not fiscally sustainable in an

environment where MWD is facing substantially increased costs and a continuing and significant decline in the demand for MWD water. Investors should be informed that in the face of this decline, MWD's board is unwilling to impose fixed charges to pay for sunk costs and stranded investments; as a result, water rates and charges can be expected to increase substantially.

The Water Authority has commented many times that we believe MWD reports about the projected demand for MWD water are misleading. For example, the chart at page A-83 of the 2017 Appendix A purports to show "Historic Water Sales" of MWD water from 1997 to 2016, inclusive. However, MWD is masking its lower sales in this chart by improperly including the Water Authority's QSA local supplies *as its own water sales*. This is even further misleading to investors by MWD comparing water sales in 1997-2002, inclusive -- when there were no Water Authority QSA supplies -- with 2003-2016, *when the availability of a significant volume of the Water Authority's QSA supplies reduced its demand for MWD water*.

Unless MWD changes its disclosures to properly account for the Water Authority's QSA water as local supplies (as it is contractually obligated to do), this method of reporting will grow more and more misleading, as the Water Authority's QSA supplies increase to 280,000 AF annually by 2021. MWD's *actual water sales were lower* by the following amounts in each of the following fiscal years:

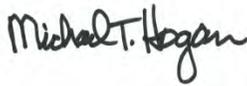
<b>Fiscal Year</b>	<b>AF</b>
2003	10,000 AF
2004	20,000 AF
2005	25,000 AF
2006	35,344 AF
2007	57,719 AF
2008	78,515 AF
2009	113,363 AF
2010	147,977 AF
2011	147,375 AF
2012	165,052 AF
2013	184,559 AF
2014	180,190 AF
2015	179,735 AF
2016	178,920 AF

By mischaracterizing the Water Authority's wheeling payments as "MWD Water Sales," MWD materially overstates its water sales. The chart on page A-83 should be modified to deduct the volumes of Water Authority QSA supplies, as noted above. MWD has

also failed in both its IRP and Urban Water Management Plan to account for a substantial amount of water supplies now being developed by its member agencies that will also permanently reduce the demand for MWD water. See January 10, 2016 letter RE Memo 8-3: Adopt the 2015 Integrated Resources Plan Update, noted above at page two, paragraph three; and May 8, 2016 letter RE Board Memo 8-6: Adopt the 2015 Urban Water Management Plan and resolution for submittal to the State of California.

We have previously commented on why MWD "Purchase Orders" are similarly misleading to the extent intended to assure investors about the future demand for MWD water; see letters dated October 8, 2012, December 27, 2012, January 14, 2013, October 13, 2014 and November 17, 2014, previously provided to all MWD board members, introduced into the record of MWD committee and board proceedings and which are incorporated herein by reference.

Sincerely,



Michael T. Hogan  
Director



Keith Lewinger  
Director



Elsa Saxod  
Director



Fern Steiner  
Director