San Diego County Water Authority
4677 Overland Avenue • San Diego, California 92123-1233
(858) 522-6600 FAX (858) 522-6568 www.sdcwa.org

MEMBER AGENCIES

Carlsbad Municipal Water District
City of Del Mar
City of Escondido
City of National City
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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

May 6, 2017

Randy Record and
Members of the Board of Directors
Metropolitan Water District of Southern California
P.O. Box 54153

RE: Board Memo 8-1: Adopt CEQA determination and approve the introduction by title only of an Ordinance Determining That The Interests Of The District Require The Use Of Revenue Bonds In The Aggregate Principal Amount of $400,000,000 To Finance A Portion Of Capital Expenditures -- **OPPOSE**

Chairman Record and Member of the Board:

We have reviewed Board Memo 8-1 seeking the Board's approval for the introduction of an Ordinance determining that the interests of MWD require the use of $400 million in revenue bonds, the use of which is limited to the purposes stated in MWD Act Section 237. We understand the action this month is to introduce the Ordinance only; however, no information has been presented by staff in order for the MWD Board to deliberate or determine, as required, that the interests of the district require additional debt to be issued at this time. In fact, we believe it is evident that the interests of the district require the Board of Directors to closely examine the factual basis why MWD apparently needs to borrow more money, as well as consider other alternatives such as reducing expenditures.

In October 2015, the Board adopted Ordinance No. 149, determining that the interests of MWD then required the use of $500 million in revenue bonds in order to fund a portion of MWD's Capital Investment Plan (CIP) **through June 30, 2018**. We opposed that Board action for the reasons detailed in our letters dated September 20, 2015 and October 10, 2015, copies of which are attached and incorporated herein by reference, including our earlier letter of July 9, 2015. Without repeating all details, the circumstances that then existed showed that MWD had to borrow money to cover all of its unbudgeted expenditures totaling more than $1.2 billion.

Now, with 13 months left to June 30, 2018, staff is back again seeking authority to issue up to $400 million in additional debt. This should be of concern to Board members because staff has informed us that every $20 million in debt issuance equates to $1 per acre-foot increase in water rates based on 2 million acre-feet of water sales, with even higher rate increases being needed if water sales are lower, as they certainly will be this fiscal year and next. In short, the issuance of debt comes at a cost that will necessarily increase water rates in the future.

During recent Finance and Insurance Committee meetings, we have questioned the manner in which staff reports "budget" numbers that include expenditures approved by the board **after** adoption of the biennial budget in April, and which therefore were not included in the cost of service or rates and charges set at that time. We have requested that staff also provide adopted budget numbers so that the Board can track and better understand how much more it is spending than it considered during budget deliberations, and potentially take actions to reduce spending rather than borrow more money than was planned. One of the reasons we are seeking to obtain a functional copy of MWD's rate model is because it would allow all of us, as board members, to assess the impacts of various options available to the Board other than borrowing more money, which comes with commensurate rate impacts as described above.

There is no reason why staff could not have provided information this month explaining why more debt is necessary now, when the October 2015 debt issuance was expected to last until the end of the next fiscal year. We do not believe it is prudent for the Board to approve the introduction of this Ordinance determining that the interests of MWD require the use of an additional $400 million in revenue bonds without requiring staff to present facts and alternatives that could support such a determination.

Sincerely,

Michael T. Hogan
Director

Keith Lewinger
Director

Elsa Saxod
Director

Fern Steiner
Director

cc: Water Authority Board of Directors

Attachment 1: September 20, 2015 Letter RE Board Memo 8-6: Approve the introduction by title only of an Ordinance Determining That The Interest of The District Require The Use of Revenue Bonds in The Aggregate Principal Amount of $500,000,000 - OPPOSE, with attached July 9, 2015 Letter

Attachment 2: October 10, 2015 Letter RE Board Memo 8-1: Adopt Ordinance No. 149 determining that the interests of Metropolitan require the use of revenue bonds in the aggregate principal amount of $500 million – OPPOSE (without attachment)

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OTHER REPRESENTATIVE

County of San Diego

September 20, 2015

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

RE: Board Memo 8-6: Approve the introduction by title only of an Ordinance Determining That The Interests of The District Require The Use of Revenue Bonds In The Aggregate Principal Amount of $500,000,000 -- **OPPOSE**

Chair Record and Members of the Board:

We have reviewed Board Memo 8-6 seeking the Board's approval for the introduction by title only of an ordinance determining that the interests of MWD require the use of revenue bonds in the aggregate principal amount of $500 million. We oppose this item because there is no factual basis for a determination by the board of directors that the use of revenue bonds as described in Board Memo 8-6 and attached Ordinance is in MWD's interest. Consideration of whether the use of revenue bonds is in MWD's interest requires a more comprehensive look at a number of actions by the MWD board that are not described in the Board Memo and have had a material impact on MWD's current financial condition.

In April 2014, rather than reducing or maintaining its existing rates , MWD's adopted biennial budget for fiscal years 2015 and 2016 increased MWD's water rates by 1.5 percent per year for fiscal years 2015 and 2016 and presented a schedule projecting rate increases of 3 – 5 percent per year through 2024. In addition, the MWD board voted to suspend tax rate reductions that would otherwise occur, claiming that the increase in tax revenues by an additional tens of millions of dollars were necessary to maintain MWD's fiscal integrity. The MWD board made this finding based on staff recommendation at the same time its cash reserves were so great that the adopted budget planned to pay 100 percent of MWD's Capital Investment Plan for fiscal years 2015 and 2016 out of cash on hand (and then slowly eases to 60 percent cash CIP financing over the remaining years through 2024). Because MWD's recently adopted budget process no longer even attempts to estimate MWD's revenues and expenses based on actual conditions -- choosing instead to set rates based on low water sales that are expected to be exceeded seven out of ten years -- since 2012, MWD has collected $800 million more than actual expenditures based on original adopted budgets. The MWD board chose to spend this money on unbudgeted expenditures, including the unprecedented increase in water conservation funding -- more than ten times the adopted budget -- from $40 million to $450 million including a hastily structured turf replacement program,[i] now all of these revenues have been spent.

MWD's use of revenue bonds would be entirely unnecessary if the MWD board adopted and followed sound fiscal policies and practices. MWD needs a long-range finance plan. MWD needs to complete the update of its Integrated Resources Plan. MWD needs a new rate structure consistent with California statutes and the Constitution. MWD needs to credibly demonstrate that these plans are functionally integrated.

The Water Authority will need more time to consider the implications of the proposed ordinance. We do not support introduction of the ordinance by title only. Lastly, Board memo 8-6 was not available with the regular board mailing. MWD's consistent late delivery of a majority of the board reports makes it extremely difficult for our staff to provide the technical support necessary for our deliberation of MWD staff recommendations. We renew past requests that board memoranda be distributed at least seven days in advance of MWD board meetings.

Sincerely,

Michael T. Hogan	Keith Lewinger	Fern Steiner	Yen C. Tu
Director	Director	Director	Director

Attachment: Water Authority's July 9, 2015 letter to MWD Board

[i] MWD's turf replacement program was poorly structured and did not incorporate recommendations from a CUWCC report that it participated in and funded. Many have raised questions about MWD's implementation of turf replacement including the most recent LA Times article: http://touch.latimes.com/#section/-1/article/p2p-84445011/

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OTHER REPRESENTATIVE

County of San Diego

July 9, 2015

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

RE: Board Memo 8-4: Adopt a resolution for the reimbursement with bond proceeds of Capital Investment Plan projects funded from the General Fund and Replacement and Refurbishment Fund -- **OPPOSE**

Chair Record and Members of the Board:

The Water Authority's MWD Delegates have reviewed the July 14, 2015 board memo 8-4 seeking the Board's authorization to declare MWD's intent to issue up to $300 million of debt to "reimburse" capital expenditures for projects funded from the General Fund and Replacement and Refurbishment (R&R) Fund. We oppose this item because staff's recommendation will obligate MWD to increase water rates by at least $15 per acre- foot without an actual board vote for the rate increase, and for the reasons further stated in this letter.

Staff's practice of presenting board actions piecemeal has paralyzed the board's ability to make sound public policy decisions. This month's action is another example. The board memo states that the debt issuance would provide MWD the "financial flexibility" desired because of the projected draw down of reserves as a result of the May action to pay for the unbudgeted conservation programs,[i] and that "expenditures for water management activities such as replenishing storage and funding transfer and exchange programs could significantly [further] draw down financial reserves in the near future." But it was staff's own recommendation in May to spend $350 million on unbudgeted conservation expenditures – namely turf removal -- that placed MWD in this precarious fiscal position. This situation was completely foreseeable.

The May action not only spent MWD's not-yet-realized excess revenue collection,[ii] it also completely drained the Water Management Fund (WMF) – established for the very purpose of covering future costs associated with replenishing storage and water transfers – to fund turf removal, an expense for which the WMF was not intended. Staff expressed no concern when it recommended to spend down the WMF. The Board was repeatedly told in May that staff's recommendation would not result in any rate impacts. But this month's action, which was precipitated entirely by May's unbudgeted expenditures, will in fact result in increases in MWD water rates by at least $15 per acre-foot. (MWD staff reported in the past that every $20 million in debt issuance equates to $1 per acre-foot increase in water rates based on 2 million acre-feet of water sales; the rate increase will be higher for lower water sales volumes.) What has changed so drastically that is causing staff to be so concerned with the lack of financial flexibility triggered by an action it recommended just only six weeks ago? Did staff not foresee when it made the recommendation to spend down the WMF in May that its "flexibility" to purchase transfer supplies and to replenish depleted dry-year storage accounts would be more limited?

We disagreed with staff's assessment in May that the increase in conservation funding would not result in rate impacts. However, we believe staff's assertion that the action would have no rate impact persuaded many Board members to support the unprecedented and unbudgeted spending. While this month's action clearly has rate implications, the board memo yet again makes no reference to the rate increases.

Since fiscal year 2012, MWD collected more than $800 million in revenues that exceed actual expenses. And since 2013 and in each year following, these over-collections have caused MWD's reserves to exceed the Board established maximum limits by hundreds of millions of dollars -- largely caused by staff's strategy, endorsed by this Board's votes of approval -- to set rates based on artificially deflated sales amounts, which staff said would be exceeded seven out of 10 years.[iii] Rather than using the over-collections to manage rate and tax increases, MWD kept and spent the monies on unbudgeted items.

Nearly as quickly as MWD amassed more than $800 million in over-collected revenues, they are now nearly all gone, and MWD is resorting to budget shell games of taking cash from the capital investment plan to cover massive spending on turf removal. It is obvious that this proposal to issue $300 million in new debt is a post-facto, 30-year debt financing of turf removal subsidies approved just weeks ago. This is not sound fiscal management.

When the biennial budget for fiscal years 2015 and 2016 was adopted, we asked that MWD use the revenue over-collection to reduce rate increases and not raise taxes, staff instead recommended using part of the over-collections to cash-fund capital projects to "avoid future rate increases." This month's 8-4 recommendation is an about-face from staff's earlier rationale in support of cash-funding the capital program.

Finally, MWD's Administrative Code (Section 5200(b)) clearly restricts the use of monies from the R&R Fund to capital program expenditures. It is unclear how staff's proposal to issue debt would afford MWD the ability to use R&R funds for operational costs related to water transfers or purchases of water to replenish storage.

For reasons stated in this letter, we oppose staff's recommendation. We urge our fellow Board members to vote no on this action as well. This action is an inappropriate attempt to debt-finance very expensive turf rebates that produce no significant immediate supply relief during the drought.

Sincerely,

Michael T. Hogan Director	Keith Lewinger Director	Fern Steiner Director	Yen C. Tu Director

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[i] MWD increased conservation spending in May by an additional $350 million and was to be funded by the following sources: 1) Water Stewardship Fund ($50 million), 2) Water Management Fund ($140 million), and 3) projected excess revenue collection that exceeded maximum reserves target ($160 million); however, board memo 9-1 this month indicates that the projected excess revenue collection is trending at $120 million, requiring the use of $40 million from Water Rate Stabilization Fund.

[ii] The May action authorized the expenditures of anticipated over-collection of $160 million, which is trending now at $120 million (see also footnote ii).

[iii] Fiscal year 2016 is a good example; according to staff, MWD's water sales at the reduced Level 3 supply allocation (15 percent reduction) will still exceed the budgeted assumption of 1.75 million acre-feet.

Attachment 2

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OTHER REPRESENTATIVE

County of San Diego

October 10, 2015

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

RE: Board Memo 8-1: Adopt Ordinance No. 149 determining that the interests of Metropolitan require the use of revenue bonds in the aggregate principal amount of $500 million -- **OPPOSE**

Chair Record and Members of the Board:

We have reviewed Board Memo 8-1 asking the Board to adopt an ordinance determining that the interests of MWD require the use of revenue bonds in the aggregate principal amount of $500 million to fund a portion of the Capital Investment Program (CIP) through June 30, 2018 and to "reimburse" MWD for capital projects it has already paid for since May 2015.[i] We oppose this item for the same reasons described in our letter in OPPOSITION to last month's board action to approve the introduction of this ordinance: namely, the board memo does not present an accurate factual basis for the MWD Board to make this determination. To the contrary, this action and other spending actions taken by the Board during the current "budget" cycle can be described as anything but consistent with sound financial practices and policies.

MWD management's budget strategy, approved by this board, of setting rates that it knows will collect revenues from water ratepayers that exceed expenses in seven out of 10 years, has led MWD to cumulatively collect $824 million more than actual expenditures based on the board's adopted "budgets" since just 2012.[ii] The biennial budget for fiscal years 2015 and 2016, adopted by the Board 18-months ago, planned to cash finance all of the CIP contained in the biennial budget. The forecasted rate schedule included in the budget document in fact was based on cash financing a majority of the $1,069.2 million of planned CIP from July 1, 2014 through June 30, 2018, with only $45.2 million from revenue bonds. Now, more than half-way through the budget cycle, and having blown through more than $800 million over budget, staff wants to increase debt for this period more than 10 times, ex post facto, to $500 million.

The Board memo attributes the need to incur this debt to the drought, and the fact that MWD's water sales and resulting revenues vary from year to year, as much as 30 percent over or under projections. Leaving aside the fact that drought (even severe drought) in Southern California should not come as a surprise to MWD, the solution is not to increase debt; it is to better manage revenues during "over" and "under" years. But MWD chooses not to do that. Rather than establish simple balancing accounts to manage revenues between high and low revenue years, staff has recommended, and this Board has approved massive expenditures outside of budget in good years, leaving MWD with insufficient revenues when they are needed. This practice is now leading MWD to do something it did not plan to do, and which its budget did not forecast: issue debt or raise rates higher than forecast. Board Memo 8-1 does not identify the real problem and does not propose an appropriate solution. MWD may very well need to issue additional bond funding for appropriate purposes at an appropriate time. But it is not credible to say that this action is in the interests of MWD unless the underlying financial policy issues are addressed.[iii]

Most troubling, Board Memo 8-1 states that without this unplanned borrowing, MWD will either have to curtail capital projects (something the Board should at least consider), use additional reserves to fund capital costs (though such reserves do not exist) or increase water rates above forecasted levels. This is information that should have been provided to the Board earlier, when staff recommended, and the Board voted to approve unbudgeted expenditures of more than $800 million. Now, having blown through all of its cash, staff is saying it needs to borrow money to avoid rate increases. This is fiscal madness.

Finally, Board Memo 8-1 contains language suggesting that staff believes that adoption of this ordinance will allow MWD to use debt to pay for things other than capital projects (bond proceeds may be used "even more broadly for the funding of 'any preliminary and incidental expenses...necessary or convenient to carry out the objects or purposes of the district'"). If this language suggests MWD may spend debt proceeds on operational expenses, we do not read Section 237 of the MWD Act relating to revenue bond purposes that way; rather, this language must be read in the context of Section 237 as a whole being related to the funding of capital projects and public works. We ask that staff clarify this point as part of the record of proceedings at our committee and board meetings.

We oppose this action. MWD needs a long-range finance plan. MWD needs to follow cost-of-service requirements of law. It needs to develop, adopt and – most critically -- follow its budgets. It is imperative that MWD get its fiscal house in order. Issuing this debt now absent all of these other actions being taken by the Board is not in MWD's interests.

Sincerely,

Michael T. Hogan Director	Keith Lewinger Director	Fern Steiner Director	Yen C. Tu Director

Attachment:

1. September 20, 2015 Water Authority letter to MWD Board RE Board Memo 8-6: Approve the introduction by title only of an Ordinance Determining that the Interests of the District require the use of Revenue Bonds in the aggregate principal amount of $500,000,000 – OPPOSE

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[i] It seems obvious that the issuance of debt is necessary in order for MWD to restore and meet its minimum cash reserve requirement. It is apparent from many actions over the past several months that MWD has engaged in a spending spree, with no cost-of-service basis for hundreds of millions of dollars of expenditures, completely disconnected from the two-year budget this Board approved in April 2014.

[ii] Of the $824 million, $741 million exceeded the agency's maximum reserve level.

[iii] Board Memo 8-1 also states that the Board "has prudently established a reserve policy designed to deal with significant changed circumstances and buffer the impacts of weather, economy and demand volatility on MWD's revenues." If that were true, staff would not need to be asking to issue debt in order to restore its depleted cash reserves.