

## Cost of Service Review

### Meeting #4

LRFP work group  
August 31, 2009  
Office of the CFO

## Agenda

- Follow-up from Meeting #3 and B&F
- SWP costs in COS
- Policy Concepts in current approach
  - MWD role
  - Changes since 2001
  - How affect approach for future
- Implications of policy changes

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## Follow-Up: Property Tax Revenues

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## Property Taxes paid 1930-2009

Fiscal Year	Shares	Total Taxes
Anaheim	1.0%	37,827,374
Beverly Hills	1.1%	42,488,884
Burbank	1.0%	39,041,026
Calleguas	3.3%	131,597,190
Central Basin	8.4%	334,503,986
Compton	0.2%	9,735,447
Eastern	2.8%	112,962,022
Foothill	0.7%	27,665,412
Fullerton	0.6%	24,653,613
Glendale	1.2%	47,771,949
Inland Empire	2.5%	101,056,920
Las Virgenes	0.7%	27,511,756
Long Beach	2.6%	101,583,806
Los Angeles	23.3%	927,587,564
MWDOC	14.1%	559,216,407
Pasadena	1.1%	44,652,126
San Diego	13.6%	542,008,860
San Fernando	0.1%	5,172,468
San Marino	0.2%	9,187,740
Santa Ana	0.8%	32,963,440
Santa Monica	1.0%	40,457,487
Three Valleys	2.3%	90,673,500
Torrance	1.1%	45,164,267
Upper San Gabriel	4.7%	184,852,862
West Basin	7.9%	312,196,487
Western	3.5%	140,164,399
<b>Total</b>	<b>100.0%</b>	<b>3,972,696,992</b>

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## Property Tax shares over time

Fiscal Year	1930-1949	1950-1969	1970-1989	1990-2009
Anaheim	0.5%	0.3%	0.4%	1.5%
Beverly Hills	3.1%	1.3%	0.9%	1.0%
Burbank	2.6%	1.5%	0.9%	0.8%
Calleguas	0.0%	1.1%	3.3%	4.1%
Central Basin	0.0%	14.9%	10.5%	5.7%
Compton	0.5%	0.5%	0.2%	0.2%
Eastern	0.0%	0.6%	2.1%	4.2%
Foothill	0.0%	1.1%	0.7%	0.7%
Fullerton	0.8%	0.5%	0.6%	0.6%
Glendale	3.2%	1.4%	1.0%	1.1%
Inland Empire	0.0%	2.3%	2.4%	2.9%
Las Virgenes	0.0%	0.1%	0.5%	1.0%
Long Beach	8.8%	3.7%	2.5%	1.9%
Los Angeles	68.0%	29.3%	20.6%	20.6%
MWDOC	0.5%	8.8%	15.8%	15.3%
Pasadena	4.1%	1.6%	0.9%	1.0%
San Diego	2.2%	10.0%	13.5%	15.6%
San Fernando	0.0%	0.0%	0.2%	0.1%
San Marino	0.8%	0.3%	0.2%	0.2%
Santa Ana	1.3%	0.7%	0.6%	1.0%
Santa Monica	2.6%	1.3%	0.9%	0.9%
Three Valleys	0.0%	2.0%	2.2%	2.6%
Torrance	1.1%	1.1%	1.2%	1.1%
Upper San Gabriel	0.0%	3.0%	6.3%	4.3%
West Basin	0.0%	10.4%	8.8%	7.1%
Western	0.0%	2.3%	2.9%	4.6%
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

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## FY2009/10 sales

Member Agency	acre-feet	% acre-feet	Revenues	% Revenues
Anaheim	21,312	1.1%	\$ 15.6	1.1%
Beverly Hills	10,467	0.6%	\$ 7.9	0.6%
Burbank	11,230	0.6%	\$ 8.4	0.6%
Calleguas	97,692	5.1%	\$ 73.1	5.3%
Central Basin	38,299	2.0%	\$ 30.1	2.2%
Compton	2,707	0.1%	\$ 2.0	0.1%
Eastern	94,852	5.0%	\$ 70.8	5.1%
Foothill	10,714	0.6%	\$ 7.9	0.6%
Fullerton	9,698	0.5%	\$ 7.2	0.5%
Glendale	18,867	1.0%	\$ 14.4	1.0%
Inland Empire	66,411	3.5%	\$ 49.3	3.6%
Las Virgenes	20,022	1.1%	\$ 14.9	1.1%
Long Beach	33,461	1.8%	\$ 24.8	1.8%
Los Angeles	364,629	19.2%	\$ 269.5	19.6%
MWDOC	206,541	10.9%	\$ 153.5	11.2%
Pasadena	20,018	1.1%	\$ 15.1	1.1%
San Diego	529,718	27.9%	\$ 356.6	25.9%
San Fernando	290	0.0%	\$ 0.2	0.0%
San Marino	1,183	0.1%	\$ 0.9	0.1%
Santa Ana	11,856	0.6%	\$ 9.4	0.7%
Santa Monica	11,820	0.6%	\$ 8.8	0.6%
Three Valleys	61,885	3.3%	\$ 46.5	3.4%
Torrance	19,165	1.0%	\$ 14.2	1.0%
Upper San Gabriel	10,861	0.6%	\$ 8.6	0.6%
West Basin	126,033	6.6%	\$ 93.9	6.8%
Western	100,270	5.3%	\$ 72.2	5.2%
<b>Total</b>	<b>1,900,000</b>	<b>100.0%</b>	<b>\$ 1,376.0</b>	<b>100.0%</b>

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## FY2009/10 sales and tax revenues

Member Agency	%Sales Revenues	% Taxes	RTS shares
Anaheim	1.1%	1.7%	1.10%
Beverly Hills	0.6%	1.0%	0.70%
Burbank	0.6%	0.9%	0.70%
Calleguas	5.3%	3.9%	6.09%
Central Basin	2.2%	5.4%	3.49%
Compton	0.1%	0.2%	0.18%
Eastern	5.1%	2.7%	4.78%
Foothill	0.6%	0.6%	0.61%
Fullerton	0.5%	0.7%	0.51%
Glendale	1.0%	1.1%	1.35%
Inland Empire	3.6%	3.9%	3.11%
Las Virgenes	1.1%	0.9%	1.24%
Long Beach	1.8%	1.9%	2.03%
Los Angeles	19.6%	19.5%	15.12%
MWDOC	11.2%	16.7%	12.36%
Pasadena	1.1%	1.0%	1.23%
San Diego	25.9%	18.0%	26.49%
San Fernando	0.0%	0.1%	0.01%
San Marino	0.1%	0.2%	0.05%
Santa Ana	0.7%	1.0%	0.69%
Santa Monica	0.6%	1.2%	0.69%
Three Valleys	3.4%	2.4%	3.93%
Torrance	1.0%	1.1%	1.14%
Upper San Gabriel	0.6%	3.5%	0.84%
West Basin	6.8%	6.7%	7.80%
Western	5.2%	3.7%	3.73%
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

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## Increase property taxes by \$10M

- Additional taxes would be an offset to SWP costs
- Net Revenue Requirement would be lower by \$10M
  - System Access rate lower by \$7M
  - RTS lower by \$3M

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## Increase property taxes by \$10M

	Full COS	Increase Prop. Tax	Change
Anaheim	15.5	15.6	0.1
Beverly Hills	7.9	8.0	0.0
Burbank	8.4	8.5	0.0
Calleguas	73.1	73.0	(0.1)
Central Basin	30.1	30.4	0.3
Compton	2.0	2.0	0.0
Eastern	70.7	70.6	(0.2)
Foothill	7.9	7.9	0.0
Fullerton	7.2	7.3	0.0
Glendale	14.3	14.4	0.0
Inland Empire	49.3	49.4	0.1
Las Virgenes	14.9	14.9	(0.0)
Long Beach	24.8	24.8	0.0
Los Angeles	269.5	269.7	0.2
MWDOC	153.4	154.1	0.6
Pasadena	15.0	15.1	(0.0)
San Diego	356.6	355.8	(0.8)
San Fernando	0.2	0.3	0.0
San Marino	0.9	0.9	0.0
Santa Ana	9.4	9.5	0.0
Santa Monica	8.8	8.9	0.1
Three Valleys	46.4	46.4	(0.1)
Torrance	14.2	14.2	0.0
Up. San Gabriel	8.5	8.9	0.3
West Basin	93.8	93.9	0.0
Western	72.1	72.1	(0.1)
MWD Average	1,376.0	1,376.4	0.4

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## Follow-up Purchase Order status

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## Purchase Order facts

- Purchase Orders were voluntarily submitted by member agencies
- Purchase Order commitment = buy 10 x 60% of Initial Base Demand over ten years
- Members with a PO can purchase up to 90% of their Base Demand at the Tier 1 rate

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## Purchase Order facts (cont'd)

- Currently six agencies have effectively met the PO commitment
- Most agencies are on track to fulfill their PO commitment
- City of Compton tracking below the PO commitment
- San Fernando and San Marino did not submit Purchase Orders

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## Purchase Order status

	Purchase Order Commitment (AF)	Cumulative Firm Sales through 12/2008 (AF)	Remaining Commitment 2009-2012 (AF)	Purchase Order Percent Remaining
Anaheim	148,267.8	128,186.5	20,081.3	13.5%
Beverly Hills	89,202.0	73,727.4	15,474.6	17.3%
Burbank	108,909.6	81,806.9	27,102.7	24.9%
Calleguas	692,003.4	685,367.7	6,635.7	1.0%
Central Basin	482,400.0	371,251.5	111,148.5	23.0%
Compton	33,720.6	17,323.0	16,397.6	48.6%
Eastern	504,663.6	596,923.1	-	0.0%
Foothill	73,312.2	67,195.0	6,117.2	8.3%
Fullerton	75,322.2	58,944.2	16,378.0	21.7%
Glendale	174,809.4	135,975.5	38,833.9	22.2%
Inland Empire	398,347.8	370,834.7	27,513.1	6.9%
Las Virgenes	137,103.0	144,224.0	-	0.0%
Long Beach	263,142.6	226,053.4	37,089.2	14.1%
Los Angeles	2,033,132.4	1,839,775.6	193,356.8	9.5%
Orange County	1,486,161.0	1,414,545.7	71,615.3	4.8%
Pasadena	141,196.8	141,750.9	-	0.0%
San Diego	3,338,035.2	2,940,119.3	397,915.9	11.9%
San Fernando	-	1,182.6	-	N/A
San Marino	-	7,709.0	-	N/A
Santa Ana	80,858.4	77,880.2	2,978.2	3.7%
Santa Monica	74,062.2	79,386.4	-	0.0%
Three Valleys	469,331.4	432,214.6	37,116.8	7.9%
Torrance	139,779.6	122,822.9	16,956.7	12.1%
Upper San Gabriel	110,076.6	106,079.1	3,997.5	3.6%
West Basin	1,045,824.6	850,298.6	195,526.0	18.7%
Western	391,791.0	466,724.5	-	0.0%
<b>Total</b>	<b>12,491,453.4</b>	<b>11,438,302.3</b>	<b>1,242,235.0</b>	

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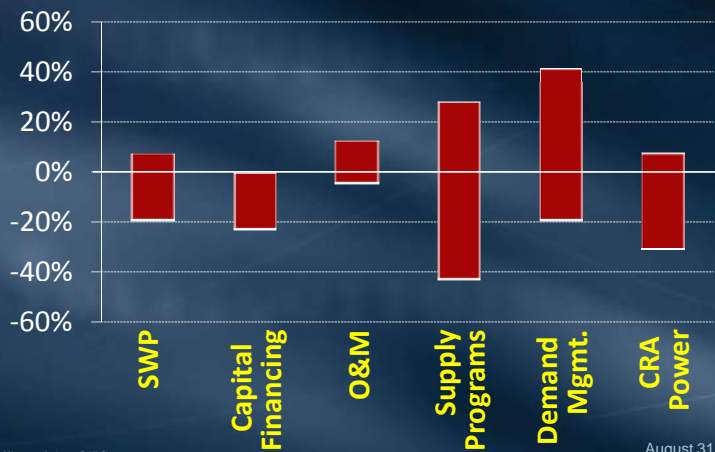
## Follow-up: Historic Cost Variability

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## Budget Variance

2005/06 to 2008/09

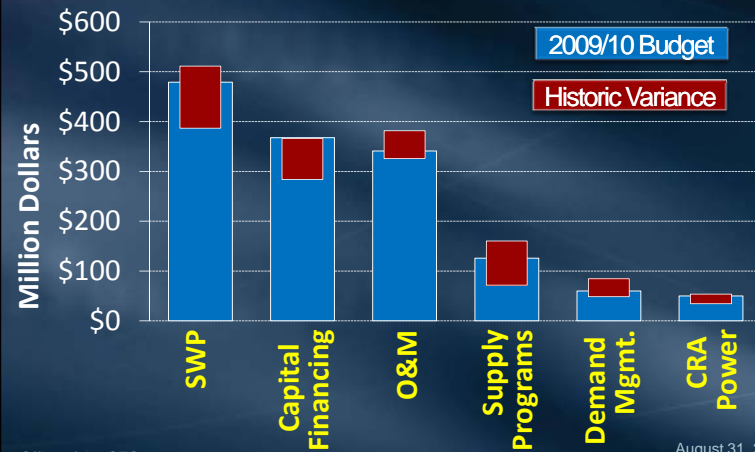


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## Budget Variance

variance based on 2005/06 to 2008/09



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## Folow-up: Comparison of Fixed Revenues

## Fixed Revenues

- Includes fixed charges such as, connection, meter, capacity, or RTS charge, plus property and sales taxes
- Fixed revenues as a percent of total revenues (water utility only)\*

Agency	Fixed Revenue share of Total Revenues
Metropolitan	15%
LADWP (excl. connection charge)	0%
SDCWA	20%
Santa Clara Water District	37%
S. Nevada Water Authority	53%
East Bay MUD	24%

\*Draft estimates based on published data or agency communication

## Policy Issues: SWP costs in COS

## Where should SWP costs be reflected in Cost of Service?

Current approach:

- Supply \$67M
- Conveyance & Aqueduct \$412M
  - Recovered in:
    - System Power Rate \$169M
    - System Access rate \$208M
    - RTS \$35M

## Where should SWP costs be reflected in Cost of Service?

### Other Alternatives:

- Consider SWP costs as Supply costs
  - Power costs would remain in System Power Rate
  - Future Delta Conveyance costs allocated to Supply
- Modified current approach
  - Maintain current approach for existing SWP facilities
  - Future Delta Improvements could be split between Conveyance and Supply
  - How to determine Delta split into Supply and Conveyance?

## Terminal Reservoirs

- Metropolitan has contract for flex storage benefits
- Castaic and Perris Reservoirs currently included in Conveyance
- Should MWD depart from DWR billing?
  - Allocate a portion of Castaic and Perris to Conveyance and a portion to Supply?

## Policy Concepts That Supported The Current Approach

## Development of the Current Structure

- Process took five years
  - Strategic planning process started in July of 1998
  - Rate structure design involved Board, member agency managers, industry experts/consultants, and Metropolitan staff
  - Significant consideration of “the law of unintended consequences”
    - Important elements were changed late in the process or deferred

## 1999 Strategic Plan Policy Principles

- Regional provider
- Local resources development
- Imported water service
- Choice and competition
- Responsibility for water quality
- Cost allocation and rate structure
- Financial integrity

## 1999 Principle Regional Provider

- Metropolitan is a regional provider of wholesale water services
- Steward of regional infrastructure
- Regional planner responsible for coordinated drought management
- Collaborative development of additional reliable supplies and capacity expansion
- Equitable allocation of water supplies during droughts

## 1999 Principle Local Resources Development

- Metropolitan supports local resource development in partnership with its member agencies
- Provide financial incentives to member agencies for conservation and local projects

## 1999 Principle Imported Water Service

- Metropolitan is responsible for providing the region with imported water, meeting the committed demands of its member agencies

## 1999 Principle Choice and Competition

- Beyond committed demands, the member agencies may choose the most cost effective additional supplies
- Additional supplies can be developed through collaborative process to strike a balance
  - Local supplies
  - Imported supplies
  - Market opportunities
  - Affordability

## 1999 Principle Responsibility For Water Quality

- Metropolitan is responsible for advocating source water quality and implementing in-basin water quality for its imported water supplies
- Assure full compliance with existing and future drinking water standards
- Meet requirements for water recycling and groundwater replenishment

## 1999 Principle Cost Allocation and Rate Structure

- Framework must address:
  - Allocation of costs
  - Financial commitments
  - Unbundling of services
  - Fair compensation for services including wheeling, peaking, growth, and others
- Recognized that the status quo may not address all these issues, so change could be necessary

## 1999 Principle Financial Integrity

- Take all necessary steps to assure the financial integrity of the agency in all aspects of its operations
- Establish a financial commitment from the member agencies that provides security for Metropolitan
  - Should not transfer undue risk to the member agencies, individually or as a whole

## Additional Concepts Also Influenced The Current Structure

- **Accountability:**
  - Define the link among costs, charges, and benefits through a cost of service approach consistent with industry guidelines
- **Equity:**
  - Ensure that member agencies and other entities pay the same rates and charges for like services
  - Provide a fair allocation of costs

## Additional Concepts Also Influenced The Current Structure

- **Environmental Responsibility:**
  - Encourage demand management by funding conservation and recycling projects/programs
  - Use pricing to encourage investments in conservation and other economical local supplies

## How Does The Current Structure Deal With These Policy Concepts?

### Tiered Supply Rates

- Tier 2 Supply Rate is higher and provides financial incentive for local supply development and conservation
- No difference in supply reliability for water purchased at Tier 1 or Tier 2 rates
- Agencies with growth in imported water demand are more likely to face Tier 2 rate
- **Policy Concept:** Regional Provider, Cost Allocation, Local Resource Development, Environmental Responsibility, Imported Water Service

## Purchase Order Commitments

- Most member agencies made purchase order commitments that will last through 2012
  - Commitments last for ten years and provide a minimum level of assurance that purchases will be made
  - Agencies were given higher Tier 1 purchase limits in return for making the commitments

• **Policy Concept:** Financial Integrity

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## Water Stewardship Rate

- Separate rate element designed to collect costs of demand management programs
- Provides funds for conservation incentives and local resource programs
- **Policy Concept:** Environmental Responsibility, Regional Provider, Local Resource Development

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## Fixed Charges: Capacity Charge

- Recovers compensation for peak system usage
- Provides incentive for member agencies to reduce peak capacity use of distribution facilities
- Helps reduce need for future capital expansion
- Provides a source of fixed revenue

• **Policy Concept:** Regional Provider, Equity, Financial Integrity, Cost Allocation

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## Fixed Charges: Readiness-To-Serve Charge

- Recovers cost for portions of system on standby for emergency service and operational flexibility
- Provides a source of fixed revenue
- Allocated to member agencies based on ten-years of historic firm water sales

• **Policy Concept:** Regional Provider, Equity, Financial Integrity, Cost Allocation

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## Unbundled Postage Stamp Rates

- Clearly shows the costs for specific class of service
- Member agencies pay the same rate for a class of service, regardless of where they are in the service area (Ex. power and conveyance costs)
- Reflects the inter-related nature of Metropolitan's conveyance and distribution facilities
- **Policy Concept:** Cost Allocation, Choice and Competition, Equity

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## Structure Allows Core Activities

- Treatment Surcharge recovers cost of water treatment responsibilities
- Water Stewardship Rate supports regional demand management activities
- Regional supply reliability
- **Policy Concept:** Regional Provider, Responsibility for Water Quality, Cost Allocation, Choice and Competition, Equity

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## Starategic Policy Discussion: IRP Board workshop Aug. 25, 2009

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## Why Look at New Policies?

- Restrictions in State Water Project supply
- Need to expedite new supplies such as seawater desalination and indirect potable reuse
- Need for greater water use efficiency
- Potential water supply reductions due to climate change and other uncertainties
- Feedback from IRP Public Forums: MWD should take a leadership role

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## Strategic Policy Impacts



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## Example IRP Policy Questions

- Appropriate level of reliability for MWD?
- MWD's role in providing new regional supplies?
- Member agency role and responsibilities?
- Should MWD offer different levels of reliability?
- Equitable benefits from LRP investments?
- What constitutes "affordability"?
- What is the willingness to pay for new supplies?

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## Schedule of MWD Initiatives

INITIATIVE	2009					2010													
	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec		
IRP Update	█					█					█								◆
Cost of Service Study	█							◆											
Long Range Finance Plan						█													
Strategic Policy Review	█					█													

## Potential Policy Approaches

- Current Approach
  - Interdependency between MWD and Member Agency responsibilities
- Imported Focus Approach
  - MWD develops imported supplies and maintains its water management assets
  - Member Agency develops local supplies
- Expanded Regional Approach
  - MWD imports and develops new supplies
- Hybrid/Combination

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## Current Approach

- MWD responsible for imported water reliability programs and projects
- Member Agencies responsible for local water supply projects
- MWD provides financial incentives for local resources development and conservation
- MWD and Member Agencies work together on in-basin groundwater conjunctive use projects

## Imported Focus Approach

- MWD focuses on Bay-Delta Solution and Development of Colorado River Aqueduct Supplies
- MWD maintains its existing water management assets (storage, water transfers/banking and conjunctive use)
- MWD financial incentives for local resources and conservation are eliminated for new projects
- Member Agencies solely responsible for new local supply development

## Expanded Regional Approach

- MWD responsible for imported water reliability programs and projects
- Member Agencies responsible for new local water supply projects
- MWD eliminates financial incentives for new local resources and conservation
- MWD develops projects for regional reliability, e.g. seawater desalination and indirect potable recycled water

## Policy discussion

## Next steps

- Set next meeting date
  - B&F discussion Sep.14
  - Board COS workshop Sep.22
- Discussion of Member Agencies' Cost of Service Alternatives
- Next meeting:
  - Discussion of potential changes for December Cost of Service