THE METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA

Basic Financial Statements

Three Months ended September 30, 2018 and 2017

(Unaudited)

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UNAUDITED
September 30, 2018 and 2017

The following discussion and analysis of The Metropolitan Water District of Southern California's (Metropolitan) financial performance provides an overview of the financial activities for the three months ended September 30, 2018 and 2017. This discussion and analysis should be read in conjunction with the basic financial statements and accompanying notes, which follow this section.

DESCRIPTION OF BASIC FINANCIAL STATEMENTS

Metropolitan operates as a utility enterprise and maintains its accounting records in accordance with generally accepted accounting principles for proprietary funds as prescribed by the Governmental Accounting Standards Board (GASB). The basic financial statements include statements of net position, statements of revenues, expenses and changes in net position, and statements of cash flows. The statements of net position include all of Metropolitan's assets, deferred outflows of resources, liabilities, and deferred inflows of resources, with the difference reported as net position, some of which is restricted in accordance with bond covenants or other commitments. The statements of revenues, expenses and changes in net position report all of Metropolitan's revenues and expenses during the periods indicated. The statements of cash flows show the amount of cash received and paid out for operating activities, as well as cash received from taxes and investment income, and cash used for construction projects, State Water Project costs and principal and interest payments on borrowed money. Certain amounts reported in fiscal year 2018 have been reclassified to conform to the fiscal year 2019 presentation. Such reclassification had no effect on the previously reported change in net position.

During the fiscal year ended June 30, 2018, Metropolitan implemented Governmental Accounting Standards Board Statement No. 75 (GASB 75), *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which addresses the accounting and financial reporting for postemployment benefits other than pensions (OPEB). Metropolitan did not restate the financial statements for the fiscal years ended June 30, 2017 and 2016 because the necessary actuarial information was not provided to Metropolitan by the California Public Employees' Retirement System (CalPERS) for the prior years presented. As of July 1, 2017, Metropolitan restated the beginning net position in the amount of $138.9 million to record the beginning deferred OPEB contributions and net OPEB liability.

CONDENSED FINANCIAL INFORMATION

Condensed Schedule of Net Position

	September 30,		
(Dollars in millions)	**2018**	2017	2016
Assets and deferred outflows of resources			
Capital assets, net	**$ 10,463.5**	$ 10,593.8	$ 10,587.8
Other assets	**1,991.9**	2,056.3	1,906.0
Deferred outflows of resources	**237.4**	210.9	182.4
Total assets and deferred outflows of resources	**12,692.8**	12,861.0	12,676.2
Liabilities and deferred inflows of resources			
Long-term liabilities, net of current portion	**5,099.9**	4,975.8	4,835.9
Other liabilities	**723.4**	1,007.4	1,016.7
Deferred inflows of resources	**46.6**	21.9	40.1
Total liabilities and deferred inflows of resources	**5,869.9**	6,005.1	5,892.7
Net position			
Net investment in capital assets, including State Water Project costs	**6,077.6**	6,081.6	6,192.7
Restricted	**404.2**	381.5	264.7
Unrestricted	**341.1**	392.8	326.1
Total net position	**$ 6,822.9**	$ 6,855.9	$ 6,783.5

Capital Assets, Net

Net capital assets include plant, participation rights, and construction work in progress, net of accumulated depreciation and amortization.

First Quarter Fiscal 2019 Compared to First Quarter Fiscal 2018. At September 30, 2018, net capital assets totaled $10.5 billion, or 82.4 percent, of total assets and deferred outflows of resources, and were $130.3 million lower than the prior year. The decrease included depreciation and amortization of $257.7 million and $135.0 million retirement of capital assets and write-off of construction in progress upon determination that no operating assets would result from the cost incurred. These decreases were offset by Metropolitan's continued expenditures on the capital investment plan of $136.9 million (including $4.2 million of capitalized interest), and net capital payments for participation rights in the State Water Project and other facilities of $125.5 million. See the capital assets section on pages 14-15 for additional information.

First Quarter Fiscal 2018 Compared to First Quarter Fiscal 2017. At September 30, 2017, net capital assets totaled $10.6 billion, or 82.4 percent, of total assets and deferred outflows of resources, and were $6.0 million higher than the prior year. The increase included Metropolitan's continued expenditures on the capital investment plan of $255.8 million (including $3.6 million of capitalized interest) and net capital payments for participation rights in the State Water Project and other facilities of $133.9 million. These increases were offset by depreciation and amortization of $269.7 million and $114.0 million retirement of capital assets and write-off of Mills Modules 1 and 2. See the capital assets section on pages 14-15 for additional information.

Other Assets

Other assets include accounts receivable, inventories, prepaid costs, and cash and investments.

First Quarter Fiscal 2019 Compared to First Quarter Fiscal 2018. At September 30, 2018, other assets totaled $2.0 billion and were $64.4 million lower than the prior year. Cash and investments were $153.8 million lower primarily due to the $250.0 million repayment of short-term revolving notes, offset by $64.3 million proceed from the issuance of the Subordinate Water Revenue Bond 2018, Series B in June 2018. This decrease was partially offset by $84.5 million higher deposits, prepaid costs, and other primarily due to $37.8 million more of prepaid water costs, which included $23.2 million or 174.5 thousand acre-feet (TAF) of higher supply storage and $17.8 million more of PVID land fallowing costs. In addition, $23.4 million of prepaid costs related to the California WaterFix advance funding agreement with DWR was recorded in September 2018. Another offset was $16.1 million higher water revenues receivable, of which $14.8 million related to higher prices and $1.3 million or 1.6 TAF related to higher volumes sold.

First Quarter Fiscal 2018 Compared to First Quarter Fiscal 2017. At September 30, 2017, other assets totaled $2.1 billion and were $150.3 million more than the prior year primarily due to $136.6 million of higher cash and investments resulting from the unspent proceeds of the $335.0 million new bond issues. In addition, water revenues receivable were $7.0 million higher, of which $5.5 million related to higher prices and $1.5 million or 1.9 TAF related to higher volumes sold.

Deferred Outflows of Resources

Deferred outflows of resources include deferred outflows related to loss on bond refundings and swap terminations, deferred outflows related to the net pension liability and net OPEB liability, and deferred outflows for effective interest rate swaps.

First Quarter Fiscal 2019 Compared to First Quarter Fiscal 2018. At September 30, 2018, deferred outflows totaled $237.4 million and were $26.5 million higher than the prior year. The increase was primarily due to $34.7 million deferred OPEB contributions due to the implementation of GASB 75. This increase was offset by $9.3 million lower deferred loss on bond refundings due to $6.3 million of scheduled amortization and $3.0 million of refunding transactions.

First Quarter Fiscal 2018 Compared to First Quarter Fiscal 2017. At September 30, 2017, deferred outflows of resources totaled $210.9 million and were $28.5 million more than the prior year. The increase was primarily due to $82.0 million net difference in projected and actual earnings related to the net pension liability. This increase was offset by $29.9 million lower deferred outflows on effective swaps due to rising interest rates and $18.6 million lower deferred outflows related to loss on bond refundings due to $12.8 million of refunding transactions and $5.8 million of scheduled amortization.

Long-term Liabilities, Net of Current Portion

Long-term liabilities, net of current portion include long-term debt, customer deposits and trust funds, net pension liability, net OPEB liability, postemployment benefits other than pensions, accrued compensated absences, obligations for off-aqueduct facilities, workers' compensation and third party claims, fair value of interest rate swaps, and other long-term obligations.

First Quarter Fiscal 2019 Compared to First Quarter Fiscal 2018. At September 30, 2018, long-term liabilities, net of current portion, totaled $5.1 billion and were $124.1 million higher than the prior year. The implementation of GASB 75 resulted in net OPEB liability that was $158.7 million more than the obligation for OPEB recorded as of September 30, 2017. The increase also included $73.3 million higher net pension liability due to $156.7 million of interest on total pension liability plus $125.7 million related to changes of assumptions from a 7.65 percent discount rate to 7.15 percent, offset by $171.6 million of pension plan investment earnings and $42.8 million of employer contributions. These increases were offset by $89.9 million of lower long-term debt, net of current portion primarily due to $152.2 million principal payments, a $32.1 million decrease related to bond refundings, as the new debt issued was less than the amount of debt refunded, and $8.6 million amortization of bond premium and discounts, offset by $64.3 million of new bonds issued and $38.7 million less current portion of long-term debt as compared to prior year. See the other liabilities section below for additional information. Additionally, there was a $25.9 million decrease in the fair value of interest rate swaps due to higher interest rates as compared to prior year. See the long-term debt section below for additional information.

First Quarter Fiscal 2018 Compared to First Quarter Fiscal 2017. At September 30, 2017, long-term liabilities, net of current portion, totaled $5.0 billion and were $139.9 million higher than the prior year. The increase included $113.4 million of higher long-term debt, net of current portion due to the issuance of $335.0 million revenue bonds offset by $159.5 million paydown of bond principal, $47.8 million related to bond refundings, as the new debt issued was less than the amount of debt refunded, and $9.9 million of scheduled amortization of bond premiums and discounts. In addition, net pension liability was $108.1 million more due to the decrease of actual pension plan investment earnings as compared to the prior year, offset by $38.4 million of employer contributions. These increases were offset by $45.6 million of lower customer deposits and trust funds, net of current portion primarily due to $50.4 million termination of the San Luis Rey trust and $31.6 million of lower fair value of interest rate swaps due to higher interest rates as compared to prior year. See the long-term debt section for additional information.

Other Liabilities

Other liabilities represent current liabilities that are due within one year. Current liabilities include accounts payable, accrued liabilities, and the current portion of long-term liabilities.

First Quarter Fiscal 2019 Compared to First Quarter Fiscal 2018. At September 30, 2018, other liabilities totaled $723.4 million, and were $284.0 million lower than the prior year primarily due to a $250.0 million repayment of short-term revolving notes and $38.7 million lower current portion of long-term debt due to required principal payments for some bond issues were lower than the prior year. In addition, the $180.0 million revolving credit agreement (RCA) that expired in June 2018 was replaced by a $200.0 million RCA increasing the self-liquidity bonds coverage by $20.0 million.

First Quarter Fiscal 2018 Compared to First Quarter Fiscal 2017. At September 30, 2017, other liabilities totaled $1.0 billion, and were $9.3 million lower than the prior year primarily due to $7.3 million lower accounts payable and accrued expenses, which included $3.1 million less of vendor obligations and $1.6 million of lower State Water Project costs.

Deferred Inflows of Resources

Deferred inflows of resources represent deferred inflows related to the net pension liability and deferred inflows for effective interest rate swaps.

First Quarter Fiscal 2019 Compared to First Quarter Fiscal 2018. At September 30, 2018, deferred inflows of resources totaled $46.6 million, and were $24.7 million higher than the prior year primarily due to a $21.9 million increase in effective swaps due to higher interest rates.

First Quarter Fiscal 2018 Compared to First Quarter Fiscal 2017. At September 30, 2017, deferred inflows of resources totaled $21.9 million, and were $18.2 million lower than the prior year. This pension related decrease included $16.1 million net difference between projected and actual earnings and $10.9 million due to change in assumptions offset by $8.8 million higher difference between actual and expected experience.

Net Investment in Capital Assets, including State Water Project Costs

Net investment in capital assets, including State Water Project costs, include amounts expended for capital improvements and State Water Project, offset by debt issued for these purposes.

First Quarter Fiscal 2019 Compared to First Quarter Fiscal 2018. At September 30, 2018, net investment in capital assets, including State Water Project costs totaled $6.1 billion and was $4.0 million lower than the prior year. This decrease included $130.3 million net decrease in capital assets offset by $128.6 million decrease in outstanding debt. See discussions of these items in the capital assets and long-term debt sections.

First Quarter Fiscal 2018 Compared to First Quarter Fiscal 2017. At September 30, 2017, net investment in capital assets, including State Water Project costs totaled $6.1 billion and was $111.1 million lower than the prior year. This decrease included $117.8 million net increase in outstanding debt offset by $6.0 million net increase in capital assets. See discussions of these items in the capital assets and long-term debt sections.

Restricted Net Position

Restricted net position includes amounts restricted for debt service payments and operating expenses, both of which are required by bond covenants.

First Quarter Fiscal 2019 Compared to First Quarter Fiscal 2018. At September 30, 2018, restricted net position totaled $404.2 million which was $22.7 million higher than the prior year. The increase is primarily due to $21.1 million higher estimated operating and maintenance expenditures in the two months subsequent to the quarter which are a component of restricted net position.

First Quarter Fiscal 2018 Compared to First Quarter Fiscal 2017. At September 30, 2017, restricted net position totaled $381.5 million which was $116.8 million higher than the prior year. The increase was primarily due to $117.2 million of higher restricted for debt service resulting from higher principal and interest payments.

Unrestricted Net Position

Unrestricted net position consists of net position items that do not meet the definition of "restricted" or "net investment in capital assets, including State Water Project costs." Certain unrestricted net position items have been designated for purposes authorized by the Board.

First Quarter Fiscal 2019 Compared to First Quarter Fiscal 2018. Unrestricted net position of $341.1 million decreased $51.7 million from the prior year which was a result of $22.7 million of higher restricted net position requirements for debt service and operating expenses. In addition, Metropolitan implemented GASB 75 in 2018, which resulted in the recording of beginning deferred OPEB contributions and net OPEB liability of $138.9 million. These decreases were offset by twelve months ended September 30, 2018 changes in net position before contributions of $104.6 million and $4.0 million of lower net investment in capital assets, including State Water Project costs.

First Quarter Fiscal 2018 Compared to First Quarter Fiscal 2017. Unrestricted net position of $392.8 million increased $66.7 million from the prior year which was the result of $116.8 million of higher restricted net position requirements for debt service and operating expenses and the twelve months ended September 30, 2017 changes in net position before contributions of $72.3 million, partially offset by a $111.1 million increase in net investment in capital assets.

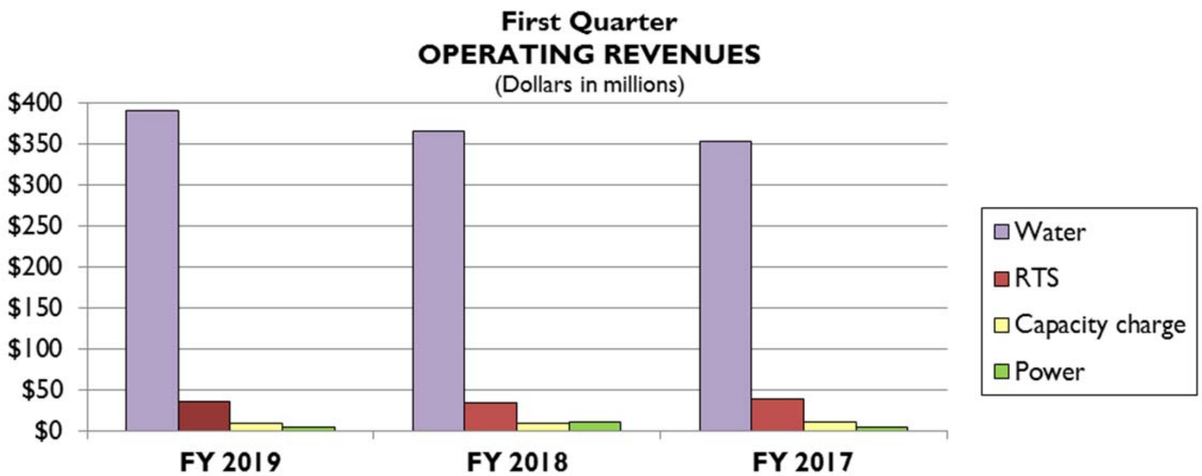
CHANGES IN NET POSITION

Condensed Schedule of Revenues, Expenses, and Changes in Net Position

	Three Months Ended September 30,		
(Dollars in millions)	**2018**	2017	2016
Water revenues	**$ 389.8**	$ 365.7	$ 352.3
Readiness-to-serve charges	**35.0**	33.8	38.3
Capacity charge	**8.9**	8.4	11.4
Power sales	**4.1**	10.3	4.6
Operating revenues	**437.8**	418.2	406.6
Taxes, net	**32.6**	30.4	28.2
Investment income	**3.7**	4.5	1.1
Other	**2.5**	1.5	1.3
Nonoperating revenues	**38.8**	36.4	30.6
Total revenues	**476.6**	454.6	437.2
Power and water costs	**(110.7)**	(124.1)	(91.4)
Operations and maintenance	**(118.8)**	(123.7)	(139.7)
Depreciation and amortization	**(81.2)**	(75.5)	(73.3)
Operating expenses	**(310.7)**	(323.3)	(304.4)
Bond interest, net of amount capitalized	**(28.7)**	(31.7)	(32.2)
Other	**(0.8)**	(1.6)	(1.0)
Nonoperating expenses	**(29.5)**	(33.3)	(33.2)
Total expenses	**(340.2)**	(356.6)	(337.6)
Changes in net position before contributions	**136.4**	98.0	99.6
Capital contributions	**—**	0.2	0.1
Changes in net position	**136.4**	98.2	99.7
Net position, at June 30,	**6,686.5**	6,757.7	6,683.8
Net position, at September 30,	**$ 6,822.9**	$ 6,855.9	$ 6,783.5

Operating Revenues

Metropolitan’s principal source of revenue is derived from the sale and availability of water, including water rates and other exchange and wheeling transactions, which typically account for approximately 85 percent of operating revenues. Metropolitan’s primary sources of water supply are the Colorado River and the State Water Project.



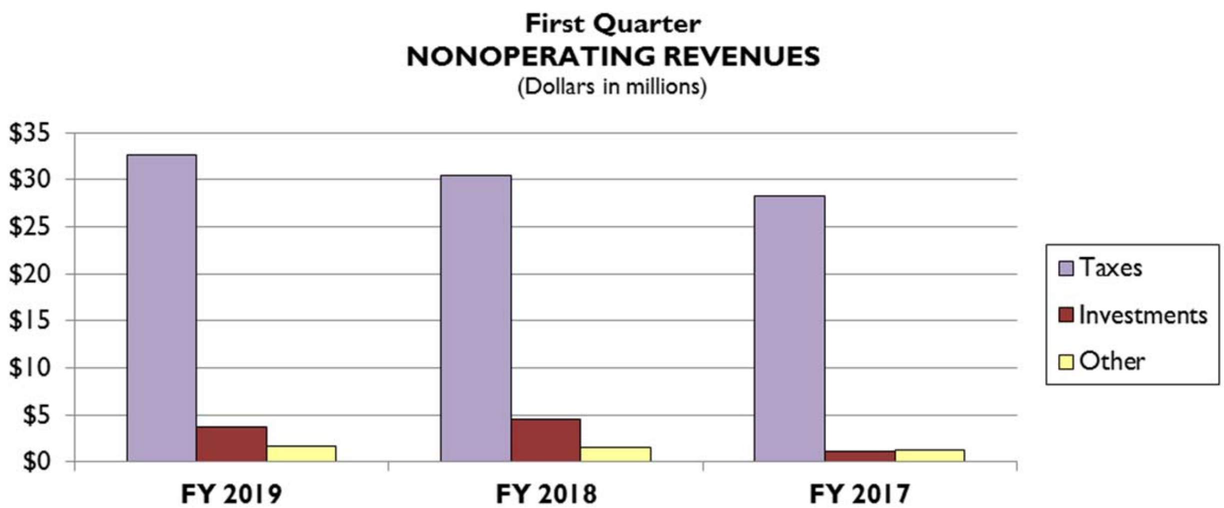
Analytical Review of Operating Revenues

First Quarter Fiscal 2019 Compared to First Quarter Fiscal 2018. For the three months ended September 30, 2018, operating revenues were $437.8 million or $19.6 million more than the prior year. The increase was primarily due to $24.1 million of higher water revenue, of which $15.1 million related to higher water rates and $9.0 million or 11.2 TAF of higher volumes sold. This increase was offset by $6.2 million of lower power recoveries revenue due to lower State Water Project allocation, as compared to prior year, resulting in decreased power generation.

First Quarter Fiscal 2018 Compared to First Quarter Fiscal 2017. For the three months ended September 30, 2017, operating revenues were $418.2 million or $11.6 million more than the prior year primarily due $13.4 million of higher water revenue, of which $19.8 million related to higher rates offset by $6.4 million of lower volumes of 8.5 thousand acre-feet (TAF).

Nonoperating Revenues

The primary source of nonoperating revenues is property taxes.



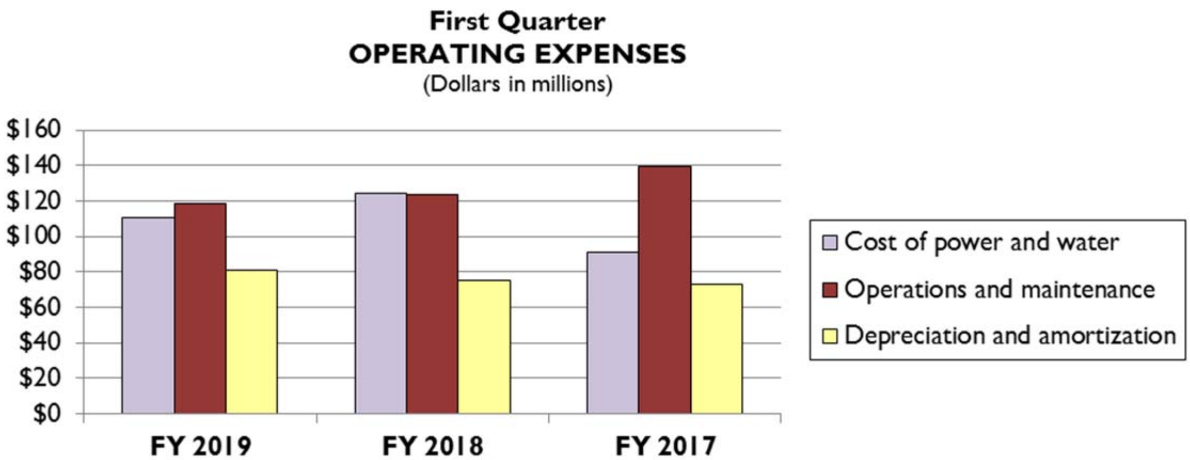
Analytical Review of Nonoperating Revenues

First Quarter Fiscal 2019 Compared to First Quarter Fiscal 2018. Nonoperating revenues for the three months ended September 30, 2018 totaled $38.8 million and were $2.4 million higher than the prior year primarily due to $2.2 million of higher property tax revenue due to timing.

First Quarter Fiscal 2018 Compared to First Quarter Fiscal 2017. Nonoperating revenues for the three months ended September 30, 2017 totaled $36.4 million and were $5.8 million higher than the prior year. The increase included $3.4 million more of investment income of which $2.0 million related to favorable change in fair value of investments and $1.6 million of higher rate of return and $2.2 million of higher taxes, net due to timing.

Operating Expenses

Operating expenses fall into three primary cost areas: power and water, operations and maintenance, and depreciation and amortization.



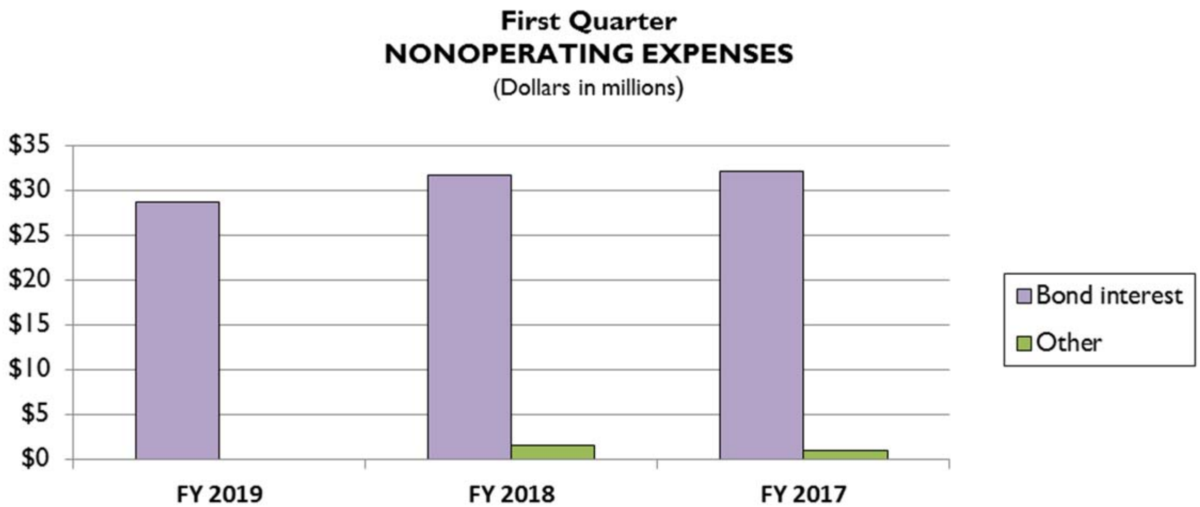
Analytical Review of Operating Expenses

First Quarter Fiscal 2019 Compared to First Quarter Fiscal 2018. For the three months ended September 30, 2018, operating expenses of $310.7 million were $12.6 million lower than prior year. The decrease was partially due to $13.4 million lower power and water costs due to lower minimum State Water Project operation, maintenance, power and replacement (OMP&R) costs related to an over collection of prior year's charges.

First Quarter Fiscal 2018 Compared to First Quarter Fiscal 2017. For the three months ended September 30, 2017 operating expenses of $323.3 million were $18.9 million higher than prior year primarily due to $32.7 million of higher power and water costs as the $46.3 million credit in fiscal year 2017 was not present in fiscal year 2018. This increase was partially offset by $16.0 million of lower operations and maintenance costs primarily due to $18.3 million lower conservation credits expenses as the $450.0 million budget in fiscal year 2015 continued to be spent down.

Nonoperating Expenses

The primary source of nonoperating expenses is interest expense on bonds, loss on disposal of plant assets and other, net.



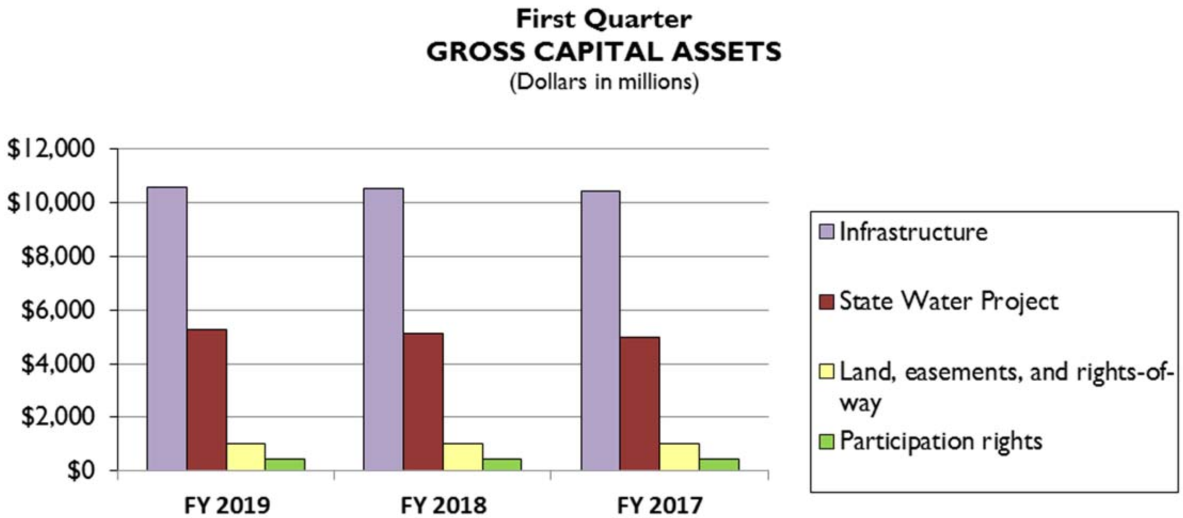
Analytical Review of Nonoperating Expenses

First Quarter Fiscal 2019 Compared to First Quarter Fiscal 2018. For the three months ended September 30, 2018 nonoperating expenses of $29.5 million were $3.8 million lower than the prior year. The decrease was primarily due to $3.0 reduction in bond interest, net of amount capitalized due to bond refunding transactions to take advantage of lower interest rates.

First Quarter Fiscal 2018 Compared to First Quarter Fiscal 2017. For the three months ended September 30, 2017 nonoperating expenses of $33.3 million were $100,000 lower than the prior year.

CAPITAL ASSETS

Capital assets include Metropolitan's water infrastructure, land and buildings, as well as participation rights in State Water Project and various other water programs.



Schedule of Capital Assets

(Dollars in millions)	September 30, 2018	2017	2016
Land, easements and rights-of-way	**$ 995.2**	$ 1,010.4	$ 1,008.0
Construction in progress	**731.9**	1,058.1	903.3
Parker power plant and dam	**13.0**	13.0	13.0
Power recovery plants	**216.2**	196.9	180.3
Other dams and reservoirs	**1,560.7**	1,549.8	1,542.2
Water transportation facilities	**3,820.7**	3,744.1	3,708.9
Pumping plants and facilities	**302.4**	294.3	293.5
Treatment plants and facilities	**2,969.8**	2,796.5	2,887.4
Buildings	**162.5**	138.9	136.1
Other plant assets	**745.1**	713.8	701.2
Pre-operating expenses original aqueduct	**44.6**	44.6	44.6
Participation rights in State Water Project	**5,254.6**	5,128.7	4,994.8
Participation rights in other facilities	**459.5**	459.7	459.7
Gross capital assets	**17,276.2**	17,148.8	16,873.0
Less accumulated depreciation and amortization	**(6,812.7)**	(6,555.0)	(6,285.2)
Capital assets, net	**$ 10,463.5**	$ 10,593.8	$ 10,587.8
Net increase from prior year	**$ (130.3)**	$ 6.0	$ 154.3
Percent change	**(1.2%)**	0.1%	1.5%

First Quarter Fiscal 2019 Compared to First Quarter Fiscal 2018. Net capital assets totaled approximately $10.5 billion and decreased $130.3 million over the prior year. The decrease included depreciation and amortization of $257.7 million and a $135.0 million retirement of capital assets and write-off of construction in progress upon determination that no operating assets would result from the cost incurred, offset by $136.9 million of construction spending, and a net increase of $125.5 million in participation rights in State Water Project and other facilities.

The major capital asset additions for the current year, excluding capitalized interest, included:

- $43.5 million for the distribution system's rehabilitation program; this program will replace or refurbish existing facilities within Metropolitan's distribution system including reservoirs, pressure control structures, hydroelectric power plants, and pipelines in order to reliably meet water demands.
- $43.5 million for the pre-stressed concrete cylinder pipe reliability (PCCP) program; this program identifies pipelines whose age, location and condition warrant refurbishment/replacement to ensure long-term reliability of Metropolitan's PCCP lines water delivery.
- $30.2 million for the improvements in infrastructure reliability at the treatment plants; this program will replace or refurbish facilities and components at Metropolitan's five water treatment plants in order to continue to reliably meet water demands.

Metropolitan's fiscal year 2019 capital investment plan includes $254.7 million principally for the distribution system and rehabilitation projects, the Colorado River Aqueduct reliability programs, the PCCP feeders upgrade, systems and information technology improvements, and water treatment plants upgrades program.

First Quarter Fiscal 2018 Compared to First Quarter Fiscal 2017. Net capital assets totaled approximately $10.6 billion and increased $6.0 million over the prior year. This increase included $255.8 million of new construction activity, and a net increase of $133.9 million in participation rights in State Water Project and other facilities. The increase was offset by depreciation and amortization of $269.7 million and $114.0 million retirement of capital assets and write-off of Mills Mods 1 and 2.

The major capital asset additions for the current year, excluding capitalized interest, included:

- $68.0 million for the distribution system's rehabilitation program.
- $37.1 million for the improvements in infrastructure reliability at the treatment plants.
- $28.1 million for the Colorado River Aqueduct (CRA) reliability and containment programs. These programs were established to provide infrastructure reliability and regulatory compliance throughout the CRA conveyance system.

DEBT ADMINISTRATION – LONG-TERM DEBT

Schedule of Long-term Debt, Including Current Portion

(Dollars in millions)	September 30, 2018	2017	2016
General obligation bonds *(a)*	**$ 60.6**	$ 74.9	$ 92.9
Revenue bonds *(a)*	**4,109.8**	4,215.5	4,060.7
State revolving loan	**—**	—	9.1
Other, net *(b)*	**204.1**	212.7	222.6
	$ 4,374.5	$ 4,503.1	$ 4,385.3
Increase (decrease) from prior year	**$ (128.6)**	$ 117.8	$ 39.2
Percent change	**(2.9%)**	2.7%	0.9%

(a) Includes refunding bonds.
(b) Consists of unamortized bond discounts and premiums.

First Quarter Fiscal 2019 Compared to First Quarter Fiscal 2018. At September 30, 2018, outstanding bonds and other long-term obligations totaled $4.4 billion, a net decrease of $128.6 million or 2.9 percent from the prior year. The decrease included $152.2 million of scheduled principal payments, $32.1 million related to bond refundings, as the new debt issued was less than the amount of debt refunded, and $8.6 million of scheduled amortization of bond premiums and discounts. These decreases were offset by the issuance of $64.3 million in revenue bonds.

First Quarter Fiscal 2018 Compared to First Quarter Fiscal 2017. At September 30, 2017, there was $4.5 billion of outstanding bonds and other long-term obligations, a net increase of $117.8 million or 2.7 percent from the prior year. The increase included new debt issued of $335.0 million offset by scheduled principal payments of $159.5 million, a $47.8 million principal reduction related to bond refundings, as the new debt issued was less than the amount of debt refunded, and $9.9 million of scheduled amortization of bond premiums and discounts.

Additional information on Metropolitan's long-term debt can be found in Note 3 to the basic financial statements.

CREDIT RATINGS

Metropolitan's credit ratings at September 30, 2018, are shown below.

	Moody's Investors Service	Standard & Poor's Global	Fitch Ratings
General obligation bonds	Aaa	AAA	AA+
Water revenue bonds-fixed rate	Aa1	AAA	AA+
Water revenue bonds-variable rate	VMIG 1	A-1+	F1+
Subordinate water revenue bonds-fixed rate	N/A	AA+	AA+
Subordinate water revenue bonds-variable rate	N/A	A-1+	F1+

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STATEMENTS OF NET POSITION

(Dollars in thousands)	September 30, 2018	2017
ASSETS AND DEFERRED OUTFLOWS OF RESOURCES	(Unaudited)	
Current Assets:		
Cash and investments, at fair value (Notes 1b and 2):		
Unrestricted (cost: $354,066 and $433,589 for 2018 and 2017, respectively)	**$ 351,829**	$ 433,771
Restricted (cost: $344,915 and $352,349 for 2018 and 2017, respectively)	**342,735**	352,496
Total cash and investments	**694,564**	786,267
Receivables:		
Water revenues	**260,447**	244,380
Interest on investments	**4,061**	4,717
Other, net (Note 1e)	**179,034**	175,687
Total receivables	**443,542**	424,784
Inventories (Note 1f)	**100,078**	113,866
Deposits, prepaid costs, and other (Note 8)	**131,575**	119,941
Total current assets	**1,369,759**	1,444,858
Noncurrent Assets:		
Cash and investments, at fair value (Notes 1b and 2):		
Unrestricted (cost: $237,814 and $305,161 for 2018 and 2017, respectively)	**236,311**	305,289
Restricted (cost: $82,413 and $73,438 for 2018 and 2017, respectively)	**83,706**	76,786
Total cash and investments	**320,017**	382,075
Capital assets:		
Plant and equipment - non depreciable (Notes 1g and 6g)	**1,727,072**	2,068,558
Plant and equipment - depreciable (Notes 1g and 6g)	**9,835,093**	9,491,706
Participation rights in State Water Project (Notes 1h and 7)	**5,254,557**	5,128,789
Participation rights in other facilities (Note 1h)	**459,489**	459,709
Total capital assets	**17,276,211**	17,148,762
Less accumulated depreciation and amortization	**(6,812,702)**	(6,554,925)
Total capital assets, net	**10,463,509**	10,593,837
Other assets, net of current portion:		
Deposits, prepaid costs, and other (Note 8)	**302,141**	229,267
Total other assets	**302,141**	229,267
Total noncurrent assets	**11,085,667**	11,205,179
Deferred Outflows of Resources:		
Loss on bond refundings (Note 1q)	**37,582**	46,876
Loss on swap terminations (Note 1q)	**26,691**	29,710
Pension related (Notes 1k, 1q and 4)	**138,405**	130,346
OPEB related (Notes 1l, 1q and 5)	**34,674**	—
Effective swaps (Note 1q)	**—**	3,994
Total deferred outflows of resources	**237,352**	210,926
Total Assets and Deferred Outflows of Resources	**$ 12,692,778**	$ 12,860,963

See accompanying notes to basic financial statements.

STATEMENTS OF NET POSITION

(Dollars in thousands)	September 30, 2018	2017
LIABILITIES, DEFERRED INFLOWS OF RESOURCES, AND NET POSITION	(Unaudited)	
Current Liabilities:		
Accounts payable and accrued expenses (Note 1i)	**$ 148,926**	$ 141,359
Revolving notes (Note 3a)	**—**	250,000
Current portion of long-term debt	**291,057**	329,769
Current portion of obligations for off-aqueduct power facilities (Note 6f)	**—**	1,203
Current portion of accrued compensated absences (Note 1j)	**19,700**	19,800
Current portion of customer deposits and trust funds	**6,318**	8,640
Current portion of workers' compensation and third party claims (Note 11)	**4,083**	5,109
Current portion of other long-term liabilities	**211,197**	206,317
Accrued bond interest	**40,259**	43,434
Matured bonds and coupons not presented for payment	**1,760**	1,764
Total current liabilities	**723,300**	1,007,395
Noncurrent Liabilities:		
Long-term debt, net of current portion	**4,083,464**	4,173,361
Revolving notes (Note 3a)	**15,600**	—
Obligations for off-aqueduct power facilities, net of current portion (Note 6f)	**—**	9,328
Accrued compensated absences, net of current portion (Note 1j)	**29,840**	26,581
Customer deposits and trust funds, net of current portion	**41,176**	41,758
Net pension liability (Notes 1k and 4)	**660,917**	587,662
Net OPEB liability (Notes 1l and 5)	**215,718**	—
Postemployment benefits other than pensions (Note 5)	**—**	57,038
Workers' compensation and third party claims, net of current portion (Note 11)	**9,831**	10,814
Fair value of interest rate swaps (Note 3e)	**41,184**	67,054
Other long-term liabilities, net of current portion	**2,204**	2,226
Total noncurrent liabilities	**5,099,934**	4,975,822
Total liabilities	**5,823,234**	5,983,217
Commitments and Contingencies (Note 6)	**—**	—
Deferred Inflows of Resources:		
Effective swaps (Note 1q)	**21,876**	**—**
Pension related (Notes 1k, 1q and 4)	**17,836**	21,896
OPEB related (Notes 1l, 1q and 5)	**6,928**	**—**
Total deferred inflows of resources	**46,640**	21,896
Total Liabilities and Deferred Inflows of Resources	**5,869,874**	6,005,113
Net Position (Note 10):		
Net investment in capital assets, including State Water Project costs	**6,062,039**	6,081,570
Restricted for:		
Debt service	**199,460**	197,799
Other	**204,723**	183,662
Unrestricted	**356,682**	392,819
Total net position	**6,822,904**	6,855,850
Total Liabilities, Deferred Inflows of Resources, and Net Position	**$ 12,692,778**	$ 12,860,963

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STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

(Dollars in thousands)	Three Months Ended September 30, 2018	2017
	(Unaudited)	
Operating Revenues (Note 1c):		
Water revenues	**$ 389,829**	$ 365,681
Readiness-to-serve charges	**35,000**	33,750
Capacity charge	**8,902**	8,424
Power sales	**4,041**	10,295
Total operating revenues	**437,772**	418,150
Operating Expenses:		
Power and water costs	**110,722**	124,112
Operations and maintenance	**118,761**	123,676
Total operating expenses	**229,483**	247,788
Operating income before depreciation and amortization	**208,289**	170,362
Less depreciation and amortization	**(81,229)**	(75,500)
Operating income	**127,060**	94,862
Nonoperating Revenues (Expenses) (Note 1n):		
Taxes, net (Note 1d)	**32,621**	30,400
Bond interest, net of $4,200 and $3,600 of interest capitalized in fiscal years 2019 and 2018, respectively (Note 1g)	**(28,727)**	(31,694)
Investment income, net	**3,673**	4,461
Other, net	**1,753**	(47)
Total nonoperating revenues, net	**9,320**	3,120
Changes in Net Position Before Contributions	**136,380**	97,982
Capital contributions (Note 1m)	**39**	183
Changes in net position	**136,419**	98,165
Net position, at June 30,	**6,686,485**	6,757,685
Net position, at September 30,	**$ 6,822,904**	$ 6,855,850

See accompanying notes to basic financial statements.

STATEMENTS OF CASH FLOWS

(Dollars in thousands)	Three Months Ended September 30, 2018	2017
Cash Flows from Operating Activities:	(Unaudited)	
Cash received from water sales	**$ 321,197**	$ 298,238
Cash received from readiness-to-serve charges	**10,394**	9,949
Cash received from capacity charge	**3,734**	3,607
Cash received from power sales	**3,692**	8,684
Cash received from other exchange transactions	**29,394**	20,911
Cash paid for operations and maintenance expenses	**(63,923)**	(56,588)
Cash paid to employees for services	**(109,614)**	(94,788)
Cash paid for power and water costs	**(110,042)**	(138,875)
Other cash flows for operating activities	**(1,049)**	(1,198)
Net cash provided by operating activities	**83,783**	49,940
Cash Flows from Noncapital Financing Activities:		
Proceeds from other collections	**2,726**	2,253
Net cash provided by noncapital financing activities	**2,726**	2,253
Cash Flows from Capital and Related Financing Activities:		
Acquisition and construction of capital assets	**(48,335)**	(42,401)
Payments for State Water Project costs	**(68,089)**	(68,288)
Proceeds from short and long-term debt	**15,600**	79,833
Payments for bond issuance costs	**(1,497)**	(802)
Principal paid on debt	**(124,025)**	(135,930)
Interest paid on debt	**(69,671)**	(74,239)
Payments for other long-term obligations	**—**	(418)
Proceeds from tax levy	**10,689**	7,142
Transfer to/from escrow trust accounts	**18,323**	(27,072)
Payment of rebatable arbitrage	**(10)**	—
Net cash used by capital and related financing activities	**(267,015)**	(262,175)
Cash Flows from Investing Activities:		
Purchase of investment securities	**(1,915,725)**	(1,623,489)
Proceeds from sales and maturities of investment securities	**1,948,580**	1,829,320
Investment income	**4,527**	3,292
Net cash provided by investing activities	**37,382**	209,123
Net change in cash	**(143,124)**	(859)
Cash at July 1,	**162,379**	902
Cash at September 30, (Note 1b)	**$ 19,255**	$ 43

See accompanying notes to basic financial statements.

STATEMENTS OF CASH FLOWS

(Dollars in thousands)	Three Months Ended September 30, 2018		Three Months Ended September 30, 2017	
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES	(Unaudited)			
Operating Income	**$**	**127,060**	$	94,862
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities:				
Depreciation and amortization expense		**81,229**		75,500
Increase in accounts receivable		**(60,607)**		(85,047)
Increase in inventories		**(2,352)**		(3,333)
Increase in deposits, prepaid costs, and other		**(165,002)**		(155,078)
Increase (decrease) in accounts payable and accrued expenses		**(6,019)**		30,387
Increase in other items		**109,474**		92,649
Total Adjustments		**(43,277)**		(44,922)
Net cash provided by operating activities	**$**	**83,783**	$	49,940
Significant Noncash Investing, Capital and Financing Activities				
Refunding bonds proceeds received in escrow trust fund	**$**	**—**	$	413,170
Debt defeased through escrow trust fund with refunding debt	**$**	**—**	$	(399,995)

RECONCILIATION OF CASH AND INVESTMENTS TO CASH

Unrestricted cash and investments (at September 30, 2018 and 2017 include $19,255 and $43 of cash, respectively)	**$**	**588,140**	$	739,060
Restricted cash and investments		**426,441**		429,282
Total cash and investments, at fair value		**1,014,581**		1,168,342
Less: carrying value of investments		**(995,326)**		(1,168,299)
Total Cash (Note 1b)	**$**	**19,255**	$	43

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1. REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Reporting Entity

The Metropolitan Water District of Southern California (Metropolitan), a special district of the State of California, was organized in 1928 by vote of the electorates of several Southern California cities following adoption of the Metropolitan Water District Act (Act) by the California Legislature. Metropolitan's primary purposes under the Act are to develop, store and distribute water, at wholesale, to its member public agencies for domestic and municipal purposes. Surplus water is sold for other beneficial uses, including agricultural use. Metropolitan's service area comprises approximately 5,200 square miles and includes portions of the six counties of Los Angeles, Orange, Riverside, San Bernardino, San Diego, and Ventura. There are 26 independent member agencies of Metropolitan, consisting of 14 cities, 11 municipal water districts, and one county water authority. Metropolitan has no financial accountability for its member agencies. Metropolitan is governed by a 38-member Board of Directors (Board) comprised of representatives of the member agencies. Representation and voting rights are based on assessed valuations of property. Each member agency is entitled to have at least one representative on the Board plus an additional representative for each full five percent of the assessed valuation of real property within the jurisdictional boundary of each member agency. Changes in relative assessed valuation do not terminate any director's term. Accordingly, the Board may, from time to time, have more or fewer than 38 directors. No single member agency has a voting majority.

The Metropolitan Water District Asset Financing Corporation (MWDAFC) was incorporated on June 19, 1996. The MWDAFC is a California nonprofit public benefit corporation formed to assist Metropolitan by acquiring, constructing, operating and maintaining facilities, equipment, or other property needed by Metropolitan and leasing or selling such property to Metropolitan. The MWDAFC is governed by a board of five directors, each of whom must be a member of Metropolitan's Board. MWDAFC had no financial operations during the three months ended September 30, 2018 or 2017. MWDAFC is a component unit of Metropolitan and its activities will be blended with those of Metropolitan for financial reporting purposes should it commence operations.

(b) Principles of Presentation

Metropolitan operates as a utility enterprise and the accompanying basic financial statements reflect the flow of economic resources measurement focus and the full accrual basis of accounting. Under full accrual accounting, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred regardless of the timing of related cash flows.

Metropolitan is accounted for as an enterprise fund and applies all applicable Governmental Accounting Standards Board (GASB) pronouncements in its accounting and reporting.

For purposes of the statements of cash flows, Metropolitan defines cash as demand account balances and cash on hand.

(c) Revenue Policies

Water revenues, which include funds received from charges for the sale and availability of water, including water rates and other exchange and wheeling transactions, is the principal source of Metropolitan's revenues. Other sources of operating revenue include readiness-to-serve charges, capacity charge, and hydroelectric power sales. Other revenues include ad valorem property taxes and investment income.

Water rates are established by the Board on a biennial basis and are supported by cost of service studies. Water rates are not subject to regulation by the California Public Utilities Commission or by any other local, state, or federal agency. Water is delivered to the member agencies on demand and revenue is recognized at the time of sale.

Metropolitan's rate structure consists of unbundled rate elements (supply, treatment, conveyance and distribution, power, and demand management) designed to provide transparency regarding the cost of specific functions to member agencies. It is designed to improve regional water resources management and accommodate a water transfer market. The rate structure also includes tiered pricing for supply, a capacity charge, and a readiness-to-serve charge.

(d) Taxing Authority

Metropolitan is expressly empowered under the Act to levy and collect taxes on all taxable property within its boundaries for the purpose of carrying on its operations and paying its obligations, subject to certain limitations in the Act, the California Revenue and Taxation Code, and the California Constitution. Property taxes are levied annually by the Board effective as of July 1, using a lien date of January 1, and are payable by property owners in two equal installments that are due on November 1 and February 1, and become delinquent after December 10 and April 10, respectively. Property taxes levied by Metropolitan are billed and collected by the counties in its service area and are remitted to Metropolitan periodically throughout the year.

Property tax revenue is used to pay Metropolitan’s general obligation bond debt service and a portion of its obligations under its contract with the state for a water supply (the State Water Contract). In setting the annual levy, Metropolitan takes into account potential delinquencies, tax allocations to the successor agencies of former redevelopment agencies, and supplemental tax collections. Metropolitan recognizes property taxes receivable on July 1 of each fiscal year and recognizes revenue over the following 12-month period beginning July 1 through June 30 (the period for which the tax is levied).

As a result of legislation enacted in 1984, commencing with the fiscal year ended June 30, 1991, tax levies , other than annexation taxes, are limited to the amount needed to pay debt service on Metropolitan’s general obligation bonds and Metropolitan’s proportionate share of general obligation bond debt service of the state under the State Water Contract. However, under the terms of the 1984 legislation, the Board may suspend this particular restriction upon a finding that doing so is essential to Metropolitan's fiscal integrity. The Board made such a finding for fiscal years ended June 30, 2014 through 2019, and maintained the tax rate for those fiscal years at the rate levied during fiscal year ended June 30, 2013 to pay a portion of State Water Contract costs other than debt service.

(e) Other Receivables

Other receivables include amounts for taxes, hydroelectric power sales, readiness-to-serve charges, and other billings.

(f) Inventories

Metropolitan's inventories are valued based on a moving-average cost. Expenses are recorded when inventories are used. Components of inventories at September 30, 2018 and 2017 were as follows:

	September 30,	
(Dollars in thousands)	2018	2017
Water in storage	$ 87,105	$ 102,058
Operating supplies	12,973	11,808
Total inventories	$ 100,078	$ 113,866

(g) Plant and Equipment

Metropolitan's capital assets include plant and equipment, which are recorded at cost. Construction costs are capitalized if they exceed $50,000 and the asset has a useful life of at least five years. The cost of constructed assets may include labor, materials, certain general and administrative expenses, and interest incurred during construction periods. Depreciation is calculated using the straight-line method based on the estimated average useful lives of the assets, which are 10 to 80 years for buildings, storage, and distribution facilities, 10 to 50 years for treatment plants and hydroelectric power recovery facilities, and 10 to 80 years for miscellaneous assets. Improvements or refurbishments with aggregated costs that meet capitalization thresholds and that extend the useful life of an existing asset by at least five years or improve the operating efficiency of the asset are capitalized.

Major computer systems software, whether purchased or internally developed, is capitalized if the cost exceeds $250,000 and the useful life is at least three years. Vehicles and operating equipment are capitalized if the cost equals or exceeds $5,000 and the useful life is at least four years. Depreciation is calculated using the straight-line method based on the estimated useful lives and ranges from 3 to 10 years for major computer systems software and 4 to 10 years for vehicles and operating equipment.

(h) Participation Rights

Metropolitan participates in various storage and water management programs entitling it to certain water rights. Projects include the State Water Project (SWP) and various storage and water management programs. Metropolitan's participation in these projects is through cash payments. The value of participation rights is equal to the amounts spent for the construction of capital assets, such as pipelines, pumping facilities, and storage facilities, and amortized over the life of the agreements. These assets are not owned by Metropolitan. Certain projects also require payments for ongoing maintenance; those payments are charged to expense as incurred (See Note 7.)

(i) Disaggregation of Payable Balances

Accounts payable and accrued expenses at September 30, 2018 and 2017 were as follows:

	September 30,	
(Dollars in thousands)	2018	2017
Department of Water Resources (State Water Project):		
Capital, operating, maintenance, power, replacement, and variable power	$ 108,001	$ 102,690
Vendors	28,963	23,743
Accrued power costs	6,746	1,305
Accrued salaries	38	4,180
Conservation credits	5,178	9,441
Total accounts payable and accrued expenses	$ 148,926	$ 141,359

(j) Compensated Absences

Metropolitan's employees earn vacation, sick, and compensatory leave in varying amounts depending primarily on length of service. Upon termination from Metropolitan service, employees are entitled to full payment for accrued vacation and compensatory leave at their final pay rates, and are entitled to payment for approximately one-half of their accrued sick leave at such rates. Metropolitan records its obligations for vacation, sick, and compensatory leave earned by eligible employees based on current pay rates. The allocations to the current and long-term portions of these vested obligations were based on experience and projections of turnover.

(k) Pension Accounting

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the Plan and additions to/deductions from the Plan's fiduciary net position have been determined on the same basis as they are reported by the CalPERS Financial Office. For this purpose, benefit payments (including refunds of employee contributions) are recognized when currently due and payable in accordance with the benefit terms. Investments are reported at fair value.

Generally accepted accounting principles require that the reported results must pertain to liability and asset information within certain defined timeframes. For this report, the following timeframes are used:

Valuation Date (VD): June 30, 2016
Measurement Date (MD): June 30, 2017
Measurement Period: July 1, 2016 to June 30, 2017

(l) OPEB Accounting

For purposes of measuring the net OPEB liability, deferred outflows of resources and deferred inflows of resources related to OPEB, and OPEB expense, information about the fiduciary net position of Metropolitan's plan (OPEB Plan) and additions to/deductions from the OPEB Plan's fiduciary net position have been determined on the same basis. For this purpose, benefit payments are recognized when currently due and payable in accordance with the benefit terms. Investments are reported at fair value.

Generally accepted accounting principles require that the reported results must pertain to liability and asset information within certain defined timeframes. For this report, the following timeframes are used:

Valuation Date (VD): June 30, 2017
Measurement Date (MD): June 30, 2017
Measurement Period: July 1, 2016 to June 30, 2017

(m) Capital Contributions

Capital contributions are comprised of federal, state, and private grants. These grants are typically of a reimbursable nature: Metropolitan first pays for the project and then the granting agency reimburses Metropolitan for its eligible expenses. The portion of the grants restricted for capital purposes are reflected as capital contributions in the statements of revenues, expenses and changes in net position when they are earned, irrespective of the timing of the receipts. Examples of capital projects where grants are received include water treatment plant improvements, such as fluoridation and water storage programs.

(n) Operating and Nonoperating Revenues and Expenses

Metropolitan's primary purpose is to provide a supplemental supply of water for domestic and municipal uses. Accordingly, Metropolitan defines operating revenues as revenues derived from the sale and availability of water, including water rates and other exchange and wheeling transactions. It also includes readiness-to-serve charges, capacity charge, and hydroelectric power sales. Operating expenses include the cost of sales and services, administrative expenses, and depreciation and amortization of capital assets.

Revenues from property taxes and investment income, as well as interest expense on outstanding debt, are related to capital and financing activities and are defined as nonoperating revenues and expenses.

(o) Restricted and Unrestricted Resources

When both restricted and unrestricted resources are available for use, it is Metropolitan's practice to use restricted resources first, then unrestricted resources as they are needed.

(p) Use of Estimates

The preparation of basic financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the basic financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(q) Deferred Outflows/Inflows of Resources

GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position* (GASB 63) requires that the difference between assets, deferred outflows of resources, liabilities, and deferred inflows of resources be reported as net position. In addition, the impact of a deferred outflow of resources on net position must be explained as is done in the following paragraph.

The net investment in capital assets, including State Water Project costs of $6.1 billion at September 30, 2018 and 2017, includes the effect of deferring the recognition of losses from bond refundings. The deferred outflows from losses on bond refundings at September 30, 2018 and 2017 were $37.6 million and $46.9 million, respectively. This is amortized and recognized as a component of interest expense in a systematic and rational manner over the remaining life of the old or the new debt, whichever is shorter.

The unrestricted net position amount of $341.1 million and $392.8 million at September 30, 2018 and 2017, respectively, includes the effect of deferring the recognition of losses from swap terminations resulting in defeasance of debt, the increase or decrease in fair value of Metropolitan's effective interest rate swaps, and deferred amounts related to pension and OPEB. The deferred outflows from losses on swap terminations resulting in debt defeasance at September 30, 2018 and 2017, respectively, were $26.7 million and $29.7 million. These deferred outflows of resources are amortized and recognized as a component of interest expense in a systematic and rational manner over the remaining life of the old debt or the life of the new debt, whichever is shorter.

The deferred outflows related to pension at September 30, 2018 and 2017, respectively, were $138.4 million and $130.3 million. The deferred inflows related to pension at September 30, 2018 and 2017 were $17.8 million and $21.9 million, respectively.

The deferred outflows and deferred inflows related to OPEB at September 30, 2018 were $34.7 million and $6.9 million, respectively.

The deferred inflow from the increase in fair value of interest rate swaps of $21.9 million at September 30, 2018 and the deferred outflows from the decline in fair value of interest rate swaps of $4.0 million at September 30, 2017 would be recognized as an investment gain or loss, respectively, upon the early termination of the swaps. Metropolitan will only terminate its interest rate swap agreements in advance of the contractual termination dates if market conditions permit. The deferred inflow and the deferred outflow also would be recognized as an investment gain or loss, respectively, if the swaps were determined no longer to be effective hedges. Finally, if the bond associated with a swap is refunded, the deferred inflow or the deferred outflow would be reduced and the deferred gain or loss on refunding, respectively, would be increased by the same amount. The deferred gain or loss on refunding would be amortized as a component of interest expense over the life of the old debt or the new debt, whichever is shorter.

(r) Fair Value Measurement

GASB Statement No. 72, *Fair Value Measurement and Application* (GASB 72) requires a government to use valuation techniques that are appropriate under the circumstances and for which sufficient data are available to measure fair value. The techniques should be consistent with one or more of the following approaches: the market approach, the cost approach, or the income approach. Metropolitan reports its investments and liabilities at fair value using market approach and cost approach.

Additionally, GASB 72 establishes a hierarchy of inputs to valuation techniques used to measure fair value. This hierarchy has three levels which are: Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that a government can access at the measurement date; Level 2 inputs are inputs—other than quoted prices—that are observable for identical assets or liabilities, either directly or indirectly; and Level 3 inputs are unobservable inputs, such as management's assumption of the default rate among underlying mortgages of a mortgage-backed security. The fair value hierarchy to Metropolitan's assets and liabilities are presented in Note 2.

(s) New Accounting Pronouncements

Metropolitan implemented the following GASB Statements in the twelve months ended September 30, 2018:

In June 2015, the GASB issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions* (GASB 75), which establishes new accounting and financial reporting requirements for OPEB and provides information provided by state and local government employers about financial support for OPEB that is provided by other entities. This statement replaces the requirements of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions and GASB 57- OPEB Measurements by Agent Multiple-Employer Plans* (GASB 45). As a result of the implementation of GASB 75, Metropolitan restated beginning net position for 2018 in the amount of $138.9 million to record the beginning deferred OPEB contributions and net OPEB liability. Metropolitan didn't restate the financial statements for the year ended June 30, 2017 because the necessary actuarial information was not available.

In March 2017, the GASB issued Statement No. 85, *Omnibus 2017* (GASB 85). The objective of this Statement is to address practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and OPEB).

Specifically, this Statement addresses the following topics: (1) Blending a component unit in circumstances in which the primary government is a business-type activity that reports in a single column for financial statement presentation, (2) Reporting amounts previously reported as goodwill and "negative" goodwill, (3) Classifying real estate held by insurance entities, (4) Measuring certain money market investments and participating interest-earning investment contracts at amortized cost, (5) Timing of the measurement of pension or OPEB liabilities and expenditures recognized in financial statements prepared using the current financial resources measurement focus (6) Recognizing on-behalf payments for pensions or OPEB in employer financial statements, (7) Presenting payroll-related measures in required supplementary information for purposes of reporting by OPEB plans and employers that provide OPEB, (8) Classifying employer-paid member contributions for OPEB, (9) Simplifying certain aspects of the alternative measurement method for OPEB, (10) Accounting and financial reporting for OPEB provided through certain multiple-employer defined benefit OPEB plans. Implementation of GASB 85 in fiscal year 2018 didn't impact any previously reported balances in the Statement of Net Position or the Statement of Revenues, Expenses and Changes in Net Position. The effect of implementing GASB 85 was reflected in the Required Supplementary Information section of Metropolitan's financial statements for the year ended June 30, 2018.

In May 2017, the GASB issued Statement No. 86, *Certain Debt Extinguishment Issues* (GASB 86). The objective of this Statement is to improve consistency in accounting and financial reporting for in-substance defeasances of debt by providing guidance for transactions in which cash and other monetary assets acquired with only existing resources – resources other than the proceeds of refunding debt – are placed in an irrevocable trust for the sole purpose of extinguishing debt. This Statement also improves accounting and financial reporting for prepaid insurance on debt that is extinguished and notes to financial statements for debt that is defeased in substance. The requirement of this statement were effective beginning in fiscal year 2018 but there were no impacts on previously reported balances in the Statements of Net Position or the Statements of Revenues, Expenses and Changes in Net Position and there was no impact on note disclosures for the current period.

Metropolitan is currently evaluating its accounting practices to determine the potential impact on the financial statements for the following GASB Statements that will be implemented in a future fiscal year:

- GASB Statement No. 83, *Certain Asset Retirement Obligations*.
- GASB Statement No. 87, *Leases*.
- GASB Statement No. 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements*.
- GASB Statement No. 89, *Accounting for Interest Cost Incurred before the End of a Construction Period*.

The following pronouncements were issued by GASB but were determined to not be applicable to Metropolitan's financial statements:

- GASB Statement No. 81, *Irrevocable Split-Interest Agreements*.
- GASB Statement No. 84, *Fiduciary Activities*.

2. CASH AND INVESTMENTS

As a public agency, Metropolitan's investment practices are prescribed by various provisions of the California Government Code and the Act, as well as by administrative policies. Metropolitan's statement of investment policy is approved annually by the Board and describes the Treasurer's investment authority, practices, and limitations. The basic investment policy objectives, in order of importance, are safety of principal, liquidity, and return on investment.

Cash and investments may or may not be restricted as to use, depending on the specific purposes for which such assets are held (see Notes 2d and 10).

A summary of Metropolitan's deposit and investment policies, information on interest and credit risks, and restricted cash and investments is provided below.

(a) Deposits

The California Government Code requires California banks and savings and loan associations to secure a local government agency's deposits by pledging government securities as collateral.

As of September 30, 2018 and 2017, Metropolitan's cash balances with financial institutions were $19,250,000 and $38,000 respectively, and cash on hand was $5,000 at each year end.

(b) Investments

Metropolitan is permitted by State law and Board policy to invest in a variety of instruments including U.S. Treasury securities, federal agencies, repurchase agreements, negotiable certificates of deposit, bankers' acceptances, prime commercial paper, government sponsored enterprises, California local agency securities, including securities issued by Metropolitan, medium-term corporate notes, time deposits, investment contracts, shares of beneficial interest, and Local Agency Investment Fund (LAIF). As of September 30, 2018 and 2017, Metropolitan had the following investments at fair value:

	September 30,	
(Dollars in thousands)	**2018**	2017
U.S. Treasury securities	**$ 267,933**	$ 342,703
U.S. Guarantees – GNMAs	**3**	4
Federal agency securities	**133,955**	133,720
Prime commercial paper	**111,695**	219,740
Medium-term corporate notes	**119,498**	127,624
Negotiable certificates of deposit	**239,977**	233,692
Shares of beneficial interest	**467**	190
Government-sponsored enterprise (GSE)	**63,233**	54,827
Municipal bonds	**10,250**	22,273
Local Agency Investment Fund	**48,315**	33,526
Total investments	**$ 995,326**	$ 1,168,299

Metropolitan categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure fair value of the assets. Level 1 are quoted prices in an active market for identical assets; Level 2 inputs are significant other observable inputs; and Level 3 inputs are significant unobservable inputs.

The following is the summary of the fair value hierarchy of the fair value of investments of Metropolitan as of September 30, 2018 and 2017:

	Fair Value Measurement Using							
(Dollars in thousands)	**9/30/2018**	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Obervable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	9/30/2017	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Obervable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Investments by fair value level:								
U.S. Treasury securities	**$ 267,933**	**$ 267,933**	**$ —**	**$ —**	$ 342,703	$ 342,703	$ —	$ —
U.S. Guarantees – GNMAs	**3**	**3**	**—**	**—**	4	4	—	—
Federal agency securities	**133,955**	**133,955**	**—**	**—**	133,720	133,720	—	—
Prime commercial paper	**111,695**	**1,087**	**110,608**	**—**	219,740	73,915	145,825	—
Medium-term corporate notes	**119,498**	**119,498**	**—**	**—**	127,624	127,624	—	—
Negotiable certificates of deposit	**239,977**	**239,977**	**—**	**—**	233,692	198,692	35,000	—
Shares of beneficial interest [(1)]	**467**	**—**	**—**	**467**	190	—	—	190
Government-sponsored enterprise (GSE)	**63,233**	**63,233**	**—**	**—**	54,827	54,827	—	—
Municipal bonds	**10,250**	**10,250**	**—**	**—**	22,273	22,273	—	—
Total investments by fair value level	**$ 947,011**	**$ 835,936**	**$ 110,608**	**$ 467**	$ 1,134,773	$ 953,758	$ 180,825	$ 190
Investments not subject to fair value level:								
Local Agency Investment Fund	**48,315**				33,526			
Total investments	**$ 995,326**				$ 1,168,299			

[(1)] As of September 30, 2018 and 2017, the balance was invested in BlackRock Treasury Trust (TTTXX).

Investments classified in Level 1 of the fair value hierarchy, valued at $835.9 million and $953.8 million as of September 30, 2018 and 2017, respectively, are valued using quoted prices in active markets.

Prime commercial paper totaling $110.6 million and $145.8 million and negotiable certificates of deposit totaling $0 and $35.0 million, as of September 30, 2018 and 2017, respectively, classified in Level 2 of the fair value hierarchy were valued using matrix pricing.

Shares of beneficial interest totaling $0.5 million and $0.2 million as of September 30, 2018 and 2017, respectively, classified in Level 3 of the fair value hierarchy were valued at the Fund's share price of $1.00.

Interest rate risk. In accordance with Metropolitan's investment policy, interest rate risk was managed by limiting the duration of the various portfolio segments. Each segment has limitations on the amount of duration exposure (see the following for specific durations).

Internally Managed Segment

This segment of the portfolio was managed against the Bank of America Merrill Lynch 3-Month Treasury Bill Index, approved by the Finance and Insurance Committee. For September 30, 2018 and 2017, the benchmark durations were 0.23 and 0.24, respectively, and the portfolio duration was permitted to vary from the duration by plus or minus 0.20. As of September 30, 2018 and 2017, Metropolitan's investments and portfolio durations for this segment were as follows:

	September 30,			
	2018		2017	
(Dollars in thousands)	**Fair value**	**Duration**	Fair value	Duration
U.S. Treasury securities	**$ 41,289**	**1.16**	$ 108,482	0.71
Federal agency securities	**127,477**	**0.02**	127,050	0.07
Prime commercial paper	**111,695**	**0.10**	219,031	0.16
Medium-term corporate notes	**50,138**	**0.10**	57,915	0.10
Negotiable certificates of deposit	**238,938**	**0.17**	232,366	0.07
Municipal bonds	**719**	**5.76**	1,475	3.58
Local Agency Investment Fund	**48,315**	**—**	33,526	—
Portfolio duration		**0.18**		0.19

Externally Managed Segment

This segment of the portfolio was managed against the Bank of America Merrill Lynch, U.S. Corporate and Government, one to five years, A-Rated and above index approved by the Finance and Insurance Committee. For September 30, 2018 and 2017, the benchmark durations were 2.62 and 2.68, respectively, and the portfolio duration was permitted to vary from the duration by plus or minus 1.50. As of September 30, 2018 and 2017, Metropolitan's investments and portfolio durations for this segment were as follows:

	September 30,			
	2018		2017	
(Dollars in thousands)	**Fair value**	**Duration**	Fair value	Duration
U.S. Treasury securities	**$ 209,648**	**2.51**	$ 216,976	2.45
U.S. Guarantees – GNMAs	**3**	**3.65**	4	4.25
Federal agency securities	**5,515**	**9.22**	6,420	9.24
Medium-term corporate notes	**67,912**	**2.67**	68,540	3.24
Shares of beneficial interest	**464**	**—**	189	—
Government-sponsored enterprise (GSE)	**63,233**	**2.33**	54,827	2.27
Portfolio duration		**2.61**		2.70

Bond Reserves and Lake Mathews Segment

Investments in the bond reserves were managed based on the requirements of each of the bond issues. The Lake Mathews trust funds were managed in a manner that preserved the principal and provided the necessary liquidity to pay its operating expenses. Per Board authorization, the Treasurer was authorized to invest these monies in excess of five years.

As of September 30, 2018 and 2017, Metropolitan’s investments and portfolio durations for this segment were as follows:

	September 30,			
	2018		2017	
(Dollars in thousands)	**Fair value**	**Duration**	Fair value	Duration
U.S. Treasury securities	**$ 16,996**	**3.08**	$ 17,245	4.09
Federal agency securities	**963**	**0.04**	250	0.03
Prime commercial paper	**—**	**—**	709	0.12
Medium-term corporate notes	**1,448**	**0.06**	1,169	0.09
Negotiable certificates of deposit	**1,039**	**0.25**	1,326	0.13
Shares of beneficial interest	**3**	**—**	1	—
Municipal bonds	**9,531**	**5.08**	20,798	5.63
Weighted average duration		**3.37**		4.53

Credit risk. Credit risk was managed by purchasing investments with the nationally recognized credit ratings specified in Metropolitan's investment policy. Additionally, the policy required monitoring the credit ratings of securities held in the portfolio, and if the securities' credit ratings were downgraded, evaluating for potential sale. For certain securities, additional requirements included consideration of net worth, length of time in business, and specified market values.

Presented in the following table is the minimum rating required, if applicable, by investment type pursuant to Metropolitan’s investment policy and State law:

Investment Type	**Minimum Rating**
U.S. Government and agencies	Not applicable.
Bankers' acceptances Prime commercial paper Negotiable certificates of deposit Time deposits	Prime quality of the highest ranking or highest letter and numerical rating ('A1', 'P1', 'F1' or higher) as provided by Moody's Investors Service, Inc., Standard & Poor's Global Ratings Services, and Fitch Ratings. Credit requirement may be waived for the maximum deposit that is insured by the Federal Deposit Insurance Corporation.
Repurchase agreements	Only with primary dealers in government securities or financial institutions with a Moody's Investors Service, Inc. or equivalent rating of 'A' or better.
Investment contracts	Not applicable. Limited to guaranteed investment contracts, or agreements collateralized with U.S. Treasury or agency securities.
Medium-term corporate notes	Rating category of at least 'A' or better, or the equivalent, by a nationally recognized rating agency.
Government-sponsored enterprise (e.g., FannieMae, FreddieMac)	Issuer's debt must be rated 'A' or higher as provided by a nationally recognized rating agency and the security must be rated in a category of 'AAA' by a nationally recognized rating agency.
Local Agency Investment Fund	Not applicable.
Shares of beneficial interest	Highest ranking of the highest letter and numerical rating provided by not less than two nationally recognized rating agencies.
California local agency securities Municipal bonds	Securities with a maturity in excess of five years must have a credit rating of at least 'AA' (may be insured) and an underlying credit rating of 'A' or better by a nationally recognized rating agency.

Metropolitan's minimum rating for government-sponsored enterprises (GSE) of 'AAA' is more restrictive than the California Government Code requirement of 'AA'.

At September 30, 2018 and 2017, Metropolitan's portfolio was invested in the following securities by rating:

		September 30,	
		2018	2017
(Dollars in thousands)	Rating	**Fair value**	Fair value
U.S. Treasury securities	N/A[1]	**$ 267,933**	$ 342,703
U.S. Guarantees – GNMAs	N/A[1]	**3**	4
Federal agency securities	AAA[2]	**133,955**	133,720
Prime commercial paper	A1/P1[3]	**111,695**	219,740
Medium-term corporate notes	A[3]	**119,498**	127,624
Negotiable certificates of deposit	F1[3]	**239,977**	233,692
Shares of beneficial interest	AAA	**467**	190
Government-sponsored enterprise (GSE)	AAA	**63,233**	54,827
Municipal bonds	A[3]	**10,250**	22,273
Local Agency Investment Fund	[4]	**48,315**	33,526
Total portfolio		**$ 995,326**	$ 1,168,299

(1) *Credit ratings are not applicable to obligations of the U.S. Government or obligations explicitly guaranteed by the U.S. Government.*
(2) *Federal Agencies are rated "AAA" by two nationally recognized rating agencies and "AA" by one nationally recognized rating agency.*
(3) *A or better e.g. F1+, A1+, AA, or AAA.*
(4) *Local Agency Investment Fund is not rated.*

Concentration of credit risk. In accordance with Metropolitan's investment policy, the minimum requirements for limiting concentration of credit risk defined the maximum percent allowable for investment in each security type as well as the percent allowable for investment by issuer per type. Generally, the maximum allowable for investment by security type varied from 20 percent, for GSE, to 100 percent for U.S. Treasury and agency securities. The percentages of investments that can be purchased by a single issuer, within each security type, ranged from 5 percent, for asset-backed securities, to 10 percent for bankers' acceptances.

The following table identifies Metropolitan's limits and the percent invested by security type based on fair value, as of September 30, 2018 and 2017.

	Investment Policy Limits	Percent of Portfolio 2018	Percent of Portfolio 2017
U.S. Treasury securities	100%	**26.92 %**	29.33 %
Federal agency securities	100%	**13.46**	11.45
Prime commercial paper	25%	**11.22**	18.81
Medium-term corporate notes	30%	**12.01**	10.92
Negotiable certificates of deposit	30%	**24.11**	20.00
Shares of beneficial interest	20%	**0.05**	0.02
Government-sponsored enterprise (GSE)	20%	**6.35**	4.69
Municipal bonds	30%	**1.03**	1.91
Local Agency Investment Fund	N/A	**4.85**	2.87
Total portfolio		**100.00 %**	100.00 %

At September 30, 2018 and 2017, Metropolitan had the following investments (obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government not listed) representing five percent or more of its investments:

(Dollars in thousands)	2018	
Federal Home Loan Bank	**$ 90,288**	**9.07 %**
Federal Home Loan Mortgage Corporation	**$ 51,558**	**5.18 %**

(Dollars in thousands)	2017	
Bank of Tokyo Mitsubishi	$ 65,666	5.62 %
Federal Home Loan Mortgage Corporation	$ 88,743	7.60 %

Custodial credit risk. At September 30, 2018 and 2017, Metropolitan's investments were insured, registered or held, in Metropolitan's name, in safekeeping at Metropolitan's bank, which was not a counterparty to the investment transactions. The exceptions were $48.3 million and $33.5 million in deposits in the California State managed LAIF as of September 30, 2018 and 2017, respectively.

The LAIF, created by California statute, is part of a pooled money investment account (PMIA). The LAIF has oversight by the Local Investment Advisory Board, which consists of five members designated by statute. The Chairman is the State Treasurer, or his designated representative.

The total amount invested by all public agencies in LAIF as of September 30, 2018 and 2017 was $20.2 billion and $20.7 billion, respectively. At September 30, 2018 and 2017, the PMIA had a balance of $88.3 billion and $74.1 billion, respectively, of which, 2.52 percent and 3.03 percent were invested in medium-term and short-term notes and asset-backed securities, respectively. The average maturity of LAIF investments as of September 30, 2018 and 2017 was 193 days and 190 days, respectively.

(c) Reverse Repurchase Agreements

Metropolitan is permitted, subject to conditions imposed by State law, to sell securities owned under written agreements and to buy back the securities on or before a specified date for a specified amount. No such reverse repurchase agreements were entered into during the fiscal years ended September 30, 2018 and 2017.

(d) Restricted Cash and Investments

Metropolitan has established a number of separate accounts, also referred to as funds, to provide for specific activities in accordance with special regulations, bond covenants, and trust arrangements. The accounts are classified as "restricted." Most restricted accounts have the minimum cash and investment balance requirements and all are nondiscretionary in terms of the use of assets. Among other things, the restricted amounts provide for payments of debt service on Metropolitan's bonds; reserves for principal and interest on outstanding bonds; payments for arbitrage tax rebate; construction of capital assets; payment of Metropolitan's operations and maintenance expenses; and payment of the costs related to the closure and postclosure maintenance of Metropolitan's solid waste landfill facility.

3. SHORT-TERM AND LONG-TERM DEBT

Metropolitan's enabling Act specifies that its indebtedness shall be limited to 15 percent of the assessed value of all taxable property within Metropolitan's service area. Existing outstanding debt of $4.390 billion and $4.753 billion at September 30, 2018 and 2017, respectively, represents less than one percent of the June 30, 2018 and 2017 total taxable assessed valuation of $2,917 billion and $2,741 billion, respectively.

Metropolitan's long-term debt consists of general obligation and revenue bond issues as well as other obligations. The general obligation bonds are secured by Metropolitan's authority to levy ad valorem property taxes. The revenue bond obligations are special limited obligations of Metropolitan and are secured by a pledge of Metropolitan's net operating revenues. Such obligations contain certain restrictive covenants, with which Metropolitan has complied. Substantially all of the bond issues contain call provisions. Substantially all of the debt proceeds have been, and are expected to continue to be, utilized to fund new facilities, improvements and betterments, and to refund outstanding bonds.

(a) Commercial Paper and Revolving Notes

Metropolitan may issue up to $200.0 million in commercial paper to fund a portion of its capital plan, as approved by Metropolitan's Board. During the twelve months ended September 30, 2018 and 2017, there was no commercial paper issued or outstanding. Metropolitan may also issue other forms of short-term debt such as revolving notes and variable rate water revenue bonds (see Note 3c).

In April 2016, Metropolitan entered into a noteholder's agreement with RBC Municipal Products, LLC ("RBC") for the purchase by RBC and sale by Metropolitan of Metropolitan's Index Notes, Series 2016 ("RBC Facility"). Also in April 2016, Metropolitan entered into a note purchase and continuing covenant agreement with U.S. Bank National Association ("US Bank"), for the purchase by US Bank and sale by Metropolitan of Metropolitan's Flexible Rate Revolving Notes, Series 2016 ("US Bank Facility," and together with the RBC Facility, the "Short-Term Revolving Credit Facilities"). Metropolitan was permitted to sell up to $200.0 million of notes under each of the Short-Term Revolving Credit Facilities for an aggregate amount of available borrowings of $400.0 million. Metropolitan may borrow, paydown and re-borrow amounts under each of the Short-Term Revolving Credit Facilities. Each of the Short-Term Revolving Credit Facilities bears interest at a variable rate of interest. The US Bank Facility resulted in interest at a basis point spread to one-month London interbank offering rate (LIBOR) for taxable borrowings or to

70 percent of one-month LIBOR for tax-exempt borrowings through December 17, 2017 and starting December 18, 2017 at a spread to the SIFMA Municipal Swap Index, while the RBC Facility bears interest at a spread to one-month LIBOR for taxable borrowings or to the SIFMA Municipal Swap Index for tax-exempt borrowings. Under the Short-Term Revolving Credit Facilities, upon a failure by Metropolitan to perform or observe its covenants, a default in other specified indebtedness of Metropolitan, or other specified events of default, each bank could terminate its commitments and declare all amounts then outstanding to be immediately due and payable. Metropolitan has secured its obligation to pay principal and interest under the Short-Term Credit Facilities as Senior Parity Obligations.

Short-term notes issued and refunded during the twelve months ended September 30, 2018 were as follows:

- On November 1, 2017, Metropolitan prepaid the $250.0 million Short-Term Revolving Credit Facilities notes issued in April 2017.

- In December 2017, Metropolitan sold $198.3 million of notes under the US Bank facility, which was paid down in June 2018.

  On June 27, 2018, Metropolitan terminated the US Bank Short-Term Revolving Credit Facility.

Short-term notes issued and refunded during the twelve months ended September 30, 2017 were as follows:

- On April 3, 2017, Metropolitan sold $250.0 million of notes under the Short-Term Revolving Credit Facilities, $125.0 million Taxable Flexible Rate Refunding Notes, Series A-1 and $125.0 million Taxable and Refunding Subseries 2017 Series B-1 Notes, to refund the notes outstanding as of fiscal year ended June 30, 2016 of $250.0 million. The $125.0 million note issued in 2017 under the RBC Facility had a maturity date of April 5, 2020 and the $125.0 million note issued in 2017 under the US Bank Facility had a maturity date of April 5, 2019.

  The Short-Term Revolving Credit Facilities requires RBC to purchase refunding notes, subject to certain terms and conditions, through the RBC Facilities expiration date of April 5, 2019. The maturity date of April 5, 2020 for the RBC Note will only be effective if RBC agrees, at its option, to extend the expiration of its Credit Facility to April 5, 2020.

- On June 1, 2017, Metropolitan sold $12.3 million of notes under the US Bank Facility, to refund $12.3 million of Special Variable Rate Water Revenue Refunding Bonds, 2013 Series E. These notes were refunded on July 3, 2017.

Long-term notes issued during the twelve months ended September 30, 2018 were as follows:

- On August 1, 2018, Metropolitan entered into a Note Purchase and Continuing Covenant Agreement with Bank of America, N.A. (BANA, and the 2018 BANA Agreement), for the purchase by BANA and sale by Metropolitan of up to $86.0 million of Metropolitan's Short-Term Revenue Certificates, 2018 Series A (the "Series 2018 Notes"). Proceeds were used to provide advances or contributions of money to pay for costs related to the California WaterFix. The Series 2018 Notes will bear interest at a variable rate of interest, at a spread to one-month LIBOR. Under the 2018 BANA Agreement, upon a failure by Metropolitan to perform or observe its covenants, a default in other specified indebtedness of Metropolitan, or other specified events of default, BANA could terminate its commitments and declare all amounts then outstanding to be immediately due and payable. Metropolitan has secured its obligation to pay principal and interest under the 2018 BANA Agreement as a Subordinate Lien Parity Obligation.

  The Series 2018 Notes are subject to mandatory tender for purchase on the scheduled mandatory tender date of July 31, 2020, or, if directed by BANA upon the occurrence and continuance of an event of default under the 2016 BANA Agreement, five business days after receipt of such direction. As of September 30, 2018, there were $15.6 million of Series 2018 Notes outstanding.

(b) General Obligation Bonds

In 1966, voters authorized Metropolitan to incur up to $850.0 million of general obligation bond indebtedness to finance a portion of Metropolitan's capital plan. The original amounts, issued as Series A through H under the 1966 authorization, totaled $850.0 million at September 30, 2018 and 2017. Metropolitan has refunded a portion of these general obligation bond issues through the issuance of refunding bonds. A total of $60.6 million and $74.9 million in general obligation bonds and general obligation refunding bonds were outstanding at September 30, 2018 and 2017, respectively.

The general obligation and general obligation refunding bond issues include both serial and term bonds that mature in varying amounts through March 2037 at interest rates ranging from 3.5 percent to 5.0 percent. The term bonds are subject to mandatory redemption prior to maturity. All general obligation bonds maturing on or after the earliest applicable call date are subject to optional redemption prior to maturity, callable on interest payment dates, and subject to early redemption.

No general obligation bonds were issued during the twelve months ended September 30, 2018 and 2017.

(c) Revenue Bonds

Pursuant to a 1974 voter authorization, additional funds, primarily for funding the capital investment plan, are obtained through the sale of water revenue bonds. Revenue bonds may be issued subject to certain conditions, including a requirement that the total of revenue bonds outstanding does not exceed the equity (net position) of Metropolitan as of the fiscal year end prior to such issuance. Metropolitan has refunded some of these revenue bonds through the issuance of refunding bonds. A total of $4.110 billion and $4.215 billion of revenue bonds and revenue refunding bonds were outstanding at September 30, 2018 and 2017, respectively.

Each fixed rate revenue and revenue refunding bond issue consists of either serial or term bonds or both that mature in varying amounts through July 2047 at interest rates ranging from 2.25 percent to 6.95 percent. The term bonds are subject to mandatory redemption prior to maturity. Substantially all revenue bonds maturing on or after the earliest applicable call date are subject to optional redemption prior to maturity, callable on any interest payment dates, and subject to early redemption.

Revenue bonds issued during the fiscal year ended September 30, 2018 were as follows:

- On June 28, 2018, Metropolitan issued $64.3 million of Subordinate Water Revenue Bonds, 2018 Series B, to finance a portion of Metropolitan's capital expenditures. The maturities extend to September 1, 2028 and are not subject to optional and mandatory redemption provisions.

Revenue bond issued during the fiscal year ended September 30, 2017 was as follows:

- On December 20, 2016, Metropolitan entered into a Continuing Covenant Agreement with Bank of America, N.A. (BANA, and the 2016 BANA Agreement), for the purchase by BANA and sale by Metropolitan of Metropolitan's $175.0 million Subordinate Water Revenue Bonds, 2016 Authorization Series A (the Subordinate 2016 Series A Bonds), which is the first series of bonds issued under the Subordinate Debt Resolution. Proceeds were used to reimburse Metropolitan for the purchase of the Delta Wetlands Properties in the San Francisco Bay\Sacramento-San Joaquin River Delta that was funded from Metropolitan's reserves in July 2016. The Subordinate 2016 Series A Bonds are Index Tender Bonds and bear interest at a variable rate of interest, at a spread to one-month LIBOR. Under the 2016 BANA Agreement, upon a failure by Metropolitan to perform or observe its covenants, a default in other specified indebtedness of Metropolitan, or other specified events of default, BANA could terminate its commitments and declare all amounts then outstanding to be immediately due and payable. Metropolitan has secured its obligation to pay principal and interest under the 2016 BANA Agreement as a Subordinate Lien Parity Obligation.

  On June 25, 2018, the 2016 BANA Agreement and the related Paying Agent Agreement were amended, and, among other changes, the scheduled mandatory tender was amended to December 21, 2020.

  The Subordinate 2016 Series A Bonds are subject to mandatory tender for purchase on the scheduled mandatory tender date of December 21, 2018, or, if directed by BANA upon the occurrence and continuance of an event of default under the 2016 BANA Agreement, five business days after receipt of such direction.

- On March 1, 2017, Metropolitan issued $80.0 million of Water Revenue Bonds, 2017 Authorization Series A, at variable rates, to finance a portion of Metropolitan's capital expenditures. The maturities extend to July 1, 2047 and are subject to optional and mandatory redemption provisions.

(d) Bond Refundings and Defeasances

Metropolitan has issued Waterworks General Obligation Refunding Bonds, Water Revenue Refunding Bonds, Special Variable Rate Water Revenue Refunding Bonds, and short-term notes to refund various issues of Waterworks General Obligation Bonds, Waterworks General Obligation Refunding Bonds, Water Revenue Bonds, Water Revenue Refunding Bonds, Special Variable Rate Water Revenue Refunding Bonds, and revolving notes previously issued. The net proceeds from these sales were used to redeem the refunded bonds and fund certain swap termination payments or to purchase U.S. Treasury securities that were deposited in irrevocable escrow trust accounts with a bank acting as an independent fiscal agent to provide for all future debt service on the bonds being refunded. As a result, those bonds are considered defeased and the related liabilities have been excluded from Metropolitan's basic financial statements.

(e) Interest Rate Swaps

Metropolitan has eight outstanding interest rate swap agreements as of September 30, 2018. These agreements require that Metropolitan pay fixed interest rates and receive interest at variable interest rates which are Metropolitan's hedging derivative instruments.

Pay-Fixed, Receive-Variable

Objective of the Swaps: In order to take advantage of low interest rates in the marketplace, Metropolitan entered into eight separate pay-fixed, receive-variable interest rate swaps at costs that were less than what Metropolitan otherwise would have paid to issue fixed rate debt in the tax-exempt municipal bond market.

Terms: The notional amounts of the swaps match the principal amounts of the associated debt in total. Metropolitan's swap agreements contain scheduled reductions to outstanding notional amounts that are expected to approximately follow scheduled or anticipated reductions in the associated long-term debt.

Fair Values: At September 30, 2018, all pay-fixed, receive-variable swaps had a negative fair value. Because the coupons on Metropolitan's variable rate bonds adjust to changing interest rates, the bonds do not have corresponding fair value changes. The fair values of the swaps were estimated using the zero-coupon method and exclude accrued interest. This method calculates the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the date of each future net settlement on the swaps.

Credit Risks: As of September 30, 2018, Metropolitan was not exposed to credit risk on the outstanding pay-fixed, receive-variable swaps that had negative fair values. However, should interest rates change and the fair values of the swaps become positive, Metropolitan would be exposed to credit risk to each swap counterparty in the amount of the derivatives' fair value. Should the counterparties to the transactions fail to perform according to the terms of the swap contract, Metropolitan would face a maximum possible loss equal to the fair value of these swaps.

All swap agreements contain specific collateral requirements that are in effect for Metropolitan and the counterparties. The swaps require different collateral levels based on credit ratings and the fair value of the swap. Generally, the fair value threshold levels are also reduced as the credit ratings are reduced. Collateral on all swaps is to be in the form of U.S. government securities that may be held by the party posting the collateral. Metropolitan had no posted collateral as of September 30, 2018.

Each swap contains cross-default provisions that allow the nondefaulting party to accelerate and terminate all outstanding transactions and to net the transactions' fair values into a single sum to be owed by, or owed to, the nondefaulting party.

As of September 30, 2018, Metropolitan has pay-fixed, receive-variable swap transactions with one counterparty in the amount of $216.0 million or 43.8 percent of the notional amount of Metropolitan's outstanding pay-fixed, receive-variable swap transactions. This counterparty is rated Aa3/A+/AA- by Moody's, Standard & Poor's Global, and Fitch Ratings, respectively.

Basis Risk: The interest rates on Metropolitan's variable rate bonds are expected to be equivalent, but not necessarily equal to the variable rate payments received from counterparties on pay-fixed, receive-variable interest rate swaps. To the extent these variable payments differ, Metropolitan is exposed to basis risk. When the rates received from the counterparties are less than the rates on variable rate bonds associated with the respective swap transactions there is a basis loss. When the rates received from the counterparties are greater than the rates on variable rate bonds associated with the respective swap transactions there is a basis gain. As of September 30, 2018, the interest rates of the variable rate debt associated with these swap transactions range from 1.10 percent to 2.58 percent. Metropolitan's variable rate payments received from the counterparties of these swaps ranged from 1.31 percent to 1.68 percent.

Termination Risk: Metropolitan may terminate any of the swaps if the other party fails to perform under the terms of the swap agreements. If any of the swaps are terminated, the associated variable rate bonds would no longer carry a synthetic fixed interest rate. Also, if at the time of termination the swap has a negative fair value, Metropolitan would be liable to the counterparty for a payment equal to the swap's fair value.

Tax Risk: As with other forms of variable rate exposure and the relationship between the taxable and tax-exempt markets, Metropolitan is exposed to tax risk should tax-exempt interest rates on variable rate debt issued in conjunction with the swaps rise faster than taxable interest rates received by the swap counterparties, due particularly to reduced federal or state income tax rates, over the term of the swap agreement.

(f) Variable Rate Bonds

The variable rate bonds bear interest at daily and weekly rates ranging from 1.10 percent to 2.58 percent as of September 30, 2018 and 0.86 percent to 1.62 percent as of September 30, 2017. Metropolitan can elect to change the interest rate period of the bonds with certain limitations. For the Water Revenue Bonds, 2000 Series B-3, Special Variable Water Revenue Refunding Bonds, 2016 Series B-1 and B-2, Water Revenue Bonds, 2017 Series A and Special Variable Water Revenue Refunding Bonds, 2018 Series A-1 and A-2, bondholders have the right to tender bonds to the paying agent on any business day with same day notice. The current terms of the Subordinate Water Revenue Refunding Bonds, 2017 Series D and Series E (SIFMA Index Mode), the Subordinate Water Revenue Bonds, 2017 Series C (SIFMA Index Mode), provide bondholders a right to tender bonds to the paying agent every 397 days. Metropolitan has entered into standby bond purchase agreements (SBPA) with commercial banks to provide liquidity for six and four separate variable rate bond issues in the amount of $482.5 million and $272.5 million as of September 30, 2018 and 2017, respectively. In addition, Metropolitan has eight and twelve series of variable rate bonds in the amounts of $761.1 million and $959.3 million as of September 30, 2018 and 2017, respectively that are not supported by an SBPA.

The Bank Bonds that would be issued under the SBPA would bear interest that is payable at a rate, depending on the agreement, that is LIBOR plus 7.50 percent; the "base rate", which is higher of the Fed Funds Rate plus 2.0 percent per annum, the Prime Rate plus 1.0 percent per annum, plus a spread of 7.0 percent, plus one percent; the "base rate" which is the higher of the Fed Funds Rate plus 2.0 percent per annum, the Prime Rate plus 1.0 percent per annum, or 7.0 percent. The principal of the Bank Bonds would be payable, depending on the agreement, either ten equal semi-annual installments commencing 180 days after purchase by the bank, or in two equal semi-annual installments commencing six months after purchase by the bank.

The $103.7 million 2016 Series B-1 and B-2 bonds have SBPAs that expire on September 19, 2019, the $80.0 million Water Revenue Bonds, 2017 Authorization, Series A, and the $88.8 million 2000 Series B-3, Water Revenue Bonds, have SBPAs that expire on March 27, 2020, and the $210.0 million Special Variable Rate Water Revenue Refunding Bonds, 2018 Series A-1 and A-2 have SBPAs that expire on June 25, 2021. According to the provisions of the Paying Agent Agreement for the bonds, the Paying Agent will draw on the SBPA two business days prior to the SBPA expiration to redeem all outstanding bonds.

The six and four separate variable-rate bonds supported by SBPAs at September 30, 2018 and 2017, respectively, have been classified as long term in the statements of net position, as the liquidity facilities give Metropolitan the ability to refinance on a long-term basis and Metropolitan intends to either renew the facility or exercise its right to tender the debt as a long-term financing. The portion that would be due in the next fiscal year in the event that the outstanding variable rate bonds were tendered and purchased by the commercial banks under the standby agreements was $129.8 million and $94.8 million at September 30, 2018 and 2017, respectively.

For three series of variable rate bonds not supported by SBPA, the Subordinate Water Revenue Bonds, 2017 Series C and Subordinate Water Revenue Refunding Bonds, 2017 Series D and 2017 Series E in the amount of $271.3 million, if the purchase price is not paid from the proceeds of remarketing or other funds, for a period of five business days following written notice by any Owner of such bonds, will constitute an event of default under the Subordinate Debt Resolutions, upon the occurrence and continuance of which the owners of 25 percent in aggregate principal amount of the Subordinate Revenue Bonds then outstanding may elect a bondholders' committee to exercise rights and powers of such owners under the Subordinate Debt Resolutions, including the right to declare the entire unpaid principal of the Subordinate Revenue Bonds then outstanding to be immediately due and payable.

The outstanding self-liquidity variable rate bonds that were not supported by a SBPA were the $87.4 million, 2013 Series D, Special Variable Rate Water Revenue Refunding Bonds, the $38.5 million, 2014 Series D, Special Variable Rate Water Revenue Refunding Bonds, and the $188.9 million, 2015 Series A-1 and A-2, Special Variable Rate Water Revenue Refunding Bonds. These variable rate bonds outstanding at September 30, 2018 and 2017 had no long-term take out provisions therefore, the entire principal amount of $314.8 million, may be tendered for purchase upon one week's notice from bondholders. However, on June 25, 2018, Metropolitan entered into a Revolving Credit Agreement (RCA), by which Metropolitan may borrow up to $200.0 million, to pay the purchase price (principal and accrued interest) of any self-liquidity bonds tendered for purchase. The RCA permits repayment of any borrowed funds over ten semi-annual installments beginning 180 days after the funds are borrowed. The RCA has a stated expiration date of June 23, 2023. This RCA replaced the agreement that expired in June 2018, by which Metropolitan may borrow up to $180.0 million. As a result of the RCAs, $114.8 million and $134.8 million were reported as current liabilities as of September 30, 2018 and September 30, 2017, respectively.

4. PENSION PLAN

(a) General Information about the Pension Plan

Plan Description

All full-time Metropolitan employees are required to participate in Metropolitan's Miscellaneous Plan with CalPERS, an agent multiple-employer public employee defined benefit pension plan. CalPERS acts as a common investment and administrative agent for participating public entities within the State of California. A menu of benefit provisions as well as other requirements is established by State statutes within the Public Employee's Retirement Law. Metropolitan selects optional benefit provisions from the benefit menu by contract with CalPERS and adopts those benefits through Board approval. CalPERS issues a separate comprehensive annual report. Copies of CalPERS' annual financial report may be obtained from its Executive Office, 400 Q Street, Sacramento, CA 95811.

Benefits Provided

CalPERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefits are based on years of credited service, equal to one year of full-time employment. Employees hired prior to January 1, 2013 (Classic members) with five years of total service are eligible to retire at age 50 with statutorily reduced benefits; employees hired after January 1, 2013 (PEPRA members) with at least five years of credited service are eligible to retire at age 52 with statutorily reduced benefits. All members are eligible for improved non-industrial disability benefits after five years of service. The death benefit is one of the following: the Basic Death Benefit, the 1959 Survivor Benefit, or the Optional Settlement 2W Death Benefit.

5. POSTEMPLOYMENT BENEFITS OTHER THAN PENSIONS (OPEB)

(a) Plan Description and Benefits Provided

Through CalPERS, Metropolitan offers medical insurance to active and retired employees, as well as their qualified dependents under the Public Employees' Medical and Hospital Care Act (PEMHCA). Under PEMHCA, health coverage for the employee continues into retirement. Current plans offered are PERS Care PPO, PERS Choice PPO, PERS Select PPO, Blue Shield HMO, and Kaiser HMO. Metropolitan participates in the CalPERS California Employers' Retiree Trust (CERBT) Fund, which is an agent multiple-employer plan available to employers to pre-fund OPEB benefits. Benefit provisions are established through negotiations between Metropolitan and its various bargaining units, which also apply to retirees. For employees hired on or after January 1, 2012, retirees must have a minimum of 10 years of PERS service and no less than five years of Metropolitan service in order to receive post-employment health benefits in accordance with PERS as per Government Code Section 22893. For employees hired prior to January 1, 2012, retirees are not required to meet the eligibility criteria. CalPERS issues a separate comprehensive annual report that includes financial statements for its CERBT Fund. Copies of CalPERS' annual financial report may be obtained from its Executive Office, 400 Q Street, Sacramento, CA 95811.

(b) Funding Policy and Contributions

Contribution requirements are established by Memorandum of Understandings negotiated between Metropolitan and its various bargaining units. During fiscal year 2018, Metropolitan contributed up to 100 percent of Blue Shield Access + HMO Bay area regional basic plan rate for represented retirees and up to 90 percent of the PERS Care PPO Los Angeles regional basic plan rate for unrepresented retirees. During fiscal years 2019 and 2018, Metropolitan contributed, net of participant contributions as determined by CalPERS, the full actuarially determined contribution rate of 13.8 percent or $27.3 million and 15.2 percent or $30.1 million, respectively. Employees are not required to contribute to the plan.

6. COMMITMENTS AND CONTINGENCIES

(a) State Water Contract (see Note 7)

Estimates of Metropolitan's share of the projected fixed costs of the State Water Project (SWP) are provided annually by the State. The estimates are subject to future increases or decreases resulting from changes in planned facilities, refinements in cost estimates, and inflation. During the next five years, payments under the State Water Contract, exclusive of variable power costs, are currently estimated by the State to be as follows:

(Dollars in thousands)	State Water Contract Payments
Year ending June 30:	
2019	$ 407,410
2020	420,264
2021	448,024
2022	449,645
2023	450,968

Metropolitan intends to exercise its option to extend its agreement with the State through 2085, which will result in annual minimum operations and maintenance costs through 2085. In addition, the amounts shown above do not contain any escalation for inflation, are subject to significant variation over time because the amounts are based on a number of assumptions, and are contingent on future events. None of the estimated long-term commitments are recorded as liabilities in the accompanying basic financial statements.

(b) Bay/Delta Regulatory and Planning Activities

The State Water Resources Control Board (State Board) is the agency responsible for setting water quality standards and administering water rights throughout California. Decisions of the State Board can affect the availability of water to Metropolitan and other water users throughout California. The State Board exercises its regulatory authority over Bay/Delta watershed supplies by means of public proceedings leading to regulations and decisions.

In September 2006, then Governor Schwarzenegger established a Delta Vision Process to identify a strategy for managing the Delta as a sustainable resource. The process was tied to legislation that created a Blue Ribbon Task Force (BRTF) and cabinet-level committee (Delta Vision Committee) tasked with developing a durable vision for sustainable management of the Delta over the long-term which addressed a full array of issues, including land use, infrastructure, flood protection, and natural resources including water supply. The BRTF released its final Delta Vision Strategic Plan in October 2008 and a final implementation report was submitted to the Governor in January 2009. Subsequently, the Delta Reform Act of 2009 was enacted, which created the Delta Stewardship Council (DSC), a seven member appointed body charged with developing a Delta Plan to support carrying out the Delta Vision, which the DSC completed on September 1, 2013. The Delta Plan anticipated the need for periodic reviews and updates in response to changing circumstances and conditions in the Delta. The DSC amended the Delta Plan in February 2016 to include an initial set of performance measures in September 2016 to exempt single-year water transfers from consideration as covered actions. DSC adopted three amendments to the Delta Plan in April 2018, including Chapter 3 updating the section on Conveyance, Storage and Operations, Chapter 7 updating the section on the Delta Levee Investment Strategy and Appendix E updating performance measures. Chapter 4 of the Delta Plan which directs agencies to restore aquatic habitat and improve water quality while respecting local land uses and expanding opportunities for nature-based recreation and tourism is also going through a public process of refining and amending the Delta Plan. DSC is working with partner agencies, stakeholders, and the public on this process which is expected to last through early 2019.

The Bay Delta Conservation Plan (BDCP), which began in 2007, is a voluntary collaboration of state, federal, and local water agencies, state and federal fish agencies, environmental organizations, and other interested parties to provide a comprehensive habitat conservation and restoration program for the Delta. In addition, the BDCP would provide the basis for permits under federal and state endangered species laws for activities covered by the plan based on the best available science, identified sources of funding, and an adaptive management and monitoring program. On April 30, 2015, the state announced its intent to include new alternatives separating the conveyance facilities and habitat restoration measures into two separate permitting efforts namely: California WaterFix and California EcoRestore. Under the California WaterFix, the new water conveyance facilities with proposed design changes would be constructed and operated. With the California EcoRestore, the focus would be on environmental restoration programs. On October 10, 2017 the Board took action to support Metropolitan's participation in California WaterFix for 25.9 percent share of the 9,000 per second (cfs) facility. On July 10, 2018, Metropolitan's Board approved the increased financial support for the unsubscribed portion of the project up to 64.6 percent or approximately $10.8 billion of total project costs estimated to be $16.7 billion. Since then, two new public joint powers authorities have been formed to aid in the implementation of California WaterFix—Delta Conveyance Design and Construction Authority (DCA) and Delta Conveyance Finance Authority (Finance Authority). At its inaugural meeting, DCA approved and signed an agreement with the California Department of Water Resources (DWR) delineating their joint partnership to construct the California WaterFix project.

(c) Imperial Irrigation District

As of September 30, 2018, Metropolitan had advanced to the Imperial Irrigation District (IID) a total of $330.3 million for construction costs, operations and maintenance costs, and indirect costs of the conservation projects. Metropolitan remains obligated to pay IID for actual operation and maintenance costs for the remainder of this agreement through at least 2041. In return, Metropolitan will receive 85,000-105,000 acre-feet in 2018 and annually thereafter depending upon the amount used by the Coachella Valley Water District. A total of at least 85,000 and 105,000 acre-feet will be/was available in calendar years 2018 and 2017, respectively, for diversion by Metropolitan.

(d) Sale of Water by the Imperial Irrigation District to San Diego County Water Authority

In April 1998, the San Diego County Water Authority (SDCWA) and IID executed an agreement (Transfer Agreement) for SDCWA's purchase from IID of Colorado River water that is conserved within IID. SDCWA is a Metropolitan member agency and one of the largest water purchasers from Metropolitan. In October 2003 the Transfer Agreement was revised as part of the Quantification Settlement Agreement (QSA) (see Note 6e). The amended Transfer Agreement sets the maximum transfer amount at 205,000 acre-feet in 2021, with the transfer gradually ramping up to that amount over an approximately twenty-year period, stabilizing at 200,000 acre-feet per year beginning in 2023. In addition, specific programs under the QSA and related agreements include lining portions of the All-American and Coachella Canals, which were completed in 2009 and conserve over 95,000 acre-feet annually. Metropolitan receives this water and delivers over 79,000 acre-feet of exchange water annually to the San Diego County Water Authority ("SDCWA").

No facilities exist to provide for delivery of conserved water acquired by SDCWA from IIF and water allocated to SDCWA that has been conserved as a result of the lining of the All-American and Coachella Canals. In 2003, the boards of directors of Metropolitan and SDCWA authorized execution of an exchange contract (the Exchange Agreement), pursuant to which SDCWA makes available to Metropolitan at its intake at Lake Havasu on the Colorado River the conserved Colorado River water. Metropolitan delivers an equal volume of water from its own sources of supply through portions of its delivery system to SDCWA. The deliveries to both Metropolitan and SDCWA are deemed to be made in equal monthly increments. In consideration for the conserved water made available to Metropolitan by SDCWA, a lower price is paid by SDCWA for the Exchange Agreement water delivered by Metropolitan. The price payable by SDCWA is calculated using the charges set by Metropolitan's Board from time to time to be paid by its member agencies for the conveyance of water through Metropolitan's facilities (see Note 1c). SDCWA has challenged the validity of Metropolitan's charges for conveyance of water that became effective January 1, 2011 and January 1, 2012, in San Diego County Water Authority v. Metropolitan Water District of Southern California; et al. On June 8, 2012, SDCWA filed a new lawsuit challenging the rates adopted by Metropolitan's Board on April 10, 2012 and effective on January 1, 2013 and January 1, 2014 (see Note 6h). On May 30, 2014, SDCWA filed a lawsuit challenging the rates adopted by Metropolitan's Board on April 8, 2014 and effective on January 1, 2015 and January 1, 2016. On April 13, 2016, SDCWA filed a new lawsuit challenging the rates and charges adopted by Metropolitan's Board on April 12, 2016 and effective on January 1, 2017 and January 1, 2018. On June 8, 2018, SDCWA filed a new lawsuit challenging the rates and charges adopted by Metropolitan's Board on April 10, 2018 and effective on January 1, 2019 and January 1, 2020. The Exchange Agreement requires Metropolitan to pay the disputed portion of the amount paid by SDCWA under the Exchange Agreement and interest thereon to SDCWA, if SDCWA prevails in a dispute over the price payable by SDCWA under the Exchange Agreement. See Claims and Litigation below.

(e) Quantification Settlement Agreement

The Quantification Settlement Agreement (QSA) is part of the California Plan, which is a plan to reduce California's use of Colorado River water to its basic apportionment of 4.4 million acre-feet per year when necessary through water conservation, transfers from higher priority agricultural users to Metropolitan's service area, and storage programs. The QSA was executed in October 2003 and establishes Colorado River water use limits for IID and the Coachella Valley Water District (CVWD). It also provides for specific acquisitions of conserved water and water supply arrangements for up to 75 years and restores the opportunity for Metropolitan to receive any special surplus water.

(f) Abandoned Off-Aqueduct Power Facilities

DWR financed the construction of certain off-aqueduct power facilities in order to provide power for water transportation purposes for the State Water Project system. Two geothermal facilities were abandoned by DWR due to insufficient steam supply to operate the plants at their planned capacities. As a result of these actions by DWR, Metropolitan recorded losses of $204.1 million in prior fiscal years. The State relieved Metropolitan of its obligation during the fiscal year ended June 30, 2018.

(g) Construction Programs and Contracts

The estimated cost, excluding contingencies, of Metropolitan's capital program for fiscal years 2019 through 2023 totals approximately $1.41 billion. However, due to various uncertainties such as lower than anticipated construction bids, permitting delays and facility shutdowns constraints, anticipated expenditures are forecasted at $200.0 million per year for the next 2 years and $250.0 million per year in fiscal years 2021 through 2023.

Over the next three years, Capital Investment Plan spending totals approximately $797.0 million with over $650.0 million targeted for major efforts such as seismic retrofits and mechanical and electrical refurbishments to major components of the Colorado River Aqueduct and Metropolitan's water treatment plants, rehabilitation through relining of the Prestressed Concrete Cylinder Pipe portions of the Allen McColloch and Rialto Pipelines, and Calabasas, Second Lower, and Sepulveda feeders, replacement/upgrade to the Supervisory Control and Data Acquisition (SCADA) system, and the Los Angeles headquarters building seismic and security upgrades.

With the completion of all major construction under the Oxidation Retrofit Program, estimated capital costs for new facilities and/or improvements that may be required to meet current water quality standards over the next 3 years are $3.3 million (see Note 6i).

(h) Claims and Litigation

SDCWA filed San Diego County Water Authority v. Metropolitan Water District of Southern California, et al. on June 11, 2010. The complaint alleges that the rates adopted by the Board on April 13, 2010, which became effective January 1, 2011 and January 1, 2012, misallocate certain State Water Contract costs to the System Access Rate and the System Power Rate, and thus affect charges for transportation of water, resulting in an overcharge to SDCWA by at least $24.5 million per year. The complaint alleges that all State Water Project costs should be allocated instead to Metropolitan's Supply Rate, even though under the State Water Contract Metropolitan is billed separately for transportation, power and supply costs. It states additionally that Metropolitan will overcharge SDCWA by another $5.4 million per year by including the Water Stewardship Rate in transportation charges.

The complaint requested a court order invalidating the rates adopted April 13, 2010, and that Metropolitan be mandated to allocate costs associated with the State Water Contract and the Water Stewardship Rate to water supply rates and not to transportation rates. Rates in effect in prior years are not challenged in this lawsuit.

SDCWA filed its First Amended Petition for Writ of Mandate and Complaint on October 27, 2011, adding five new claims to this litigation, two of which were eliminated from the case on January 4, 2012. The three remaining new claims were for breach of the Exchange Agreement between Metropolitan and SDCWA (see Note 6d) due to a price based on allegedly illegal rates; improper exclusion of SDCWA's payments under this Exchange Agreement from calculation of SDCWA's preferential rights to purchase Metropolitan supplies and illegality of a "rate structure integrity" provision in conservation and local resources incentive agreements between Metropolitan and SDCWA. The rate structure integrity provision permitted the Board to terminate incentives payable under conservation and local resources incentive agreements between Metropolitan and a member agency due to certain actions by the member agency to challenge the rates that are the source of incentive payments. In June 2011, Metropolitan's Board authorized termination of two incentive agreements with SDCWA under the rate structure integrity provision in such agreements after SDCWA filed its initial complaint challenging Metropolitan's rates. SDCWA filed a Second Amended Petition for Writ of Mandate and Complaint on April 17, 2012, which contained additional allegations but no new causes of action.

On June 8, 2012, SDCWA filed a new lawsuit challenging the rates adopted by Metropolitan on April 10, 2012 and effective on January 1, 2013 and January 1, 2014. The complaint contained allegations similar to those in the Second Amended Petition for Writ of Mandate and Complaint and new allegations asserting Metropolitan's rates, adopted in April 2012, violate Proposition 26.

SDCWA filed a Third Amended Petition for Writ of Mandate and Complaint on January 23, 2013, to add new allegations that Metropolitan's rates adopted in April 2010 did not meet the requirements of Proposition 26. The court granted Metropolitan's motion to strike allegations relating to Proposition 26 on March 29, 2013, expressly ruling that SDCWA may not allege a violation of Proposition 26 in its challenge to the rates adopted in April 2010. This ruling did not affect SDCWA's separate challenge to Metropolitan's rates adopted in April 2012, which also includes Proposition 26 allegations.

Following trial of both lawsuits in two phases, concluding on January 23, 2014 and April 30, 2015, respectively, the Superior Court of the State of California, County of San Francisco (the "Superior Court"), issued its Final Judgment and a Peremptory Writ of Mandate in the 2010 and 2012 SDCWA v. Metropolitan cases. Metropolitan appealed the trial court's decision in each case, and SDCWA filed a cross-appeal of the court's ruling on the rate structure integrity claim and an attorneys' fees order.

On June 21, 2017, the California Court of Appeal released its decision in the appeals and cross-appeal filed by Metropolitan and SDCWA, respectively. The Court of Appeal ruled that Metropolitan may lawfully include its State Water Project transportation costs in the System Access Rate and System Power Rate that are part of the Exchange Agreement's price term, and may also lawfully include the System Access Rate in the wheeling rate, reversing the trial court decision on this issue. The Court held Metropolitan's allocation of the State Water Project transportation costs as its own transportation costs is proper and does not violate the wheeling statutes (Water Code, § 1810, et seq.), Proposition 26 (Cal. Const., art. XIII C, §1, subd. (e)), Government Code section 54999.7, the common law, or the terms of the parties' Exchange Agreement.

The Court of Appeal also ruled that the administrative record before it for the rates in calendar years 2011 through 2014 did not support Metropolitan's inclusion of its Water Stewardship Rate as a transportation cost in the Exchange Agreement price or the wheeling rate, under the common law and wheeling statutes. Having made that determination, the Court of Appeal stated it need not evaluate the issue under any other law. The court did not address the allocation of the Water Stewardship Rate in subsequent years based on a different record. The court noted, and in a subsequent modification confirmed, that its holding does not preclude Metropolitan from including the Water Stewardship Rate in Metropolitan's full service rate.

The Court of Appeal held that because the Water Stewardship Rate was included in the Exchange Agreement price, there was a breach by Metropolitan of the Exchange Agreement in 2011 through 2014. The Court of Appeal remanded the case to the trial court for a redetermination of damages in light of its ruling concerning the Water Stewardship Rate. The Court of Appeal agreed with the trial court that statutory prejudgment interest applies with respect to any damages award, not a lesser contractual interest. The court reversed the trial court by finding that the Exchange Agreement may entitle SDCWA to attorneys' fees for the second phase of the case concerning breach of contract, but directed the trial court on remand to make a new determination of the prevailing party, if any. The cases were therefore remanded to the trial court for a review of both damages and attorneys' fees.

With respect to other issues considered on appeal, the Court of Appeal upheld the trial court's ruling that Metropolitan improperly excludes SDCWA's payments under the Exchange Agreement in Metropolitan's calculation of SDCWA's preferential rights. The court also ruled that SDCWA had the constitutional right to challenge the rate structure integrity provision in Metropolitan's conservation and local resources incentive agreements, and found that the rate structure integrity provision was invalid and unenforceable as an unconstitutional condition on the provision of a public benefit.

On September 27, 2017, the California Supreme Court denied SDCWA's petition for review, declining to consider the Court of Appeal's decision. The Court of Appeal's decision is therefore final.

On July 25, 2018, the Superior Court issued an order regarding the scope of the matters to be reconsidered by the Superior Court on remand pursuant to the Court of Appeal decision. With respect to the Superior Court's re-determination of damages in light of the Court of Appeal's ruling that the administrative record for calendar years 2011 through 2014 did not support Metropolitan's inclusion of its demand management costs in the Exchange Agreement price, the Superior Court ruled that it will award SDCWA $28,678,190.90 in contract damages for breach of the Exchange Agreement, plus prejudgment interest at 10 percent per annum. The Superior Court determined that Metropolitan is not entitled in the remand proceedings to show what it could have lawfully charged SDCWA for demand management costs and to deduct that from SDCWA's damages.

The Superior Court further ruled that SDCWA is not entitled in the remand proceedings to litigate the issue of "offsetting benefits" under the wheeling statutes for the parties' Exchange Agreement. The Superior Court found that such claim is both outside the scope of remand and waived.

The Superior Court also ruled that SDCWA is entitled to judgment on its declaratory relief cause of action declaring the rate structure integrity provision in Metropolitan's conservation and local resources incentive agreements invalid and unenforceable, SDCWA is entitled to further proceedings to litigate the issue of an entitlement to monetary restitution for 2011 through 2014, and the parties shall also litigate in further proceedings the issue of what prospective relief SDCWA may be entitled to in connection with this cause of action.

Finally, the Superior Court confirmed, as the parties agreed, that it will conduct further proceedings for a redetermination of the prevailing party and attorneys' fees in this matter.

On September 14, 2018, Metropolitan filed a Petition for Writ of Mandate with the California Court of Appeal, requesting the court to require the Superior Court to recalculate contract damages for breach of the Exchange Agreement, to include a set-off for the additional sums SDCWA would have paid had Metropolitan collected the Water Stewardship Rate through the price charged to water purchasers as SDCWA argued was correct.

Due to SDCWA's litigation challenging Metropolitan's rates, and pursuant to the Exchange Agreement between Metropolitan and SDCWA, as of September 30, 2018, Metropolitan held $55.2 million in a designated fund, the Exchange Agreement Set-Aside Fund. See "–Financial Reserve Policy." This amount includes the disputed Water Stewardship Rate payments for calendar years 2011 through the present, and interest earned by Metropolitan thereon. The amount held does not include statutory prejudgment interest or any post-judgment interest, attorneys' fees, or costs the Court may award. The Set-Aside Fund also does not include any amounts applicable to the rate structure integrity provision declaratory relief cause of action, because that claim does not involve disputed payments under the Exchange Agreement.

In May 2014, SDCWA filed a new lawsuit asserting essentially the same rate claims and breach of contract claim in connection with the Board's April 2014 rate adoption. Metropolitan filed its answer on June 30, 2014. On February 9, 2015, pursuant to stipulation by the parties, the San Francisco Superior Court ordered that the case be stayed. Metropolitan is unable to assess at this time the likelihood of success of this case, any possible appeal or any future claims.

On April 13, 2016, SDCWA filed a new lawsuit that alleges all rates and charges for 2017 and 2018 adopted by Metropolitan's Board on April 12, 2016 violate the California Constitution, statutes, and common law. The Petition for Writ of Mandate and Complaint asserts misallocation of costs as alleged in the previous cases listed above and additional claims of over-collection and misallocation of costs and procedural violations. Following a stipulated order issued by the court on November 10, 2016, SDCWA filed a First Amended Petition for Writ of Mandate and

Complaint and the court ordered the case stayed pending final resolution of the 2010 and 2012 SDCWA v. Metropolitan cases' appeals. The amended petition/complaint adds allegations of the same Exchange Agreement breach as in the previous cases listed above and breach of a provision that requires Metropolitan to set aside disputed amounts, relating to the manner in which Metropolitan has set aside the amounts; requests a judicial declaration that, if a judgment is owed to SDCWA under the Exchange Agreement, SDCWA will not be required to pay any portion of that judgment; and requests a refund to SDCWA of any amount Metropolitan has collected in excess of the reasonable costs of the services provided or, alternatively, a reduction in SDCWA's future fees. Metropolitan is unable to assess at this time the likelihood of success of this case, any possible appeal or any future claims.

On June 9, 2017, SDCWA filed a new Petition for Writ of Mandate and Complaint challenging the Readiness-to-Serve (RTS) Charge and Capacity Charge for 2018 adopted by Metropolitan's Board on April 11, 2017. These two charges are set annually, and SDCWA's 2016 lawsuit included a challenge to these two charges for 2017. The new lawsuit similarly alleges the 2018 RTS Charge and Capacity Charge violate the California Constitution, statutes, and common law. The petition/complaint asserts misallocation of costs. Metropolitan was served with the petition/complaint on June 20, 2017. On July 18, 2017, SDCWA filed a first amended petition/complaint to add the Metropolitan's Board action of July 11, 2017 to make minor corrections to the RTS Charge. Metropolitan is unable to assess at this time the likelihood of success of this case, any possible appeal or any future claims.

On June 8, 2018, SDCWA filed a new lawsuit in Los Angeles Superior Court that alleges all rates and charges for 2019 and 2020 adopted by Metropolitan's Board on April 10, 2018 violate the California Constitution, statutes, and common law. The Petition for Writ of Mandate and Complaint asserts the Water Stewardship Rate is unlawful per se and its collection in transportation charges is also unlawful; failure to provide wheelers a reasonable credit for "offsetting benefits" pursuant to Water Code Section 1810, *et seq*., which SDCWA contends (and Metropolitan disputes) applies to the parties' Exchange Agreement; over-collection and misallocation of costs, including misallocation of Metropolitan's California WaterFix costs as its transportation costs; and specified procedural violations. SDCWA states in the Petition and Complaint that it intends to amend its complaint to allege additional claims against Metropolitan, including but not limited to a claim for breach of contract. Metropolitan is unable to assess at this time the likelihood of success of this case, any possible appeal or any future claims.

A number of other suits and claims arising in the normal course of business are pending against Metropolitan. In the opinion of Metropolitan's General Counsel, the adverse results, if any, of such legal actions on these suits and claims will not have a material effect on Metropolitan's financial position, changes in net position, or liquidity.

(i) Drinking Water Quality Standards

Under the Safe Drinking Water Act Amendments of 1996, Congress required the United States Environmental Protection Agency to set new drinking water quality standards. New standards to control microbial pathogens and disinfection byproducts (DBPs) became effective in 2002. These rules are known as the Interim Enhanced Surface Water Treatment Rule and the Stage 1 Disinfectants/Disinfection By-Product Rule. These standards became more stringent in a second set of regulations effective 2006. The second set of regulations (the Stage 2 Disinfectants/Disinfection Byproducts Rule and the Long-Term 2 Enhanced Surface Water Treatment Rule) did not require additional capital investment by Metropolitan.

Metropolitan identified ozone disinfection as the most cost-effective option to minimize the production of DBPs and achieve other water quality objectives. Ozone is now used as the primary disinfectant at the Diemer, Jensen, Mills, and Skinner plants. Construction of ozonation facilities at the Weymouth plant was completed in October 2017. The estimated cost of implementing ozone treatment at all five plants is approximately $1.1 billion.

(j) Reid Gardner Generating Station

Reid Gardner Generating Station (Plant) is a 557 megawatt coal-fired plant located near Moapa, Nevada. The Plant is owned and operated by Nevada Energy (NE). In 1983, DWR entered in to a Participation Agreement to import power from the Plant to serve the State Water Project energy needs. DWR's interest in the Plant terminated on July 25, 2013. DWR and NE negotiated the terms of the divestiture including DWR's obligations to mitigate any environmental impacts associated with the electricity generated for DWR over the past thirty years. Metropolitan paid approximately 75.0 percent of DWR's costs associated with the generation of electricity at the Plant and will pay this proportion of DWR's assigned mitigation costs.

(k) Landfill Obligation

Federal and State laws and regulations require that Metropolitan perform certain maintenance and monitoring functions at its sole landfill site for 30 years after closure. They further require that a separate funding mechanism be established to ensure that sufficient funds are available for closure and postclosure costs. In October 1995, the landfill was closed and management's estimate of closure and postclosure costs for this site totaled approximately $2.0 million. The required thirty-year postclosure maintenance and monitoring of the landfill officially started in January 1998; after the installation of the landfill's final cover was completed. Approximately $5,000 was expended for postclosure maintenance and monitoring activities during the three months ended September 30, 2018 and no expenses were incurred during the three months ended September 30, 2017.

The actual cost of postclosure care may be higher due to inflation, changes in technology, or changes in landfill laws or regulations. Funding of these costs has been derived from a separate trust account that has been established for closure and postclosure costs. The balance of the trust account is sufficient to cover the landfill liability.

7. PARTICIPATION RIGHTS IN STATE WATER PROJECT

Metropolitan is one of 29 water suppliers contracting with the State of California for a system to provide water throughout much of California. Under the terms of the State Water Contract, as amended, Metropolitan is obligated to pay allocable portions of the cost of construction of the system and ongoing operations and maintenance costs through at least the year 2035, regardless of the quantities of water available from the project (see Note 6a). Metropolitan and the other contractors may also be responsible to the State for certain obligations of any contractor who defaults on its payments to the State.

Approximately 37 percent of Metropolitan's total expenditures during the three months ended September 30, 2018 and 2017, pertained to its net payment obligations for the State Water Project. These payments were primarily based on the contractual water delivery request, the annually requested and actual deliveries received, and the cost of power required for such deliveries, offset by credits received from the project.

Management's present intention is to exercise Metropolitan's option to extend the contractual period to at least 2085, under similar terms, based on the Agreement in Principle reached in 2014. This corresponds to an estimated 125-year service life for the original facilities. The State is obligated to provide specified quantities of water throughout the life of the contract, subject to certain conditions.

The State has power generation facilities associated with its reservoirs and aqueducts. The power generated is utilized by the system for water transportation purposes. Power generated in excess of system needs is marketed to various utilities and California's power market. The revenues resulting from sales of excess power reduce the costs of pumping. Metropolitan and the other water contractors are responsible for repaying the capital and operating costs of the power facilities regardless of the amount of power generated (see Note 6f).

Metropolitan capitalizes its share of system construction costs as participation rights when such costs are billed by the State (see Notes 1h and 6a). Metropolitan's share of system operations and maintenance costs is charged to expense.

Metropolitan amortizes a portion of capitalized participation rights each month using a formula that considers the total estimated cost of the project, the estimated useful life, and estimated production capacity of the assets based upon information provided by the State of California. In fiscal year 2006, the formula was modified to use maximum annual contracted deliveries as the production capacity estimate as previous estimates of total production were less reliable than expected. Amortization expense totaled $32.8 million and $31.9 million for the three months ended September 30, 2018 and 2017, respectively.

8. DEPOSITS, PREPAID COSTS, AND OTHER

Balances at September 30, 2018 and 2017 were as follows:

(Dollars in thousands)	September 30, 2018	September 30, 2017
Prepaid water costs	**$ 181,624**	$ 143,837
Prepaid costs-Delta Habitat conservation and conveyance	**58,627**	58,627
Prepaid costs-California WaterFix	**23,400**	—
Prepaid expenses	**12,462**	10,339
Preliminary design/reimbursable projects	**12,487**	12,589
Other	**145,116**	123,816
Total deposits, prepaid costs, and other	**433,716**	349,208
Less current portion	**(131,575)**	(119,941)
Noncurrent portion	**$ 302,141**	$ 229,267

(a) Prepaid Water Costs

Metropolitan has entered into several water exchange and storage agreements with other agencies. These agreements provide Metropolitan with additional reliable water supplies to supplement deliveries of Colorado River and State Water Project water. Metropolitan is also actively pursuing other agreements, both within and outside its service area, to provide additional water supplies. The exchange and storage agreements generally provide for advance delivery of water during periods when water is available. At a later time when water is needed, these programs can then return water to improve Metropolitan's reliability. Expenditures associated with these agreements have been recorded as prepaid costs and are charged to cost of water as the water is withdrawn. At September 30, 2018 and 2017, prepaid water costs totaled approximately $181.6 million and $143.8 million, respectively, based on volumes of 913,000 acre-feet and 739,000 acre-feet, as of such dates.

(b) Prepaid Costs—Delta Habitat Conservation and Conveyance

In March 2009, Metropolitan, other State Water Project contractors, federal Central Valley Project contractors, and the U.S. Department of Interior's Bureau of Reclamation entered into funding agreements with DWR. The agreements are known collectively as the Delta Habitat Conservation and Conveyance Program (DHCCP) Funding Agreement and the Bay Delta Conservation Plan and Delta Habitat Conservation and Conveyance Plan (BDCP - DHCCP) Supplemental Funding Agreement. Metropolitan's three-year DHCCP agreement provides funding of approximately $35.0 million for Metropolitan's share (24 percent). Metropolitan's two-year BDCP-DHCCP agreement provides funding of approximately $25.0 million (25 percent). The funding provided by both agreements supports development of the BDCP which was later on adapted as California WaterFix (see Note 6b) through environmental analysis, planning and design of Delta conservation measures including Delta water conveyance options. With the approval of the California WaterFix, DWR intends to refund Metropolitan for funds advanced through these agreement for planning and environmental studies through bond financing actions.

(c) Preliminary Design/Reimbursable Projects

Metropolitan engages in preliminary design activities prior to obtaining Board approval of capital projects. The costs of these designs are recorded as prepaid costs. Once Board approval is obtained, these costs are added to the cost of the relevant construction project.

Reimbursable projects include work Metropolitan is contracted to perform for outside, non-related parties, and is subsequently billed for reimbursement.

9. DEFERRED COMPENSATION AND SAVINGS PLANS

For the benefit of its employees, Metropolitan has adopted a deferred compensation plan in accordance with Section 457 of the Internal Revenue Code. Generally, eligible employees may defer receipt of a portion of their salary until termination, retirement, death, or unforeseeable emergency. Until the funds are paid or otherwise made available to the employee, the employee is not obligated to report the deferred salary for income tax purposes.

Investment of the funds is managed by a third-party administrator, accordingly, at September 30, 2018 and 2017, neither the plan assets nor the related liability were included in the accompanying basic financial statements.

The third-party administrator coordinates the investment of the deferred amounts in available investment vehicles per the instructions of each participant. Metropolitan's Treasurer serves as Trustee for the deferred compensation plan. Metropolitan is not liable to its employees for any losses that may be incurred in connection with their participation in this plan.

Metropolitan has established another compensation deferral arrangement in accordance with Section 401(k) of the Internal Revenue Code. The 401(k) Consolidated Savings Plan is available to substantially all employees. Amounts deferred by participants, Metropolitan matching contributions, and accumulated earnings thereon are fully vested. Deferred amounts and matching contributions are transferred by Metropolitan each pay period to a third-party administrator who coordinates the investment of such proceeds in a variety of investment vehicles in accordance with the instructions of each participant. The Treasurer serves as Trustee for the savings plan. Metropolitan is not liable to its employees for any losses that may be incurred in connection with their participation in this plan.

Metropolitan has established a matching contribution program on behalf of each participating employee in the savings plan. Metropolitan's contribution is subject to a maximum of 4.5 percent of the employee's total cash compensation.

10. NET POSITION

Net position is classified as either restricted, unrestricted, or net investment in capital assets, including State Water Project Costs.

Net investment in capital assets, including State Water Project costs consist of capital assets, net of accumulated depreciation and amortization, and reduced by the outstanding balances of any bonds, notes, or other borrowings attributable to the acquisition or construction of those assets and deferred outflows and inflows of resources related to debt. Metropolitan's capital assets, including State Water Project costs include plant and equipment (Note 1g), participation rights in State Water Project (Notes 1h and 7), and participation rights in other facilities. Net investment in capital assets, including State Water Project costs were approximately $6.1 billion at September 30, 2018 and 2017.

The restricted component of net position are those items that have external constraints placed on them by creditors, grantors, contributors, or laws or regulations of other governments, or imposed by law through constitutional provisions of enabling legislation. Restricted net position totaled $404.2 million and $381.5 million at September 30, 2018 and 2017, respectively, of which $199.5 million and $197.8 million, respectively, represents principal and interest set aside for the next bond payment. The remaining $204.7 million and $183.7 million, respectively, relates to estimated operating and maintenance expense for October and November of the subsequent fiscal quarter. Each of these requirements is related to bond covenants.

The unrestricted component of net position are those items that do not meet the definition of “restricted” or “net investment in capital assets, including State Water Project costs.” Unlike the restricted net position, the Board has discretion in determining the use and establishing minimum/maximum balance requirements for the unrestricted cash and investment portion of net position. The Board may at any time change or eliminate amounts established for these purposes. Unrestricted net position totaled $341.1 million and $392.8 million at September 30, 2018 and 2017, respectively.

11. RISK MANAGEMENT

Metropolitan is exposed to various risks of loss related to the design, construction, treatment, and delivery of water resources. Metropolitan self-insures most of its property losses, the first $25.0 million for general liability, fiduciary liability and directors’ and officers’ liability, and $5.0 million for workers’ compensation. Metropolitan supplements its self-insurance program with $75.0 million excess general liability coverage, $60.0 million excess fiduciary liability coverage, $65.0 million excess for directors’ and officers’ liability coverage, and statutory limits excess workers’ compensation coverage. Special insurance policies carried include aircraft hull and liability, a limited property damage policy, crime insurance, specialty crime coverage, and travel accident coverage. Coverage types and limits for fiscal year 2018 were unchanged from fiscal year 2017. Settlement amounts did not exceed the self-insurance or insurance coverage limits in any of the past three years.

Liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Liabilities include an estimated amount for claims that have been incurred but not reported (IBNR). Claims liabilities are calculated considering the effects of inflation, recent claim settlement trends including frequency and amount of payouts, and other economic and social factors. The present value of liabilities for unpaid claims is based on a 1.5 percent annual interest rate over the life of the claims.

12. SUBSEQUENT EVENT

On October 1, 2018, Metropolitan disbursed $23.4 million to DWR for preconstruction planning costs of the California WaterFix in accordance with an advance funding agreement entered into in August 2018. The agreement provides funding of approximately $41.5 million for Metropolitan's share (33 percent). The full funding amount will be remitted in December 2018. DWR intends to refund Metropolitan for funds advanced through this agreement through bond financing actions.

On November 1, 2018, the California Court of Appeal determined that at this stage of the cases, it would not review the issue detailed in the September 14, 2018, Petition for Writ of Mandate filed by Metropolitan. Metropolitan may raise this issue again on any later appeal from the cases' final judgment.

On November 13, 2018, SDCWA submitted a Government Code Claim giving notice that, absent resolution of its claims by settlement, SDCWA intends to amend the Petition and Complaint filed by SDCWA on June 8, 2018, with respect to rates and charges for 2019 and 2020 to allege breach of the exchange agreement, rate refunds, restitution with respect to the Rate Structure Integrity clause, and other damages and losses.