

Long Range Finance Plan Rate Refinement Discussions

Meeting #1
August 10, 2011

Agenda

- Background/scoping
 - Process
 - Timeline
- Discussion of policies leading to current rate structure
 - 1999 Statement of Common Interests
 - Strategic Planning Steering Committee principles for preferred rate structure
 - Objectives
- Next steps

Background/Scoping

Background of Recent Discussions

- LRF Rates Subgroup started mid-2007 to discuss refinement of existing rate structure
- Topics covered:
 - Appropriate level of discount for Replenishment and IAWP
 - Treated Water Peaking cost recovery
 - Growth charge to recover infrastructure costs (Tier 2 addresses impact of Growth on supply costs)
 - Tier 1 versus Tier 2 differential
 - Cost of Service review

Outcomes of Recent Discussions

- Eliminate the IAWP
- Increase the Tier 1 versus Tier 2 differential
- Implement the Delta Supply Surcharge
- Board affirmed the Cost-of-Service approach

Upcoming Issue

- Purchase Orders expire December 31, 2012
- Path to move forward
 - Continue Purchase Orders?
 - Adjustments to rate structure?
 - Non-binding notices of intention to renew were received from:
Anaheim, Beverly Hills, Burbank, Calleguas, Central Basin, Eastern, Foothill, Fullerton, Glendale, Inland Empire, Las Virgenes, Long Beach, Los Angeles, MWDOC, Santa Ana, Three Valleys, Torrance, Upper San Gabriel, West Basin and Western

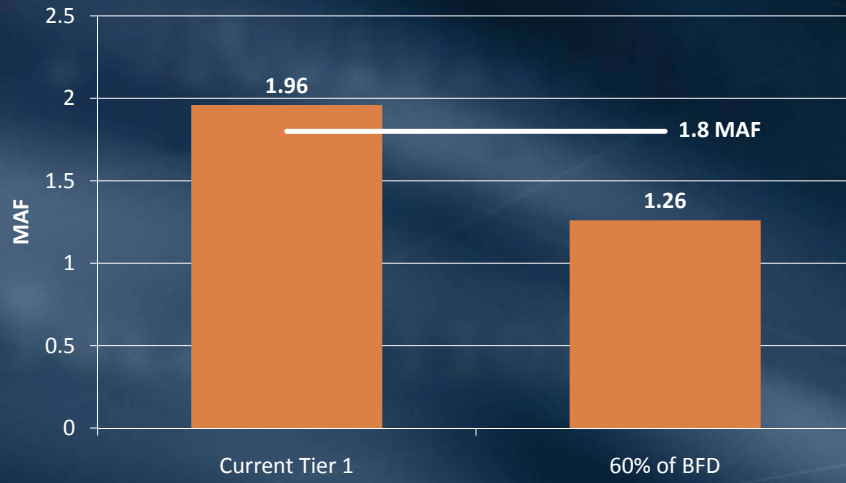
Summary of Purchase Orders

- Level of commitment was set at 60% of the IBFD to allow for wet hydrology
 - Growing agencies (Calleguas, Eastern, Western, Las Virgenes) had met their commitments by the end of the sixth year
 - All but three agencies had met their commitments by the end of the eighth year
- Agencies not meeting their commitment only pay the Supply portion of the rates on undelivered water
- A condition of the phase out of the IAWP allowed participating member agencies to increase their Tier 1 limits for IAWP opt-outs; total of Tier 1 limit for CY 2012 is 1.96 MAF

What if Member Agencies do not Extend the current Purchase Orders?

- Relevant sections of the Administrative Code:
 - § 4122. Base Firm Demand; Initial Base Firm Demand.
 - § 4401. Rates.
 - § 4404. Purchase Orders.
- Without Purchase Orders, the Tier 1 limit drops to 60% of Base Firm Demand

Impact of No Extension of Purchase Orders, CY 2012 Tier 1 Limits



Rate Refinement Process

Process to Define Post 2012

- Status Quo
- Rate Structure adjustments
- Change or eliminate Purchase Orders

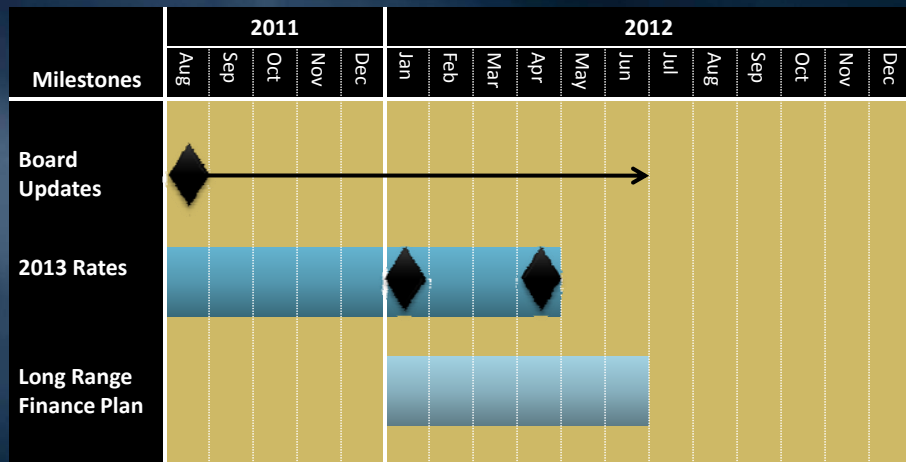
What Issues are on the Table?

- Fixed revenue generation
- Replenishment (Workgroup report in September)
- Growth charge for infrastructure
- Tier 1 limit / trading Tier 1 limits
- Treated water cost recovery
- Aligning the WSAP and implementation of rates and charges
- Fixed commitment to pay for the system (contracts)
- Compton: Purchase Order commitment shortfall
- Additional items to be considered based on Member Agency feedback

Timeline

- July 2011 Member Agency Managers meeting: open up discussions
- Kick off August 2011
- August 2011 F&I: Oral Report
- Target completion for summer of 2012

Timeline : LRFP / Rate Refinement



Discussion of Rate Structure

Statement of Common Interests included in the Strategic Policy Principles of 1999:



Statement of Common Interests

- **Regional Provider:** In this capacity, MWD is the steward of regional infrastructure and the regional planner responsible for drought management and the coordination of supply and facility investments.
- **Financial Integrity:** The MWD Board will take all necessary steps to assure the financial integrity of the agency in all aspects of its operations.
- **Local Resources Development:** MWD supports local resources development in partnership with its member agencies and by providing its member agencies with financial incentives for conservation and local projects.
- **Imported Water Service:** MWD is responsible for providing the region with imported water, meeting the committed demands of its member agencies.

Statement of Common Interests (cont'd)

- **Choice and Competition:** Beyond committed demands, member agencies may choose the most cost-effective additional supplies from MWD, local resource development, or market transfers. These additional supplies can be developed through a collaborative process to balance opportunities with affordability.
- **Responsibility for Water Quality:** MWD is responsible for advocating source water quality and implementing in-basin water quality for imported supplies provided by MWD to assure full compliance with existing and future primary drinking water standards and to meet requirements for water recycling and groundwater replenishment.
- **Cost Allocation and Rate Structure:** The fair allocation of costs and financial commitments for MWD's investments in supplies and infrastructure will be addressed in a revised rate structure. Committed demand has yet to be determined. The revised rate structure will address allocation of costs, financial commitment, unbundling of services, and fair compensation for services.

Strategic Planning Steering Committee principles for selecting the preferred rate structure:



Strategic Planning Steering Committee principles

- The rate structure should be fair.
- The rate structure should be based upon stability of MWD's revenue and coverage of its costs.
- The rate structure should provide certainty and predictability.
- The rate structure should not place a class of customers in a position of significant economic disadvantage.
- The rate structure should be reasonably simple and easy to understand.
- Any dry-year allocation should be based upon need.

Sales Forecast for 2020:

- 1996 IRP : 3.1 MAF
- 2004 IRP Update: 2.6 MAF
- 2010 IRP Update: 1.85 MAF
 - Calendar Year 2012 Tier 1 limit: 1.96 MAF

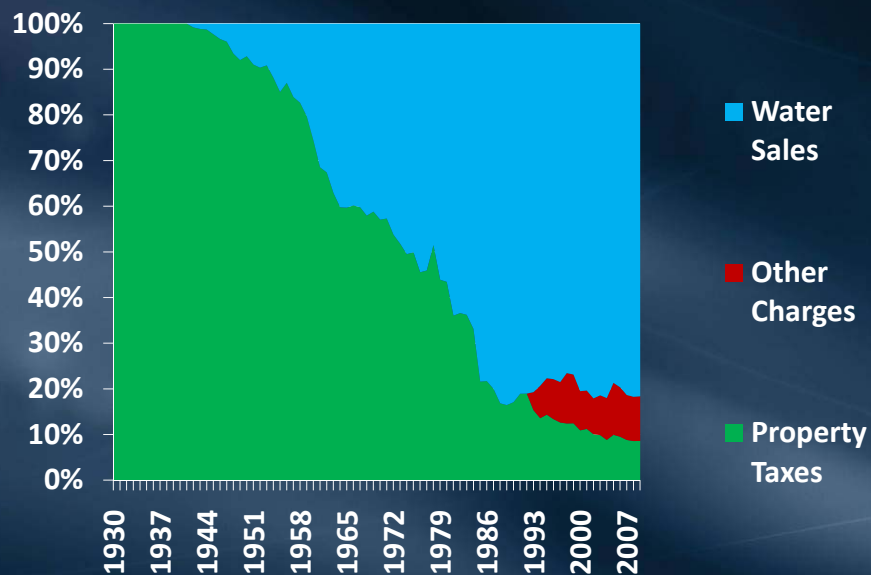
Rate Refinement Objectives: Question #1

- The principles and framework described above were developed after the 1996 IRP, which forecasted sales of 3.1 MAF by 2020. The 2010 IRP Update is projecting sales of 1.85 MAF in 2020. Given the lower sales forecast, are the principles and framework goals above still relevant? Are any listed above not relevant?

Rate Refinement Objectives: Question #2

- The current rate structure is highly dependent on volumetric sales revenue. Given Metropolitan's current and future business environment of selling less water compared to the 1996 IRP, does the current rate structure require changes?

Historical Revenue Sources



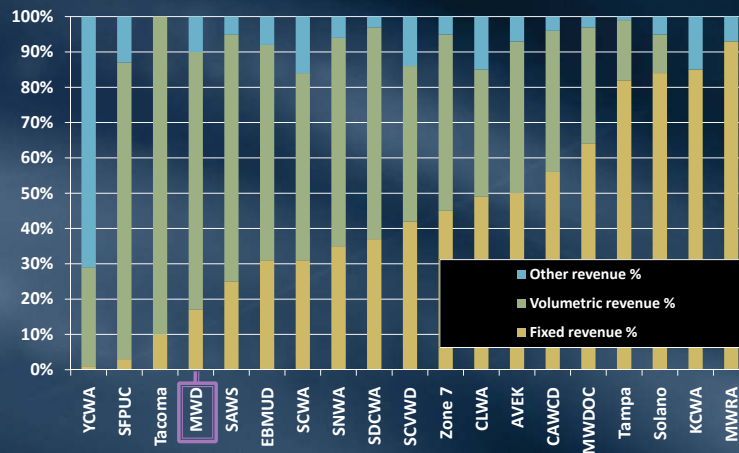
Rate Refinement Objectives: Question #3:

- What about the future of the Purchase Order? The Purchase Order established a member agency's Tier 1 limit for purchasing full service water. The current aggregated total of member agency Tier 1 limits in CY 2012 is 1.96 MAF. Is the current limit appropriate? Should all agencies be in Tier 2? What value is provided by a Tier 2 price if all sales are effectively in Tier 1?

Rate Refinement Objectives: Question #4:

- Given the objectives of Revenue Stability and Providing Certainty and Predictability, should the level of fixed charges and/or commitments increase? If so, what level of fixed charges and/or commitments are appropriate?

Fixed Revenues as a % of Total Revenues



Examples of Member Agency Fixed Charges

- Standby Charge
 - Fixed charge per parcel or acre, assessed on property taxes, used to offset the RTS
- Property tax assessment
 - Provides revenues for General District expenses
- Retail Meter Charge
 - \$/meter assessed on all retail meters within the service area
- Monthly Water Service Charge
 - \$/cfs based on meter capacity

Next Steps

- Feedback from today's meeting
 - Help determine future discussions
- Refine or reaffirm principles
- Begin discussions on specific issues