

- **Board of Directors**
Audit, Budget and Finance Committee

December 11, 2001 Board Meeting

9-2

Subject

Authorize (a) payments for increased calendar year 2001 State Water Project charges; (b) payments for State Water Project and Devil Canyon/Castaic contracts for 2002 Statement of Charges; and (c) increase in fiscal year 2001/02 State Water Project budget

Description

Increase in Calendar Year 2001 State Water Project Charges

The variable energy costs for the State Water Project (Project) have increased dramatically during CY 2001. During the months of January through May 2001, costs to purchase energy for the Project were significantly higher than planned. The Department of Water Resources (DWR) has estimated that its power costs to operate the Project this year have exceeded its power revenue from the contractors by \$160 million, of which Metropolitan's share is estimated at \$117 million.

Under the provisions of Metropolitan's water supply contract, the DWR would normally collect this money owed by Metropolitan in CY 2003 – two years after the expenses were incurred. However, the magnitude of the money owed by the contractors has resulted in the DWR increasing the energy unit rate for water delivered during CY 2001. The increased rate would result in State Water Project payments exceeding the amount approved by the Board for 2001.

To help mitigate these increased energy costs, the DWR has returned prior-year energy credits that would normally be received in 2002. These credits are being returned early for the exclusive purpose of offsetting the additional 2001 energy payments. For Metropolitan, these credits total \$49 million. When used to offset Metropolitan's \$117 million share of the Project's increased variable charges for this year, the net increase in 2001 energy charges is \$68 million. As a result, the Chief Executive Officer's (CEO) authorization of \$352 million to pay State Water Project charges in 2001 will fall short of the total amount needed, which is \$420 million.

Attachment 1 is a comparison of the authorized 2001 Statement of Charges and the revised 2001 charges based on the new billing rate being used by the DWR.

In certain respects the timing of increases in the unit rates is not consistent with the State Water Contract. However, Metropolitan and other contractors are cooperating to address the DWR's resulting cash flow problems. Ultimately, Metropolitan and the other contractors would have to make these payments with interest.

Calendar Year 2002 Statement of Charges

Metropolitan's CY 2002 Statement of Charges totals \$563 million, which is considerably higher than the estimated 2001 State Water Project costs of \$420 million. The DWR has very conservatively estimated its variable energy costs used to determine Metropolitan's 2002 Statement of Charges. Utilizing more realistic power costs, Metropolitan staff estimates that the State Water Project costs will total \$440 million. Metropolitan staff anticipate that the DWR will collect sufficient variable energy payments to cover its actual energy costs well before the end of 2002, and then suspend variable payments for the balance of the year. Additionally, the 2002 Statement of Charges is based on Metropolitan's request to take nearly its full share of Project entitlement water. Actual deliveries, however, may be lower if supply conditions remain dry, which may also result in a lower

annual payment. Therefore, it is likely that the actual 2002 State Water Project costs will be lower than is indicated in the Statement of Charges.

Attachment 2 is a comparison of the 2002 Statement of Charges with the estimated 2001 Project costs.

An independent auditor's report, verifying that the 2002 Statement of Charges complies with Metropolitan's State Water Project contract, is being completed. Copies of a summary of the report and the complete audit report will be available from the Executive Secretary at least a week prior to the board meeting. The preliminary audit findings result in an \$18.6 million decrease in Metropolitan State Water Project charges. Additionally, the audit confirms that the 2002 Statement of Charges is consistent with Metropolitan's SWP contract.

Increase in Fiscal Year 2001/02 Budget

With the increased 2001 State Water Project energy costs and the conservatively high variable rate in the 2002 Statement of Charges, Metropolitan staff has projected that the FY 2001/02 budget will not be sufficient to cover Project costs. The FY 2001/02 State Water Project budget is \$296 million; the current projected FY 2001/02 costs are \$327 million, or \$31 million more than what is budgeted. The increase in costs will be offset by lower than budgeted power costs on the Colorado River Aqueduct.

Attachment 3 compares the FY 2001/02 budgeted versus projected costs.

Policy

Metropolitan Water District Administrative Code § 5112: State Water Contract Payments

California Environmental Quality Act (CEQA)

Options #1, #2

The proposed actions are not defined as projects under CEQA, because they involve continuing administrative activities (Section 15378(b)(2) of the State CEQA Guidelines). In addition, the proposed actions are not subject to CEQA because they involve other government fiscal activities, which do not involve any commitment to any specific projects that may result in potentially significant physical impacts on the environment (Section 15378(b)(4) of the State CEQA Guidelines).

The CEQA determination for all options is: Determine that the proposed actions are not subject to CEQA per Sections 15378(b)(2) and 15378(b)(4) of the State CEQA Guidelines.

Board Options/Fiscal Impacts

Option #1

Adopt the CEQA determination and authorize the CEO to:

- (a) Approve and make payments up to a total of \$420 million determined to be due and payable under the terms of the State Water Service and Devil Canyon/Castaic contract for CY 2001;
- (b) Approve and make payments up to \$440 million determined to be due and payable under the terms of the State Water Service and Devil Canyon/Castaic contract for CY 2002, consistent with Metropolitan staff projections of 2002 Project energy costs;
- (c) Approve and make payments up to \$563 million if actual power costs exceed Metropolitan estimates and direct the CEO to report to the Board if power costs will exceed Metropolitan estimates; and
- (d) Increase FY 2001/02 State Water Project budget by \$31 million – from \$296 million to \$327 million.

Fiscal Impact: Payments for CY 2001 would increase by \$68 million. Anticipated payment for CY 2002 would be \$440 million, which is consistent with Metropolitan estimates of the cost of power in 2002. The maximum potential payment for CY 2002 would be for \$563 million. FY 2001/02 costs would exceed budget by \$31 million.

Option #2

Adopt the CEQA determination and instruct the CEO to:

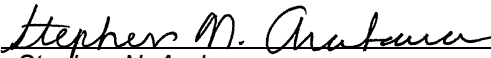
- (a) Not make payments above the previously approved CY 2001 Statement of Charges of \$352 million;
- (b) Approve and make payments up to \$440 million determined to be due and payable under the terms of the State Water Service and Devil Canyon/Castaic contract for CY 2002, consistent with Metropolitan staff projections of 2002 Project energy costs; and
- (c) Not change FY 2001/02 State Water Project budget.

Fiscal Impact: Payments for CY 2001 would not increase. The DWR would likely withhold Metropolitan's rate management credits in 2002, resulting in a loss of \$19 million that may not be recovered. Metropolitan would have to pay the \$68 million owed plus interest for incurred CY 2001 increased energy costs during CY 2003, assuming the DWR could carry the financial liability without impact until that time. Potential negative impact on the DWR credit rating may negatively impact interest costs paid by Metropolitan.

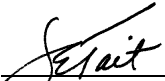
Maximum payment for CY 2002 would be limited to \$440 million. If additional CY 2002 payments were needed beyond this level, additional Board authorization would be requested. FY 2001/02 budget would not need to be increased.

Staff Recommendation

Option #1


 Stephen N. Arakawa
 Manager, Water Resource Management

11/28/2001
 Date

for 
 Ronald R. Gastelum
 Chief Executive Officer

11/28/2001
 Date

Attachment 1 - Comparison of Original & Revised Statement of Charges for CY 2001 SOC and Revised CY 2001 SOC

Attachment 2 - Comparison of Metropolitan's Statement of Charges for revised CY 2001 and CY 2002

Attachment 3 - SWP Payments and Water Deliveries Budgeted v. Actual and Projected July 2001 - June 2002 (Cash Fiscal Year)

Comparison of Original & Revised Statement of Charges for CY 2001 SOC and Revised CY 2001 SOC				
(\$ Thousands)				
	Actual		Difference	
	Original SOC CY 2001	Revised SOC CY 2001	\$	%
			Revised SOC 2001 Over/(Under) Original SOC 2001	% Over/(Under) Original SOC 2001
CAPITAL				
Delta Water	23,420	23,420	0	0.00 %
Rate Reduction Credit	(6,013)	(6,013)	0	0.00 %
Net Delta Capital	\$ 17,407	\$ 17,407	\$ -	0.00 %
Transportation with Devil Canyon - Castaic	72,689	72,689	0	0.00 %
Rate Reduction Credit	(12,694)	(12,694)	0	0.00 %
Net Trans Capital	\$ 59,995	\$ 59,995	\$ -	0.00 %
East Branch Enlargement	42,640	42,640	0	0.00 %
Water System Revenue Bond Surcharge	32,056	32,056	0	0.00 %
TOTAL CAPITAL	\$ 152,098	\$ 152,098	\$ -	0.00 %
MIN OMP&R				
Delta	24,760	24,760	0	0.00 %
Transportation with Devil Canyon - Castaic	61,532	61,532	0	0.00 %
East Branch Enlargement	13,032	13,032	0	0.00 %
TOTAL MIN OMP&R	\$ 99,325	\$ 99,325	\$ -	0.00 %
POWER				
Off Aqueduct Power Facilities (OAPF)	68,636	74,249	5,613	8.18 %
Transportation Variable Power	32,096	94,769	62,674	195.27 %
TOTAL POWER	\$ 100,732	\$ 169,018	\$ 68,287	67.79 %
TOTAL SWP CHARGES	\$ 352,155	\$ 420,441	\$ 68,287	19.39 %
<p>Based on Adjusted CY 2001 SOC dated 12/22/00</p> <p>Revised CY 2001:</p> <ul style="list-style-type: none"> - Increased OAPF \$5.6 million - Increased Transportation Variable Power \$112.4 million - Less CY 2000 Variable Power Overpayment to offset CY 2001 Increased Costs \$49.8 million 				

Comparison of Metropolitan's Statement of Charges for revised CY 2001 and CY 2002				
(\$ Thousands)				
	Actual		Difference	
	Revised SOC CY 2001	SOC CY 2002	\$	%
			SOC 2002 Over/(Under) Revised SOC 2001	% Over/(Under) Revised SOC 2001
CAPITAL				
Delta Water	23,420	23,050	\$ (370)	(1.58)%
Rate Reduction Credit	(6,013)	(6,013)	\$ -	0.00 %
Net Delta Capital	\$ 17,407	\$ 17,037	\$ (370)	(2.13)%
Transportation with Devil Canyon - Castaic	72,689	76,872	\$ 4,183	5.75 %
Rate Reduction Credit	(12,694)	(12,694)	\$ -	0.00 %
Net Trans Capital	\$ 59,995	\$ 64,178	\$ 4,183	6.97%
East Branch Enlargement	42,640	32,992	\$ (9,649)	(22.63)%
Water System Revenue Bond Surcharge	32,056	32,705	\$ 649	2.03 %
TOTAL CAPITAL	\$ 152,098	\$ 146,912	\$ (5,186)	(3.41)%
MIN OMP&R				
Delta	24,760	25,571	\$ 811	3.28 %
Transportation with Devil Canyon - Castaic	61,532	85,630	\$ 24,098	39.16 %
East Branch Enlargement	13,032	(5,934)	\$ (18,967)	(145.53)%
TOTAL MIN OMP&R	\$ 99,325	\$ 105,267	\$ 5,942	5.98%
POWER				
Off Aqueduct Power Facilities	74,249	70,984	\$ (3,264)	(4.40)%
Transportation Variable Power	94,769	240,560	\$ 145,790	153.84 %
TOTAL POWER	\$ 169,018	\$ 311,544	\$ 142,526	84.33%
TOTAL SWP CHARGES	\$ 420,441	\$ 563,723	\$ 143,282	34.08%
Based on Revised CY 2001 SOC dated 10/24/01 Based on CY 2002 SOC dated 07/01/01				

SWP PAYMENTS and WATER DELIVERIES				
Budgeted v. Actual and Projected				
July 2001 - June 2002 (Cash Fiscal Year)				
(\$ Millions)				
	Budget	Projected**	Difference	
			\$	%
			Actual Over/(Under) Budget	% Actual Over/(Under) Budget
CAPITAL				
Delta	\$17.39	\$8.50	(\$8.89)	(51.12)%
Transportation with Devil Canyon - Castaic	60.04	34.48	(25.56)	(42.57)%
Water System Revenue Bond Surcharge	32.00	32.38	0.38	1.19 %
East Branch Enlargement - Debt Service	43.19	38.99	(4.20)	(9.72)%
TOTAL CAPITAL	\$152.62	\$114.35	(\$38.27)	(25.08)%
MIN OMP&R				
Delta	\$22.70	\$25.10	\$2.40	10.57 %
Transportation with Devil Canyon - Castaic	76.31	71.58	(4.73)	(6.20)%
East Branch Enlargement	8.06	4.91	(3.15)	(39.08)%
TOTAL MINIMUM OMP&R	\$107.07	\$101.59	(\$5.48)	(5.12)%
POWER				
Off-Aqueduct Power Facilities	\$63.21	\$75.23	\$12.02	19.02 %
Transportation Variable *	16.09	106.58	90.49	562.40 %
TOTAL POWER	\$79.30	\$181.81	\$102.51	129.27%
CREDITS/REFUNDS	-\$43.04	-\$71.03	(\$27.99)	65.03%
TOTAL NET SWP CHARGES	\$295.95	\$326.72	\$30.77	10.40%
TOTAL DELIVERIES (MAF) Billed to MWD during Cash Fiscal Year	0.923	1.079	0.156	16.90%
Total Net \$/AF	\$321	\$303		
Power \$/AF	\$86	\$168		
* excludes Desert & Coachella				
** Jul - Oct Actual, Nov - Jun Projected				