

- **Board of Directors**
Business and Finance Committee

June 12, 2007 Board Meeting

8-2

Subject

Approve fiscal year 2007/08 budget actions

Description

GENERAL MANAGER'S BUSINESS PLAN

The General Manager's Business Plan outlines the strategic priorities, initiatives, and actions to be carried out in fiscal year 2007/08. This year's Business Plan is based on Chairman Timothy Brick's sustainability initiative and the Board's priorities as discussed during the April 2007 Board Retreat. These strategic priorities include:

- Sustainability** - Faced with continuous change and new emerging issues within our communities, economy, and environment, a sustainable water supply is increasingly critical. This means that Metropolitan and its member agencies will necessarily work together and with regulatory, wastewater, storm water, and other agencies in the watershed to ensure that water is used efficiently and effectively throughout the water cycle.
- Energy** - As energy costs become a more significant part of the overall budget (currently, energy accounts for about 24 percent of the expenditure budget, not including the Capital Investment Plan), managing market risk and rising costs is an increasingly important activity. In addition, legislation regarding greenhouse gas emissions and renewable resources, along with expiring contracts will require Metropolitan to work with the Department of Water Resources in new ways to secure reliable, cost-effective supplies of energy.
- Water** - Metropolitan's mission to supply a safe, reliable supply of high quality water will be supported as Metropolitan updates its Integrated Water Resources Plan, emphasizing the need for local resources and conservation.
- Communications Technology** - Effective automation and interactive technology are keys to increasing the efficiency of Metropolitan's business processes and communications with the Board, member agencies, and internal, as well as external communications with legislators, media, and the public. In FY 2007/08, Metropolitan will develop a strategy to fully utilize the various communication technologies and techniques to ensure the widest dissemination of relevant information.
- Workforce** - Metropolitan will continue to invest in its employees to prepare for changes in the workforce as long-term employees begin to retire and new employees are hired. Training and recruitment are going to be critical as the water supply, treatment, and delivery system becomes more complicated. Among the actions included in 2007/08 are leadership forums with top management, succession planning, and opportunities for peer-to-peer networking.
- Business Processes** - Metropolitan is committed to minimizing its resource use and environmental impacts associated with its day-to-day business functions. In 2007/08, Metropolitan will seek ways to use renewable energy resources at its facilities, reduce the waste stream associated with Metropolitan's activities, and implement water-use efficiency measures at all of our facilities.
- Finance** - The foundation for Metropolitan's success in securing water supplies is its strong financial standing. Metropolitan will work with its member agencies to update the Long Range Finance Plan in 2007/08 to ensure that this foundation remains solid.

These priorities are supported in the proposed 2007/08 budget.

FY 2006/07 ACCOMPLISHMENTS

Metropolitan met all water demands over the past fiscal year, met or surpassed all water quality regulations, and continued to manage finances in a prudent and effective manner. Standard and Poor's recognized these accomplishments when they upgraded the long-term credit rating on Metropolitan's revenue bond debt to AAA from AA+ even as Metropolitan faced the driest year on record in Los Angeles and the Department of Water Resources was involved in a lawsuit that could have resulted in the shutdown of the pumps that deliver water over the California Aqueduct to Metropolitan. Some of the other accomplishments include:

- Operated the treatment and distribution system and coordinated with member agencies to meet demands during outages that, for the first time in Metropolitan history, included all five treatment plants and the Colorado River Aqueduct in the same fiscal year;
- Maintained 100 percent compliance with all drinking water regulations at Metropolitan's five water treatment plants and within the distribution system;
- Maintained dry-year supplies in storage at about 2.4 million acre-feet, pending conditions on the State Water Project;
- Continued construction work on the Water Treatment Plant Improvement, CRA Reliability, and Conveyance and Distribution System Reliability Programs on schedule and within budget;
- Maintained AA+ revenue bond rating from Fitch and Aa2 from Moody's while being upgraded to AAA by Standard and Poor's;
- Limited the overall increase in water rates and charges in 2008 to 5.8 percent;
- Banked 50,000 acre-feet of water in Lake Mead and completed a Seven States proposal on Colorado River operations; and
- Updated and expanded the conservation and recycled water programs.

In 2007/08, Metropolitan will face many of the same challenges it faces today, including continued challenges to Colorado River supplies; the always uncertain outlook for State Water Project supplies, especially in light of below-average precipitation; regional support for ongoing member agency efforts to develop conservation, recycling, groundwater recovery, and seawater desalination; managing Metropolitan's extensive Capital Investment Plan (CIP) supporting continued water supply reliability and quality for Southern California, managing Metropolitan's real property assets, and providing necessary training and support for our workforce.

The year's rainfall and snow pack in Northern California was significantly below normal, resulting in a 60 percent allocation (1.1 million acre-feet) of water from the State Water Project. As a result, supplies will need to be carefully managed to meet demands in 2007/08. This below-average precipitation experience, when combined with the long-range forecasts of unfavorable impacts due to global warming, reinforce the importance of continued investments in effective water supply and system improvements to provide the region with long-term water supply reliability into the future. Although the winter of 2007 has resulted in historically low precipitation in Southern California, the local groundwater basin levels are good. In addition, groundwater basin managers continued to purchase available imported supplies to replenish the basins.

The region continued to experience strong economic growth during 2006, adding an estimated 239,000 people to the service area and experiencing an increase in taxable sales of almost 7.5 percent. Reflecting a stabilizing of the residential housing market in Southern California, building permits declined for the second consecutive year in 2006 with a total of approximately 86,000 permits issued. Although this contrasts with the roughly 103,600 permits issued in 2005, it is still above the average number of annual housing starts (80,000) for the ten-year period 1997-2006.

FY 2007/08 BUDGET SUMMARY

To help ensure a reliable water supply funded through predictable and affordable water rates, Metropolitan must continue to work creatively with its member agencies to manage the challenges of: the rising cost of energy; implementing and financing the capital investment program; and operating and maintaining new infrastructure. To this end, capital projects were prioritized and scheduled for 2007/08 with resources applied toward critical projects. With up to 83 projects in construction and 322 active projects in 68 programs, the FY 2007/08 CIP

expenditures are forecast to be about \$498 million. In addition, almost \$425 million of capital expenditures were deferred or eliminated from the five-year forecast period. The FY 2007/08 operations and maintenance (O&M) budget is only \$5.8 million or 1.8 percent higher than the \$324 million 2006/07 budget. This compares to an 11.6 percent increase in 2006/07, an increase of 2.6 percent in 2005/06, and a flat budget in 2004/05. Thus, the O&M budget has increased by an annual average of 3.9 percent per year during this four-year period. This increase is discussed more fully later in this letter and the budget summary.

PERFORMANCE MEASUREMENT

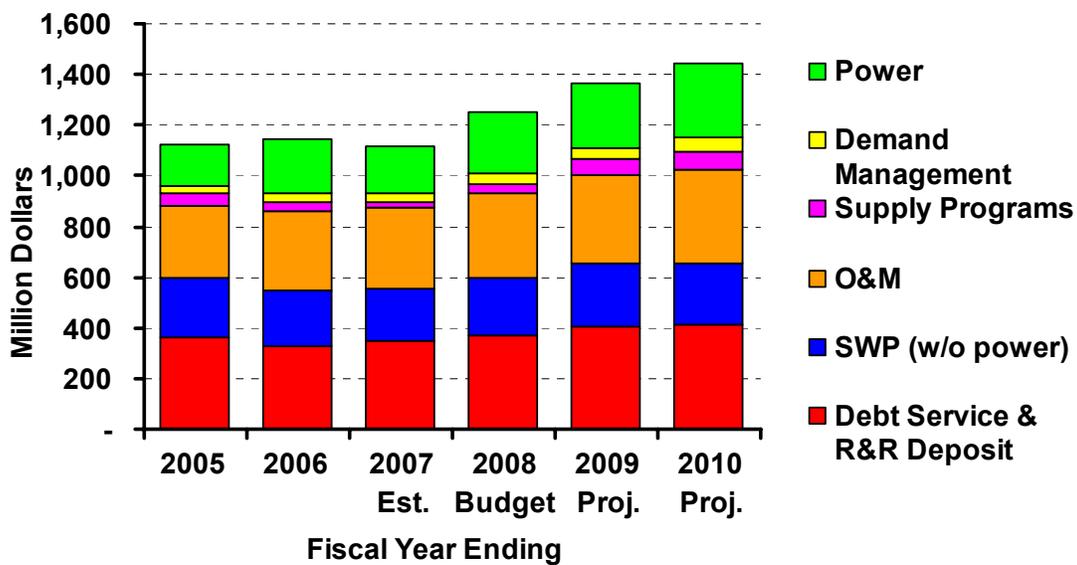
Performance measures are one of several methods used to monitor success in implementing the General Manager’s Business Plan. As in past years, the 2007/08 budget includes performance measures for the General Manager’s department as well as measures specific to each of the groups.

BUDGET TREND

To provide a longer-term picture of Metropolitan’s costs, Figure 1 shows the major expenditure categories over the past two years, the estimate for the current fiscal year, as well as the projection for the following three years. As shown in Figure 2, from FY 2004/05 through FY 2006/07, expenditures are expected to stay relatively flat (not including construction funded with bond proceeds).

However, from 2006/07 through 2009/10, expenditures are forecast to increase by about \$326.2 million, or about 8.9 percent annually. The primary cost drivers from 2006/07 through 2009/10 are a \$110.2 million increase in the cost of power on the State Water Project and Colorado River, a \$65.2 million increase in debt service costs, and a \$56.6 million increase in supply program costs. Other cost increases include a \$45 million increase in O&M due to inflation and negotiated salary and benefit increases, \$35.9 million increase for replacement and operating costs on the State Water Project, and a \$13.3 million increase for ongoing investment in local projects through the Local Resources Program and Conservation Credits Program.

Figure 1. Six-year Expenditure Trend



USES OF FUNDS

As shown in Table 1, the total FY 2007/08 uses of funds are budgeted at \$1.84 billion, an increase of \$55.2 million (3.1 percent) from the 2006/07 budget. Total cash outlays for SWC payments, supply programs, Colorado River Aqueduct (CRA) power, debt service, demand management programs, O&M, and the CIP are budgeted at \$1.69 billion. This is \$41.6 million (2.5 percent) greater than the 2006/07 budget and \$122.5 million (7.8 percent) greater than projected. In addition, \$85 million of water revenues will be deposited to the Replacement and Refurbishment fund to finance a portion of the replacements and refurbishments in the CIP. This is \$10 million less than 2006/07 and will be increased if water rates exceed 2.23 million acre-feet.

SWC costs are estimated to be \$52.2 million higher than the 2006/07 budget. Power costs on the SWP are estimated to be \$215.7 million for the delivery of about 1.66 million acre-feet into the service area. Under the contract, Metropolitan is responsible for payment for 1.55 million acre-feet (Coachella Valley Water District and Desert Water Agency are responsible for the majority of the remaining 0.11 million acre-feet under terms of the exchange agreement). The estimated average cost of power is about \$139 per acre-foot, almost 25 percent higher than in the 2006/07 budget. This increase is due to higher generating costs at Reid Gardner #4 as a result of increased environmental compliance and coal costs, combined with higher variable costs due to less generation and resulting lower revenues from Hyatt Thermalito.

Supply programs are estimated to be \$5.7 million higher than the 2006/07 budget. The increase is due primarily to increased support for the Semitropic Groundwater Storage and Exchange Program.

CRA power costs are expected to increase \$5.3 million from the 2006/07 budget for diversion of about 732,000 acre-feet. This increase cost reflects the purchase of more supplemental power at higher market rates and also slightly higher unit prices for Hoover- and Parker-based resources.

Total demand management costs are budgeted at \$42.9 million, \$5.1 million higher than the 2006/07 budget, and include incentive payments made under Metropolitan's Local Resources Program (LRP) of \$21.2 million and \$12 million for the Conservation Credits Program. The Board also requested that External Affairs increase its conservation messaging and advertising in light of the extremely dry year. The approximately \$4 million effort is not included in Table 1.

O&M costs for 2007/08 are expected to increase by about \$5.8 million (1.8 percent) from the 2006/07 budget. This increase is considerably lower than the 4.04 percent regional rate of inflation over the 12 months through March 2007. In accordance with bargaining unit agreements, rising labor costs account for \$8.4 million (4.1 percent) of the total increase in O&M compared to the 2006/07 budget. Offsetting this increase is a reduction of \$7.4 million reflecting completion of the PC Replacement Program. The remainder of the increase is due primarily to an increase in outside and professional services of about \$1.4 million supporting water quality, environmental safety, security, and property maintenance. Additionally, almost \$1.2 million is included to cover basic operation and maintenance of the Center for Water Education facility and to fund the Water Congress, and \$0.6 million is included for rising fuel costs. Operating equipment will increase by \$1.4 million (16.7 percent) primarily to augment water quality monitoring capability through the purchase of advanced laboratory equipment and improve hazardous material safety through purchase of new chlorine trailers.

The total personnel complement for 2007/08 is 2,069 positions, decreasing by one position from the 2006/07 budget. The planned increase of 25 full-time regular positions to aid in the delivery of capital projects on schedule and on budget was deferred in light of the revised CIP schedule. Any significant changes in personnel will be dependent on long-range staffing plan inputs related primarily to CIP impacts and an external review of maintenance management practices.

The 2007/08 CIP is \$498.4 million, or \$62.9 million lower than the 2006/07 budget. The CIP includes 83 projects in construction with a total of 322 active projects in 68 programs. Major expenditures include: treatment plant improvements (\$220.1 million) including the Oxidation Retrofit Program (\$155.5 million) and the Diemer Treatment Plant Improvements Program (\$33.3 million); 216 replacement and refurbishment projects (\$122.5 million); the Inland Feeder Project (\$69.3 million); Perris Valley Pipeline (\$25.1 million); DVL recreation (\$9.6 million); and the North Reach of San Diego Pipeline No. 6 (\$2.9 million).

SOURCES OF FUNDS

As shown in Table 1, FY 2007/08 sources of funds will total \$1.84 billion. This includes receipts of \$1.24 billion, with water sales receipts of \$928.6 million accounting for 75 percent of receipts. These receipts are based on projected water sales of 2.23 million acre-feet and include the board-approved increase in overall rates and charges of about 5.8 percent, effective January 1, 2008. Other revenues include readiness-to-serve charge revenues of \$82 million, revenues from the capacity charge of \$32.7 million, and tax and annexation revenues of about \$96.2 million. Interest earnings are expected to be about \$16.4 million higher than the 2006/07 budget, reflecting rising interest rates and a higher estimated construction fund balance. Power and other miscellaneous receipts are expected to generate about \$22.2 million due primarily to higher estimated water demands and higher power rates.

Capital projects will be funded from a combination of existing bond funds and revenues. Fund withdrawals from the Refurbishment and Replacement and General Fund will provide \$109.8 million. In addition, bond fund proceeds will provide about \$388.6 million toward the CIP. Consistent with plans to gradually draw down the Water Transfer Fund, about \$20 million in water transfer and storage program costs will be funded from the WTF. In addition, about \$74.1 million will be drawn from the Water Rate Stabilization Fund to offset the need for greater rate increases.

The revenue bond debt service coverage ratio is forecasted to be 1.76 times in 2007/08. This is lower than the target of 2 times revenue bond debt service. The fixed charge coverage is expected to be at the 1.20 target.

Table 1. 2007/08 Annual Budget Uses and Sources of Funds – Cash Basis (Dollars in Millions)

	2005/06 Actual	2006/07 Budget	2006/07 Projected	2007/08 Budget	2007/08 Budget Compared to	
					2006/07 Budget	2006/07 Projected
USES OF FUNDS						
Expenditures						
State Water Contract	406.4	395.9	369.5	448.0	52.2	78.5
Supply Programs	101.8	52.9	36.3	58.5	5.7	22.2
Colorado River Power	27.0	21.9	21.3	27.2	5.3	5.9
Debt Service	228.6	251.3	252.7	281.7	30.4	29.0
Demand Management	31.8	37.8	39.1	42.9	5.1	3.8
Departmental O&M *	264.9	264.3	275.7	275.6	11.3	(0.1)
Treatment Chemicals, Solids & Power	31.5	36.3	31.4	36.2	(0.2)	4.8
Other O&M	27.5	23.0	17.7	17.7	(5.3)	0.0
Sub-total Expenditures	1,119.6	1,083.4	1,043.8	1,187.9	104.5	144.1
Capital Investment Plan	444.5	561.3	520.0	498.4	(62.9)	(21.6)
Fund Deposits						
R&R and General Fund	83.7	95.0	95.0	85.0	(10.0)	(10.0)
Revenue Bond Construction	-	-	111.5	-	-	(111.5)
Water Stewardship Fund	10.9	2.1	5.7	-	(2.1)	(5.7)
Interest for Construction & Trust Funds	15.3	3.8	17.7	13.6	9.8	(4.1)
Increase in Required Reserves	25.3	35.3	60.1	51.2	15.9	(8.9)
Increase in Rate Stabilization Fund		-	32.6	-	-	(32.6)
Sub-total Fund Deposits	142.8	136.2	322.5	149.8	13.6	(172.7)
TOTAL USES OF FUNDS	1,706.9	1,780.9	1,886.3	1,836.2	55.2	(50.1)
SOURCES OF FUNDS						
Receipts						
Taxes	94.9	94.3	94.7	93.7	(0.6)	(1.0)
Annexations	2.9	1.5	2.5	2.5	1.0	-
Interest Income	28.8	35.6	54.7	52.0	16.4	(2.7)
Hydro Power	26.7	23.0	45.0	45.1	22.1	0.2
Fixed Charges (RTS & Capacity Charge)	111.4	112.6	112.9	114.7	2.1	1.8
Water Sales Revenue	813.8	848.2	888.5	928.6	80.3	40.0
Miscellaneous Revenue	24.0	6.2	6.2	6.3	0.1	0.1
Bond Proceeds	278.6	381.8	496.7	-	(381.8)	(496.7)
Sub-total Receipts	1,381.0	1,503.4	1,701.2	1,242.9	(260.5)	(458.3)
Fund Withdrawals						
Water Transfer Fund	63.4	20.0	20.0	20.0	-	-
R&R and General Fund	83.5	165.1	165.1	109.8	(55.3)	(55.3)
Bond Funds for Construction	89.9	26.1	-	388.7	362.6	388.7
Water Stewardship Fund	-	-	-	0.8	0.8	0.8
Decrease in Required Reserves	-	-	-	-	-	-
Decrease in Rate Stabilization Fund	86.5	66.4	-	74.1	7.7	74.1
Sub-total Fund Withdrawals	325.9	277.6	185.1	593.3	315.7	408.2
TOTAL SOURCES OF FUNDS	1,706.9	1,780.9	1,886.3	1,836.2	55.2	(50.1)

Totals may not foot due to rounding.

* 2007/08 Budget does not include an additional \$4 million for conservation outreach and advertising.

RESERVES

The maximum reserve level target for the Water Rate Stabilization and Revenue Remainder funds on June 30, 2008 is estimated to be about \$431.8 million. Based on projected receipts and expenditures, it is estimated that the total balance in the Water Rate Stabilization and Revenue Remainder funds will be about \$237.2 million on June 30, 2008, about \$57.1 million over the minimum reserve level of \$180.1 million. Total reserves are estimated to be \$964.8 million on June 30, 2008.

The budget was presented and discussed at the May 22, 2007, Board Workshop. In addition, each of the Groups and Departments presented their budgets during the April and May Board Committee meetings.

[Attachment 1](#), FY 2007/08 Budget Summary, discusses the sources of funds including receipts and fund withdrawals and uses of funds including expenditures and fund deposits.

Policy

Metropolitan Water District Administrative Code Section 5107: Annual Budget

California Environmental Quality Act (CEQA)

CEQA determination for Options #1 and #2:

The proposed actions are not defined as a project under CEQA, because they involve continuing administrative activities, such as general policy and procedure making (Section 15378(b)(2) of the State CEQA Guidelines). In addition, the proposed actions are not subject to CEQA because they involve the creation of government funding mechanisms or other government fiscal activities, which do not involve any commitment to any specific project, which may result in a potentially significant physical impact on the environment (Section 15378(b)(4) of the State CEQA Guidelines). For those anticipated projects listed in the budget that may require subsequent board approval, a CEQA review will be carried out and, if appropriate, environmental documentation for such projects will be prepared and processed in accordance with CEQA and the State CEQA Guidelines.

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

Board Options

Option #1

Adopt the CEQA determination and

- a. Approve the FY 2007/08 Budget;
- b. Appropriate \$906.2 million for the projected annual cash outlays for Metropolitan O&M and operating equipment, power costs on the Colorado River Aqueduct, SWP operations, maintenance, power and replacement costs and SWP capital charges; demand management programs including the local resources and conservation credits program; and costs associated with supply programs paid from the Water Transfer Fund;
- c. Appropriate as continuing appropriations, \$281.7 million for FY 2007/08 debt service on Metropolitan general obligation and revenue bonds;
- d. Authorize the use of \$85 million in operating revenues to fund Replacement and Refurbishment and General Fund construction and up to an additional \$10 million if water sales exceed 2.23 million acre-feet;
- e. Approve an additional \$4 million for conservation outreach and advertising in the External Affairs budget; and
- f. Authorize the General Manager to accept up to \$0.6 million in grant funds awarded from the California Air Resources Board (CARB) toward the replacement of three heavy equipment units including: one backhoe/loader (BIN 0415), one motor-grader (BIN 0416), and one front-end loader/tool carrier (BIN 0417), and authorize \$0.2 million in operating equipment funds as grant matching funds for same.

Fiscal Impact: \$1.35 billion

Business Analysis: Appropriate funds and authorize the use of those funds for the specified continuing business operations of Metropolitan

Option #2

Adopt the CEQA determination and approve the FY 2007/08 Budget with changes as recommended by the Board.

Fiscal Impact: Impact depends on adopted changes.

Business Analysis: Appropriate funds and authorize the use of those funds for business operations of Metropolitan, with changes as recommended by the Board

Staff Recommendation

Option #1



Brian G. Thomas
Chief Financial Officer

5/29/2007
Date



Jeffrey Kightlinger
General Manager

5/29/2007
Date

Attachment 1 – Fiscal Year 2007/08 Budget Summary

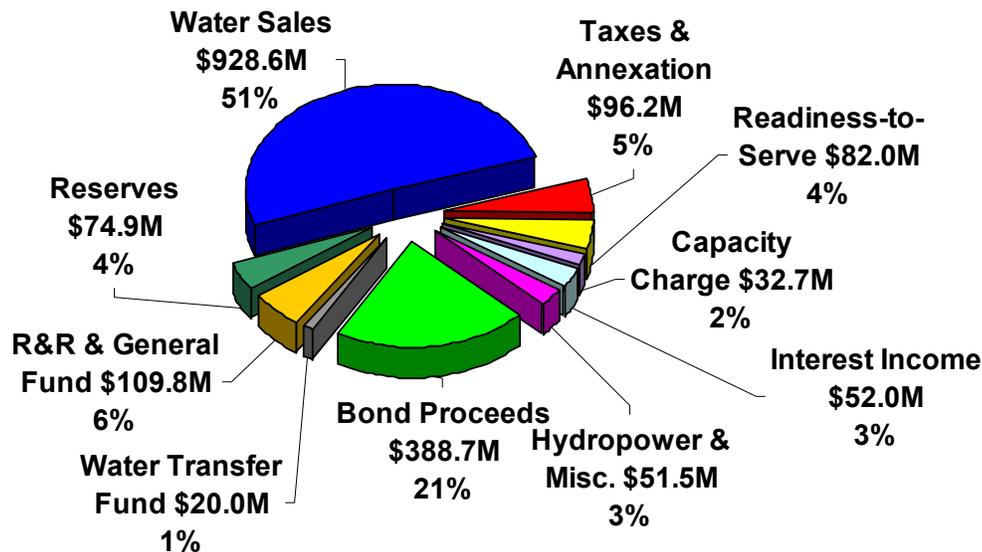
BLA #4853

Fiscal Year 2007/08 Budget Summary

The annual budget includes a discussion of cash basis sources and uses of funds. The budget is developed and monitored on a cash basis. This means that revenues and expenses are recognized when cash is received and when cash is disbursed. Accrual basis accounting records recognize revenues and expenses

in the period they are earned and incurred regardless of whether cash has been received or disbursed. A pro forma statement of operations is prepared on an accrual basis and included as Appendix 1 for reference.

Figure 3. 2007/08 Sources of Funds (\$1.84 billion dollars)



SOURCES OF FUNDS

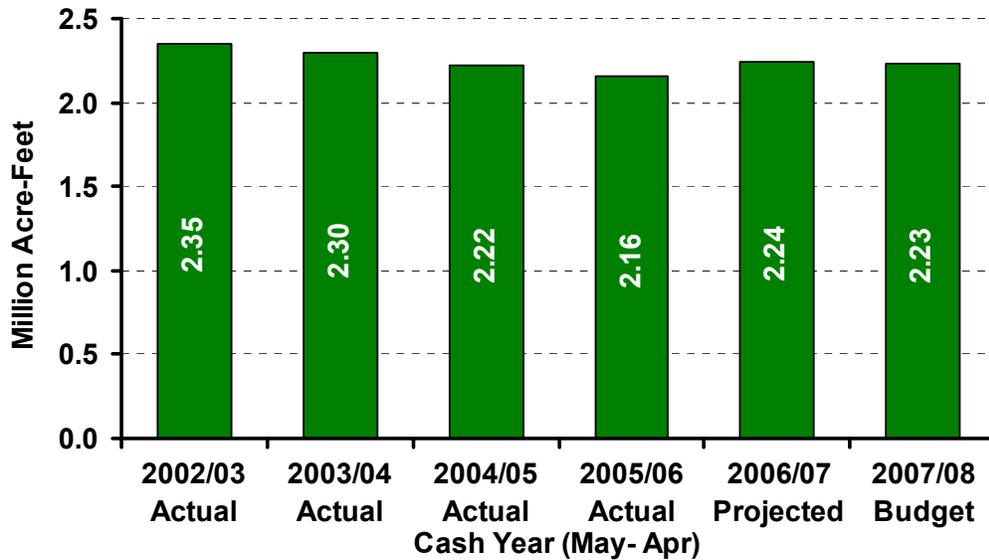
Estimated receipts from water sales, the readiness-to-serve (RTS) charge, the capacity charge, taxes, annexation fees, interest income, power recoveries, and other miscellaneous income are projected to be \$1.24 billion for fiscal year 2007/08 and constitute the major revenue sources for Metropolitan. This is \$121.3 million more than the 2006/07 budget. The increase in revenues is due to higher than expected water sales and rate increases in 2007 and 2008. Figure 3 shows the major sources of funds. Summaries of sources and uses of funds are shown in Tables 7 and 8. A description of each revenue source is included in the Glossary of Terms.

Water Sales

Water sales receipts are budgeted at \$928.6 million and are based on rates and charges adopted by the Board for calendar years 2007 and 2008, as shown in Table 2.

The 2008 rates shown in Table 2 reflect a \$30 per AF increase in the full service Tier 1 rate and a \$2 million increase in the RTS charge. These rates reflect Metropolitan’s cost of service. The overall effect of these changes results in an average rate increase of approximately 5.8 percent.

Figure 4. Five-Year Trend of Water Sales



Water sales for 2007/08 are estimated to be 2.23 MAF during the May through April period (cash year). This estimate served as the basis of the 2008 cost-of-service study and resulting water rates.

The 2007/08 cash year water sales include 1.75 MAF of firm sales, 0.18 MAF of replenishment sales, 0.14 MAF of agricultural sales, and 0.07 MAF of exchanges under the San Diego County Water Authority (SDCWA) Exchange Agreement for the SDCWA/Imperial Irrigation District (IID) transfer. Treated sales are estimated to be 1.40 MAF or 63 percent of total sales. Figure 4 shows the five-year trend of water sales.

Taxes and Annexation Fees

Revenues from taxes and annexation fees, which will be used to pay voter-approved debt service on general obligation bonds and a portion of the capital costs of the SWC, are estimated to be \$96.2 million.

Capacity and Readiness-to-Serve Charges

The Capacity Charge and Readiness-to-Serve Charge for 2007/08 is estimated to generate \$114.7 million or \$2.1 million more than the 2006/07 budget.

Other Revenue

Interest earnings are estimated to total \$52.0 million, including trust accounts and construction funds. This represents a \$16.4 million increase from the 2006/07 Budget due to higher interest rates and a higher estimated construction fund balance. Receipts from hydroelectric and CRA power sales are estimated to be \$45.1 million, higher by \$22.1 million due to higher estimated water demands and higher power rates. This estimate is consistent with actual experience in 2006/07.

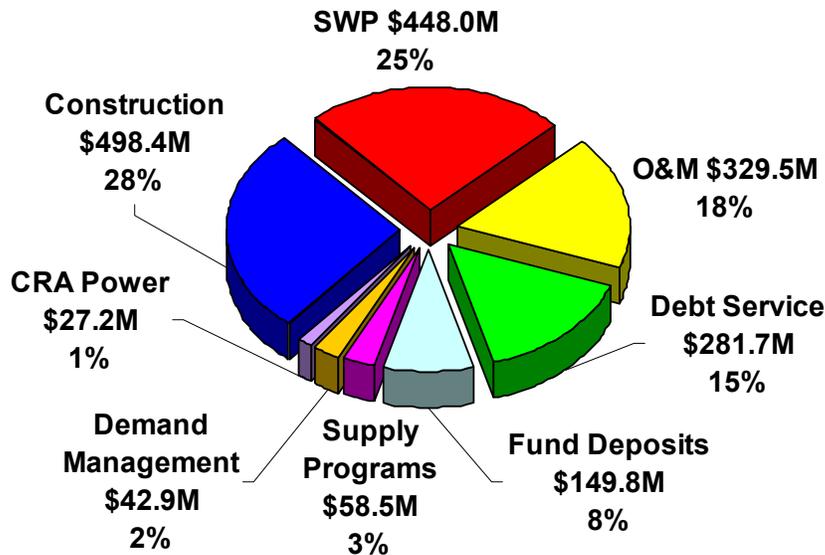
Other Sources

No bonds are expected to be issued in 2007/08. Approximately \$500 million of new money revenue bonds were issued in FY 2006/07. The CIP funding requirements will be met from existing bond funds (\$388.6 million), current operating funds (\$85.0 million from the R&R and General Funds) and available R&R fund balances (\$24.8 million). Finally, about \$20 million will be withdrawn from the Water Transfer Fund to pay for certain water transfer and storage programs. In 2007/08, a total of \$1.84 billion will be available for expenditures and other obligations.

Table 2. 2007/08 Water Rates and Charges

	Effective January 1st, 2007	Effective January 1st, 2008
Tier 1 Supply Rate (\$/AF)	\$73	\$73
Tier 2 Supply Rate (\$/AF)	\$169	\$171
System Access Rate (\$/AF)	\$143	\$143
Water Stewardship Rate (\$/AF)	\$25	\$25
System Power Rate (\$/AF)	\$90	\$110
Full Service Untreated Volumetric Cost (\$/AF)		
Tier 1	\$331	\$351
Tier 2	\$427	\$449
Replenishment Water Rate Untreated (\$/AF)	\$238	\$258
Interim Agricultural Water Program Untreated (\$/AF)	\$241	\$261
Treatment Surcharge (\$/AF)	\$147	\$157
Full Service Treated Volumetric Cost (\$/AF)		
Tier 1	\$478	\$508
Tier 2	\$574	\$606
Treated Replenishment Water Rate (\$/AF)	\$360	\$390
Treated Interim Agricultural Water Program (\$/AF)	\$364	\$394
Readiness-to-Serve Charge (\$M)	\$80	\$82
Capacity Charge (\$/cfs)	\$6,800	\$6,800

Figure 5. 2007/08 Uses of Funds (\$1.84 billion dollars)



USES OF FUNDS

Total uses of funds are \$1.84 billion. Figure 5 shows the breakdown of expenditures and other obligations that make up the Uses of Funds for 2007/08.

Colorado River Aqueduct Power

CRA power costs are projected to be \$27.2 million based on pumping 732 thousand acre-feet (TAF) at Whitsett Intake Pumping Plant. This is \$5.3 million more than the 2006/07 budget, which includes the diversion of 767 TAF. This increase from the 2006/07 budget reflects buying more supplemental power at higher market costs, and also somewhat higher unit costs for long-term contract resources (Hoover and Parker).

State Water Contract

SWC expenditures of \$448.0 million are budgeted to be \$52.2 million more than the current year’s budget.

SWC power costs are expected to be \$215.7 million or \$55.8 million more than the 2006/07 Budget and include the cost for pumping about 1.55 million acre-feet. An additional 102,000 acre-feet will be delivered through the DWCV exchange and DWCV transfer. The average unit cost of SWC power is expected to be about \$139 per acre-foot, almost 25% higher than in

the 2006/07 budget. This increase is due to higher generating costs at Reid Gardner #4 as a result of increased environmental compliance and coal costs, combined with higher variable costs due to less generation and resulting lower revenues from Hyatt Thermalito.

Minimum operations, maintenance, power, and replacement charges are \$12.2 million lower than the 2006/07 Budget. Capital charges are expected to be \$8.6 million more than the 2006/07 budget.

Demand Management Costs

Metropolitan provides financial assistance to its member agencies for the development of local water recycling and groundwater recovery projects through the Local Resource Program (LRP). Metropolitan also provides financial assistance for the development of conservation programs through the Conservation Credits Program (CCP).

As part of the LRP, Metropolitan has entered into agreements to provide financial assistance to 62 water-recycling projects. Forty-four of these projects are in operation and the remaining 18 projects are under design or construction. Recycling projects that receive Metropolitan

contributions are expected to produce 115,000 acre-feet of recycled water, principally for landscape irrigation, groundwater recharge, and industrial uses. In 2007/08, Metropolitan is expected to spend \$21.2 million on these efforts.

Metropolitan also has also entered into agreements to provide financial assistance to 24 projects to recover contaminated groundwater. Eighteen of these groundwater recovery projects are in operation and are expected to produce about 53,000 acre-feet in 2007/08 at a cost to Metropolitan of \$9.7 million.

As we look ahead, the public outreach campaign is shifting the focus of water conservation from inside the home to outdoor water use, which accounts for the majority of residential water use.

The CCP provides financial assistance to local agencies for conservation programs. The 2007/08 Budget contains \$12.0 million for the CCP to provide funding for residential, commercial, industrial, and landscape conservation.

Operations and Maintenance

The 2007/08 O&M budget, including operating equipment purchases, is estimated to be \$329.5 million. This is \$5.8 million more than the current year budget of \$323.7 million or an increase of 1.8 percent. The O&M increase is considerably lower than the rolling average regional inflation of 3.5 percent for the five years ending July 31, 2006.

Labor costs, not including those charged to construction, are \$213.0 million, which is \$8.4 million, or 4.1 percent higher than the 2006/07 budget of \$204.6 million

A summary of the 2007/08 O&M budget is shown in Table 3, which shows that the total departmental budget increased 3.7 percent compared with the 2006/07 budget. This year's budget also includes \$650,200 to operate and maintain the Center for Water Education (CWE) facility. This budget reflects the cost of utilities, security and building maintenance only for the CWE. Program costs have not been included, as those decisions have not yet been determined by the Board.

A detailed departmental budget for each group is included in the 2007/08 Departmental Budget book. Figure 6 provides the distribution of departmental O&M by organization. The Water System Operations Group (WSO) accounts for 58 percent of the total departmental budget. Figure 7 summarizes the total departmental budget by expenditure type, of which 62 percent is for salaries and benefits.

Table 3. 2007/08 Operations & Maintenance Annual budget (dollars)

Departmental Units	2006/07 Budget	2006/07 Projected	2007/08 Budget	Change			
				2007/08 to 2006/07 Budget	%	2007/08 to 2006/07 Projected	%
Office of the General Manager	\$ 6,559,300	\$ 6,966,300	\$ 7,604,600	\$ 1,045,300	15.9%	\$ 638,300	9.2%
Water Systems Operations	173,602,600	182,827,100	181,667,500	8,064,900	4.6%	(1,159,600)	(0.6%)
Water Resource Management	18,317,800	18,038,100	18,766,000	448,200	2.4%	727,900	4.0%
Corporate Resources	65,179,000	65,248,700	66,991,000	1,812,000	2.8%	1,742,300	2.7%
Real Property Development & Mgmt	5,202,200	5,560,800	5,356,300	154,100	3.0%	(204,500)	(3.7%)
External Affairs	16,911,500	16,104,600	17,168,600	257,100	1.5%	1,064,000	6.6%
Office of the Chief Financial Officer	9,403,400	9,686,700	9,636,300	232,900	2.5%	(50,400)	(0.5%)
Human Resources	10,250,100	10,707,300	10,249,800	(300)	(0.0%)	(457,500)	(4.3%)
Subtotal - General Manager's Dep.	305,425,900	315,139,600	317,440,100	12,014,200	3.9%	2,300,500	0.7%
General Counsel	9,966,100	9,967,900	10,265,000	298,900	3.0%	297,100	3.0%
General Auditor	2,768,100	2,485,200	2,838,000	69,900	2.5%	352,800	14.2%
Ethics Office	602,900	525,200	620,200	17,300	2.9%	95,000	18.1%
Overhead Credit from Construction	(18,134,600)	(21,000,000)	(19,430,100)	(1,295,500)	7.1%	1,569,900	(7.5%)
Total Departmental Budget	300,628,400	307,117,900	311,733,200	11,104,800	3.7%	4,615,300	1.5%
Other O&M							
PC Replacement	8,400,000	6,100,000	987,600	(7,412,400)	(88.2%)	(5,112,400)	(83.8%)
Center for Water Education	-	-	650,200	650,200	NA	650,200	NA
Association Dues	2,190,900	1,777,900	2,200,000	9,100	0.4%	422,100	23.7%
Contingency	3,266,900	-	3,295,000	28,100	0.9%	3,295,000	NA
Leases	421,000	300,000	430,000	9,000	2.1%	130,000	43.3%
Property Tax	480,000	496,300	515,000	35,000	7.3%	18,700	3.8%
Subtotal - Other	14,758,800	8,674,200	8,077,800	(6,681,000)	(45.3%)	(596,400)	(6.9%)
TOTAL OPERATIONS & MAINTENANCE	315,387,200	315,792,100	319,811,000	4,423,800	1.4%	4,018,900	1.3%
Operating Equipment	8,275,200	9,056,300	9,658,800	1,383,600	16.7%	602,500	6.7%
GRAND TOTAL	\$ 323,662,400	\$ 324,848,400	\$ 329,469,800	\$ 5,807,400	1.8%	\$ 4,621,400	1.4%

Figure 6. 2007/08 Departmental Budget by Organization
(without overhead credit, \$331.2 million)

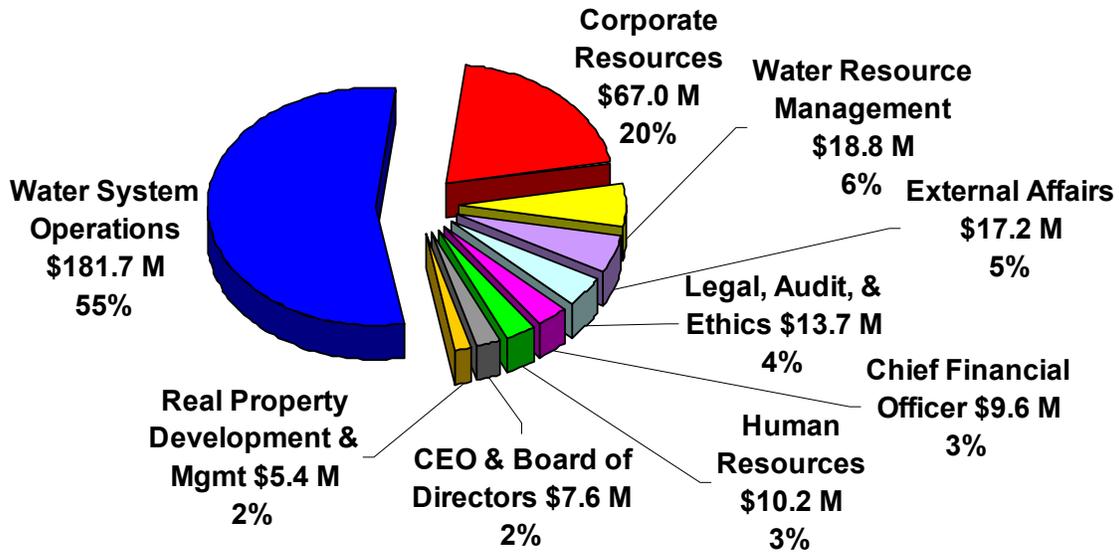
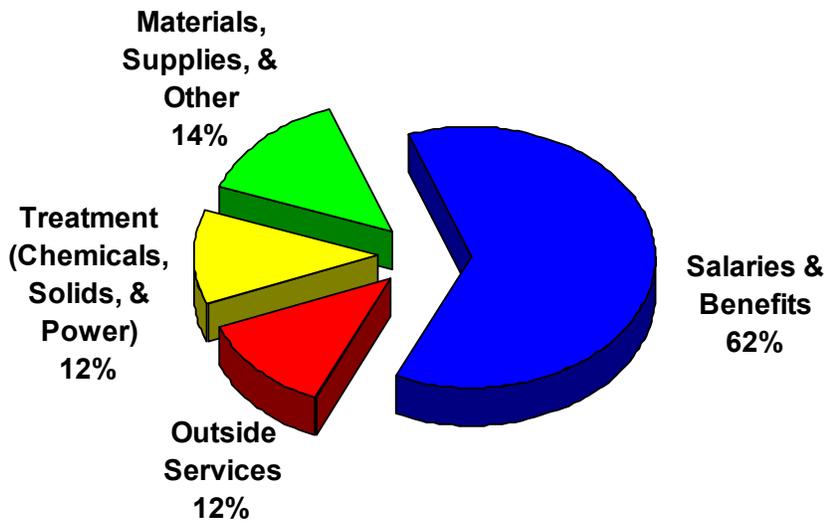


Figure 7. 2007/08 Departmental Budget by Expenditure Type



Labor

The total personnel complement (including temporary workers) for 2007/08 is 2,069 positions, down 1 position from 2006/07. O&M personnel are up by 7 full-time-equivalent (FTE) positions to 1,686.

Positions dedicated to capital work are down 8 positions. The personnel complement is broken down on Tables 4 and 5.

Table 4. Regular and Temporary Positions

	2004/05 Budget	2005/06 Budget	2006/07 Budget	2007/08 Budget	Change from 2006/07
Regular Full Time Positions	1,946	1,965	2,024	2,021	-3
District Temporary Positions	27	33	35	39	4
Agency Temporary Positions	45	28	11	9	-2
Total	2,018	2,026	2,070	2,069	-1

Table 5. O&M and Capital Staffing Levels

	2006/07			2007/08		
	O&M	Capital	Total	O&M	Capital	Total
Regular Full Time Positions	1,648	376	2,024	1,656	365	2,021
District and Agency Temporary Positions	31	15	46	30	18	48
Total	1,679	391	2,070	1,686	383	2,069

Supply Programs

Major supply program expenditures for 2007/08 are estimated to be \$58.5 million and include:

- \$14.4 million for the Palo Verde Land Management Program;
- \$14.4 million for the Kern Delta Program (deferred from 2006/07);
- \$9.4 million for operating and maintaining the IID/MWD conservation agreement;
- \$8.5 for the Semitropic Groundwater Storage and Exchange Program;
- \$4.0 million for the Arvin-Edison Storage Program;
- \$2.3 million for the San Bernardino Valley Municipal Water District agreement;
- \$2.3 million for the Multi Species Habitat Conservation Plan;
- \$1.6 million for water purchases of IID Water via the Salton Sea Restoration Fund;
- \$1.3 million for Sacramento Valley Water Transfer Options; and
- \$0.3 million for the O&M costs of groundwater storage programs in Metropolitan's service area.

Of the total \$58.5 million supply program cost, \$38.5 million will be funded from current operating revenues while \$20.0 million will be funded from the Water Transfer Fund (WTF). These storage programs are expected to yield 115 TAF and generate 202 TAF of transfer water.

In accordance with board policy, deposits to the WTF ended in 2003/04. The estimated ending balance on June 30, 2007 is \$20.7 million.

Annual Capital Investment Plan

The CIP for 2007/08 is estimated to be \$498.4 million. The CIP is funded by a combination of debt and current operating revenues (R&R and General Fund). The details of each project within the CIP are discussed in the 2007/08 Capital Investment Plan Budget book.

The 2007/08 CIP is \$62.9 million lower than the 2006/07 Budget. Major CIP projects in design and/or construction include:

- \$220.1 million for improvements on Metropolitan's five treatment plants, including the Oxidation Retrofit Program (ORP) and the Skinner Expansion Project;
- \$122.5 million for 216 replacement and refurbishment (R&R) projects;
- \$69.3 million for the Inland Feeder project;
- \$25.1 million for the Perris Valley Pipeline project;
- \$9.6 million for DVL Recreation; and
- \$2.9 million for San Diego Pipeline No. 6.

The projects listed above account for 90 percent of the total 2007/08 CIP expenditures. Figure 8 shows the major project categories in the 2007/08 CIP.

These projects are also categorized by the service functions that are the foundation of Metropolitan's cost-of-service water rates including source of supply, conveyance, storage, treatment, distribution, and general. The 2007/08 expenditure plan by major service function is shown in Figure 9.

Figure 8. 2007/08 Capital Investment Plan by Major Project Category

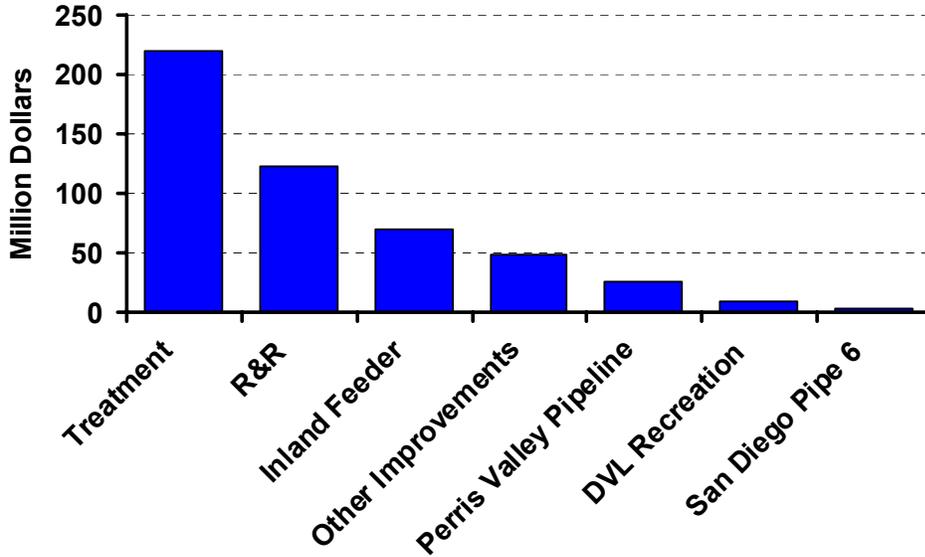
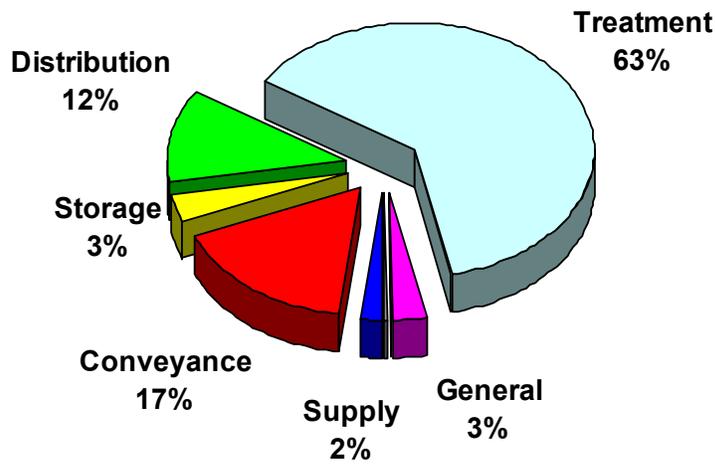


Figure 9. 2007/08 Capital Investment Plan by Service Function



Cash Funded Capital

The 2007/08 CIP includes estimated R&R programs totaling \$122.5 million and an additional \$37.5 million to be paid from the General Fund. The combined cash financing from current operating funds for the R&R and General Fund will total \$85.0 million. After paying for General Fund expenditures, \$47.5 million of operating funds is available for R&R expenditures. In order to ensure a reliable delivery system, an additional \$50.2 million of R&R will be funded from bond proceeds and \$24.8 will be funded from available R&R fund balances.

Debt Service

The portion of the CIP that is not cash funded will be funded from bond proceeds. In 2007/08, \$388.7 million of capital will be funded with bond proceeds. Debt service payments are budgeted to be \$281.7 million and include \$48.6 million in G.O. Bond debt service, \$225.6 million in revenue bond debt service, \$5.0 million in variable rate debt administration costs (liquidity, remarketing fees, and broker-dealer fees), and \$2.5 million for State Revolving Fund Loan payments. Total debt service costs are \$30.4 million more than the 2006/07 budget.

Metropolitan currently has \$4.13 billion in outstanding debt. Of this amount, \$3.78 billion is revenue bond debt, of which 22 percent is in a variable rate mode. In May 2007 Metropolitan is expecting to issue an additional \$500 million of bonds, of which \$100 million will be in a variable rate mode.

Over the next five years, it is expected that an additional \$1.16 billion in debt will be issued to fund the CIP. The cost of debt over this period is assumed to be 3.5 percent and 5.0 percent, respectively, for variable and fixed rate debt in 2007/08.

Reserve Transfers

During the 2007/08 budget year, \$74.1 million is projected be withdrawn from the Water Rate Stabilization Fund.

Fund Balances and Reserve Levels

Metropolitan operates as a single enterprise fund for financial statements and budgeting purposes. Through its Administrative Code, Metropolitan identifies a number of accounts, which are referred to as funds, to separately track uses of monies for specific purposes as summarized in Table 8. Fund balances are budgeted to be \$964.8 million at June 30, 2008. Of that total, \$727.6 million is restricted by bond covenants, contracts, or board policy, and \$237.2 million is unrestricted. Table 6 shows a breakdown of reserves by fund type. Figure 10 shows the distribution of funds by type.

The minimum and maximum Water Rate Stabilization Fund reserve levels are estimated to be \$180.1 million and \$431.8 million, respectively, at June 30, 2008. Based on projected receipts and expenditures, it is estimated that the balance in the Water Rate Stabilization and Revenue Remainder Funds will total about \$237.2 million. This is \$57.1 million over the minimum reserve level and within the Board's reserve policy guidelines.

Table 6. Projected Fund Balances at June 30, 2008 (dollars in millions)

	Restricted		Unrestricted	Total
	Contractual	Board		
Operating Funds	197.9	128.0		325.8
Debt Service Funds	274.7			274.7
Construction Funds	125.2		-	125.2
Reserve Funds*			237.2	237.2
Water Transfer Fund		0.7		0.7
Trust and Other Funds	1.2			1.2
Total	598.9	128.7	237.2	964.8

Totals may not foot due to rounding.

* includes Water Rate Stabilization Fund and the Revenue Remainder Fund

Figure 10. Fund Distribution by Type at June 30, 2008

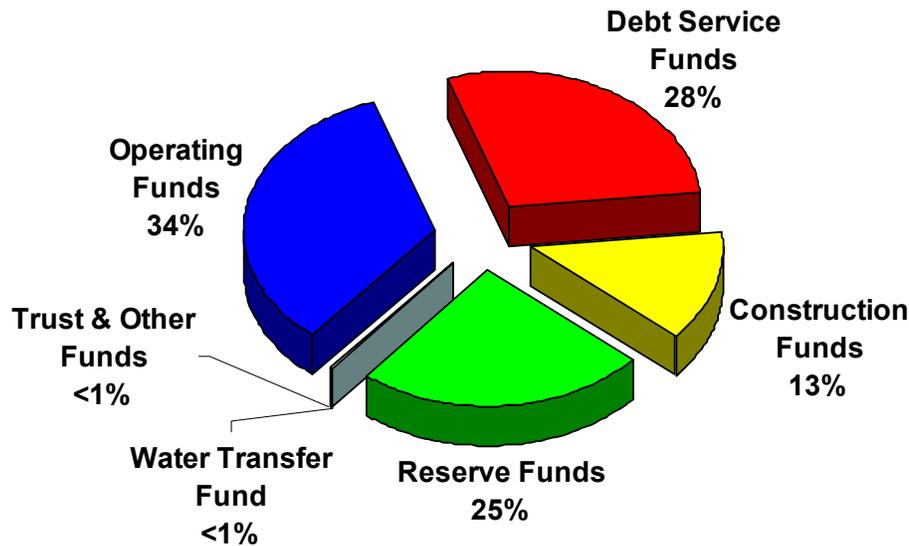


Table 7. 2007/08 Budget Sources and Uses of Funds (dollars in millions)

	2005/06 Actual	2006/07 Budget	2006/07 Projected	2007/08 Budget	2007/08 Budget Compared to	
					2006/07 Budget	2006/07 Projected
USES OF FUNDS						
Expenditures						
State Water Contract	406.4	395.9	369.5	448.0	52.2	78.5
Supply Programs	101.8	52.9	36.3	58.5	5.7	22.2
Colorado River Power	27.0	21.9	21.3	27.2	5.3	5.9
Debt Service	228.6	251.3	252.7	281.7	30.4	29.0
Demand Management	31.8	37.8	39.1	42.9	5.1	3.8
Departmental O&M	264.9	264.3	275.7	275.6	11.3	(0.1)
Treatment Chemicals, Solids & Power	31.5	36.3	31.4	36.2	(0.2)	4.8
Other O&M	27.5	23.0	17.7	17.7	(5.3)	0.0
Sub-total Expenditures	1,119.6	1,083.4	1,043.8	1,187.9	104.5	144.1
Capital Investment Plan	444.5	561.3	520.0	498.4	(62.9)	(21.6)
Fund Deposits						
R&R and General Fund	83.7	95.0	95.0	85.0	(10.0)	(10.0)
Revenue Bond Construction	-	-	111.5	-	-	(111.5)
Water Stewardship Fund	10.9	2.1	5.7	-	(2.1)	(5.7)
Interest for Construction & Trust Funds	15.3	3.8	17.7	13.6	9.8	(4.1)
Increase in Required Reserves	25.3	35.3	60.1	51.2	15.9	(8.9)
Increase in Rate Stabilization Fund	-	-	32.6	-	-	(32.6)
Sub-total Fund Deposits	142.8	136.2	322.5	149.8	13.6	(172.7)
TOTAL USES OF FUNDS	1,706.9	1,780.9	1,886.3	1,836.2	55.2	(50.1)
SOURCES OF FUNDS						
Receipts						
Taxes	94.9	94.3	94.7	93.7	(0.6)	(1.0)
Annexations	2.9	1.5	2.5	2.5	1.0	-
Interest Income	28.8	35.6	54.7	52.0	16.4	(2.7)
Hydro Power	26.7	23.0	45.0	45.1	22.1	0.2
Fixed Charges (RTS & Capacity Charge)	111.4	112.6	112.9	114.7	2.1	1.8
Water Sales Revenue	813.8	848.2	888.5	928.6	80.3	40.0
Miscellaneous Revenue	24.0	6.2	6.2	6.3	0.1	0.1
Bond Proceeds	278.6	381.8	496.7	-	(381.8)	(496.7)
Sub-total Receipts	1,381.0	1,503.4	1,701.2	1,242.9	(260.5)	(458.3)
Fund Withdrawals						
Water Transfer Fund	63.4	20.0	20.0	20.0	-	-
R&R and General Fund	83.5	165.1	165.1	109.8	(55.3)	(55.3)
Bond Funds for Construction	89.9	26.1	-	388.7	362.6	388.7
Water Stewardship Fund	-	-	-	0.8	0.8	0.8
Decrease in Required Reserves	-	-	-	-	-	-
Decrease in Rate Stabilization Fund	86.5	66.4	-	74.1	7.7	74.1
Sub-total Fund Withdrawals	325.9	277.6	185.1	593.3	315.7	408.2
TOTAL SOURCES OF FUNDS	1,706.9	1,780.9	1,886.3	1,836.2	55.2	(50.1)

Totals may not foot due to rounding.

* 2007/08 Budget does not include an additional \$4 million for conservation outreach and advertising.

Table 8 2007/08 Sources and Uses by Fund (dollars in millions)

Fiscal Year Ending June 30th, 2008 (\$ in Millions)	All Funds	Operating Funds								Debt Service Funds	Reserve Funds*	Construction Funds		Trust & Other Funds
		General	Water Revenue	O&M	Water Standby	Water Transfer	Water Stewardship	Self-Insured Retention	State Contract			R&R	Revenue Bond Construction	
Beginning of Year Balance	1,408.3	53.1	-	133.5	0.6	20.7	32.2	25.3	68.4	250.2	298.2	24.8	500.3	1.2
USES OF FUNDS														
Expenditures														
State Water Contract	448.0	-	-	296.7	-	-	-	-	151.3	-	-	-	-	-
Supply Programs	58.5	-	-	38.5	-	20.0	-	-	-	-	-	-	-	-
Colorado River Power	27.2	-	-	27.2	-	-	-	-	-	-	-	-	-	-
Debt Service	281.7	2.6	-	5.0	-	-	-	-	-	274.2	-	-	-	-
Demand Management	42.9	-	-	42.9	-	-	-	-	-	-	-	-	-	-
Departmental O&M	275.6	-	-	275.6	-	-	-	-	-	-	-	-	-	-
Treatment Chemicals, Sludge & Power	36.2	-	-	36.2	-	-	-	-	-	-	-	-	-	-
Other O&M	17.7	9.7	-	8.1	-	-	-	-	-	-	-	-	-	-
Sub-total Expenditures	1,187.9	12.2	-	730.2	-	20.0	-	-	151.3	274.2	-	-	-	-
Capital Investment Plan	498.4	37.5	-	-	-	-	-	-	-	-	-	72.3	388.7	-
Fund Deposits														
R&R and General Fund	85.0	37.5	-	-	-	-	-	-	-	-	-	47.5	-	-
Revenue Bond Construction	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Water Stewardship Fund	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Interest for Construction & Trust Funds	13.6	-	-	-	-	-	-	-	-	-	-	-	13.6	0.1
Increase in Required Reserves	51.2	-	-	11.3	-	-	-	-	2.3	24.5	13.1	-	-	-
Increase in Rate Stabilization Fund	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Sub-total Fund Deposits	149.8	37.5	-	11.3	-	-	-	-	2.3	24.5	13.1	47.5	13.6	0.1
TOTAL USES OF FUNDS	1,836.2	87.2	-	741.5	-	20.0	-	-	153.6	298.7	13.1	119.8	402.2	0.1
SOURCES OF FUNDS														
Receipts														
Taxes	93.7	-	-	-	-	-	-	-	45.1	48.6	-	-	-	-
Annexations	2.5	-	-	-	-	-	-	-	2.5	-	-	-	-	-
Interest Income	52.0	2.4	-	6.2	0.0	0.5	1.4	1.1	3.1	11.6	11.6	0.5	13.6	0.1
Hydro Power	45.1	-	24.0	21.1	-	-	-	-	-	-	-	-	-	-
Fixed Charges (RTS & Capacity Charge)	114.7	-	114.7	-	-	-	-	-	-	-	-	-	-	-
Water Sales Revenue	928.6	-	928.6	-	-	-	-	-	-	-	-	-	-	-
Miscellaneous Revenue	6.3	6.3	-	-	-	-	-	-	-	-	-	-	-	-
Bond Proceeds	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Sub-total Receipts	1,242.9	8.7	1,067.3	27.3	0.0	0.5	1.4	1.1	50.7	60.2	11.6	0.5	13.6	0.1
Fund Withdrawals														
Transfer Fund	20.0	-	-	-	-	20.0	-	-	-	-	-	-	-	-
R&R and General Fund	109.8	37.5	-	-	-	-	-	-	-	-	-	72.3	-	-
Bond Funds for Construction	388.7	-	-	-	-	-	-	-	-	-	-	-	388.7	-
Water Stewardship Fund	0.8	-	-	-	-	-	0.8	-	-	-	-	-	-	-
Decrease in Required Reserves	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Decrease in Rate Stabilization Fund	74.1	-	-	-	-	-	-	-	-	-	74.1	-	-	-
Sub-total Fund Withdrawals	593.3	37.5	-	-	-	20.0	0.8	-	-	-	74.1	72.3	388.7	-
TOTAL SOURCES OF FUNDS	1,836.2	46.2	1,067.3	27.3	0.0	20.5	2.2	1.1	50.7	60.2	85.7	72.8	402.2	0.1
Inter-Fund Transfers	-	41.1	(1,067.3)	714.2	(0.0)	(0.5)	(2.2)	(1.1)	103.0	238.5	(72.6)	46.9	-	-
End of Year Balance	964.8	53.1	-	144.8	0.6	0.7	31.4	25.3	70.7	274.7	237.2	-	125.2	1.2

Totals may not foot due to rounding.

* includes Water Rate Stabilization Fund, Water Treatment Surcharge Stabilization Fund, and the Revenue Remainder Fund