



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

April 14, 2009 Board Meeting

Revised 8-2

Subject

Approve proposed 2009/10 fiscal year budget

Description

The proposed 2009/10 budget reflects the significant input of the Board and member agencies over the past three months. This budget review included three detailed Board Workshops on January 6, February 24, and March 24, 2009. In addition, the budget was discussed and debated at the January 9, February 12, and March 9, 2009 Business and Finance Committee meetings as well as other caucuses and meetings throughout Metropolitan's service area. This unprecedented review process was developed in response to today's economic climate and water supply situation. As a result, the proposed 2009/10 budget expenditures will be \$70.3 million less than the 2008/09 budget. The proposed expenditures shown in Table 1 total \$1.8 billion, including operating expenditures, capital expenditures, and debt service.

Table 1. Budget Summary – Total Expenditures (Dollars in Millions)

	2007/08 Actual	2008/09 Budget	2008/09 Projected	2009/10 Proposed	Change from:	
					2008/09 Budget	2008/09 Projected
Expenditures						
State Water Contract	\$ 464.3	\$ 488.6	\$ 413.2	\$ 478.8	\$ (9.8)	\$ 65.6
Supply Programs	71.9	147.2	80.6	125.5	(21.7)	44.9
Colorado River Power	18.9	45.9	40.0	49.8	3.8	9.8
Debt Service	272.9	313.8	281.9	330.7	17.0	48.8
Demand Management	49.3	53.7	76.4	59.8	6.2	(16.6)
Departmental Operations & Maint. (O&M)	300.3	290.4	295.4	289.3	(1.1)	(6.0)
Treatment Chemicals, Solids & Power	27.4	35.2	33.1	32.8	(2.3)	(0.3)
Other O&M	23.4	23.4	23.5	18.7	(4.8)	(4.8)
Sub-total Expenditures	1,228.4	1,398.2	1,244.0	1,385.5	(12.7)	141.4
Capital Investment Plan	419.4	468.9	399.7	412.1	(56.8)	12.4
TOTAL Expenditures and CIP	\$1,647.8	\$1,867.0	\$1,643.7	\$1,796.7	\$ (70.3)	\$ 153.0

Totals may not foot due to rounding.

ACTIONS TO MANAGE THE BUDGET

In response to both the cost drivers noted above, and the need to meet the Board's priorities, the proposed 2009/10 departmental operations and maintenance (O&M) budget is \$8.2 million less than the 2008/09 budget, and \$11.1 million less than projected O&M expenditures. In order to meet these levels, and to offset rising costs (e.g., health insurance premiums, retirement costs, chemical prices and merit increases), over \$25 million in reduction measures have been taken, including the following actions:

- a. **Labor costs** – The proposed 2009/10 budget does not include an increase in base salaries. Existing agreements with Metropolitan’s bargaining units include a minimum annual increase in base salaries equal to 2 percent (about \$4.2 million). These contracts expire at June 30, 2009 and interest based negotiations have been initiated. The budget includes benefit cost increases, including retirement and medical, of \$2.8 million as well as merit increases and promotions equal to \$4.1 million. This \$6.9 million increase in labor costs due to benefits and promotions is offset by approximately \$3.8 million in reductions resulting from a reduction of 32 positions in the operating and maintenance functions and a hiring freeze that will result in an increase in the vacancy factor of 1 percent to 5.5 percent. The combined effect of increased retirement and medical costs, merit increases and promotions, offset by staff reductions and vacancy rate increases is a \$3.1-million increase in labor costs.
- b. **Reduced conservation outreach and program expenditures** – The 2009/10 budget includes about \$3.8 million for conservation advertising, \$1.1 million less than in the 2008/09 budget. Conservation incentives and administrative costs are budgeted at about \$19.1 million, \$20 million less than the approved expenditures for 2008/09. Given the current water supply conditions, earned media is expected to provide a significant share of the conservation message over the next fiscal year. As a result, this area of Metropolitan’s program has been reduced.
- c. **Reduction in DVL Visitors Center and marina expenditures** – The 2009/10 marina budget has been reduced by \$275,000, reflecting a shift of security from Riverside County Sheriff to Securitas and the concessionaire. The 2009/10 budget includes about \$200,000 for the Visitors Center at Diamond Valley Lake, a reduction of about \$150,000. This reflects Metropolitan’s efforts to partner with another enterprise to operate the Center and Marina and/or take other actions to reduce ongoing costs at the Center.
- d. **Operating Equipment** – Operating equipment expenditures will be reduced by \$3.8 million from the 2008/09 budget of \$9 million. Staff will work to evaluate need and make optimal use of equipment that has experienced lower utilization and replace the oldest, least reliable equipment.
- e. **Chemicals, Solids, and Power** – The 2009/10 budget includes reduced expenditures for chemicals used in the treatment process and solids handling based sales of 1.9 million acre-feet. Lower flows are expected to be observed at the treatment facilities due to these demand reductions. In addition to lower flows, Metropolitan will work with vendors to obtain more favorable pricing given current economic conditions (although chemical prices are still higher than in 2008/09.) In total these actions result in a \$2.4-million reduction to the budget compared to the budget presented in January.
- f. **Travel, Training, and Conferences** – All “discretionary” activities have been reviewed, including staff travel, outside services and board inspection trips to ensure that only critical functions are in the budget. Travel, training, and conference expenses are down \$0.8 million compared to the 2008/09 budget, while inspection trips are budgeted at \$438,000, a reduction of \$192,000 from 2008/09.
- g. **Budget Contingency and Insurance** – The 2009/10 budget does not include a budget contingency, which would normally be set at \$3.5 million to provide flexibility to deal with unexpected costs during the course of the fiscal year. Employment practices liability insurance, an insurance category discussed with the Board, but not currently held by Metropolitan, will not be purchased. This, along with a reduction in the budget for insurance premiums reduces the 2009/10 proposed budget by an additional \$300,000.
- h. **Outside Services** – The 2009/10 budget represents an overall reduction in outside services, including conservation administration costs, of about \$2.2 million. Included within this budget are Professional Services of \$16.6 million, about \$2.7 million lower than the 2008/09 projected and \$0.6 million lower than the 2008/09 budget. In addition to these reductions, staff will be negotiating with service providers for reductions in contract costs in light of current economic conditions to realize additional savings during the course of the fiscal year.

A summary of the operating and maintenance budget is provided in Table 2 below.

Table 2. Budget Summary – Operations and Maintenance

	2007/08 Actual	2008/09 Budget	2008/09 Projected	2009/10 Proposed	Change from:	
					2008/09 Budget	2008/09 Projected
Salaries & Benefits	201,483,200	201,593,800	203,312,500	204,714,300	3,120,500	1,401,800
Chemicals, Solids, and Power*	27,439,700	35,163,000	33,133,400	32,837,200	(2,325,800)	(296,200)
Outside Services	33,633,700	38,867,800	41,009,200	36,695,900	(2,171,900)	(4,313,300)
Materials & Supplies	19,567,142	21,075,300	21,962,100	21,457,400	382,100	(504,700)
Cargill Settlement	10,348,000	1,604,900	4,755,000	1,604,900	-	(3,150,100)
Other	50,604,747	41,714,300	38,880,750	38,271,335	(3,442,965)	(609,415)
Operating Equipment	7,988,900	9,008,600	7,000,000	5,252,800	(3,755,800)	(1,747,200)
Total	351,065,389	349,027,700	350,052,950	340,833,845	(8,193,855)	(9,219,105)
Total Budgeted Positions	2,069	2,052	2,052	2,019	(33)	(33)

* Costs associated with treatment plants only.

FY 2009/10 BUDGET SUMMARY

As summarized in Table 1, the proposed 2009/10 expenditure budget totals \$1.8 billion. This is about \$70 million less than the 2008/09 budget. Proposed 2009/10 expenditures are expected to be about \$153 million greater than projected 2008/09 expenditures. Metropolitan has lost a substantial portion of its State Water project (SWP) water allocation because of the critically dry conditions and the regulatory cutback in SWP deliveries.

Metropolitan is anticipating increased diversions of about 150,000 acre-feet from the Colorado River compared to the 2008/09 budget.

In order to meet the challenge of providing reliable, high quality water at reasonable rates, projects in the Capital Investment Plan (CIP) were prioritized and scheduled with resources applied toward those deemed most critical. As a result, the projection for expenditures on the capital program for fiscal year 2009/10 is \$412.1 million, or \$56.8 million lower than the 2008/09 budget. Continuing to meet the financing requirements of the ongoing CIP will nonetheless result in an increase in debt service of \$17 million compared to the 2008/09 budget. For fiscal year 2009/10, the CIP includes over 330 active projects in 65 programs with approximately 25 major construction contracts.

In the area of operations and maintenance (O&M), the total 2009/10 budget is about \$8.2 million lower compared to the \$349 million 2008/09 budget. This would be the third year that O&M expenditures would have remained at approximately \$350 million. This information is discussed more fully in the 2009/10 Proposed Budget Summary (Attachment 1). There are three primary cost drivers in 2009/10:

- a. **Debt Service** – As Metropolitan funds its ongoing CIP, debt service continues to rise. It is projected that debt service in 2009/10 will be \$330.7 million, or \$48.8 million greater than projected in 2008/09 (and about \$17.0 million higher than budgeted in 2008/09). There are three reasons for this increase: (1) increased debt for the ongoing capital program; (2) higher interest rates on fixed rate debt and higher cost for liquidity for the variable rate program; and (3) a shift in principal payments from the 2008/09 fiscal year to 2009/10 as bonds were refunded in 2008.
- b. **State Water Project Costs** – The cost for the State Water Project continues to rise, even in the face of lower deliveries. The State Water Contract is a “take-or-pay” contract, and Metropolitan is obligated to

pay the capital and operating costs, even if no water is delivered. In 2009/10, the cost of the project is estimated to be \$478.8 million, \$65.6 million more than projected for 2008/09. Included in the cost estimates are more than \$14 million to finance the environmental and preliminary engineering for the long-term infrastructure necessary to improve reliability in the Delta, along with \$4.7 million for actions to help address species in the Delta.

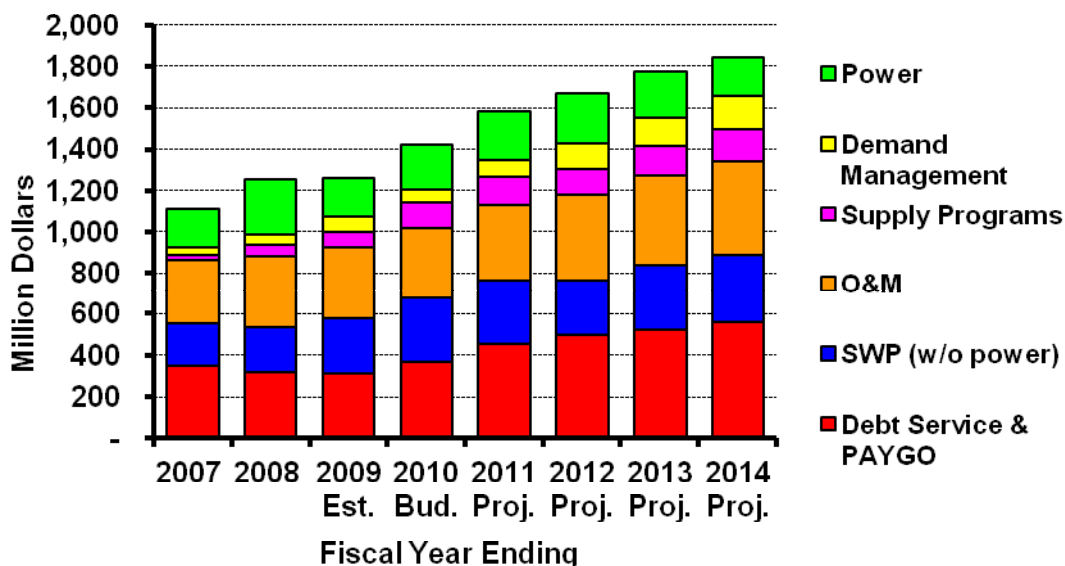
- c. **Water Supply Programs** – Due to the reductions in Metropolitan’s Colorado River supplies in 2003 and the continuing pressures on its State Water Project supplies due to hydrology and pumping restrictions imposed to protect endangered fish (e.g., Delta smelt), Metropolitan has been developing alternative supply sources including water transfers and exchanges. The cost of these programs is expected to be \$125.5 million in 2009/10, \$44.9 million higher than projected expenditures in 2008/09. This budget item includes \$26.2 million for the purchase of water through the State Drought Water Bank in calendar years 2009 and 2010, along with ongoing purchases from existing programs such as Kern Delta, Semitropic, the conservation program with the Imperial Irrigation District, and an expansion of the Palo Verde Irrigation District Land Management Program. Projected expenditures in 2008/09 are lower than budget, reflecting a reduction in projected payments to the San Bernardino Valley Municipal Water District and a shift in payment for reduced deliveries of water from the Drought Water Bank from 2008/09 to 2009/10.

Capital Funding – Ongoing investments in Metropolitan’s infrastructure will total about \$412.1 million. This is \$56.8 million less than the 2008/09 budget, reflecting changes in project scheduling. The 2009/10 budget includes the issuance of an additional \$550 million of fixed rate bonds over the course of fiscal year 2009/10, with \$130.3 million of the bond proceeds deposited into the construction fund to enable the program to move forward beyond the end of the fiscal year. This deposit is reflected in the budget summary, although the funds will not be expended until the following fiscal year.

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 four years. From 2006/07 through 2013/14, expenditures are forecast to increase by about \$731 million, or about 7.5 percent annually. The primary cost drivers from 2009/10 to 2013/14 are a \$196-million increase in debt service and PAYG expenditures, a \$102-million increase in demand Management costs, a \$112-million increase in O&M, and a \$25-million increase in supply program costs.

Figure 1. Seven-year Expenditure Trend



USES OF FUNDS

Total cash outlays for State Water Contract (SWC) payments, supply programs, Colorado River Aqueduct (CRA) power, debt service, demand management programs, O&M, and the CIP are budgeted at \$1.79 billion. This is \$69.5 million (3.7 percent) less than the 2008/09 budget and \$153.8 million (9.3 percent) greater than projected. About \$36.7 million of water revenues will be deposited to the Replacement and Refurbishment fund to pay for a portion of this work in the CIP. This is \$58.3 million less than budgeted for 2008/09. Given the challenges associated with rising rates and an uncertain water supply period, it is prudent to take action to preserve reserve funds and temporarily reduce Pay-As-You-Go (PAYGO) funding.

SOURCES OF FUNDS

As shown in Table 3, 2009/10 sources of funds will total \$2.03 billion. This includes receipts of \$1.9 billion, with water sales receipts of \$1.08 billion accounting for 57 percent of receipts. These receipts are based on projected water sales of 1.9 million acre-feet and include an assumed increase in rates and charges of 19.7 percent, effective September 1, 2009. Other revenues include readiness-to-serve charge revenues of \$103.0 million, revenues from the capacity charge of \$33.3 million, and tax and annexation revenues of about \$91.4 million. Interest earnings are expected to be \$34.2 million, or about \$8.8 million lower than the 2008/09 budget, reflecting lower estimated fund balances. Power and other miscellaneous receipts are expected to generate about \$32.9 million.

Capital projects will be funded from a combination of existing bond funds and revenues. Revenues will be used to fund about \$36.7 million of the capital costs. In addition, existing bond funds will provide \$375.4 million toward the CIP. With a 19.7-percent overall increase in base rates and charges on September 1, 2009, about \$87.6 million would still be drawn from the Revenue Remainder Fund, Water Stewardship Fund, and Water Rate Stabilization Fund.

FINANCIAL RATIOS

The revenue bond debt service coverage ratio is forecasted to be lower than the target of 2 times revenue bond debt service. Depending on the actual increase in rates and charges, the debt service coverage ratio is expected to be about 1.5 times in 2009/10. This ratio is expected to increase over the next two years to 2.0 as water revenues increase and anticipated water rate increases are implemented.

RESERVES

Based on projected receipts and expenditures, it is estimated that the total balance in the Water Rate Stabilization, Revenue Remainder, and Water Stewardship funds will be about \$186.5 million on June 30, 2010, about \$45.2 million under the minimum reserve level and below the Board's reserve policy guidelines.

Attachment 1, FY 2009/10 Proposed Budget Summary, discusses the sources of funds, including receipts and fund withdrawals, and uses of funds, including expenditures and fund deposits, in more detail.

Table 3. 2008/09 Annual Budget Uses and Sources of Funds – Cash Basis (Dollars in Millions)

	2007/08 Actual	2008/09 Budget	2008/09 Projected	2009/10 Proposed Budget	2009/10 Proposed Budget Compared	
					2008/09 Budget	2008/09 Projected
USES OF FUNDS						
Expenditures						
State Water Contract	\$ 464.3	\$ 488.6	\$ 413.2	\$ 478.8	\$ (9.8)	\$ 65.6
Supply Programs (1)	71.9	147.2	80.6	125.5	(21.7)	44.9
Colorado River Power	18.9	45.9	40.0	49.8	3.8	9.8
Debt Service	272.9	313.8	281.9	330.7	17.0	48.8
Demand Management	49.3	53.7	76.4	59.8	6.2	(16.6)
Departmental O&M	300.3	290.4	295.4	289.3	(1.1)	(6.0)
Treatment Chemicals, Solids & Power	27.4	35.2	33.1	32.8	(2.3)	(0.3)
Other O&M	23.4	23.4	23.5	18.7	(4.8)	(4.8)
Sub-total Expenditures	1,228.4	1,398.2	1,244.0	1,385.5	(12.7)	141.4
Capital Investment Plan	419.4	468.9	399.7	412.1	(56.8)	12.4
Fund Deposits						
R&R and General Fund	42.9	95.0	30.0	36.7	(58.3)	6.7
Revenue Bond Construction	-	-	-	130.3	130.3	130.3
Water Stewardship Fund	-	-	-	-	-	-
Interest for Construction & Trust Funds (2)	19.4	4.6	3.4	0.0	(4.6)	(3.4)
Increase in Required Reserves	77.0	23.2	45.8	61.3	38.0	15.4
Increase in Rate Stabilization Fund	-	-	-	-	-	-
Sub-total Fund Deposits	139.3	122.9	79.3	228.3	105.4	149.0
TOTAL USES OF FUNDS	\$ 1,787.1	\$ 1,989.9	\$ 1,723.0	\$ 2,025.8	\$ 35.9	\$ 302.9
SOURCES OF FUNDS						
Receipts						
Taxes	\$ 97.7	\$ 94.4	\$ 95.8	\$ 90.4	\$ (3.9)	\$ (5.3)
Annexations	2.7	2.5	1.0	1.0	(1.5)	-
Interest Income	64.9	43.0	33.2	34.2	(8.8)	1.0
Hydro Power	41.1	35.2	24.4	24.1	(11.2)	(0.3)
Fixed Charges (RTS & Capacity Charge)	114.0	119.7	119.7	136.3	16.7	16.6
Water Sales Revenue	967.8	1,022.1	976.0	1,078.6	56.5	102.6
Miscellaneous Revenue	7.1	7.1	7.1	8.8	1.7	1.7
Bond Proceeds and Reimbursements	29.2	272.7	195.6	528.0	255.3	332.4
Sub-total Receipts	1,324.4	1,596.7	1,452.8	1,901.5	304.8	448.7
Fund Withdrawals						
Water Transfer Fund	19.8	7.8	9.2	-	(7.8)	(9.2)
R&R and General Fund	65.2	95.0	30.0	36.7	(58.3)	6.7
Bond Funds for Construction (3)	325.7	110.0	185.8	-	(110.0)	(185.8)
Water Stewardship Fund	5.9	15.1	23.9	0.9	(14.3)	(23.0)
Decrease in Required Reserves (4)	-	101.5	-	29.9	(71.5)	29.9
Decrease in Rate Stabilization Fund (5)	46.1	63.8	21.4	56.8	(7.0)	35.4
Sub-total Fund Withdrawals	462.7	393.3	270.2	124.3	(268.9)	(145.9)
TOTAL SOURCES OF FUNDS	\$ 1,787.1	\$ 1,989.9	\$ 1,723.0	\$ 2,025.8	\$ 35.9	\$ 302.9

(1) 2007/08 exclude \$28.7M for Drop 2 paid from the R&R Fund

(2) 2007/08 includes \$1.0M of interest for the WTF

(3) 2008/09 includes \$60 million from Proposition 50.

(4) 2009/10 Budget is expected to draw down the Revenue Remainder Fund \$29.9 million, \$45.2 million below the required minimum reserve.

(5) 2009/10 Budget is expected to draw down the Water Rate Stabilization Fund to zero, with an \$56.8 million withdrawal.

Totals may not foot due to rounding.

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 2009/10 Budget;
- b. Appropriate \$1.05 billion 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;
- c. Appropriate as continuing appropriations, \$330.7 million for 2009/10 debt service on Metropolitan general obligation and revenue bonds;
- d. Authorize the use of \$36.7 million in operating revenues to fund Replacement and Refurbishment expenditures in 2009/10; and
- e. Authorize the use of \$30 million in operating revenues to fund Replacement and Refurbishment expenditures in 2008/09.

Fiscal Impact: \$1.42 billion in FY 2009/10

Business Analysis: Funds are necessary for the continuing business operations of Metropolitan.

Option #2

Adopt the CEQA determination and approve the 2009/10 Budget with changes as recommended by the Board.

Fiscal Impact: Impact depends on adopted changes.

Business Analysis: Funds are necessary for the continuing business operations of Metropolitan.

Staff Recommendation

Option #1



Brian G. Thomas
Chief Financial Officer

4/7/2009

Date



Jeffrey Kightlinger
General Manager

4/7/2009

Date

Attachment 1 – FY 2009/10 Proposed Budget Summary

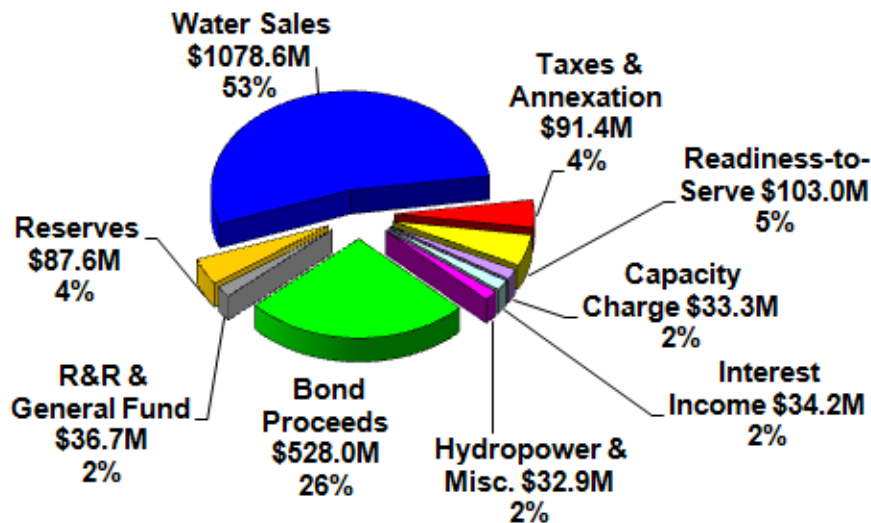
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Budget Summary

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, by contrast, recognize revenues and expenses in the period they are earned and incurred regardless of whether cash has been received or disbursed.

Figure 1. 2009/10 Sources of Funds (\$2.03 billion dollars)



SOURCES OF FUNDS

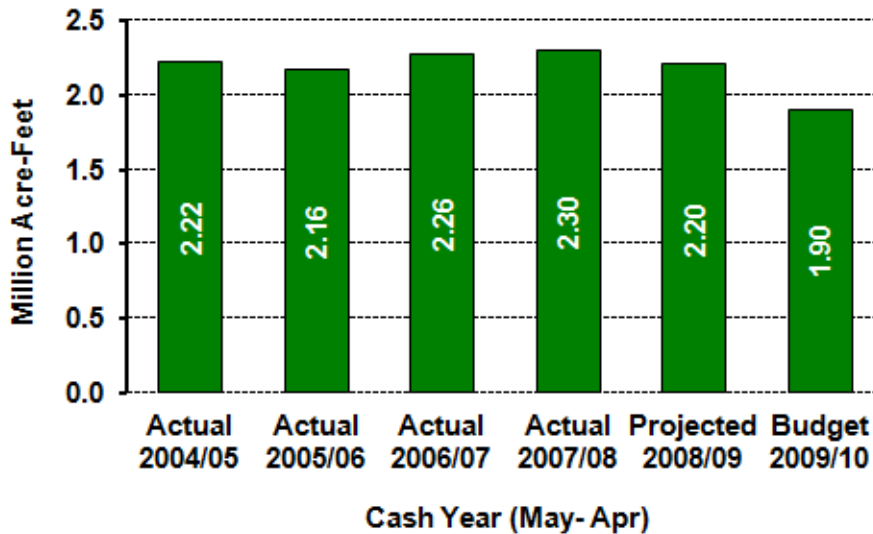
Estimated receipts from water sales, the readiness-to-serve (RTS) charge, the capacity charge, taxes, annexation fees, interest income, power recoveries, and other miscellaneous income are projected to be \$1.37 billion for fiscal year 2009/10 and constitute the major revenue sources for Metropolitan. This is \$49.5 million more than the 2008/09 Budget. The increase in revenues is due to increases in water rates in 2009 and 2010. Figure 1 shows the major sources of funds. Summaries of sources and uses of funds are shown in Tables 6 and 7 at the end of this section. A description of each revenue source is included in the Glossary of Terms.

Water Sales

Receipts from water sales are budgeted at \$1,078.6 million and are based on rates and charges adopted by the Board for January 1, 2009 and an increase in base rates and charges of 19.7 percent on September 1, 2009.

These rates do not fully recover the cost-of-service and additional draws from reserves are expected to meet necessary expenditures in 2009/10.

Figure 2. Five-Year Trend of Water Sales



Water sales for 2009/10 are estimated to be 1.90 million acre-feet (MAF) during the May through April period (cash year).

The 2009/10 cash year water sales include 1.75 MAF of firm sales, zero replenishment sales, 56 thousand acre-feet (TAF) of agricultural sales, and 52 TAF of exchanges under the San Diego County Water Authority (SDCWA) Exchange Agreement for the SDCWA/Imperial Irrigation District (IID) transfer and 45 TAF of water for the All American & Coachella Canal Lining Project. Treated sales are estimated to be 1.12 MAF or 59 percent of total sales. Figure 2 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 State Water Contract (SWC), are estimated to be \$91.4 million.

Capacity and Readiness-to-Serve Charges

The Capacity Charge and Readiness-to-Serve Charge for 2009/10 are estimated to generate \$103.0 million and \$33.3 million, respectively, or \$16.7 million more in total than in the 2008/09 budget.

Other Revenue

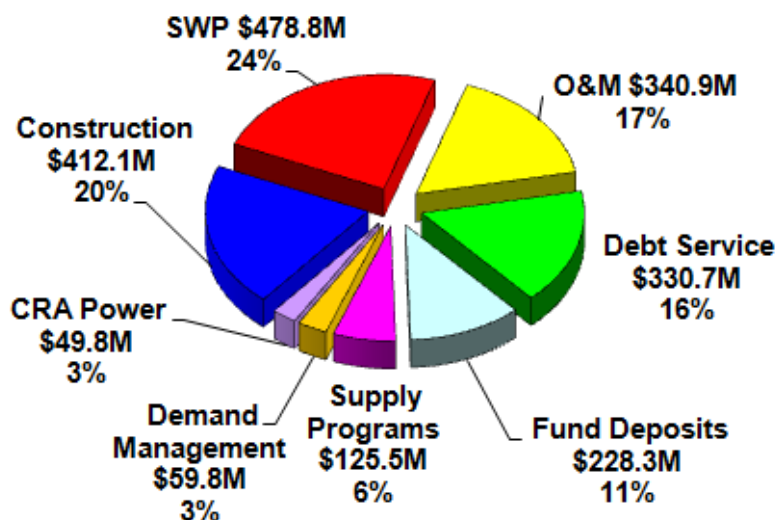
Interest earnings are estimated to total \$34.2 million, including trust accounts and construction funds. This represents an \$8.8 million decrease from the 2008/09 Budget due primarily to lower estimated fund balances. Receipts from hydroelectric and Colorado River Aqueduct (CRA) power sales are estimated to be \$24.1 million, lower by \$11.2 million due to lower hydroelectric generation from the lower water deliveries and higher flows on the CRA resulting in lower sales of supplemental power.

Other Sources

To meet the on-going funding requirements of the CIP, Metropolitan plans to issue \$550 million of fixed rate bonds in 2009/10. These bonds are expected to generate \$505.6 million in bond proceeds of which \$375.4 million will be used to fund the CIP in

2009/10. The remaining CIP funding requirements will be met from current operating funds (i.e., \$36.7 million from the Replacement & Refurbishments (R&R) and General Funds). In 2009/10, a total of \$2.03 billion will be available for expenditures and other obligations.

Figure 3. 2009/10 Uses of Funds (\$2.03 billion dollars)



USES OF FUNDS

Total uses of funds are \$2.03 billion. Figure 3 shows the breakdown of expenditures and other obligations that make up the Uses of Funds for 2009/10.

Colorado River Aqueduct Power

CRA power costs are projected to be \$49.8 million based on pumping 1.04 MAF at Whitsett Intake Pumping Plant. This is \$3.8 million more than the 2008/09 budget, which included the diversion of 882 TAF. This increase from the 2008/09 budget reflects the higher pumping volumes.

State Water Contract

State Water Contract (SWC) expenditures of \$478.8 million are budgeted to be \$9.8 million less than the current year's budget.

SWC power costs are expected to be \$168.6 million or \$47.5 million lower than the 2008/09 Budget and include the cost for pumping about 846 TAF. The average unit cost of SWC power is expected to be about \$199 per acre-foot.

SWC minimum operations, maintenance, power, and replacement charges are

\$34.6 million higher than the 2008/09 Budget. Capital charges are expected to be \$3.1 million higher than the 2008/09 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 61 water-recycling projects. Fifty-five of these projects are in operation and the remaining six projects are under design or construction. Recycling projects that receive Metropolitan contributions are expected to produce 165 TAF of recycled water, principally for landscape irrigation, groundwater recharge, and industrial uses. In 2009/10, Metropolitan is expected to spend \$27.4 million on these efforts. In addition, as part of the Board approved 5-yr Supply Plan, the 2009/10 Budget includes \$2.3 million to support private recycling projects and to directly fund new local resource facilities. These efforts are expected to produce an additional 5 TAF in 2009/10.

Metropolitan has also entered into agreements to provide financial assistance to 24 projects to recover contaminated groundwater. Twenty-one of these groundwater recovery projects are in operation and are expected to produce about 57 TAF in 2009/10 at a cost to Metropolitan of \$10.4 million.

The Conservation Credits Program (CCP) provides financial assistance to customers in Metropolitan's service area for water conservation programs. The 2009/10 budget contains \$19.1 million for the CCP to provide rebate funding for residential, commercial, industrial, and landscape conservation activities. This budget includes \$5.0 million for the recently created Accelerated Public Sector Water Efficiency Partnership

Demonstration Program which provides enhanced incentives for a limited time to public agencies to encourage retrofitting old fixtures and equipment for more water efficient ones.

OPERATIONS AND MAINTENANCE

The 2009/10 Proposed O&M Budget, including operating equipment purchases, is estimated to be \$340.9 million. This is \$8.2 million less than the 2008/09 budget of \$349.0 million and \$11.1 million less than the current year projected expenditures. The O&M budget is the result of significant management efforts to reduce costs while meeting the Board's priorities.

Labor costs, not including those charged to construction, are \$204.7 million, which is \$3.1 million, or 1.5 percent higher than the 2008/09 Budget of \$201.6 million. This increase is primarily to account for a projected increase in CalPERS employer contributions totaling about \$2.8 million. Merit increases and promotions of \$4.1 million were largely offset by \$3.8 million in cuts achieved by reducing 32 regular and temporary O&M positions and increasing vacancy rates to reflect a hiring freeze. No base salary increase was included in the 2008/09 budget pending completion of bargaining unit negotiations. Had current bargaining unit MOU provisions been used, labor costs would have increased by an additional \$4.2 million.

Further O&M reductions include: \$3.8 million in operating equipment purchases, elimination of the \$3.5 million budget contingency, a \$2.4 million decrease in variable water treatment costs due to reduced treated water sales, a \$2.2 million decrease in outside services, and a \$1.1 million decrease in conservation advertising. Additional cuts have been made to sponsorships, inspection trips, recreation at Diamond Valley Lake, travel, training, and insurance premiums.

A summary of the 2009/10 O&M Budget is shown in Table 1.

Figure 4 provides the distribution of departmental O&M by organization.

Including variable treatment costs, the Water System Operations Group (WSO) accounts for 56 percent of the total departmental budget.

Figure 5 summarizes the total departmental budget by expenditure type, of which 63 percent is for salaries and benefits.

Table 1. 2009/10 Operations & Maintenance Annual budget (dollars)

Departmental Units	2007/08 Actual	2008/09 Budget	2008/09 Projected	2009/10 Proposed Budget	Change			
					2009/10 to 2008/09 Budget	%	2009/10 to 2008/09 Projected	%
Office of the General Manager	\$ 8,835,000	\$ 8,403,700	\$ 8,576,900	\$ 7,815,600	\$ (588,100)	(7.0%)	\$ (761,300)	(8.9%)
Water Systems Operations w/o Variable Treatment	157,859,100	154,896,700	157,621,500	159,273,500	4,376,800	2.8%	1,652,000	1.0%
Water Resource Management	19,541,800	19,086,000	21,819,800	19,680,200	594,200	3.1%	(2,139,600)	(9.8%)
Corporate Resources	59,048,500	62,321,600	62,166,500	59,819,300	(2,502,300)	(4.0%)	(2,347,200)	(3.8%)
Real Property Development & Mgmt	10,722,500	12,007,400	11,982,300	11,250,700	(756,700)	(6.3%)	(731,600)	(6.1%)
Human Resources	11,197,300	11,453,500	11,631,700	10,843,900	(609,600)	(5.3%)	(787,800)	(6.8%)
Office of the Chief Financial Officer	7,609,600	7,839,200	7,996,200	7,837,400	(1,800)	(0.0%)	(158,800)	(2.0%)
External Affairs	18,503,800	20,537,000	20,077,600	18,236,700	(2,300,300)	(11.2%)	(1,840,900)	(9.2%)
Subtotal - General Manager's Dep.	293,317,600	296,545,100	301,872,500	294,757,300	(1,787,800)	(0.6%)	(7,115,200)	(2.4%)
General Counsel	9,235,600	10,165,000	10,161,600	10,165,000	-	0.0%	3,400	0.0%
General Auditor	2,715,400	2,719,000	2,719,000	2,719,000	-	0.0%	-	NA
Ethics Office	594,400	613,000	604,300	609,600	(3,400)	(0.6%)	5,300	0.9%
Overhead Credit from Construction	(19,169,400)	(19,622,700)	(20,000,000)	(18,921,300)	701,400	(3.6%)	1,078,700	(5.4%)
Total Departmental Budget	286,693,600	290,419,400	295,357,400	289,329,600	(1,089,800)	(0.4%)	(6,027,800)	(2.0%)
Other O&M								
Cargill Settlement (1)	10,348,000	1,604,900	4,755,000	1,604,900	-	NA	(3,150,100)	(66.2%)
PC Replacement	2,152,000	-	-	-	-	NA	-	NA
Performance Programs	551,800	690,800	600,000	650,000	(40,800)	(5.9%)	50,000	8.3%
Association Dues	2,165,600	1,875,000	2,166,800	2,180,000	305,000	16.3%	13,200	0.6%
Contingency	-	1,300,000	-	-	(1,300,000)	(100.0%)	-	NA
Insurance	12,527,589	8,000,000	8,000,000	8,000,000	-	NA	-	NA
Leases	504,200	446,000	456,000	472,600	26,600	6.0%	16,600	3.6%
Taxes	691,000	520,000	520,000	530,400	10,400	2.0%	10,400	2.0%
Subtotal - Other	28,940,189	14,436,700	16,497,800	13,437,900	(998,800)	(6.9%)	(3,059,900)	(18.5%)
TOTAL OPERATIONS & MAINTENANCE	315,633,789	304,856,100	311,855,200	302,767,500	(2,088,600)	(0.7%)	(9,087,700)	(2.9%)
Operating Equipment	7,988,900	9,008,600	7,000,000	5,252,800	(3,755,800)	(41.7%)	(1,747,200)	(25.0%)
Variable Treatment	27,442,700	35,163,000	33,133,400	32,837,200	(2,325,800)	(6.6%)	(296,200)	(0.9%)
GRAND TOTAL	\$ 351,065,389	\$ 349,027,700	\$ 351,988,600	\$ 340,857,500	\$ (8,170,200)	(2.3%)	\$ (11,131,100)	(3.2%)

Totals may not foot due to rounding

(1) 2008/09 projected includes approximately \$3 million for attorney fees resulting from the PERS settlement.

Figure 4. 2009/10 Departmental Budget by Organization
 (without overhead credit, \$345.1 million)

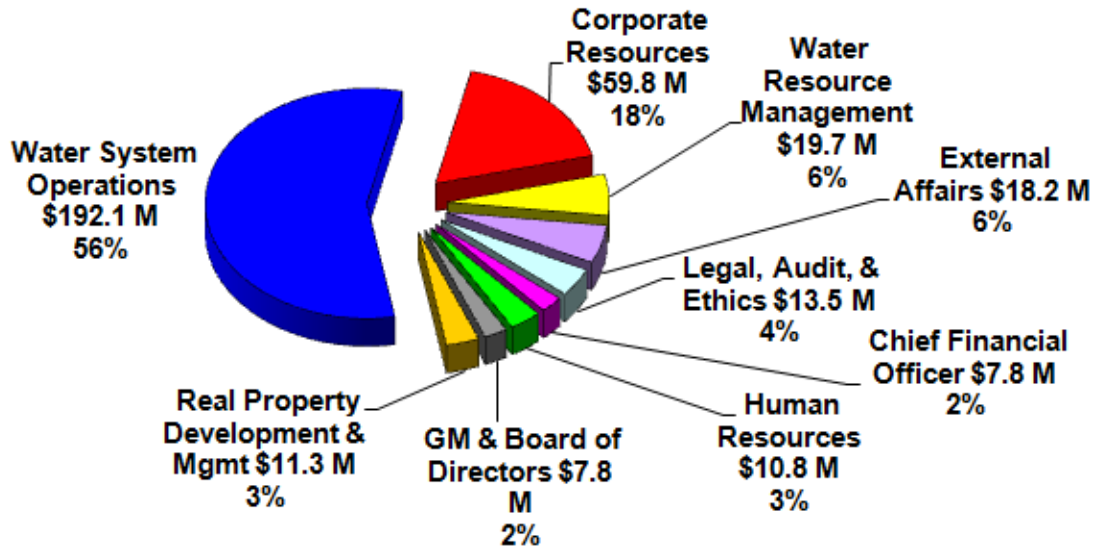
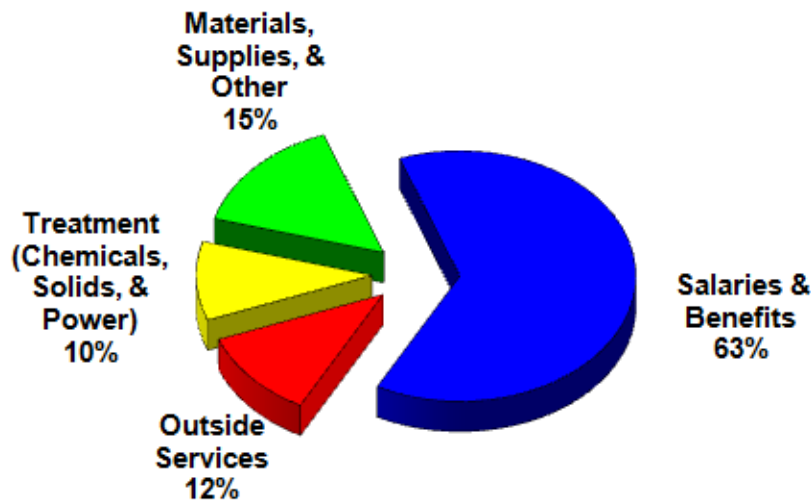


Figure 5. 2009/10 Departmental Budget by Expenditure Type



LABOR

The total personnel complement (including temporary workers) for 2009/10 is 2,019 positions, down 33 positions from 2008/09. O&M personnel are down by 32 full-time-equivalent (FTE) positions to 1,662. Positions dedicated to capital work are down by 1. The

personnel complement is broken down on Tables 3 and 4. The O&M budget includes an increased vacancy rate of about 5.5 percent (compared to the 4.5% vacancy rate in the 2008/09 budget).

Table 2. Regular and Temporary Positions

	2006/07 Budget	2007/08 Budget	2008/09 Budget	2009/10 Proposed Budget	Change from 2008/09
Regular Full Time Positions	2,024	2,021	2,021	2,000	-21
District Temporary Positions	35	39	23	16	-7
Agency Temporary Positions	11	9	8	3	-5
Total	2,070	2,069	2,052	2,019	-33

Table 3. O&M and Capital Staffing Levels

	2008/09			2009/10		
	O&M	Capital	Total	O&M	Capital	Total
Regular Full Time Positions	1,671	350	2,021	1,643	357	2,000
District and Agency Temporary Positions	23	8	31	19	-	19
Total	1,694	358	2,052	1,662	357	2,019

Supply Programs

Major supply program expenditures for 2009/10 are estimated to be \$125.5 million and include:

- \$37.9 million for the Palo Verde Irrigation District (PVID) Land Management Program;
- \$26.2 million for the Drought Water Bank;
- \$17.0 million for Colorado Programs;
- \$14.6 for the Semitropic Groundwater Storage and Exchange Program;
- \$11.0 million for In-Basin Projects;
- \$9.7 million for operating and maintaining the IID/MWD conservation agreement;
- \$5.8 million for the Arvin-Edison Storage Program;
- \$2.8 million for the Kern Delta Program (deferred from 2006/07); and
- \$0.5 million for other northern California transfers.

These storage programs are expected recover 251 TAF of previously stored groundwater supplies and generate 482 TAF of transfer water, after accounting for losses through the Delta.

ANNUAL CAPITAL INVESTMENT PLAN

The Capital Investment Plan (CIP) for 2009/10 is estimated to be \$412.1 million and 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 Capital Investment Plan section of the 2009/10 Proposed Budget book.

The 2009/10 CIP is \$56.8 million lower than in 2008/09. Major CIP projects in design and/or construction include:

- \$185.0 million for improvements to Metropolitan's five treatment plants, including the Oxidation Retrofit Program (ORP) and the Treatment Plant Improvements Program;
- \$93.7 million for 156 R&R projects;
- \$49.6 million for the Inland Feeder project; and
- \$13.4 million for the Hayfield Groundwater Storage Program.

The projects listed above account for 83 percent of the total 2009/10 CIP expenditures. Figure 5 shows the major project categories in the 2009/10 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 2009/10 expenditure plan by major service function is shown in Figure 6.

Figure 5. 2009/10 Capital Investment Plan by Major Project Category

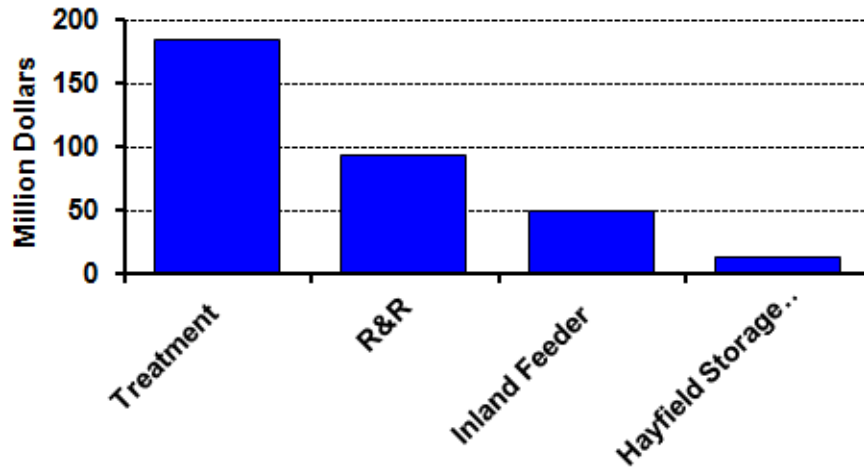
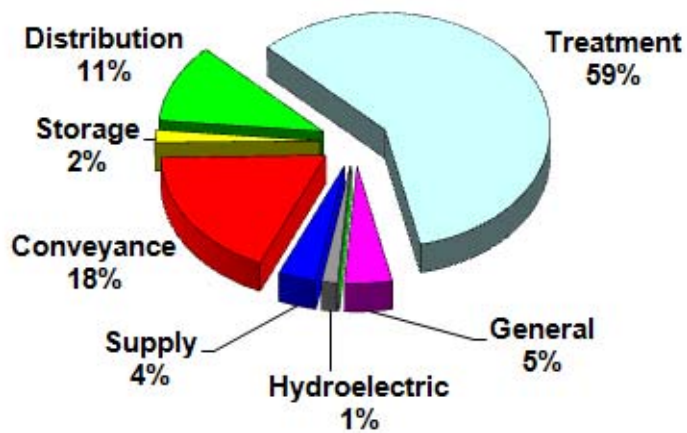


Figure 6. 2009/10 Capital Investment Plan by Service Function



Cash Funded Capital

The 2009/10 CIP includes Replacement & Refurbishment (R&R) and other projects (funded from General Fund) totaling \$118.3 million. The combined cash financing from operating revenues for the R&R and General Fund will total \$36.7 million. In order to ensure a reliable delivery system, the remaining \$81.6 million of R&R will be funded from bond proceeds.

Debt Service

The portion of the CIP that is not funded from cash will be funded from bond proceeds. In 2009/10, \$358.0 million of capital will be funded with bond proceeds. Debt service payments are budgeted to be \$330.7 million and include \$48.5 million in G.O. bond debt service, \$267.5 million in revenue bond debt service, \$12.2 million in variable rate debt administration costs (liquidity, remarketing fees, and broker-dealer fees), and \$2.6 million for State Revolving Fund Loan payments. Total debt service costs are \$17.0 million more than the 2008/09 Budget.

Metropolitan currently has \$4.6 billion in outstanding debt. Of this amount, \$4.4 billion is revenue bond debt, of which 23 percent is in a variable rate mode.

Over the next five years, it is expected that an additional \$1.34 billion in debt will be issued to fund the CIP. The cost of debt over this period is assumed to be 2.5 percent and 5.0 percent for variable rate and fixed rate debt, respectively.

Reserve Transfers

The 2009/10 budget will require use of \$87.6 million of reserves plus the 19.7% rate increase in September 2009. The Water Rate Stabilization Fund (WRSF) is expected to be drawn down to zero with the use of \$56.8 million. In addition, the Revenue Remainder Fund is expected to be drawn down \$29.9 million and the Water Stewardship Fund (WSF) is expected to be drawn down to zero with the use of \$0.9 million.

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 6. Fund balances are budgeted to be \$1,044.1 million at June 30, 2010. Of that total, \$823.9 million is restricted by bond covenants, contracts, or board policy, and \$220.0 million is unrestricted. Table 4 shows a breakdown of reserves by fund type. Figure 7 shows the distribution of funds by type.

The minimum and maximum reserve fund targets are estimated to be \$231.7 million and \$565.3 million, respectively, at June 30, 2010. Based on projected receipts and expenditures, it is estimated that the balance in the WRSF, Revenue Remainder Fund, and WSF will total about \$186.5 million, about \$45.2 million less than the minimum target.

Table 4. Projected Fund Balances at June 30, 2010 (dollars in millions)

	Restricted		Unrestricted	Total
	Contractual	Board		
Operating Funds	238.3	106.7		345.0
Debt Service Funds	332.0			332.0
Construction Funds	145.8		33.8	179.5
Reserve Funds*			186.5	186.5
Water Transfer Fund		-		-
Trust and Other Funds	1.2			1.2
Total	717.2	106.7	220.2	1,044.1

* includes Water Rate Stabilization Fund and the Revenue Remainder Fund
 Totals may not foot due to rounding.

Figure 7. Fund Distribution by Type at June 30, 2010

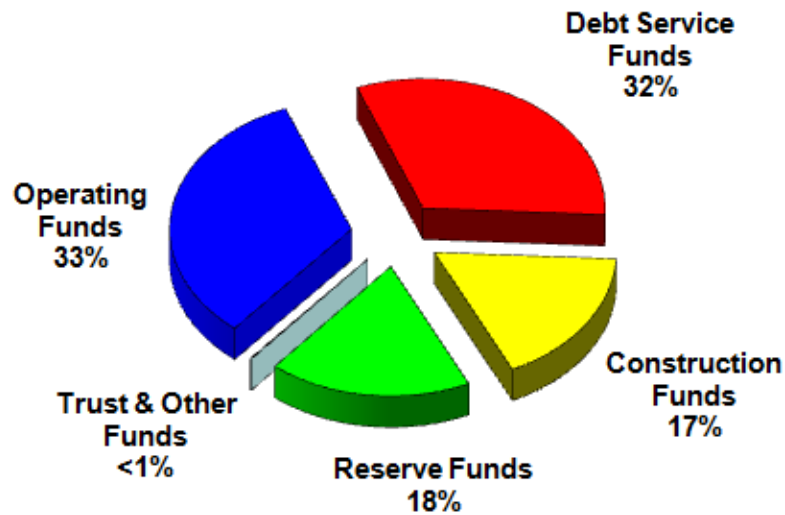


Table 5. 2009/10 Budget Sources and Uses of Funds (dollars in millions)

	2007/08 Actual	2008/09 Budget	2008/09 Projected	2009/10 Proposed Budget	2009/10 Proposed Budget Compared	
					2008/09 Budget	2008/09 Projected
USES OF FUNDS						
Expenditures						
State Water Contract	\$ 464.3	\$ 488.6	\$ 413.2	\$ 478.8	\$ (9.8)	\$ 65.6
Supply Programs (1)	71.9	147.2	80.6	125.5	(21.7)	44.9
Colorado River Power	18.9	45.9	40.0	49.8	3.8	9.8
Debt Service	272.9	313.8	281.9	330.7	17.0	48.8
Demand Management	49.3	53.7	76.4	59.8	6.2	(16.6)
Departmental O&M	300.3	290.4	295.4	289.3	(1.1)	(6.0)
Treatment Chemicals, Solids & Power	27.4	35.2	33.1	32.8	(2.3)	(0.3)
Other O&M	23.4	23.4	23.5	18.7	(4.8)	(4.8)
Sub-total Expenditures	1,228.4	1,398.2	1,244.0	1,385.5	(12.7)	141.4
Capital Investment Plan	419.4	468.9	399.7	412.1	(56.8)	12.4
Fund Deposits						
R&R and General Fund	42.9	95.0	30.0	36.7	(58.3)	6.7
Revenue Bond Construction	-	-	-	130.3	130.3	130.3
Water Stewardship Fund	-	-	-	-	-	-
Interest for Construction & Trust Funds (2)	19.4	4.6	3.4	0.0	(4.6)	(3.4)
Increase in Required Reserves	77.0	23.2	45.8	61.3	38.0	15.4
Increase in Rate Stabilization Fund	-	-	-	-	-	-
Sub-total Fund Deposits	139.3	122.9	79.3	228.3	105.4	149.0
TOTAL USES OF FUNDS	\$ 1,787.1	\$ 1,989.9	\$ 1,723.0	\$ 2,025.8	\$ 35.9	\$ 302.9
SOURCES OF FUNDS						
Receipts						
Taxes	\$ 97.7	\$ 94.4	\$ 95.8	\$ 90.4	\$ (3.9)	\$ (5.3)
Annexations	2.7	2.5	1.0	1.0	(1.5)	-
Interest Income	64.9	43.0	33.2	34.2	(8.8)	1.0
Hydro Power	41.1	35.2	24.4	24.1	(11.2)	(0.3)
Fixed Charges (RTS & Capacity Charge)	114.0	119.7	119.7	136.3	16.7	16.6
Water Sales Revenue	967.8	1,022.1	976.0	1,078.6	56.5	102.6
Miscellaneous Revenue	7.1	7.1	7.1	8.8	1.7	1.7
Bond Proceeds and Reimbursements	29.2	272.7	195.6	528.0	255.3	332.4
Sub-total Receipts	1,324.4	1,596.7	1,452.8	1,901.5	304.8	448.7
Fund Withdrawals						
Water Transfer Fund	19.8	7.8	9.2	-	(7.8)	(9.2)
R&R and General Fund	65.2	95.0	30.0	36.7	(58.3)	6.7
Bond Funds for Construction (3)	325.7	110.0	185.8	-	(110.0)	(185.8)
Water Stewardship Fund	5.9	15.1	23.9	0.9	(14.3)	(23.0)
Decrease in Required Reserves (4)	-	101.5	-	29.9	(71.5)	29.9
Decrease in Rate Stabilization Fund (5)	46.1	63.8	21.4	56.8	(7.0)	35.4
Sub-total Fund Withdrawals	462.7	393.3	270.2	124.3	(268.9)	(145.9)
TOTAL SOURCES OF FUNDS	\$ 1,787.1	\$ 1,989.9	\$ 1,723.0	\$ 2,025.8	\$ 35.9	\$ 302.9

(1) 2007/08 exclude \$28.7M for Drop 2 paid from the R&R Fund

(2) 2007/08 includes \$1.0M of interest for the WTF

(3) 2008/09 includes \$60 million from Proposition 50.

(4) 2009/10 Budget is expected to draw down the Revenue Remainder Fund \$29.9 million, \$45.2 million below the required minimum reserve.

(5) 2009/10 Budget is expected to draw down the Water Rate Stabilization Fund to zero, with an \$56.8 million withdrawal.

Totals may not foot due to rounding.

Table 6. 2009/10 Sources and Uses by Fund (dollars in millions)

Fiscal Year Ending June 30th, 2010 (\$ in Millions)	All Funds	Operating Funds							Debt Service Funds	Reserve Funds (1)	Construction Funds		Trust & Other Funds
		General	Water Revenue	O&M	Water Standby	Water Stewardship	Self-Insured Retention	State Contract			R&R	Revenue Bond Construction	
Beginning of Year Balance	940.2	62.8	-	167.1	1.1	0.9	25.2	72.6	287.0	273.2	33.8	15.5	1.1
USES OF FUNDS													
Expenditures													
State Water Contract	478.8	-	-	319.6	-	-	-	159.2	-	-	-	-	-
Supply Programs	125.5	-	-	125.5	-	-	-	-	-	-	-	-	-
Colorado River Power	49.8	-	-	49.8	-	-	-	-	-	-	-	-	-
Debt Service	330.7	2.6	-	12.2	-	-	-	-	316.0	-	-	-	-
Demand Management	59.8	-	-	59.8	-	-	-	-	-	-	-	-	-
Departmental O&M	289.3	-	-	289.3	-	-	-	-	-	-	-	-	-
Treatment Chemicals, Sludge & Power	32.8	-	-	32.8	-	-	-	-	-	-	-	-	-
Other O&M	18.7	5.3	-	13.4	-	-	-	-	-	-	-	-	-
Sub-total Expenditures	1,385.5	7.8	-	902.5	-	-	-	159.2	316.0	-	-	-	-
Capital Investment Plan	412.1	36.7	-	-	-	-	-	-	-	-	-	375.4	-
Fund Deposits													
R&R and General Fund	36.7	36.7	-	-	-	-	-	-	-	-	-	-	-
Revenue Bond Construction	130.3	-	-	-	-	-	-	-	-	-	-	130.3	-
Water Stewardship Fund	-	-	-	-	-	-	-	-	-	-	-	-	-
Interest for Construction & Trust Funds	0.0	-	-	-	-	-	-	-	-	-	-	-	0.0
Increase in Required Reserves	61.3	-	-	8.4	-	-	-	7.9	45.0	-	-	-	-
Increase in Rate Stabilization Fund	-	-	-	-	-	-	-	-	-	-	-	-	-
Sub-total Fund Deposits	228.3	36.7	-	8.4	-	-	-	7.9	45.0	-	-	130.3	0.0
TOTAL USES OF FUNDS	2,025.8	81.2	-	910.9	-	-	-	167.1	361.0	-	-	505.6	0.0
SOURCES OF FUNDS													
Receipts													
Taxes	90.4	-	-	-	-	-	-	42.8	47.6	-	-	-	-
Annexations	1.0	-	-	-	-	-	-	1.0	-	-	-	-	-
Interest Income	34.2	2.2	-	5.9	0.0	0.0	0.9	2.6	10.7	7.8	1.2	2.8	0.0
Hydro Power	24.1	-	23.4	0.7	-	-	-	-	-	-	-	-	-
Fixed Charges (RTS & Capacity Charge)	136.3	-	136.3	-	-	-	-	-	-	-	-	-	-
Water Sales Revenue	1,078.6	-	1,078.6	-	-	-	-	-	-	-	-	-	-
Miscellaneous Revenue	8.8	8.8	-	-	-	-	-	-	-	-	-	-	-
Bond Proceeds	528.0	-	-	-	-	-	-	-	22.4	-	-	505.6	-
Sub-total Receipts	1,901.5	11.0	1,238.3	6.6	0.0	0.0	0.9	46.5	80.7	7.8	1.2	508.4	0.0
Fund Withdrawals													
Transfer Fund	-	-	-	-	-	-	-	-	-	-	-	-	-
R&R and General Fund	36.7	36.7	-	-	-	-	-	-	-	-	-	-	-
Bond Funds for Construction	-	-	-	-	-	-	-	-	-	-	-	-	-
Water Stewardship Fund	0.9	-	-	-	-	0.9	-	-	-	-	-	-	-
Decrease in Required Reserves (2)	29.9	-	-	-	-	-	-	-	-	29.9	-	-	-
Decrease in Rate Stabilization Fund (3)	56.8	-	-	-	-	-	-	-	-	56.8	-	-	-
Sub-total Fund Withdrawals	124.3	36.7	-	-	-	-	-	0.9	-	86.8	-	-	-
TOTAL SOURCES OF FUNDS	2,025.8	47.7	1,238.3	6.6	0.0	0.9	0.9	46.5	80.7	94.6	1.2	508.4	0.0
Inter-Fund Transfers	-	33.5	(1,238.3)	904.3	(0.0)	(0.9)	(0.9)	120.6	280.3	(94.6)	(1.2)	(2.8)	-
End of Year Balance	1,044.1	62.8	-	175.5	1.1	-	25.2	80.5	332.0	186.5	33.8	145.8	1.2

(1) includes Water Rate Stabilization Fund, Water Treatment Surcharge Stabilization Fund, and the Revenue Remainder Fund
 (2) 2009/10 Budget is expected to draw down the Revenue Remainder Fund \$29.9 million, \$45.2 million below the required minimum reserve.
 (3) 2009/10 Budget is expected to draw down the Water Rate Stabilization Fund to zero, with an \$56.8 million withdrawal.
 Totals may not foot due to rounding.