

# Audited Financial Statements June 30, 2010

Business and Finance Committee  
November 8, 2010

# Background

- The financial statements reflect the operating results and financial condition of an entity
- Annual audit required by bond covenants and single audit

# Background (continued)

- Metropolitan is an Enterprise Fund (footnote 1b)
  - Accounting and reporting similar to business entities
  - Generally accepted accounting principles (GAAP)
    - Governmental Accounting Standards Board
      - 59 statements
    - Financial Accounting Standards Board
      - 102 statements -- through 11/30/89

# Background (continued)

- Classified financial statements
  - Current and noncurrent assets and liabilities
    - Current assets – will be used within 12 months
    - Current liabilities – may be paid within 12 months (pages 54 and 55)
  - Operating and nonoperating revenues and expenses
- Investments and derivatives stated at fair market value; all other accounts stated at cost

# Two New Pronouncements

- GASB 51 – Accounting and Financial Reporting for Intangible Assets
  - No change to State Water Project – capital costs recorded as prepaid asset and amortized through 2052 (footnote 10)
- GASB 53 – Accounting and Financial Reporting for Derivative Instruments
  - Change in accounting and reporting for interest rate swap agreements
  - Fair value now included in financial statements as well as footnotes (footnotes 1q and 5f)

# Change in Balance Sheets

- Assets and Deferred Outflows (page 14)
  - Deferred Outflows new line item for effective interest rate swaps – moves information from footnotes to financial statements
- Liabilities (page 15)
  - Fair value of interest rate swaps new line item – moves information from footnotes to financial statements
- 2009 restated for comparability reflecting new accounting rules for interest rate swaps

# Statements of Revenues and Expenses Restated

- 2009 restated for comparability reflecting new accounting rules for interest rate swaps
- 2009 net income reduced \$4.7 million reflecting write-off of 'deemed terminated' and ineffective hedges
- 2010 net income includes \$3.1 million for write-off of 'deemed terminated' and ineffective hedges



# Statements of Cash Flows

(pages 18 and 19)

- No restatements – no cash impact from new accounting rules relating to interest rate swaps
- No budget or rate impact from new accounting rules relating to interest rate swaps
  - If swaps held to maturity or terminated at a gain, a one time increase in net revenue will be recognized



# Balance Sheet – Assets

(\$ Billions)

	<u>FY10</u>	<u>FY09 (Restated)</u>	<u>Change</u>
Cash & Investments - FMV	\$ 1.095	\$ 1.064	\$ 0.031
Prepaid SWP costs	1.412	1.400	0.012
Plant, net	8.464	8.210	0.254
Other	0.553	0.593	(0.040)
	<b>\$ 11.524</b>	<b>\$ 11.267</b>	<b>\$ 0.257</b>

# Balance Sheet – Assets

(\$ Billions)

	FY10	FY09 (Restated)	Change
Cash & Investments - FMV	\$ 1.095	\$ 1.064	\$ 0.031
Prepaid SWP costs	1.412	1.400	0.012
Plant, net	8.464	8.210	0.254
	0.553	0.593	(0.040)
	<b>\$ 11.524</b>	<b>\$ 11.267</b>	<b>\$ 0.257</b>

95% of total assets

# Balance Sheet – Assets

(\$ Billions)

		FY10	FY09 (Restated)	Change
<b>Cash &amp; Investments - FMV</b>		\$ 1.095	\$ 1.064	\$ 0.031
<b>Restricted</b>	\$ 645M	1.412	1.400	0.012
<b>Unrestricted</b>	<u>450M</u>	8.464	8.210	0.254
	\$ 1,095M	0.553	0.593	(0.040)
		<b>\$ 11.524</b>	<b>\$ 11.267</b>	<b>\$ 0.257</b>

# Cash & Investments – FMV

June 30, 2010

(\$ Millions)


	Contractual Restricted	Board Restricted	Unrestricted
O&M Fund	\$ 169.3		
Bonds – Principal & Interest	165.8		
Bond reserves	132.4		
Construction	137.8		
Trust funds	40.4		
Stabilization funds			\$ 298.9
State Contract		\$ 68.9	
Self Insurance		25.4	
R&R			34.0
General fund - Desalination		18.9	
Other		1.9	1.8
	<b>\$ 645.7</b>	<b>\$ 115.1</b>	<b>\$ 334.7</b>

**\$449.8**

# Balance Sheet – Assets

(\$ Billions)

	<u>FY10</u>	<u>FY09 (Restated)</u>	<u>Change</u>
Cash & Investments - FMV	\$ 1.095	\$ 1.064	\$ 0.031
Prepaid SWP costs	1.412	1.400	0.012
Plant, net	8.464	8.210	0.254
Other	0.553	0.593	(0.040)
	<b>\$ 11.524</b>	<b>\$ 11.267</b>	<b>\$ 0.257</b>



# Balance Sheet – Assets

(\$ Billions)

		FY10	FY09 (Restated)	Change
<b>Accounts receivable:</b>				
Water sales	\$ 186.2M			
Taxes & annexations	22.6			
Other (power, interest)	20.6	\$ 1.095	\$ 1.064	\$ 0.031
<b>Water inventories:</b>				
In-basin	65.9	1.412	1.400	0.012
Outside basin	85.9	8.464	8.210	0.254
Deferred outflow swaps	61.5			
Bay-Delta prepayments	29.9	0.553	0.593	(0.040)
Prepaid natural gas hedging	14.2			
Feasibility/reimb proj	19.4			
Supplies – inventory	12.4			
Other	34.4			
	<u>\$ 553.0M</u>	\$ 11.524	\$ 11.267	\$ 0.257

# Balance Sheet – Liabilities and Net Assets (Equity)

(\$ Billions)

	<u>FY10</u>	<u>FY09 (Restated)</u>	<u>Change</u>
Long-term debt	\$ 4.770	\$ 4.672	\$ 0.098
Net assets (equity)	6.146	6.043	0.103
Other	0.608	0.552	0.056
	<b>\$ 11.524</b>	<b>\$ 11.267</b>	<b>\$ 0.257</b>



# Balance Sheet – Liabilities and Net Assets (Equity)

(\$ Billions)

	FY10	FY09 (Restated)	Change
Long-term debt	\$ 4.770	\$ 4.672	\$ 0.098
Net assets (equity)	6.146	6.043	0.103
	0.608	0.552	0.056
	<b>\$ 11.524</b>	<b>\$ 11.267</b>	<b>\$ 0.257</b>

95% of total

# Balance Sheet – Liabilities and Assets (Equity)

FMV swaps	\$148.2 M
OPEB	106.3
Payable to DWR (incl OAPF)	81.9
Interest payable	75.5
Accrued compensation	47.0
Customer deposits/trusts	42.8
Power costs payable	43.1
Vendors	25.1
W/C & 3 <sup>rd</sup> Party	16.7
Other	<u>21.4</u>
	<b>\$608.0M</b>

(\$ Billions)

	FY10	FY09 (Restated)	Change
	\$ 4.770	\$ 4.672	\$ 0.098
	6.146	6.043	0.103
	0.608	0.552	0.056
	<b>\$ 11.524</b>	<b>\$ 11.267</b>	<b>\$ 0.257</b>

# Income Statement

(\$ Billions)

	FY10	FY09 Restated	Change
Operating revenues	\$ 1.165	\$ 1.136	\$ 0.029
Operating expenses	(0.829)	(0.842)	0.013
Depreciation/amortization	(0.246)	(0.226)	(0.020)
Non-op rev/exp, net	<u>0.008</u>	<u>0.032</u>	<u>(0.024)</u>
<b>Net income</b>	<b>0.098</b>	<b>0.100</b>	<b>(0.002)</b>
Capital contributions	<u>0.005</u>	<u>0.066</u>	<u>(0.061)</u>
<b>Increase in equity</b>	<b>\$ 0.103</b>	<b>\$ 0.166</b>	<b>\$ (0.063)</b>

# Income Statement

(\$ Billions)

	FY09		
	FY10	Restated	Change
Operating revenues	\$ 1.165	\$ 1.136	\$ 0.029
Operating expenses			0.013
Depreciation/amortization			(0.020)
Non-op rev/exp, net			<u>(0.024)</u>
<b>Net income</b>			<b>(0.002)</b>
Capital contributions			<u>(0.061)</u>
<b>Increase in equity</b>	<b>\$ 0.103</b>	<b>\$ 0.166</b>	<b>\$ (0.063)</b>

Water sales:			
Price	\$ 180.5 M		
Volume	<u>(169.2)</u>		
	11.3		
RTS	16.0		
Other	<u>1.7</u>		
	29.0 M		

# Income Statement

(\$ Billions)

	FY09		
	FY10	Restated	Change
Operating revenues	\$ 1.165	\$ 1.136	\$ 0.029
Operating expenses	(0.829)	(0.842)	0.013
Depreciation/amortization		(0.026)	(0.020)
Non-op rev/exp		0.002	(0.024)
<b>Net income</b>		0.000	<b>(0.002)</b>
Capital contributions		0.066	<b>(0.061)</b>
Increase in equity		0.066	<b>\$ (0.063)</b>

Cost of water:		
Price	\$ (99.7) M	
Volume	<u>68.1</u>	
	(31.6)	
Water mgt programs	24.8	
Insurance claims	14.9	
Other	<u>4.9</u>	
	13.0 M	

# Income Statement

(\$ Billions)

	FY10	FY09 Restated	Change
Operating revenues	\$ 1.165	\$ 1.136	\$ 0.029
Operating expenses	(0.829)	(0.842)	0.013
Depreciation/amortization	(0.246)	(0.226)	(0.020)
Non-op rev/exp, net	<u>0.008</u>	<u>0.032</u>	<u>(0.024)</u>
<b>Net income</b>			<b>(0.002)</b>
Capital contribution			<u>(0.061)</u>
<b>Increase in equity</b>			<b>\$ (0.063)</b>

Interest expense \$ (29.9) M  
 Property taxes ( 7.3)  
 Investment income 13.2  
 \$ (24.0)



# Income Statement

(\$ Billions)

	FY10	FY09 Restated	Change
Operating revenues	\$ 1.165	\$ 1.136	\$ 0.029
Operating expenses	(0.829)	(0.842)	0.013
Depreciation/amortization	(0.246)	(0.226)	(0.020)
Non-op rev/exp, net	<u>0.008</u>	<u>0.032</u>	<u>(0.024)</u>
<b>Net income</b>	<b>0.098</b>	<b>0.100</b>	<b>(0.002)</b>
Capital contributions	<u>0.005</u>	<u>0.066</u>	<u>(0.061)</u>
<b>Increase in equity</b>			<b>(0.063)</b>

Prop 13 and 50 grants



# Cash Flow (\$ Millions)

	<u>FY10</u>	<u>FY09</u>	<u>Change</u>
Cash provided by operations	\$ 331.1	\$ 358.2	\$ (27.1)
Cash used for financing activities	(339.2)	(404.3)	65.1
Cash provided by investments	<u>7.0</u>	<u>47.9</u>	<u>(40.9)</u>
Change in cash	\$ (1.1)	\$ 1.8	\$ (2.9)
Beginning cash	1.8	--	1.8
Ending cash	\$ 0.7	\$ 1.8	\$ (1.1)

# Cash Flow (\$ Millions)

	FY10	FY09	Change
Cash provided by operations	\$ 331.1	\$ 358.2	\$ ( 27.1)
Cash used for final			
Water transfers		\$(39.6)M	65.1
SWP variable/O&M costs		(23.1)	
Cash provided by i			
Water sales (incl wheeling)	23.0	27.9	<u>( 40.9)</u>
Conservation		18.5	
Local projects		<u>(5.9)</u>	\$ ( 2.9)
Change in			
Beginning		\$(27.1)M	1.8
Ending cash	\$ 0.7	\$ 1.8	\$ (1.1)

# Cash Flow (\$ Millions)

	FY10	FY09	Change
Cash provided by operations	\$ 331.1	\$ 358.2	\$ ( 27.1)
Cash used for financing activities	(339.2)	(404.3)	65.1
Cash provided		\$99.0 M	<u>( 40.9)</u>
Less construction spending		56.9	
Collect capital grants		(20.4)	\$ ( 2.9)
Higher SWP capital costs		(52.5)	
Less new debt issued		(13.2)	1.8
Higher debt service costs		<u>( 4.7)</u>	\$ (1.1)
Other, net		\$65.1 M	

# Cash Flow (\$ Millions)

	FY10	FY09	Change
Cash provided by operations	\$ 331.1	\$ 358.2	\$ (27.1)
Cash used for financing activities	(339.2)	(404.3)	65.1
Cash provided by investments	7.0	47.9	<u>(40.9)</u>
Change			\$ (2.9)
Beginning			1.8
Ending			\$ (1.1)

Higher net purchases of investment securities and lower interest earnings

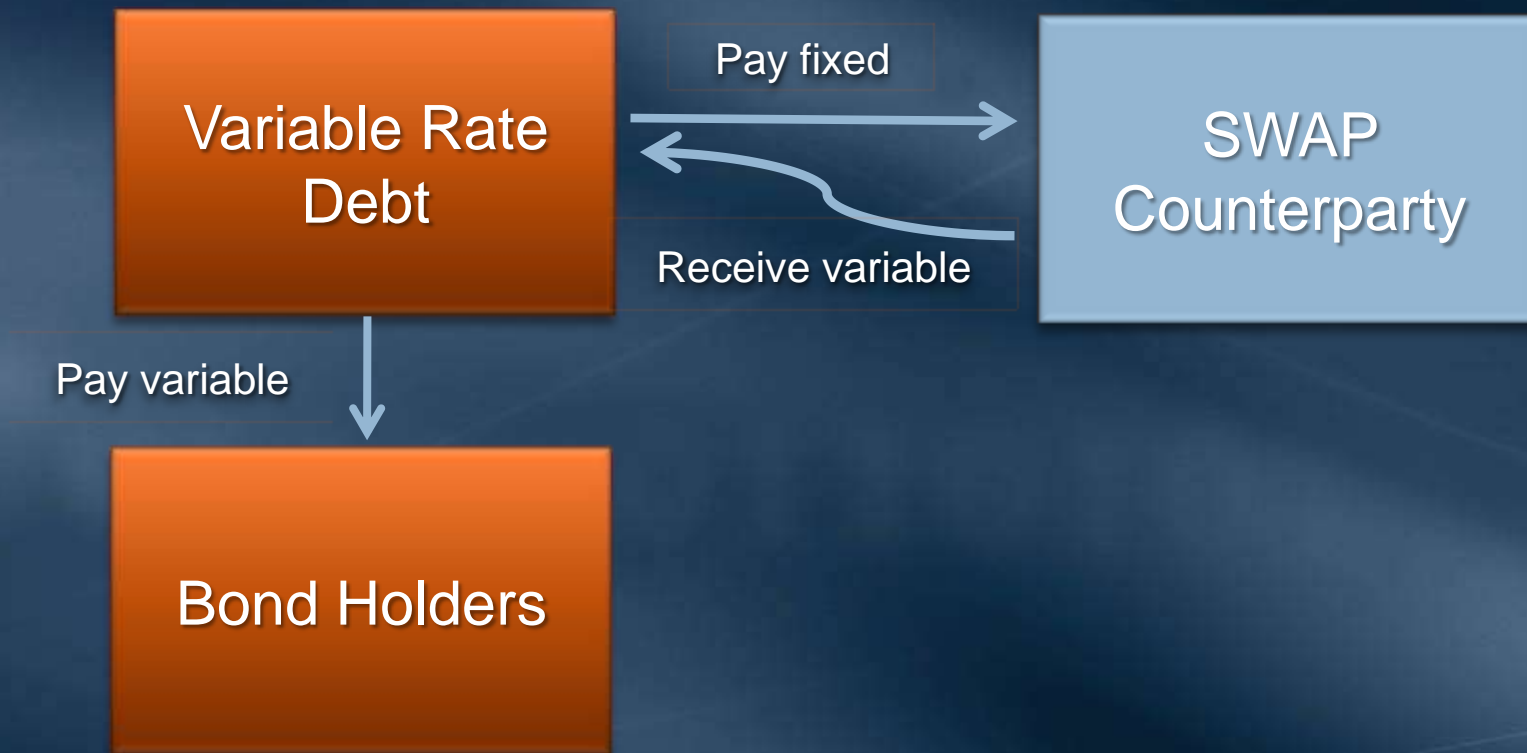
# Interest Rate Swaps

June 30, 2010

- Objective – manage interest rate risk and reduce debt service payments
- 17 swap agreements
- 15 effective; 2 ineffective
- 8 ‘deemed terminations’ due to refunding variable rate debt associated with swap agreements
  - Swap agreements re-associated with other outstanding variable rate debt

# Deemed Termination and Re-Association

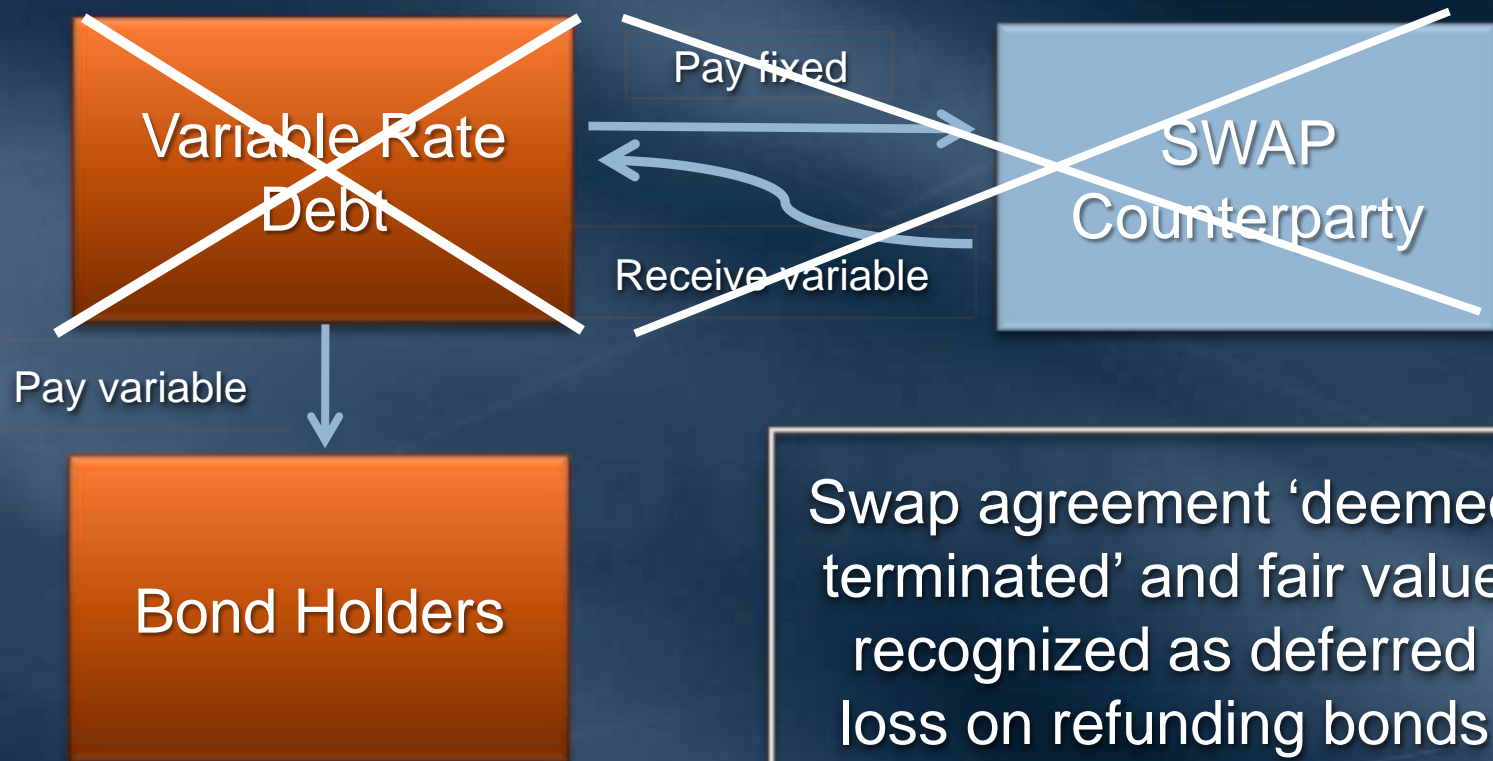
## 1. Typical swap agreement structure





# Deemed Termination and Re-Association

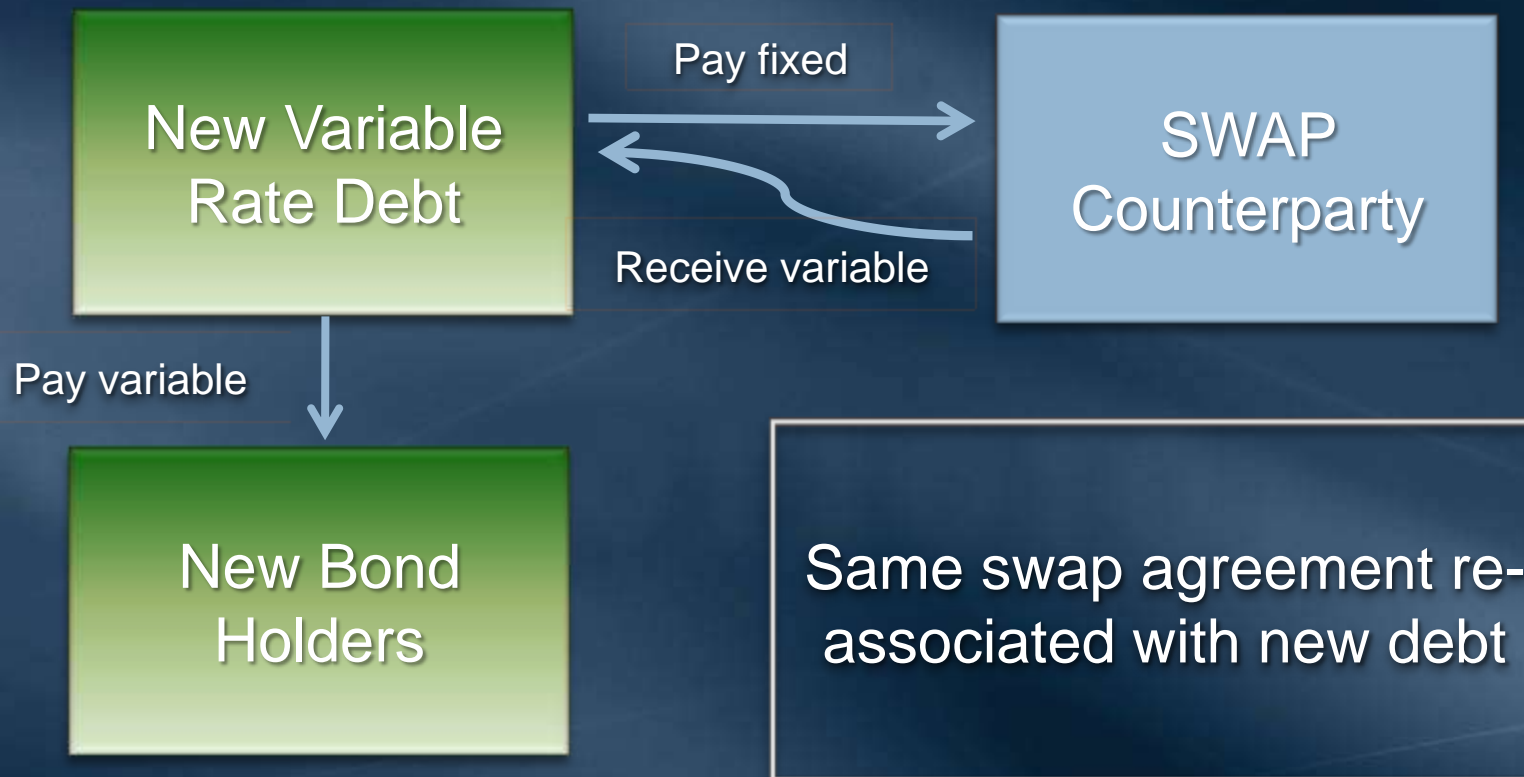
## 2. Variable debt refunded





# Deemed Termination and Re-Association

## 3. Swap agreement re-associated with new variable rate debt



# Interest Rate Swaps

June 30, 2010

(\$ millions)

	Fair Market Value	Accounting
Effective (15)	(\$61.5)	Deferred outflow
Ineffective (2)	0.5	Recognize income or (loss)
Refunded	(87.2)	Defer loss on refunding
	<b>(\$148.2)</b>	

# Interest Rate Swaps

June 30, 2010

(\$ millions)

	Fair Market Value	Accounting
Effective (15)	(\$61.5)	Deferred outflow
Ineffective (2)	0.5	Recognize income or (loss)
Refunded	(87.2)	Defer loss on refunding
	<b>(\$148.2)</b>	

## Balance Sheet

Assets & Deferred Outflows		Liabilities and Net Assets	
Deferred outflow	\$61.5	FMV of SWAPS	(\$61.5)

# Interest Rate Swaps

June 30, 2010

(\$ millions)

	Fair Market Value	Accounting
Effective (15)	(\$61.5)	Deferred outflow
Ineffective (2)	0.5	Recognize income or (loss)
Refunded	(87.2)	Defer loss on refunding
	<b>(\$148.2)</b>	

## Balance Sheet

Assets & Deferred Outflows		Liabilities and Net Assets	
Deferred outflow	\$61.5	FMV of SWAPS	(\$61.0)
		Net assets	(0.5)

# Interest Rate Swaps

June 30, 2010

(\$ millions)

	Fair Market Value	Accounting
Effective (15)	(\$61.5)	Deferred outflow
Ineffective (2)	0.5	Recognize income or (loss)
<b>Refunded</b>	<b>(87.2)</b>	<b>Defer loss on refunding</b>
	<b>(\$148.2)</b>	

## Balance Sheet

Assets & Deferred Outflows		Liabilities and Net Assets	
Deferred outflow	\$61.5	<b>FMV of SWAPS</b>	<b>(\$148.2)</b>
		Net assets	(0.5)
		<b>Long-term debt</b>	<b>87.2</b>

# Interest Rate Swaps

June 30, 2010

(\$ millions)

	Fair Market Value	Accounting
Effective (15)	(\$61.5)	Deferred outflow
Ineffective (2)	0.5	Recognize income or (loss)
Refunded	(87.2)	Defer loss on refunding
	<b>(\$148.2)</b>	

## Balance Sheet

Assets & Deferred Outflows		Liabilities and Net Assets	
<b>Deferred outflow</b>	<b>\$61.5</b>	<b>FMV of SWAPS</b>	<b>(\$148.2)</b>
		Net assets	(0.5)
		Long-term debt	87.2

# Interest Rate Swaps

June 30, 2010

(\$ millions)

	Fair Market Value	Accounting
Effective (15)	(\$61.5)	Deferred outflow
Ineffective (2)	0.5	Recognize income or (loss)
Refunded	(87.2)	Defer loss on refunding
	<b>(\$148.2)</b>	

## Income Statement

Revenues		Expenses	
Investment Income	\$1.5		
Change in FMV -- 6/30/09 = \$(1.0M); 6/30/10 = \$0.5M; change = \$1.5M			



# Interest Rate Swaps

June 30, 2010

(\$ millions)

	Fair Market Value	Accounting
Effective (15)	(\$61.5)	Deferred outflow
Ineffective (2)	0.5	Recognize income or (loss)
<b>Refunded</b>	<b>(87.2)</b>	<b>Defer loss on refunding</b>
	<b>(\$148.2)</b>	

## Income Statement

Revenues		Expenses	
		<b>Bond interest expense</b>	<b>\$4.6</b>
		Deferred loss on refunding is amortized over the life of the old or new debt, whichever is shorter	

# FY 2010 Net Income Impact Accounting for Interest Rate Swaps

(\$ millions)

Investment Income	\$1.5
Bond interest expense	(4.6)
<b>Impact on net income</b>	<b>\$(3.1)</b>

# Footnotes

- 50 pages
- In addition to describing what is on the face of the financial statements, footnotes also disclose what is not recorded on the statements
  - SWP – footnote 9(a), page 60
    - \$8.1 billion obligation to the state (excludes variable)
    - Only \$54 million of obligation recorded

# Footnotes (continued)

- OPEB Obligation – RSI, page 72 and footnote 8, page 58
  - \$404.2 million obligation
  - \$106.3 million of obligation recorded representing the unpaid portion of the annual required contribution for the past 5 years
- Pension Obligation – RSI, page 72 and footnote 7, page 56
  - \$102.5 million obligation
  - Not recorded because annual required contribution paid in full each year

# Footnotes (continued)

- Subsequent Events – page 71
  - Events that occurred after June 30, 2010, but before financial statements were issued
  - 2 debt refundings
  - 4 interest rate swap agreements were assigned by UBS to Deutsche Bank
    - Agreements considered terminated
    - Loss of \$18.7 million FMV may be recognized in fiscal year 2010/11
      - GASB preparing Technical Bulletin to address accounting treatment

