



- Board of Directors  
*Finance and Insurance Committee*

5/10/2011 Board Meeting

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**8-2**

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**Subject**

Consider City of Compton's request to withdraw purchase order agreement

**Description**

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**Summary**

Twenty-four member agencies signed voluntary Purchase Orders effective January 1, 2003, committing to purchase minimum quantities of water from Metropolitan over a ten-year period and receiving more of their purchases at the lower Tier 1 supply rate. Since signing its Purchase Order commitment, the City of Compton (Compton) has improved its operations to make better use of local groundwater resources, thereby lessening their reliance on imported water supplies. Compton is asking to withdraw its Purchase Order commitment, resulting in a lower annual amount of water that can be purchased at the Tier 1 full service rate and making Compton subject to the Tier 2 Supply Rate on past and future water purchases.

**Background**

In October 2001, the Board adopted a new rate structure effective January 1, 2003. One of the components of the new rate structure was a Purchase Order to provide for commitment from the member agencies to purchase a minimum amount of water over a ten-year period. Purchase Orders were: (1) voluntary; (2) offered price incentives to member agencies by allowing more water deliveries to be purchased at the lower-priced Tier 1 Supply Rate; (3) offered an additional level of financial commitment to Metropolitan; and (4) were not tied to reliability.

The Purchase Order covers a ten-year term beginning January 1, 2003 and ending December 31, 2012. The maximum annual firm demands from fiscal year 1989/90 through fiscal year 2001/02 were used to establish each member agency's Initial Base Firm Demand (IBFD). In exchange for this commitment, the member agency could purchase an amount of firm water supply equal to 90 percent of its IBFD in any given year at the lower Tier 1 Supply Rate. An agency that did not execute a Purchase Order could purchase up to 60 percent of its IBFD at the lower Tier 1 Supply Rate. The terms and conditions of the Purchase Order were uniform for all member agencies.

Two options were made available to member agencies: (1) enter into a purchase order and receive a higher amount of Tier 1 price certainty; and (2) not enter into a purchase order at all and purchase less water at Tier 1 rates. The second option was more appealing to agencies that purchase small amounts of water from Metropolitan. Twenty four agencies entered Purchase Order agreements while the cities of San Fernando and San Marino did not.

Table 1 summarizes Compton's Purchase Order status as of calendar year 2010. Compton's IBFD was 5,680.2 acre-feet. Its Purchase Order commitment was 60 percent of the IBFD times ten years, for a total commitment of 33,720.6 acre-feet, or an average of 3,372.1 acre-feet of firm purchases per year. Compton's Tier 1 limit was established as 90 percent of its IBFD, or 5,058.1 acre-feet. Had Compton not signed the Purchase Order, its Tier 1 limit would have been 60 percent of its IBFD, or 3,372.1 acre-feet. As shown in Table 1, through 2010, Compton had purchased 3,804.3 acre-feet less than would be required to remain on track to meet its Purchase Order commitment over the ten-year period.

**Table 1: Compton's Purchase Order Commitment**

Calendar Year	Firm AF Purchased	With a Purchase Order			Without a Purchase Order	
		Tier 1 limits	Annual Commitment	Shortfall	Tier 1 limits	Tier 2 purchases
2003	3,159.6	5,058.2	3,372.1	212.5	3,372.1	0
2004	3,010.9	5,058.2	3,372.1	361.2	3,372.1	0
2005	3,065.6	5,058.2	3,372.1	306.5	3,372.1	0
2006	3,034.6	5,058.2	3,372.1	337.5	3,372.1	0
2007	3,062.6	5,058.2	3,372.1	309.5	3,372.1	0
2008	2,561.7	5,058.2	3,372.1	810.4	3,372.1	0
2009*	2,772.3	5,058.2	3,203.5	431.2	3,372.1	0
2010*	1,999.4	5,058.2	3,034.9	1,035.5	3,372.1	0
* Annual Commitment adjusted for the SAP				<u>3,804.3</u>		<u>0.0</u>

The city has confirmed that its lower water purchase trend will continue due to operational changes that have occurred since signing the Purchase Order Agreement. After signing the Purchase Order, Compton received funds from Proposition 13 in December 2005 and the Environmental Protection Agency in 2008 to offset the costs of constructing new wells. The rehabilitation of its wells significantly increased Compton's pumping capacity out of the Central Basin. The additional pumping capacity realized by the system improvements negated the need to purchase imported water supplies from Metropolitan.

At this time, Compton does not expect to meet its Purchase Order commitment by December 31, 2012. Compton staff did not foresee that they would receive substantial funds to improve their pumping operations. Had Compton staff known they would receive the funds and realized the implications of the well rehabilitation projects, they would not have signed the Purchase Order, which was an option provided to all member agencies. Compton is requesting that it be allowed to withdraw its Purchase Order, revise its Tier 1 limit lower, and pay the Tier 2 Supply Rate on any future water purchases over the revised lower limit. As shown on Table 1, Compton would not have purchased any water at the Tier 2 rates in prior years even with the lower Tier 1 limit. Withdrawal of the Purchase Order will not affect Metropolitan revenues collected to date. There is no impact on water rates and charges resulting from this action. Compton acknowledges and accepts that it will be at greater risk of paying Tier 2 rates in the future by this proposal. If the Purchase Order is not withdrawn, Compton faces penalties under the Purchase Order of approximately \$750,000 to \$1 million at the end of 2012.

**Policy**

Metropolitan Water District Administrative Code Section 4404: Purchase Orders

**California Environmental Quality Act (CEQA)**

CEQA determination for Option #1:

The proposed action is not defined as a project under the California Environmental Quality Act (CEQA), because it involves continuing administrative activities, such as general policy and procedure making (Section 15378(b)(2) of the State CEQA Guidelines). In addition, the proposed action is not subject to CEQA because it involves 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).

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

CEQA determination for Option #2:

None required

**Board Options**

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**Option #1**

Adopt the CEQA determination and authorize the General Manager to execute a withdrawal of Compton's Purchase Order effective January 1, 2003.

**Fiscal Impact:** None to date. Metropolitan would forego potential penalties under the Purchase Order of approximately \$750,000 to \$1 million at the end of 2012 but receive Tier 2 pricing on any Tier 2 sales that might result in calendar years 2011 through 2012.

**Option #2**

Take no action.

**Fiscal Impact:** If withdrawal is not allowed, Compton faces penalties under the Purchase Order of approximately \$750,000 to \$1 million at the end of 2012.

**Staff Recommendation**

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Option #1

  
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Thomas E. DeBacker  
Interim Chief Financial Officer

4/25/2011  
Date

  
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Jeffrey Lightinger  
General Manager

4/28/2011  
Date

Ref# cfo12608538