



# Use of Wholesale Water Contracts

Finance & Insurance Committee

Item 7a

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# Overview

- Background
- Wholesale Water Contracts
  - What are they?
  - Where, when, and why are they used?
- Examples of Wholesale Contracts
  - California agencies and others
- Summary of Findings

# Why Use Contracts?

Water for resale

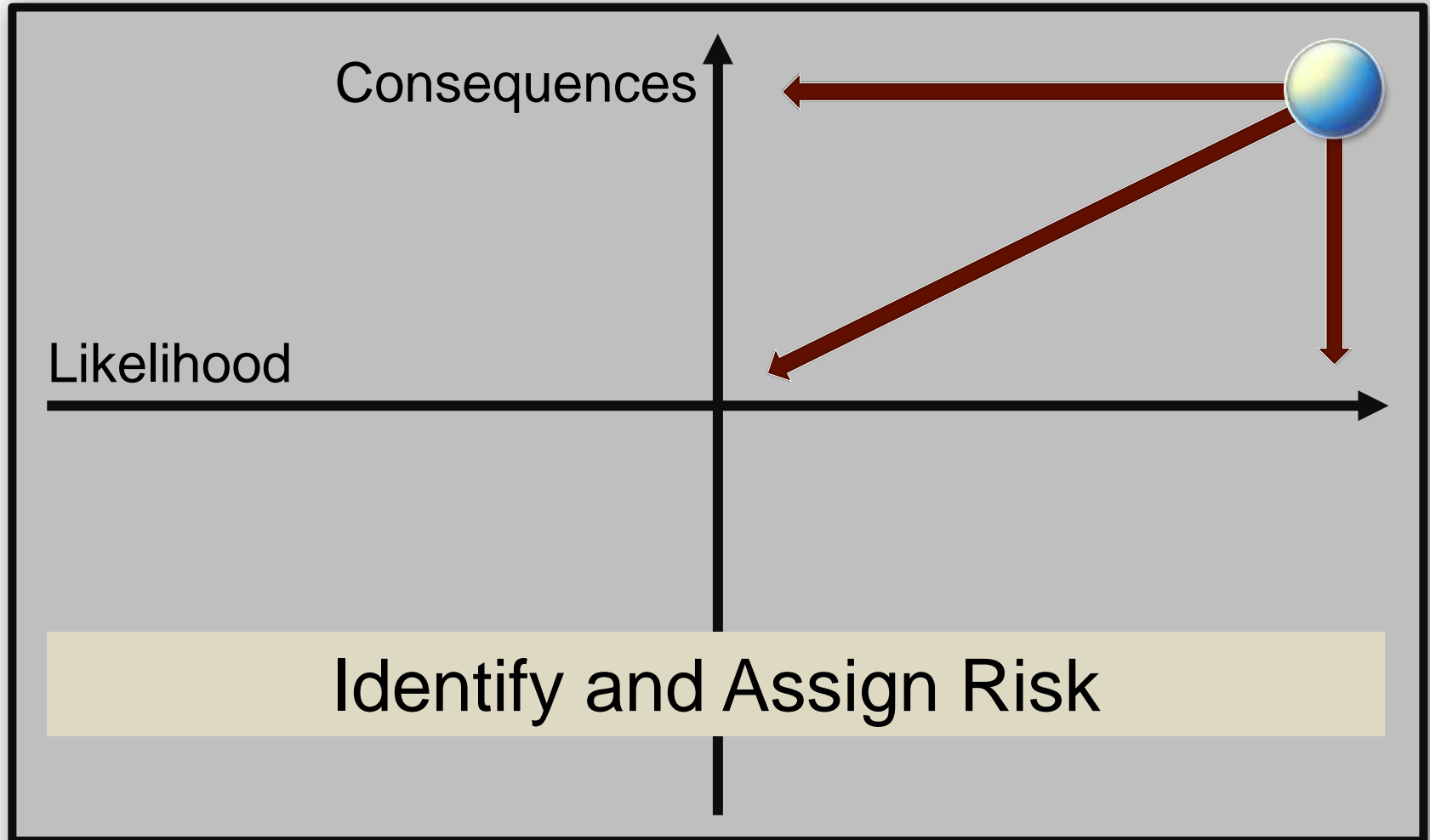
Revenue stability/certainty

Secure financing for projects

Ensure access to project or service

Use of contracts alone doesn't guarantee the revenue stream

# Risk Management



# Aspects of Contracts

- Usually arms-length transactions between different legal/contractual entities
- Length – Mid- to long-term
- For infrastructure, usually associated with a radial extension or a discrete project
- Based on customer-specific cost allocation or assignment



# Revenue-Cost Recovery

- Many ways to design rates to recover costs
- Revenue structure: volumetric rates, fixed charges, or both (a “Retail” approach”)
- Contracts
  - Take or Pay
  - Joint participation
  - Contracts for services
- Among wholesale agencies, wide variation in approaches

# Take or Pay Contracts

## Buyer is obliged:

- **(a)** to take delivery of and pay for an agreed minimum quantity of goods or services; or **(b)** in the event that Buyer does not take specified quantity, pay the equivalent cost for the difference between specified quantity and that actually taken
- Variation – Buyer declines delivery or takes partial delivery, but pays reduced amount or penalty, Seller free to sell elsewhere

## Objectives of take or pay provisions:

- Ensures Buyer that vendors produce necessary goods
- Provides Seller an identified funding stream to finance new infrastructure
- Protects Seller against impacts of volatile swings in demand

# Other Contract Types

## Joint Participation

- Used for projects with multiple participants
- Each participant pays their pro rata share of costs, whether fixed or variable
- Agreement provides a method to pass through costs

## Contracts for Services

- Often needed for project financing
- Provide specific services, such as treatment or supply
- Structure can be fixed, volumetric, or both
- Fees and/or rates, whether fixed or volumetric, are negotiable and may differ from what the agency providing the service would charge themselves



A photograph of a water treatment facility. In the foreground, there are several large, rectangular aeration basins filled with water. A metal grate is visible in the lower-left corner. In the background, there are several buildings, including a prominent one with a dome and a tower, and a large cylindrical tank. The sky is clear and blue.

# Examples of Use of Contracts within Water Industry

# CA Department of Water Resources

- Contracts with 29 water agencies for State Water Project
- Contract runs through 2035, includes provisions for continued service beyond contract term
- Agencies obligated to pay fixed charges regardless of quantity of water delivered, variable charges associated only with actual deliveries
  - **Fixed charges** – capital and operations and maintenance
  - **Variable charges** - cost of energy consumed in pumping
  - CY2012 estimate of charges: 74% fixed, 26% variable
- Allocation of costs based on each contractor's proportional use of facilities or "reaches"



# Santa Clara Valley Water District

- Take or pay contracts for treated water with 8 retail water agencies
- Contract revenues from treated water sales make up over 50% of total revenues
- Contracts cover both fixed and variable costs
- Original intent of contracts was to cover costs for build out of treated water system
- Purchases over contract minimums are charged “non-contract” rate, which varies based on water supply conditions

# Contra Costa Water District

- Wholesale treated and untreated supplies to 7 water retailers,  $\approx$  30% of total water sales
- Some customers have contracts for minimum annual quantities of raw water
  - Payments support Los Vaqueros Reservoir bonds
- Other customers have treatment capacity leases + minimum purchase agreements for treated water
  - Payments support treatment plant investments by CCWD

# City of Houston, TX

- Take or pay contracts to:
  - Large industrial users
  - MUDs who own their own system
  - Small Cities
- Contracts for both treated and raw water
  - Take or pay for minimum water demand
  - Excess of take or pay minimum charged surcharge
- Maximum of 40 years with renewal option
- Allows for ease in system monitoring and encouraging consistent use by large users
- Increases stability of revenue stream



# Denver Water and Aurora Water, CO

- South Metro Water Supply Authority and wholesale partners: Denver-Aurora
- Guaranteed minimum deliveries phase-in:
  - Begins in 2015-16, ramps up to 5,000 AF in 2020
  - Post 2020: guaranteed 10,000 AF per year of water over 10 year “blocks”
- Once Authority has paid for 100,000 AF during the 10-year block, no further minimum payment is required during that block
- Covers cost of infrastructure investment

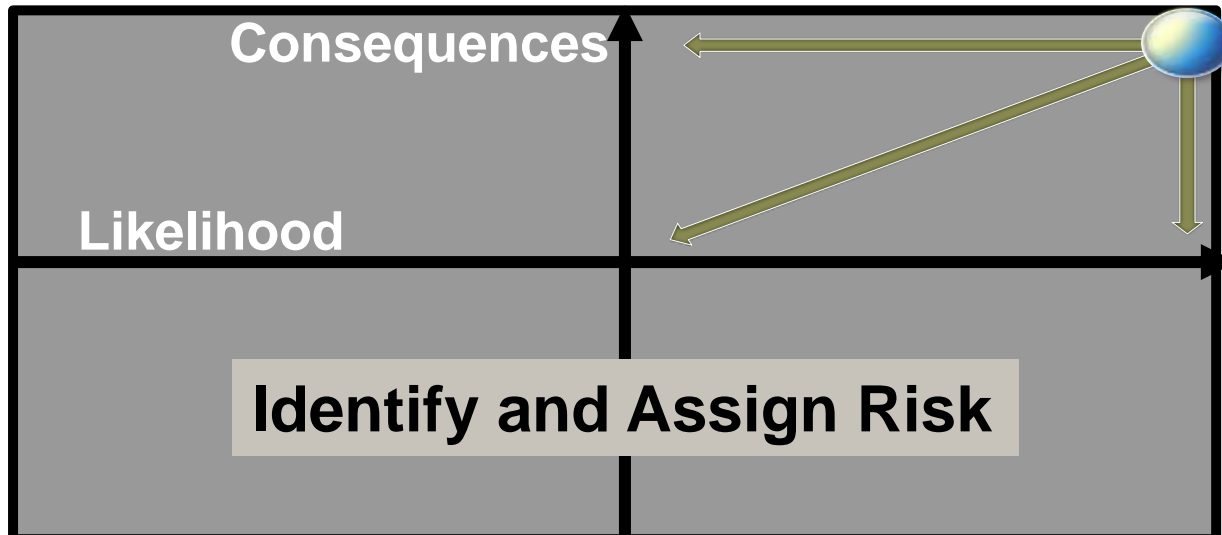


# Tampa Bay Water

- A regional provider created in 1999 by existing local governments to address needed capital investments
- Provide treated water service to 6 Member Governments
- Contract-service arrangement
  - Approximately 80% of total costs are fixed
  - Fixed costs covered by fixed charges
  - Assessed based on prior years actual water use
  - Year-end true-up based on “actuals”

# Summary of Findings – Contracts can:

- Vary significantly in purpose and structure
- Support project financing
- Provide revenue stability
- Contain provisions to separately pay for capital and operating costs (fixed v. variable)
- Create incentives
- Foster regionalization





# MWD Challenges

- MWD originally established as a “supplemental” provider
- 26 Member Agencies with “unique” needs-demands
- All “use” MWD differently
- Radial extension vs. discrete project
- Use of Purchase Orders
- Balancing of fixed charges and variable rates

# Discussion and Questions



# Contact Information

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