

**THE METROPOLITAN WATER DISTRICT
OF SOUTHERN CALIFORNIA**

**SUMMARY REPORT ON THE
AUDIT OF METROPOLITAN'S 2021 CHARGES
FOR THE STATE WATER PROJECT
ISSUED BY STATE OF CALIFORNIA DEPARTMENT OF
WATER RESOURCES**



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INDEPENDENT AUDITOR'S REPORT

The Metropolitan Water District
of Southern California
Los Angeles, California

Report on the 2021 Statement of Charges

We have audited the accompanying 2021 Statement of Charges for the State Water Project submitted to the Metropolitan Water District of Southern California (Metropolitan) by the State of California Department of Water Resources (Department).

Management's Responsibility for the Statement of Charges

The Department's management is responsible for the preparation and fair presentation of the Statement of Charges in conformity with the provisions of the State Water Project contract between Metropolitan and the Department. The Department's management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the Statement of Charges that is free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on the Statement of Charges based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Statement of Charges is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the Statement of Charges. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the Statement of Charges, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the Statement of Charges in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the Statement of Charges.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

To the Board of Directors
The Metropolitan Water District of Southern California

Basis for Qualified Opinion

In conformity with the requirements of Metropolitan's State Water Project contract with the Department, a significant portion of the Statement of Charges is based on current estimates of future costs which are not susceptible to audit verification. The Statement of Charges is also based on interpretations made by the Department's management relating to various provisions of the State Water Project contract. Many of these interpretations are the subject of ongoing negotiations. In addition, Metropolitan's contract provides that any overpayment or underpayment, by reason of error in computation or other causes, shall be adjusted in the next succeeding year. Accordingly, the Statement of Charges issued to Metropolitan is a tentative billing which is subject to adjustment when final costs are known and when resolution of unsettled issues described in our reports and others are agreed upon.

Opinion

In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary if the matters described in the preceding paragraph were susceptible to audit verification, the 2021 Statement of Charges referred to above is fairly presented, in all material respects, in conformity with the provisions of Metropolitan's State Water Project contract as we understand them.

Basis of Accounting

The Statement of Charges was prepared by the Department to comply with the provisions of the State Water Project contract between Metropolitan and the Department, which require a contractual basis of accounting which is a basis of accounting other than accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Intended Use

This report is intended solely for the information and use of Metropolitan and the Department and is not intended to be and should not be used by anyone other than these specified parties.

Richardson & Company, LLP

November 30, 2020

THE METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA

2021 STATE WATER PROJECT CHARGES

	Cost Components			Total
	Variable ^{1/}	Minimum	Capital	
<u>WATER SUPPLY CONTRACT</u>				
Transportation Charge	\$214,292,314	\$123,894,703	\$ 35,370,075 ^{2/}	\$373,557,092
Off-Aqueduct Power Facilities Charge ^{1/}		4,705,113		4,705,113
Delta Water Charge		99,738,657	57,650,635 ^{2/}	157,389,292
East Branch Enlargement		7,797,766	29,686,548	37,484,314
Water System Revenue Bond Surcharge			45,221,634	45,221,634
Tehachapi Second Afterbay Facilities			4,907,262	4,907,262
<u>DEVIL CANYON – CASTAIC CONTRACT</u>				
Operations and maintenance – Article 17(b)		12,953,290		12,953,290
Debt service on bonds – Article 17(a)			7,819,975	<u>7,819,975</u>
			TOTAL ^{3/}	<u><u>\$644,037,972</u></u>

The accompanying report is an integral part of our presentation of the Statement of Charges.

1/ Based on a water delivery schedule of 1,146,900 acre-feet.

2/ Amounts include Urban Rate Reduction credits of \$12,309,861 in the transportation charge and \$6,145,141 in the Delta Water Charge and reflects permanent Table A transfer credits in the transportation charge of \$3,626,043 as stated under Articles 41, 51, and 53 of the Monterey Amendment.

3/ Metropolitan pays the capital cost component in semi-annual payments and the minimum and variable cost components in monthly payments.

LIST OF ABBREVIATIONS

BDCP	Bay Delta Conservation Plan
CAISO	California Independent System Operator
CARA	Cost Allocation and Repayment Analysis System
DHCCP	Delta Habitat Conservation and Conveyance Program
FERC	Federal Energy Regulatory Commission
FEMA	Federal Emergency Management Agency
FRPA	Fish Restoration Program Agreement
JPOD	Joint Point of Diversion
LADWP	Los Angeles Department of Power and Water
O&M	Operations & Maintenance
P2100	The FERC project number for the Oroville Facilities
P2426	The FERC project number for the South SWP Hydropower facilities
SAP/CARA	The Department's billing system for State Water Project charges
SAP	The Department's business information and accounting system
SMIF	Surplus Money Investment Fund
SWPAO	State Water Project Analysis Office
UCA	Utility Cost Accounting
USBR	United States Bureau of Reclamation
WSRB	Water System Revenue Bond

THE METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA
 COMPARISON OF THE 2020 AND 2021 STATEMENTS OF CHARGES
 (IN MILLIONS)

	Transportation Charge			Delta Water Charge		East Branch Enlargement		Water System Revenue Bonds	Total	
	Capital	Minimum	Off-Aqueduct Minimum Variable	Capital	Minimum	Capital	Minimum			
2020 Statement of Charges dated July 1, 2019	\$ 49.6	\$ 177.8	\$ 4.7	\$ 194.2	\$ 57.5	\$ 92.4	\$ 29.0	\$ 9.6	\$ 42.7	\$ 657.5
Revisions									2.9	2.9
2020 Statement of Charges dated December 1, 2019	49.6	177.8	4.7	194.2	57.5	92.4	29.0	9.6	45.6	660.4
Increase (decrease) due to changes in:										
Estimated costs	(2.7)	4.5		19.3	3.6	7.9		0.1		32.7
Water gains and losses and reservoir storage changes		(15.0)								(15.0)
Past cost adjustments	(0.1)	(30.5)		5.0	(2.4)	(0.7)	0.1	(1.9)		(30.5)
Change in debt service	1.2						0.6		(0.3)	1.5
Recovery generation				(4.5)	(1.0)	0.1				(5.4)
Allocations among contractors	0.1			0.3					(0.1)	0.3
NET CHANGE	(1.5)	(41.0)	-	20.1	0.2	7.3	0.7	(1.8)	(0.4)	(16.4)
2021 Statement of Charges dated July 1, 2020	\$ 48.1	\$ 136.8	\$ 4.7	\$ 214.3	\$ 57.7	\$ 99.7	\$ 29.7	\$ 7.8	\$ 45.2	\$ 644.0

Note: The transportation capital and minimum charges include charges relating to the Devil Canyon-Castaic Contract and Tehachapi Second Afterbay.

Comparison of the 2021 and 2020 Statements of Charges

As shown on the previous page, Metropolitan's 2020 charges increased by \$2.9 million in the 2020 rebill of the Statement of Charges. This increase was due mainly to the inclusion of \$28.2 million of Oroville Spillway debt service and cover as part of water systems debt service. This increase was partially offset by \$22.8 million in additional revenue collected through other components due to update of costs funded with water systems bond proceeds. Metropolitan's 2021 charges decreased by \$16.4 million compared to the 2020 rebill of the Statement of Charges. The more significant of these changes are the result of the following items:

TRANSPORTATION CAPITAL: The decrease of \$1.5 million in the transportation capital component is primarily due to the following:

Decreased cost estimates \$ (2.7 million)

The 2020 cost estimates decreased as a result of the following:

\$8.2 million decrease because 1970 costs of \$162 million are fully amortized

\$1.7 million decrease due to 2019 actual costs being lower than the previous estimates by \$19 million

Offsetting these decreases is the following increase:

Cost estimates for 2020 totaling \$113 million were added to the capital component calculation causing a \$7.2 million increase to Metropolitan's charges. Some of the more significant projects are:

Reservoirs

Perris Dam remediation project and tower improvements	\$ 9.3 million
Pyramid Dam spillway investigations	7.9 million
Castaic Dam and Reservoir valve refurbishment, stream release repair and tower bridge retrofit	3.5 million
Perris Seepage recovery	3.4 million
Bethany Dam restoration	3.3 million
Cedar Springs Dam spillway repair and seepage collection system	2.1 million

Powerplants and pumping plants

Devil Canyon governor control replacement, penstock rehabilitation and generator replacement	5.1 million
Edmonston roof and elevator replacement and pump refurbishment	3.6 million
Protective relay project for the plants	3.1 million
Banks pump refurbishment and voltage regulator refurbishment	3.0 million
Dos Amigos voltage regulator refurbishment and discharge line design and construction	2.9 million

Aqueducts and pipelines

Subsidence studies and canal repairs	19.5 million
Peace Valley Pipeline remediation	2.2 million
Delta Field Division radial gate refurbishment	1.4 million

Irrigation crossing pipe inspections and repairs	\$ 1.2 million	
<u>Other structures and systems</u>		
Financial Management Enhancement Project	7.9 million	
Fire modernization design and construction	7.4 million	
Transmission operator registration	5.2 million	
Old Banks landfill cap	4.0 million	
Security upgrades and enhancements	2.6 million	
Centralized Control System Migration Phase 4	2.1 million	
Water and power reporting system	1.3 million	
Seismic bridge retrofits	1.2 million	
Optical network replacement	1.2 million	
<u>Regulatory compliance</u>		
Skinner Fish Facility projects	2.1 million	
<u>Change in the past cost adjustment</u>		\$ (0.1 million)
<u>Change in Tehachapi Second Afterbay debt service</u>		1.2 million
<u>Change in credit related to permanent water transfers</u>		0.1 million
TOTAL CHANGE IN TRANSPORTATION CAPITAL COMPONENT		\$ (1.5 million)
TRANSPORTATION MINIMUM: The decrease in the transportation minimum component of \$41.0 million is due primarily to the following increases and decreases:		
<u>Changes in estimated costs</u>		
Decrease in annual cost estimates for 2020 and 2021 O&M		\$ (4.3 million)
Increase in cost estimates for 2020 and 2021 due primarily to increased planned extraordinary activity totaling \$15 million		8.8 million
Increase in statewide costs	\$ 11 million	
Increase in power and pumping plant costs	7 million	
Increase in intake and aqueduct costs	3 million	
Increase in regulatory compliance costs	2 million	
Decrease in dam and reservoir costs	(1 million)	
Decrease in other maintenance costs	(7 million)	
Total change in estimated costs		4.5 million
<u>Revisions to 2020 and 2021 estimated water gains and losses and reservoir storage changes</u>		(15.0 million)
<u>Changes in past cost adjustments</u>		
Adjustment of 2019 costs from estimates to actual		(16.6 million)
Decrease for the 2020 Statement of Charges past cost adjustment		(11.2 million)
Impact of additional year of interest on the prior over and underpayments		(2.1 million)
Correction of improperly billed costs		(0.6 million)
Capitalization of projects previous included in the minimum component		(0.1 million)
Update of historical water gains/losses and reservoir storage adjustments		0.1 million
Total change in past cost adjustments		(30.5 million)
TOTAL CHANGE IN TRANSPORTATION MINIMUM COMPONENT		\$ (41.0 million)

OFF-AQUEDUCT MINIMUM: Costs for Metropolitan’s off-aqueduct minimum component did not change significantly between 2020 and 2021.

TRANSPORTATION VARIABLE: The variable component increased by \$20.1 million between 2020 and 2021. This increase results from the following:

Changes in estimated power costs \$ 23.9 million

Overall, net power costs for the Project increased by \$15.8 million due to:

- Increase of \$6.5 million in variable transmission costs
- Increase of \$5.5 million in short-term power purchases
- Increase of \$4.2 million in intermediate term power purchases
- Increase of \$2.1 million in the cost of recovery generation
- Decrease of \$0.1 million in miscellaneous power charges
- Decrease of \$1.3 million in revised cost estimates at Hyatt-Thermalito
- Decrease in CAISO estimated charges of \$2.1 million
- Decrease of \$3.4 million in long-term power purchases
- Decrease in power revenue from the Lodi Energy Center of \$4.8 million
- Decrease of \$2.7 million in CAISO ancillary services revenue
- Increase of \$3.1 million in CAISO renewable energy revenue

Due to the large drawdown expected at Castaic Lake for 2021, Metropolitan’s share of the variable charge increase is higher than the total

Change in replacement charges

Actual 2019 replacement costs are less than what was originally budgeted and 2021 estimates are lower than 2020 estimates (4.6 million)

Total change in estimated costs 19.3 million

Changes in past cost adjustments

Increase for the 2019 actual costs being higher than estimates 10.2 million
 Additional year of interest in the calculation of over/underpayment 2.0 million
 Adjustment to 2018 and prior power costs for updates and corrections (0.5 million)
 Decrease for the 2020 Statement of Charges past cost adjustment (6.7 million)

Total change in past cost adjustments 5.0 million

Changes in recovery generation credits (4.5 million)

The decrease is primarily due to Metropolitan’s increased deliveries of 34,620 acre-feet to the West Branch and higher mill rates on the East Branch.

Changes in allocations among contractors 0.3 million

Metropolitan shifted 34,620 acre-feet of deliveries from the East Branch to the West Branch. All other contractors water deliveries decreased by 5,093 acre-feet.

TOTAL CHANGE IN TRANSPORTATION VARIABLE COMPONENT \$ 20.1 million

DELTA WATER CHARGE CAPITAL: The Delta Water Charge capital component increased \$0.2 million primarily due to the following:

Changes in estimated costs

Net \$107 million increase in estimated capital project costs for 2020 through 2023 \$ 3.6 million

Dams, reservoirs and aqueducts (Increase of \$121 million)

Improvements at Oroville Dam	\$ 48.0 million
Sisk Dam remediation	38.3 million
Gate repairs in the Oroville Facilities	14.1 million
Oroville Spillway recovery, less potential FEMA reimbursement	9.6 million
Bethany Dam restoration, rodent repairs and valve refurbishment	4.0 million
California Aqueduct aqueduct and gate repairs	3.4 million
Fish screens at Sherman and Twitchell Islands	1.7 million
Improvements at the Upper Feather River dams	1.0 million
Lake Oroville forecast informed reservoir operations strategy	0.9 million
Improvements at the Thermalito facilities	0.2 million
Suisun Marsh gate refurbishments	0.1 million
Clifton Court Forebay Dam armoring and gate refurbishment	(0.1 million)

Pumping Plants and Powerplants (Increase of \$70 million)

Hyatt Powerplant upgrades and refurbishments	47.2 million
Gianelli Pumping-Generating Plant repairs	11.9 million
Thermalito Powerplant restoration, activation and upgrades	8.5 million
Banks Pumping Plant repairs	2.6 million

Other (Increase of \$53 million)

Oroville Division bridge retrofits, security enhancements and other projects	23.4 million
Statewide management, communication and reporting upgrades	15.4 million
San Luis Field Division security upgrades, fire safety modernization and other projects	8.0 million
Delta Field Division security enhancements and other projects	3.4 million
North San Joaquin Division landfill cap and O&M Center upgrades	2.3 million

Regulatory Compliance (Decrease of \$137 million)

Yolo Bypass fish projects for expected USBR contribution	(63.5 million)
FRPA programs for property restoration and land purchases	(44.8 million)
Salmon Protection Technology Study delays	(31.5 million)
Feather River fish projects	(0.4 million)
Delta Habitat Conservation Plan	0.5 million
Projects required as part of the FERC P2100 license	0.8 million
Skinner Fish Facility projects	1.9 million

Total change in estimated costs 3.6 million

Changes in past cost adjustments:

Actual costs for 2019 were lower than estimated mainly for FRPA and Yolo Bypass Restoration (2.4 million)

Total change in past cost adjustments (2.4 million)

Changes in the capital credit for Hyatt-Thermalito

Revision of debt service for FERC relicensing and other capital projects	\$ (1.0 million)
Total change in recovery generation revenues	<u>(1.0 million)</u>

TOTAL CHANGE IN DELTA WATER CHARGE CAPITAL COMPONENT **\$ 0.2 million**

DELTA WATER CHARGE MINIMUM: The increase of \$7.3 million in the Delta Water Charge minimum component is primarily due to the following:

Changes in estimated costs

Increase of \$43 million for 2020 through 2021 for major O&M activities \$ 1.8 million

Reservoirs, aqueducts and water supply (Increase of \$14 million)

Oroville Facilities projects (spillway recovery, FERC requirements)	\$ 14.5 million
California Water Plan update	0.3 million
Delta seismic studies	0.3 million
Bethany Dam studies	(0.2 million)
State Water Project dam safety program	(1.4 million)

Pumping Plants and Powerplants (Increase of \$5 million)

Hyatt Powerplant inspections and repairs	4.4 million
Gianelli Pumping-Generation Plant upgrades	0.3 million
Banks Pumping Plant HVAC replacement	0.2 million

Other costs (Increase of \$20 million)

Fiscal Services utility billing and debt administration	15.2 million
Statewide power and water programs	3.4 million
Salton Sea costs improperly billed	2.0 million
Division of O&M baseline costs at Delta and San Luis	2.0 million
SWPAO, mainly for project repayment and financial analysis	0.7 million
Division of Engineering statewide operations	0.6 million
Asset management program	0.6 million
Technology change management system	0.2 million
Oroville strategic risk communication plan	0.2 million
Statewide ADA studies and controller refurbishments	(0.1 million)
Property management costs	(0.3 million)
Power and Risk Office	(0.6 million)
Sealing and paving roads in the Oroville Field Division	(1.9 million)
Old Banks Landfill costs transferred to capital component	(1.9 million)

Changes in 2020 through 2021 adjustments (Increase of \$4 million)

Storage changes and aqueduct gains/losses allocated to the Gianelli Pumping-Generating Plant and the San Luis Reservoir	4.3 million
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<u>Increased O&M cost estimates for 2022 to 2035</u>	<u>6.1 million</u>
Total change in estimated costs	<u>7.9 million</u>

Changes in past costs adjustments

Adjustment of 2019 costs from estimates to actual costs	(0.5 million)
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Corrections and adjustments to 1999 to 2018 costs	\$ (0.2 million)
Total change in past costs adjustments	<u>(0.7 million)</u>

Changes in the operating credits for Hyatt-Thermalito

Power revenue credits changed due to revised projected O&M costs for the Oroville Powerplants.	0.1 million
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Total change in recovery generation revenues	<u>0.1 million</u>
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TOTAL CHANGE IN DELTA WATER CHARGE MINIMUM COMPONENT	<u>\$ 7.3 million</u>
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EAST BRANCH ENLARGEMENT CAPITAL: The East Branch Enlargement capital component increased by \$0.7 million between 2020 and 2021 due to the following:

<u>Change in debt service between 2020 and 2021</u>	\$ 0.6 million
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<u>Change in past cost adjustment for debt service in 2020 and prior</u>	<u>0.1 million</u>
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TOTAL CHANGE IN EAST BRANCH ENLARGEMENT CAPITAL COMPONENT	<u>\$ 0.7 million</u>
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EAST BRANCH ENLARGEMENT MINIMUM: The East Branch Enlargement minimum component decreased by \$1.8 million between 2020 and 2021 due to the following

<u>Changes in estimated costs</u>	\$ 0.1 million
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<u>Changes in past cost adjustments</u>	(1.9 million)
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Cost estimates for 2020 increased by \$0.2 million

The past cost adjustment in the 2020 Statement of Charges decreased current charges by \$0.9 million.

Revisions to costs for 2019 and prior in total were \$1.2 million lower than previous amounts.

TOTAL CHANGE IN EAST BRANCH ENLARGEMENT MINIMUM COMPONENT	<u>\$ (1.8 million)</u>
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WATER SYSTEM REVENUE BOND SURCHARGE: The Water System Revenue Bond Surcharge decreased by \$0.4 million as a result of the following:

<u>Change in debt service</u>	\$ (0.3 million)
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Decrease of \$0.8 million for bond cover and debt service on power projects

Decrease of \$0.2 million due to the increase in revenue collected through other components

Increase of \$0.7 million due to higher scheduled debt service in 2021 for previous bond series

<u>Change in allocation among contractors:</u>	<u>(0.1 million)</u>
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TOTAL CHANGE IN WATER SYSTEM REVENUE BOND SURCHARGE	<u>\$ (0.4 million)</u>
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Future Potential Refunds and Adjustments

Metropolitan's estimated 2021 charges of \$644 million do not include certain credits, refunds and adjustments that are expected in 2021 as part of the Department's normal accounting and billing process. The refunds below are expected to reduce Metropolitan's 2021 billings by approximately \$71.3 million.

	<u>Estimated Refund Date</u>		
<u>Cover – Water System Revenue Bond (WSRB)</u>			
January 2020	April 2021	\$ 12,098,000	
July 2020	October 2021	<u>12,098,000</u>	\$ 24,196,000
<u>Cover – East Branch Enlargement (EBE)</u>			
March 2020	April 2021	2,920,000	
September 2020	October 2021	<u>2,920,000</u>	5,840,000
<u>Cover – Tehachapi Second Afterbay</u>			
March 2020	April 2021	488,000	
September 2020	October 2021	<u>488,000</u>	976,000
<u>SMIF Interest - WSRB</u>			
July 2020 - December 2020	April 2021	797,000	
January 2021 - June 2021	October 2021	<u>797,000</u>	1,594,000
<u>SMIF Interest - EBE</u>			
July 2020 - December 2020	April 2021	242,000	
January 2021 - June 2021	October 2021	<u>242,000</u>	484,000
<u>SMIF Interest - Reserve Account/Federal Securities</u>			
July 2008 - December 2019	Unknown		21,231,000
<u>Power Debt Service</u>			
2020 power debt service	May 2021		11,198,000
<u>Devil Canyon and Tehachapi Second Afterbay</u>			
2020 Devil Canyon debt service	May 2021	3,032,000	
2020 Tehachapi debt service	May 2021	<u>2,736,000</u>	<u>5,768,000</u>
TOTAL ESTIMATED REFUND			<u><u>\$ 71,275,000</u></u>

The 2021 variable and off-aqueduct charges may be reduced further if 2021 costs are determined to be overstated during the year. Also, amounts described in this section are in addition to the credits, refunds and adjustments related to audit findings that are summarized on page 26.

The Department believes that the allocation methodology for returning excess debt service reserves and the springing amendment funds should also be used to refund earnings on federal securities and SMIF interest on the debt service reserve account. The Department estimates that SMIF interest on the reserve account and earnings on federal securities totaling \$44.2 million has accumulated. The Department intends to retain \$10.0 million, which will not be refunded until an allocation methodology has been developed. The remaining \$34.2 million may be returned in 2021, of which Metropolitan's share is estimated to be \$21,231,000.

ISSUES RELATED TO THE 2021 STATEMENT OF CHARGES

During our audits, we encountered a number of issues related to the calculation of the Statements of Charges that have been or need to be addressed by the Department. Some of these issues result in errors in the Statement of Charges.

Statement of Charges Preparation. Since the implementation of SAP in 1999, responsibility for certain aspects of the accounting and cost allocation systems that support the Statement of Charges have shifted from the accounting department to program managers and SWPAO. Initially, these changes resulted in an increase in audit findings. One significant change was the ability for program managers to create cost objects and determine the allocation of the costs to reach when, prior to the implementation of SAP, this analysis was performed by accounting department personnel with knowledge of the cost allocation and billing system. An example of a finding that occurred in the past is the inclusion of the Gorman Creek emergency repair costs in the transportation minimum component, even though the costs appeared to meet the qualifications for capitalization. Since the conversion to SAP, SWPAO created the Program Control Section to oversee the cost allocation. The program managers have more knowledge of the allocation of costs for billing purposes and the Department created a committee to review the capitalization of costs. Similar capitalization errors have not been noted in recent years.

As a result of the SAP upgrade in 2006, the cost allocation and calculation of the Statement of Charges is now performed in a separate system in SAP from the financial accounting system. The system used for cost allocation is based on the historical information extracted from the financial accounting system. The assurance that all costs are properly transferred from the financial accounting system to the cost allocation system is vital and we recommend the Department continue to validate the completeness and accuracy of the amounts used for the determination of the Statement of Charges.

Prior to the conversion to SAP, corrections and adjustments to historical costs were made by the accounting department but now SWPAO may also initiate changes to historical costs. We believe that changes to historical costs should be made with concurrence by accounting department personnel. Previously, revisions to the accounting records could not be posted to historical years for cost allocation purposes. As a result, adjustments to the financial accounting records were made by Fiscal Services to the current fiscal year and if additional entries were needed to reflect the adjustment in the proper year, these were sometimes made by SWPAO. The Department created an additional entry field for transactions in the financial accounting system in 2014 allowing adjustments to be reflected in any historical period for cost allocation purposes. This change allows for adjustments to historical years to be posted by the accounting department and limits the number of adjustments made by SWPAO to those needed for cost allocation purpose that cannot be reflected through accounting adjustments.

We have also noted an increased reliance on spreadsheets by SWPAO since the implementation of SAP. Spreadsheets are being used to calculate future cost projections, East Branch Enlargement charges, the Water System Revenue Bond Surcharge, portions of the variable energy charges, Off-Aqueduct Power Facilities charges, the transportation capital component and the Delta Water Rate. SWPAO believes these spreadsheets ensure the Statement of Charges is calculated in accordance with the water supply contracts and allow for greater flexibility in making late revisions during the calculation of the Statement of Charges. We agree the spreadsheets result in calculations that are in accordance with the water supply contracts. Some of the spreadsheets are large and complex, which results in the potential for errors and

causes an administrative burden on SWPAO staff. We recommend the Department incorporate the functions that are feasible in the new Cost Allocation and Billing System.

In addition to a shifting of responsibility and use of spreadsheets, we have noted that some audit findings are not being corrected timely. Several years ago, a group of employees within SWPAO were assigned responsibility for reviewing and correcting audit findings. We continue to meet with the group, which has resulted in the correction of audit findings. These meetings are effective in the resolution of some types of errors, but there remain findings, especially those related to policy issues, that require involvement of other Department staff and the contractors to be resolved.

We recommend the Department continue to identify the risks associated with the processes and procedures in place for the preparation of the Statement of Charges and, where weaknesses are identified, changes should be implemented to ensure accurate billings and timely corrections.

Chargeability and Funding of Projects

During our audits, we have noted disputed costs that the contractor believe are improperly being included in the Statement of Charges. These costs include those the contractors contend partially or completely benefit purposes other than water supply and also costs that benefit others besides the State Water Project contractors. Some of these costs include:

- The design of a new road to a Lake Oroville boat ramp, which the Department feels is necessary for security reasons, but the contractors believe benefits recreation.
- The aquatic weeds program, where work is currently focused in the Clear Lake area. This project benefits the Delta and the State Water Project, but it also benefits other water agencies that do not appear to be contributing to the project.
- Carbon sequestration and rice research at Sherman and Twitchell Islands, which the Department felt was necessary to address subsidence, but the contractors did not believe had a water supply purpose.
- The extensiveness of the compliance work being performed in the Delta.
- Boat ramps that are used by both the Department and the public.
- Security for project facilities during 4th of July events.

These discrepancies appear to be due to the Department and contractors having different views on the types of costs that are chargeable to the contractors. We recommend the Department and contractors agree on criteria for determining reimbursable costs based on the water supply contract and the settlement letters.

We also recommend the Department determine the funding sources of projects as they are being developed and continue to evaluate the funding yearly as the projects are budgeted. Ideally, funding commitments from outside sources should be obtained prior to the start of the project so the costs/benefits of the projects can be better evaluated and the contractors are not temporarily or permanently financially responsible for the project if outside funding is not obtained. The Department should periodically obtain feedback from the contractors on the worthiness of proposed and existing projects.

Finalization of Energy Charges and Variable Billing Recalculation. The Department has not finalized power costs since 1997, resulting in 22 years of variable charges subject to adjustment. In the past,

SWPAO, in conjunction with the accounting department, would periodically update preliminary power costs until final power costs could be determined. We have received updates to preliminary power costs for some years as the Department updates the power valuation recorded in the accounting system. The use of the outdated information has resulted in errors that span several years, such as those for the Oroville power adjustment.

Water System Revenue Bond (WSRB) Surcharge Calculation. In conjunction with the development of the new SAP/CARA system in 2000, the Department developed a calculation of the WSRB Surcharge using the SAP/CARA system. However, this system produced a Surcharge that was significantly different from the estimated Surcharge amounts calculated as part of the 2000 Statement of Charges. As a result, in the 2001 to 2011 Statements of Charges, the Department calculated the WSRB Surcharge using the relative proportion of the Surcharge to total debt service from the 2000 Statement of Charges and applied that proportion to WSR bonds debt service costs for each year.

For the 2012 through 2015 Statements of Charges, the Department manually prepared a WSRB Surcharge calculation in accordance with Article 50 of the Water Service Contract; however, outdated bond proceed amounts were used in the calculation. We noted that the bond proceeds used to determine the base upon which the Surcharge was calculated was understated approximately \$380 million each year because the Department used the bond proceeds schedule from the 2000 Statement of Charges and added projects originating since then, instead of using the most current allocation of bond proceeds schedule. As a result, incorrect proceeds amounts were used to calculate the amount of capital costs that are recovered through the transportation capital and Delta Water Charge capital components at the Project Interest Rate. Since certain costs being recovered from the Delta Water Charge and transportation capital components are excluded, while the corresponding debt service costs are being included in the calculation of the Surcharge, the Surcharge is overstated. Starting with the December rebill of the 2015 Statement of Charges, the Department began using an interim method agreed to by the contractors that included an amount of bond proceeds up to the amount of actual capital expenditures used in the calculation of the conservation capital and transportation capital components at the Project Interest Rate. The difference between costs and proceeds was eliminated in the rebill of the 2020 Surcharge and the 2021 Surcharge.

This methodology is considered to be interim because the Department has never reconciled project costs to the proceeds received. The Surcharge is based on an allocation of proceeds for water system and other facilities that could change once this reconciliation is completed. The Department has contracted for the preparation of the reconciliation, which is expected to be completed in 2021. Using the results of this reconciliation, the Surcharge calculations will be corrected in a future Statement of Charges. In addition, there are a number of audit findings related to the Surcharge calculations from several years ago and also findings related to the capital components that will affect the Surcharge calculation, including East Branch Enlargement cost allocation issues that need to be resolved before the Surcharge calculations can be considered final. These findings, as well as the reconciliation of project costs, will affect all Surcharge calculations prior to 2000. We will monitor the Department's status in revising these prior calculations.

In addition, the Department's original methodology for determining the revenue for Water System Projects collected through the Conservation component used in the Surcharge resulted in an understatement of the revenue and an overcollection through the Surcharge. The Department revised the methodology for the 2020 Statement of Charges. The amount overbilled to Metropolitan is estimated to

be at least \$75 million for 1989 to 2019. The Department is in the process of evaluating the amount of the overcollection and developing a proposal to correct the error.

Debt – Cost Reconciliation. In part due to our audit finding related to the overcharge of the contractors through the Water System Revenue Bond Surcharge beginning in the 2001 Statement of Charges, the Department is in the process of reconciling the proceeds from previous bond issuances to the amounts recorded in the cost allocation system. As part of our meetings and work outside of the audit of the Statement of Charges, we have met with the Department and the consultant to obtain an understanding of the methodology used in the analysis. We have also reviewed the results provided by the consultant. A list of questions requesting clarification on how amounts in the analysis were determined has been discussed with the Department, and they are in the process of making revisions to the reconciliation. Once this reconciliation process is finalized, it is expected the Department will address pending issues including the over collection of amounts through the Water System Revenue Bond Surcharge and the return of interest and debt service reserves.

USBR Use of Facilities. The USBR and the Department regularly contract for water to be delivered to the USBR through the Banks Pumping Plant. For the 2018 Statement of Charges, the Department billed the USBR \$4,661,000 for a portion of 2013 and for 2014 and 2015 water. The USBR paid \$3,657,000 in December 2016, which was credited in the 2018 Statement of Charges. The remaining \$1,004,000 was disputed. In 2019, the Department agreed to rescind the remaining balance and apply credits earned by the USBR for water conveyed by them for the Department in 2014 and 2017 against the Department's charges.

Grid Management Charges. CAISO, formed in 1996 as part of the State's deregulation plan, operates regional transmission facilities and charges grid management fees for its services. The Department determined that the charges billed to the Department by CAISO include grid management charges related to all energy usage, including those related to United States Bureau of Reclamation (USBR) water deliveries, and that the entire amount of these costs were being billed to the state water contractors. In July 2012, the Department received \$5.45 million from a settlement with the USBR in satisfaction of \$6.5 million in charges assignable to the USBR for 2005 through 2012. In September of 2014, the Department filed a claim under the Contracts Disputes Act of 1978, which grants contracting officers the authority to resolve claims between a contractor and the Federal government. The Department is seeking \$10.5 million for energy scheduling costs incurred from 1998 through 2004 on behalf of the USBR.

Coastal Branch Reallocation. Beginning with the 2011 Statement of Charges, the Department manually reallocated transportation minimum costs previously charged to three Coastal Branch reaches on a state-wide basis. The Department decided that because the Coastal contractors provide all the necessary operation and maintenance for these reaches, they should not be allocated transportation minimum charges. As a result, in the 2021 Statement of Charges, transportation minimum costs for the years 2000 through 2019 totaling \$2,950,000 were manually reallocated from the three Coastal Branch reaches to other reaches on the aqueduct, increasing Metropolitan's transportation minimum component by \$1,711,000. We noted that some reallocated costs are for the overall management of the State Water Project, rather than direct maintenance of those reaches. As a result, we do not believe they should be excluded from these Coastal Branch reaches. Coastal encasement project costs were also reallocated state-wide but are specific to the Coastal Branch. We discussed this issue with the Department, and they agreed that an analysis of the transportation minimum costs assigned to these Coastal reaches should be

performed before this reallocation is made permanently in the system. We will continue to discuss this issue with the Department and Metropolitan.

Reallocation of Recreation Costs. Metropolitan has contended that the Department inappropriately included, in Metropolitan's bills, charges for the recreation and fish and wildlife enhancement portion of facilities financed with Water System Revenue Bonds. As a partial solution for funding recreation debt service costs, the Department revised the recreation allocation percentage for certain Delta facilities costs from 14% to 3.3% for minimum and 3.4% for capital, which shifted additional costs retroactively to Metropolitan and the other contractors. The Department believes this change better reflects the purpose of these facilities and their recreation and fish and wildlife enhancement cost structure. The impact of this reallocation of costs was a cumulative increase to Metropolitan's conservation capital and minimum components by \$54,553,000 and \$36,276,000, respectively, in the 2007 through 2021 Statements of Charges.

In 2012, the Legislature appropriated funds for recreation and fish and wildlife enhancement from the Harbors and Watercraft Revolving Fund. Of the \$10.0 million annual appropriation, \$7.5 million is for current costs and \$2.5 million is for past recreation obligations incurred as of December 31, 2011. The Davis Dolwig Amendment also required the revision of the project purpose factors at the Dos Amigos plant and downstream. This change in project purpose factors results in an increase in the amounts allocated to recreation at Castaic, Silverwood and Perris Lakes and a decrease in the amounts allocated to recreation for other reaches. We estimate the change in project purpose factors result in a net \$10.3 million decrease in costs allocated to Metropolitan from 2013 to 2019.

The Department refunds in cash the annual \$2.5 million allocation to offset increases in contractors' charges due to the change in the project purpose factors. Initially, the Department returned the full \$2.5 million each year to the contractors, but the Department revised the methodology to only refund amounts up to the extent the contractors' charges increased. The portion of the \$2.5 million that was not refunded, which cumulatively totaled \$7,137,000 as of July 2019, will be returned when increases in the contractors' charges due to the change in project purpose factors exceeds \$2.5 million. Due to the revision in the refund methodology, Metropolitan was previously refunded \$2,567,000, which will be offset against future refunds. The appropriations through 2019 have been returned to the contractors.

Each year, the \$7.5 million is applied to capital and minimum recreation, fish and wildlife enhancement costs at reaches upstream from the Dos Amigos plant. We will monitor these items to ensure the proper adjustments and refunds are given to Metropolitan.

Springing Amendment. On April 1, 2002, the Department amended provisions of the General Bond Resolution relating to the Debt Service Reserve Account, reducing the amount of reserves the Department is required to maintain. Between 2008 and 2012, refunds totaling \$72.1 million have been returned, of which Metropolitan's share was \$43.9 million. In 2014, interest earnings on the debt service reserve of \$9.3 million was returned to the contractors, of which Metropolitan's share was \$5.8 million. Additional refunds will be provided when the reconciliation of project costs compared to bond proceeds is completed in 2021.

Delta Fish Agreement Amendment Four. An agreement was signed between the Department and the Department of Fish and Game (DFG) on December 30, 1986 to provide payments to offset fish losses

caused by operations in the Delta. On October 18, 2010, the Department and the DFG signed the Fish Restoration Program Agreement (FRPA) which the contractors did not support. The program goal is to mitigate SWP impacts on sensitive fish species in the Delta and will create or restore fish habitat and include other activities with the intent to satisfy requirements in various biological opinions. The FRPA capital and extraordinary minimum estimates included in the 2021 Statement of Charges total \$170 million for 2020 through 2023. Actual capital and extraordinary minimum costs incurred through 2019 total \$117 million.

East Branch Enlargement. During April 1986, Metropolitan and the Department entered into Amendment No. 19, known as the East Branch Enlargement Amendment, to the basic Water Service Contract, which established the basis for repayment of the costs of enlarging the East Branch of the California Aqueduct. The Enlargement work was in addition to the Mojave Division modification to correct the basic capacity deficiency. The methodology used by the Department to allocate costs to the Enlargement and the modification is still considered an interim or temporary approach that has not been officially accepted by the contractors. The Department has indicated that consideration will be given to Metropolitan's concerns while developing the revised East Branch Enlargement allocation methodology. Because these allocation issues affect the Cost Debt reconciliation and the WSRB Surcharge, which the Department plans to finalize in 2021, resolution of the East Branch cost allocation issues has become a higher priority. East Branch Contractors and the Department are currently negotiating a final methodology for East Branch and East Branch Enlargement cost allocation.

The Department has also indicated that the project purpose split allocating a portion of East Branch Enlargement costs to recreation and the Downstream Distribution allocation of variable costs to the East Branch Enlargement will both be eliminated in the future.

As part of the Department's review of costs during the Debt-Cost reconciliation, it was determined that \$24.9 million in transportation capital costs were improperly recorded as recreation costs as a result of the manual reallocation of East Branch Enlargement capital costs. If these costs were reclassified from recreation to the transportation capital component for the 2021 Statement of Charges, Metropolitan's transportation capital charge would have been approximately \$2,725,000 higher.

Uncollected Power Revenues. In April 2012, the Department received \$11.5 million from CAISO as settlement for outstanding uncollected power revenues from 2000 and 2001. The Department credited the contractors in the 2013 Statement of Charges, however, later determined that these credits are partially related to non-Project energy and reversed the credits in the 2014 Statement of Charges. The Department has determined \$5,124,000 of the settlement applies to Project revenues. For the 2018 Statement of Charges, the Department reduced net power costs for 1998 to 2002 for this amount, net of the impact of interest. The Department has indicated they will discuss the allocation methodology with the auditors in the future.

Oroville Spillway Emergency. In February 2017, the flood control (main) spillway and emergency spillway at Lake Oroville both suffered severe damage as a result of heavy rainfall. The incident was declared a federal disaster in April 2017 making it eligible for assistance through the Federal Emergency Management Agency (FEMA). Up to 75 percent of eligible response and recovery costs will be reimbursed by FEMA. The actual costs incurred for the response was roughly \$160 million. The Department expects to receive reimbursement from FEMA for 75% of most of the response costs.

Governor Brown suspended Water Code section 11465 for the response and recovery costs in April 2017, which allowed for the exclusion of these costs from the Statement of Charges.

In April 2017, the Department entered into a contract to repair the flood control and emergency spillways. The Department has incurred approximately \$953 million in recovery costs through December 31, 2019 and expects to spend an addition \$77 million. The Department has obtained an \$800 million commercial paper line of credit to provide temporary funding specifically for repairs of the Oroville spillways. The Department has request reimbursement for 75% of the recovery costs, but FEMA has indicated \$346 million of the costs are ineligible for reimbursement. The Department, with the contractors' approval, included the Oroville Spillway costs in the 2021 Statement of Charges, but also included a credit for 75% of the costs for the potential FEMA reimbursement. If the Department does not receive reimbursement for 75% of the costs from FEMA or other funding sources, additional costs will be charged to the contractors when the suspension of Water Code section 11465 is rescinded.

Project Order 36. In March 1968, the Department issued 50-year revenue bonds to assist in the financing of the State Water Project. The bonds were secured by the revenue from the power sale contract entered in November 1967 with three major utilities to sell the power generated from the Hyatt Thermalito Powerplants for \$16,150,000 per year. The Department cancelled the power sale contract in 1977, began operations as a utility in 1983 and retired all the Oroville revenue bonds by 1994. When the revenue bonds were retired, the Department issued Project Order 36 stating the capital portion of the Oroville power revenue would continue to be valued at the revenue bond payment amount of \$14,650,000 per year through the original bond maturity date of November 2017. In addition to the \$14,650,000, the Department began including the debt service payments for capital projects related to the Powerplants in capital power revenue. The Department temporarily extended Project Order 36 for the 2018 through 2021 Statement of Charges. As a result, the \$14,650,000 was included in power revenue as a variable cost in 2018 through 2021. The Department has indicated they will discuss the proposed methodology with the contractors. If the Department revises the value of the capital power revenue, Metropolitan's variable and Delta Water Charge components would change.

Contract Extension. In 2014, the Department and the contractors reached an agreement in principle to extend the water supply contracts through 2085. As part of the proposed agreement, the billing methodology for some components will be revised. The Conservation minimum component will be billed to recover costs in the year they are incurred, and the Conservation and transportation capital components will be billed based on the contractors' share of debt service related to the costs incurred. The billing transition date for the new method will be the first calendar year, six months after the effective date of the contract extension. Costs incurred prior to the billing transition date will continue to be billed based on the current methodology until they are fully recovered in 2035. The Department's most recent estimate for the effective date of the new methodology is January 1, 2024. The Department is developing a new Cost Allocation and Billing System to calculate the Statement of Charges using the revised billing methodology.

Use of Facilities for Contractor Deliveries Outside Their Service Area. Multiple agreements have been signed between State Water Project contractors for non-permanent transfers and exchanges of water. Some of these agreements result in water being delivered to contractors outside their normal service area, such as deliveries to the San Luis Reservoir for a South Bay contractor. Previously, the Department has not assessed a use of facilities charge if one party to the contract has capacity in the portion of the

aqueduct being used. Since 2017, contractors have signed amendments to contracts resulting in a use of facility charge when they do not have capacity in the aqueduct at the temporary delivery points. Deliveries have been made that are subject to a use of facility charge, but the Department has not billed these amounts. The Department has recently indicated they plan to continue their original interpretation that a use of facility charge is not required if one party to the agreement has capacity in the aqueduct.

Article 13b. At Metropolitan's request, we reviewed payments made by the Department for litigation and claims filed against the State Water Project. These included payments resulting from claims filed through the Victim Compensation and Government Claims Board, the State Personnel Board, lawsuits and threatened lawsuits. Article 13b of Metropolitan's water supply contract with the Department states the contractors shall not be held liable for damage caused by project water prior to the passage through a delivery structure. We noted costs included in the Statement of Charges that appear to meet the definition under Article 13b. We also noted payments to employees and former employees for the settlement of claims that were charged to the contractors. These appeared to be related to personnel issues and not costs necessary to deliver project water, so they should not be charged to the contractors. We will continue to monitor these costs and whether they are billed to the contractors.

Delta Conveyance Facility and Sites Reservoir. The Department and contractors have had discussions related to the Delta Conveyance Facility and Sites Reservoir. Metropolitan's charges will increase if these projects are agreed to and billed in the future.

TABLE A

**Summary of Settled Audit Findings Resulting in Changes to
the 2021 Statement of Charges**

Throughout the year, we worked with Metropolitan's representatives and the Department to resolve audit exceptions. The following is a brief summary of the items resolved during which affected the 2020 revised Statement of Charges and the 2021 Statement of Charges.

Items	Effect on Metropolitan's 2021 Costs Increase(Decrease)
Findings corrected in the rebill to the 2020 Statement of Charges:	
1. 2020 debt service and cover for the Oroville Spillway recovery of \$28.1 million were included as part of water systems debt service in the revised Surcharge. (Refer to page 27)	\$ 15,224,000
2. The Department updated costs for Water Systems Conservation projects used in the Surcharge calculation, resulting in a \$22.8 million decrease in the Surcharge component. (Refer to page 27)	(12,345,000)
	<u>\$ 2,879,000</u>
Findings corrected in the 2021 Statement of Charges:	
3. Cap and Trade emission allowances expected to be used in 2019 of \$3,353,000 were included in the variable component, but were also included in the year they were purchased, resulting in an overstatement of the variable component. This discrepancy has been eliminated since the 2019 amounts billed are now actual costs. (Refer to page 28)	\$ (1,872,000)
4. Amounts related to contract retentions from 1999 to 2004 totaling \$1.4 million were improperly charged to the contractors. Adjustments were made to transfer these amounts back to a suspended cost center. (Refer to page 28)	(625,000)
5. The 2019 Hyatt Thermalito power revenue used in the calculation of the Delta Water Charge was updated to reflect current costs, resulting in an increase of net costs by \$3,185,000. (Refer to page 28)	131,000
	<u>\$ (2,366,000)</u>

The following item included on Table B in the prior year, was subsequently determined to no longer be an error:

6. The commitment fees for the Series 2 commercial paper line are being allocated Statewide. (Refer to page 28)

TABLE B

**Summary of Audit Findings Projected to Result in Changes to
the 2022 Statement of Charges**

Throughout our examination, we worked with Department and Metropolitan representatives to resolve findings which arose during our audit of the 2021 Statement of Charges. We will work with the Department to ensure the correction of these findings in the 2022 Statement of Charges.

Items	Effect on Metropolitan's 2022 Costs Increase (Decrease)
<u>New Findings</u>	
1. Administrative fees and the settlement payment totaling \$1,460,000 received for litigation related to the construction of the Tehachapi Second Afterbay were not included in the variable component. (Refer to pages 28 and 29)	\$ (1,168,000)
2. The payment for peaking capacity foregone at the Castaic Powerplant of \$582,500 for 2021 was omitted from net power costs. (Refer to page 29)	(517,000)
3. The budgeted costs for the design and construction of a road to access a boat ramp at Lake Oroville totaling \$4.6 million are improperly charged to the contractors. (Refer to page 29)	(189,000)
4. Budgeted costs related to the Salton Sea totaling \$3.4 million were improperly included in the calculation of the Delta Water Charge. (Refer to page 29)	(139,000)
5. Credits in the cost allocation system totaling \$224,000 were not posted in time to be included in the 2021 Statement of Charges. (Refer to page 29)	(10,000)
6. Adjustments in the cost allocation system totaling \$27,000 that reallocate costs from a Delta cost center to a statewide cost center are no longer necessary. (Refer to page 29)	(9,000)
7. Adjustments in the cost allocation system totaling \$13,000 are improperly posted to a statewide cost center. (Refer to page 29)	(6,000)
8. A formula error in the calculation of the Delta Water Charge resulted in the overstatement of costs by \$40,000. (Refer to page 29)	(2,000)
9. Relicensing costs of \$9,000 for the south State Water Project hydropower facilities that were not paid with bond proceeds are improperly excluded from net power costs. (Refer to pages 29 and 30)	7,000
10. Costs used to calculate the potential FEMA reimbursement for the Oroville Spillway were overstated by \$303,000, resulting in a larger than intended credit being included in the Delta Water Charge. (Refer to page 30)	11,000
11. Capital costs totaling \$853,000 are not assessing properly in the costs allocation system, resulting in the amounts being excluded from the transportation capital component. (Refer to page 30)	40,000

Items	Effect on Metropolitan's 2022 Costs Increase (Decrease)
12. Bond fees allocated to Devil Canyon Second Afterbay debt service totaling \$82,000 for 2004 to 2008 have not yet been included in the variable component. (Refer to page 30)	\$ 65,000
13. Offsetting entries for credits related to the disposal of \$3,247,000 in emission allowance intangible assets transferred to the cost allocation system were not posted at the time the 2021 Statement of Charges was prepared. (Refer to page 30)	1,766,000
<u>Previously Reported Findings</u>	
14. Costs totaling \$211 million, partially allocated to recreation prior to the implementation of SAP, were billed entirely to the conservation minimum component. (Refer to page 30)	(5,002,000)
15. Hyatt-Thermalito operating costs for 1999 through 2019 included in the computation of the variable charges were overstated by \$1,964,000, and 1999 through 2019 credits for Hyatt-Thermalito operating costs included in the Delta Water Charge were overstated by \$1,280,000. (Refer to pages 30 and 31)	(3,529,000)
16. Costs totaling \$13,411,000 for Gorman Creek Improvement Channel emergency repairs were included in the transportation minimum component instead of the transportation capital component. (Refer to page 31)	(3,509,000)
17. Net power costs and revenues, transmission, station service and peaking costs for 1998 through 2019 were not recorded or were recorded incorrectly in the accounting system. (Refer to page 31)	(2,895,000)
18. The Department changed the methodology for collecting fish replacement costs, resulting in a difference of \$3,255,000 between actual costs and wheeling credits and amounts included in the variable charges. (Refer to page 31)	(2,604,000)
19. Suisun Marsh construction and O&M costs of \$59,994,000, that were to be reimbursed by the State General Fund depending upon the availability of Tideland Oil and Gas Revenue, are included in the contractors' charges. (Refer to pages 31 and 32)	(2,466,000)
20. Costs totaling \$4,684,000 for Gorman Creek Improvement Channel – South of Orwin Way emergency repairs were included in the transportation minimum component instead of the transportation capital component. (Refer to page 32)	(2,429,000)
21. Certain costs charged to Coastal reaches totaling \$2.9 million were improperly reallocated statewide. (Refer to page 32)	(1,711,000)
22. Funding of \$3.7 million to the California Department of Food and Agriculture from 2014 to 2019 to prevent the spread of hydrilla to the Delta and State Water Project would be more appropriately paid with Priority 4 or General Fund monies. (Refer to page 32)	(1,527,000)

Items	Effect on Metropolitan's 2022 Costs Increase (Decrease)
23. Costs from 2007 to 2019 totaling \$31,081,000 related to damage occurring from project water prior to passing through delivery structures should not be charged to the contractors under Article 13b. (Refer to page 32)	\$ (1,414,000)
24. Fish stocking costs at Pyramid, Silverwood, and Castaic Lakes totaling \$1.7 million were improperly included in the contractors' charges. (Refer to page 32)	(1,179,000)
25. Cap and Trade emission allowances expected to be used in 2020 of \$1,730,000 were included in the variable component, but the allowances were also included in the year they were purchased, resulting in a double billing of these costs in the variable component. (Refer to pages 32 and 33)	(876,000)
26. Fish restoration consulting costs of \$904,000 were incorrectly included in the contractors' charges. (Refer to page 33)	(827,000)
27. Settlement payments and legal costs from 2007 to 2019 totaling \$4,233,000 for claims filed by employees and former employees appear incorrectly charged to the contractors. (Refer to page 33)	(796,000)
28. Aqueduct lining repair costs at reach 20B totaling \$2,542,000 for 2011 through 2017 are being allocated to the minimum component when it appears that these costs meet the criteria for capitalization. (Refer to page 33)	(710,000)
29. The minimum costs from January to June 1999 totaling \$1,509,000 for the downstream distribution were erroneously reversed in the SAP system. (Refer to page 33)	(579,000)
30. Lake Perris maintenance costs for 2005 to 2017 totaling \$471,000 were allocated to the contractors instead of to the recreation purpose. (Refer to page 33)	(539,000)
31. Payments totaling \$5,456,000 for a mitigation land purchase, a rice research project and levee maintenance costs were improperly included in the contractors' charges. (Refer to page 33)	(265,000)
32. Outdated debt service amounts were used to determine the Devil Canyon Second Afterbay charges for 2003 to 2005 in the variable component. (Refer to page 34)	(190,000)
33. The costs for the purchase of greenhouse gas emission allowances were charged to the year of purchase rather than to the year of use. (Refer to page 34)	(149,000)
34. Costs totaling \$2,357,000 for restroom refurbishment, 4th of July activities, boat dock repairs, boating safety training and fishing festivals were included in the contractors' charges. (Refer to page 34)	(143,000)
35. Coastal Branch power costs for 1998 through 2004 totaling \$178,000 were recorded incorrectly. (Refer to page 34)	(142,000)
36. The adjustment to the 2005 rate management credit to correct errors in previous credits was understated. (Refer to page 34)	(79,000)

Items	Effect on Metropolitan's 2022 Costs Increase (Decrease)
37. Costs for repairs to boat ramps open to the general public, 4 th of July events and work done on behalf of the Department of Parks and Recreation totaling \$594,000 were improperly charged to the contractors. (Refer to page 34)	\$ (60,000)
38. A \$108,000 entry to correct a misposting of Delta Conveyance Program costs was inadvertently double posted. (Refer to page 34)	(51,000)
39. Payments of \$565,000, made to a reclamation district for a carbon sequestration program on Sherman Island, were incorrectly included in the contractors' charges. (Refer to page 35)	(31,000)
40. Recreation costs of \$44,000, incurred primarily by the Integrated Regional Water Management office, are incorrectly included in the contractors' charges. (Refer to page 35)	(27,000)
41. Power costs were understated and recovery generation credits were overstated due to an incorrect 2002 Alamo mill rate and the use of an outdated 1999 San Luis amount. (Refer to page 35)	(10,000)
42. Costs totaling \$189,000 related to 4 th of July events in 2012 to 2016 at Lake Oroville were charged to the contractors. (Refer to page 35)	(9,000)
43. Charges totaling \$106,000 for a 4 th of July event in 2007 were incorrectly assessed to the contractors. (Refer to page 35)	(8,000)
44. Costs totaling \$9,000 related to the relicensing of southern facilities were improperly included in the transportation minimum component. (Refer to page 35)	(6,000)
45. The calculated power benefit for the South Bay Improvement included in variable costs for 2004 to 2006 is overstated by \$1,000. (Refer to page 35)	(1,000)
46. Debt service amounts for the Tehachapi Afterbay were understated by \$85,000 for 2004 through 2005 in the calculation of the variable component. (Refer to page 35)	68,000
47. The update of the allocation factors used to allocate 2005 power costs to the powerplants improperly excluded costs recorded prior to the SAP conversion in 2006. (Refer to page 36)	893,000
48. FERC relicensing costs for 1998 through 2019 used in the transportation variable and the Delta Water Rate calculations were outdated. (Refer to page 36)	2,986,000
NET BENEFIT	<u>\$ (29,967,000)</u>

TABLE C**Summary of Audit Findings Resulting in Credits, Refunds and Adjustments**

Audit findings affect not only the Statement of Charges but also the amounts of credits, refunds and adjustments the Department issues to Metropolitan. The following is a brief summary of the items found during our audit that affect credits, refunds and adjustments.

Items	Effect on Metropolitan's Future Costs Increase (Decrease)
<u>Previously Reported Findings</u>	
1. Outdated bond proceed information was used to calculate the 2001 to 2019 WSRB Surcharge. (Refer to page 36)	\$ (93,000,000)
2. Amounts collected through the 1989 to 2019 Surcharge component were overstated by \$135 to \$150 million due to an understatement in the revenue collected in the Conservation component for water systems projects. (Refer to page 36)	(75,000,000)
3. The Department collected amounts between 1998 and 2014 for additional capacity in the aqueduct related to permanent water transfers. The amounts collected were refunded to the contractors in December 2015, but interest has not yet been returned. This amount represents interest on the funds at the Project Interest Rate. (Refer to page 36)	(10,755,000)
4. Certain Coastal Branch capital cost repayment amounts were excluded from the computation of the 2000 WSRB Surcharge. (Refer to page 36)	(632,000)
5. An inconsistent project purpose split was used to compute the 1990 to 1993 WSRB Surcharge. (Refer to page 37)	(555,000)
6. Incorrect costs were used to compute the 1992 WSRB Surcharge. (Refer to page 37)	(100,000)
7. Errors were noted in the calculation of the SMIF interest refund. (Refer to page 37)	6,000
8. Administrative charges related to the Cap and Trade program of \$135,000 in 2013 and \$81,000 in 2015 were transferred from the variable component to the Off-Aqueduct Component and have not yet been billed. (Refer to page 37)	150,000
NET BENEFIT	<u>\$ (179,886,000)</u>

DISCUSSION OF OUR SERVICES, AUDIT FINDINGS
AND GENERAL COMMENTS

In conformity with the contract between The Metropolitan Water District of Southern California (Metropolitan) and Richardson & Company, LLP, we have audited the 2021 Statement of Charges submitted to Metropolitan by the State of California Department of Water Resources (Department).

Scope of the Assignment. The primary service we perform for Metropolitan is the audit of the annual Statement of Charges under Metropolitan's Water Service Contract with the Department. In addition to our audit work, we perform special projects as requested by Metropolitan's staff in areas such as investigating financial and accounting matters, disputes over Department policy and in negotiating contract amendments and administrative changes in the Department's management of the State Water Project. We also participate with Metropolitan in water contractor meetings that serve as a forum for resolving accounting, billing and budgeting issues, including meetings of the State Water Contractor (SWC) Audit-Finance Committee and the Contract Billing Support Section (Dispute Resolution Group).

Reporting. The more significant findings and results of our audit, special projects work and participation in meetings are presented in two reports prepared after the completion of our annual audit: a comprehensive report that serves as a working document between the auditors, Department and Metropolitan staff and a summary report that is provided to Metropolitan's Board of Directors and management addressing the results of our audit.

Audit Findings. Our goal is to provide Metropolitan with a thorough audit. The engagement is divided into forty-seven separate areas and fieldwork is completed primarily from April through October. Computer auditing techniques are used to test posting, mathematical accuracy and select samples from data files. The following are the more significant findings of our audit. The changes reflected in the rebill of the 2020 Statement of Charges and the 2021 Statement of Charges are summarized in Table A on pages 21, those projected to be reflected in the 2022 Statement of Charges are summarized in Table B on pages 22 to 25 and those that will affect credits, refunds and adjustments are summarized in Table C on page 26.

Findings Resulting in Changes to the Rebill of the 2020 Statement of Charges:

- The Department inadvertently excluded the 2020 debt service and cover for the Oroville Spillway recovery of \$22.5 million and \$5.6 million, respectively, from water systems debt service in the 2020 Surcharge calculation. The Department corrected this error in a rebill of the 2020 Statement of Charges. Metropolitan's Surcharge in the rebill of the 2020 Statement of Charges increased by \$15.2 million. (TABLE A, Item 1)
- The Department updated costs for Water Systems conservation projects used in the rebill of the 2020 Surcharge calculation to eliminate the difference between costs and bond proceeds. The Surcharge decreased by \$22.8 million, which decreased Metropolitan's Surcharge component by \$12.3 million. (Table A, Item 2)

Findings Resulting in Changes to the 2021 Statement of Charges:

- The Department included \$3,353,000 in the variable component in the 2019 Statement of Charges for Cap and Trade emission allowances expected to be used in 2019. The cost of these emission allowances were also included in the variable component in the year they were purchased, resulting in \$3,353,000 being included in Metropolitan's variable component twice. Since 2019 power costs are now billed based on actual costs, this discrepancy no longer exists, resulting in a decrease in Metropolitan's 2019 variable component of \$1,872,000. (Table A, Item 3)
- Adjustments were made in 2010 to transfer balances representing retentions on construction contracts from 1999 through 2004 to cost centers included in the Statement of Charges. Since the contractors are billed for the full amount of the invoice, including the retention portion, this transfer resulted in the double billing of costs totaling \$1.4 million. These adjustments were reversed in the 2021 Statement of Charges, resulting in Metropolitan's transportation minimum and Delta Water Charge components decreasing by \$566,000 and \$59,000, respectively. (TABLE A, Item 4)
- The 2019 Hyatt Thermalito minimum power revenue used in the calculation of the Delta Water Charge was updated to reflect the most current costs. As a result, Metropolitan's Delta Water Charge increased by \$131,000. (TABLE A, Item 5)

The following item included on Table B in the prior year, was subsequently determined to no longer be an error:

- The Department obtained a separate commercial paper line specifically to pay for the costs of the Oroville Spillway recovery and restoration. The fees for this commercial paper line are being allocated statewide as has been done historically for these type of costs. Since this commercial paper line is restricted in use for the Oroville Spillway reconstruction, we originally believed it would be more appropriate to allocate these costs specifically to Oroville. After further discussion with the Department, we agree that if the original commercial paper line been used to pay for the Oroville Spillway costs, the fees would have been allocated statewide. As a result, the statewide allocation for the fees associated with the Oroville specific commercial paper line appears reasonable. (TABLE A, Item 6)

Findings Projected to Result in Changes to the 2022 Statement of Charges:**New Findings**

- The Department received \$1,460,000 for a legal settlement and administrative fees for a dispute related to the construction of the Tehachapi Second Afterbay. The Department recorded the credits in the accounting system, but since the costs were credited back to the Tehachapi Second Afterbay, which is billed to the contractors based on debt service not costs, this credit did not have a direct impact on the Statement of Charges. The Department reflected the settlement payment in the Tehachapi Second Afterbay capital cost component included in the 2020 Statement of Charges, but the payment has not been reflected in the variable component. As a result, Metropolitan's variable component is overstated by \$1,168,000. The Department has

indicated the credit will be reflected in the 2020 variable component in future Statement of Charges. The Department also indicated the credit will be included in the invoice rate to reduce the variable payments made by the contractors in 2020. (TABLE B, Item 1)

- The LADWP payment of \$582,500 for peaking capacity foregone at the Castaic Powerplant by the Department for 2021 was not included in the calculation of the variable component. As a result, Metropolitan's 2021 transportation variable component in the Statement of Charges is overstated by \$517,000. The Department has indicated this credit will be included in the invoice rate, so there will not be an error in the variable payments made by Metropolitan in 2021. (TABLE B, Item 2)
- The Department included in the calculation of the Delta Water Charge \$4.6 million for budgeted design and construction costs of a new road to access a boat ramp at Lake Oroville. The Department feels the current road poses a security risk to the spillway so it is appropriate to charge the costs to water supply. The contractors believe the road benefits recreation. Metropolitan's Delta Water Charge is overstated by \$189,000 as a result of these costs being billed to the contractors. (TABLE B, Item 3)
- Budgeted costs related to the Salton Sea totaling \$3,402,000 for 2020 to 2022 were improperly included in the 2021 Statement of Charges. Costs were included in the calculation of the Delta Water Charge, which results in an overstatement to Metropolitan's Delta Water Charge of \$139,000. (TABLE B, Item 4)
- The Department received a \$224,000 reimbursement in 2019, but a credit was not recorded in the cost allocation system until after the 2021 Statement of Charges was prepared. As a result, Metropolitan's Delta Water Charge is overstated by \$10,000. (TABLE B, Item 5)
- The Department made entries in the billing system to correct the assignment of Delta costs that were improperly being allocated statewide. However, entries posted in the cost allocation system continue to transfer \$27,000 in costs from a Delta cost center to a statewide cost center. Metropolitan's transportation minimum component and Delta Water Charge is overstated by \$11,000 and understated by \$2,000, respectively. (TABLE B, Item 6)
- As previously discussed, the Department made entries in the billing system to correct the allocation of Delta costs that were improperly being allocated statewide. Entries posted in the cost allocation system related to the original costs that have been transferred continue to allocate \$13,000 statewide. Metropolitan's transportation minimum component is overstated by \$6,000. (TABLE B, Item 7)
- The Department uses a spreadsheet to compute the Delta Water Charge, instead of using the SAP system. We noted formula errors in the calculation resulted in the overstatement of costs by \$40,000. Metropolitan's Delta Water Charge is overstated by \$2,000. (TABLE B, Item 8)
- The license for the south State Water Project hydropower facilities expires in 2022. The relicensing costs for these facilities are power costs that are recovered through the variable component. Currently, the Department is issuing bonds to pay for the costs and including the

debt service in the variable component instead of the actual costs. We noted relicensing costs totaling \$9,000 incurred in 2013 that were not bonded for and have not been included in the variable component. As a result, Metropolitan's variable component is understated by \$7,000. (TABLE B, Item 9)

- We noted a \$303,000 discrepancy in the amounts used to determine the FEMA reimbursement for the Oroville Spillway resulted in a \$228,000 understatement of net costs included in the Delta Water Charges calculation. As a result, Metropolitan's Delta Water Charge is lower by \$11,000 in the Statement of Charges than if the actual cost amount was used. The FEMA reimbursement included in the Statement of Charges was based on estimates and will be adjusted to the actual reimbursements received in the future. (TABLE B, Item 10)
- We noted capital costs totaling \$853,000 were not properly assessing in the cost allocation system, resulting in the exclusion of these amounts from the calculation of the Statement of Charges. As a result, Metropolitan's transportation capital component is understated by \$40,000. (TABLE B, Item 11)
- Bond fees totaling \$82,000 were reclassified from debt service for the East Branch Enlargement to the Devil Canyon Second Afterbay. The revisions to the Devil Canyon Second Afterbay debt service have not yet been reflected in the variable component, resulting in a \$65,000 overstatement to Metropolitan's variable component. (TABLE B, Item 12)
- Entries made in the financial accounting system to record the surrender of emission allowances are improperly being included as credits in the cost allocation system. As a result, the Department makes manual entries in the cost allocation system to offset these amounts. We noted adjustments in 2018 totaling \$3,247,000 were not posted to offset emission allowance entries at the time the 2021 Statement of Charges was prepared. As a result, Metropolitan's variable, transportation minimum and Delta Water Charge components are understated by \$1,576,000, \$175,000 and \$15,000, respectively. (TABLE B, Item 13)

Previously Reported Findings

- Upon conversion to the SAP system in 1999, the Department revised the allocation of certain conservation costs, including Bay-Delta environmental protection studies, compliance monitoring, environmental protection support, planning model development, Delta facilities planning and Bay-Delta proceedings, such that they were allocated 100% to the contractors; whereas in the previous system, these costs were partially allocated to the recreation Project purpose. As a result of this change, \$207,925,000 of minimum costs and \$3,368,000 of capital costs from 1999 through 2019 are being allocated entirely to the contractors, instead of a portion being allocated to the recreation Project purpose, which results in the overstatement of Metropolitan's Delta Water Charge by \$5,002,000 in the 2001 through 2021 Statements of Charges. (TABLE B, Item 14)
- The 1999 to 2019 Hyatt-Thermalito O&M costs included in the variable component are overstated by \$1,964,000 and the credits included in the computation of the Delta Water Charge for 1999 to 2019 are overstated by \$1,280,000 due to the Department not using actual O&M

costs. The effect of these errors is to overstate Metropolitan's transportation variable component, including the interest impact, by \$3,647,000 and to understate Metropolitan's Delta Water Charge by \$118,000 in the 2021 Statement of Charges. (TABLE B, Item 15)

- The Department included \$13,411,000 of costs for Gorman Creek Improvement Channel emergency repairs in the transportation minimum component. The Department considers the inclusion of these costs in the transportation minimum component proper because they believe that the repair work is to bring the facility back to normal conditions and is not a betterment. However, these repairs appear to meet the qualifications for capitalization under the Department's capitalization policy. The inclusion of these costs in the transportation minimum component overstates Metropolitan's transportation minimum component by \$12,083,000 and understates the transportation capital component for all years by \$8,574,000 in the 2021 Statement of Charges. (TABLE B, Item 16)
- Power costs totaling \$1,500,000 and sales totaling \$2,039,000 for 1998 through 2019, were not recorded or were recorded incorrectly in the accounting system. In addition, transmission minimum costs totaling \$4,799,000 and station service credits totaling \$170,000 were not recorded properly in the accounting system. These errors result in an overstatement of Metropolitan's transportation minimum component by \$3,279,000, and an understatement of the variable and Delta Water Charge components by \$380,000 and \$4,000, respectively, in the 2021 Statement of Charges. (TABLE B, Item 17)
- The Department determined that actual fish replacement costs should be included in the variable charges instead of the amounts calculated using the Delta Fish Agreement computation. This change in methodology requires a reconciliation of the amounts collected to date to actual costs incurred since the inception of the Agreement. We prepared a reconciliation of these charges and wheeling credits and determined that the fish replacement charges are overstated by approximately \$3,255,000. As a result, we estimate that Metropolitan's variable component included in the 2021 Statement of Charges is overstated by \$2,604,000. (TABLE B, Item 18)
- The construction and O&M costs associated with the Suisun Marsh are to be paid 40% by the Department, 40% by the United States Bureau of Reclamation and 20% by the State General Fund according to the Suisun Marsh Preservation Agreement. However, we noted that 100% of the historical costs are being included in the cost accounting system, of which the contractors are allocated 96.7% of Suisun Marsh O&M costs and 96.6% of the Suisun Marsh capital costs. After receiving the credit for the USBR's 40% share, the contractors are being charged 56.7% of O&M costs and 56.6% of capital costs for Suisun Marsh, compared to the 40% that was agreed upon in the Agreement. This additional 16.7% of minimum and 16.6% of capital costs represents the amounts that were to be reimbursed by the State General Fund depending upon the availability of Tideland Oil and Gas Revenue. The State's share of the Suisun Marsh costs through June 1988 was offset against the Department's liability to the California Water Fund through the offset legislation. The additional 16.7% of minimum and 16.6% of capital costs incurred since June 1988 total \$49,793,000 and future costs from 2020 to 2035 total \$10,201,000. As a result, the Delta Water Charge of Metropolitan's 2021 and future Statements of Charges are higher by \$2,466,000 a year through 2035. The Department does not anticipate that Tideland Oil and Gas

Revenue will be available to cover the State's share of expenditures incurred since June 1988 and the Department was not allowed to offset these expenditures against the California Water Fund liability. Thus, the contractors will continue to be charged for the additional Suisun Marsh costs under the Water Supply Contracts. (TABLE B, Item 19)

- Gorman Creek Improvement Channel – South of Orwin Way emergency repair costs totaling \$4,684,000 were included in the transportation minimum component. This project appears to meet the qualifications for capitalization. The inclusion of these costs in the 2021 Statement of Charges overstates Metropolitan's transportation minimum component by \$4,318,000 and understates the transportation capital component by \$1,889,000 for all years in Metropolitan's 2021 Statement of Charges. (TABLE B, Item 20)
- Certain costs totaling \$2.9 million at three Coastal reaches were manually reallocated statewide to transportation minimum reaches because the Coastal contractors maintain these reaches. However, these allocated costs that were removed include Coastal encasement costs and general management of the State Water Project, which we believe should still be allocated to these Coastal reaches. This adjustment results in an increase to Metropolitan's transportation minimum component of \$1,711,000 in the 2021 Statement of Charges. (TABLE B, Item 21)
- The Department provided approximately \$3.7 million in funding to the California Department of Food and Agriculture from 2014 to 2019 to prevent the spread of hydrilla to the Delta and the State Water Project. Currently, the focus of this project is eradicating and monitoring hydrilla at Clear Lake, but the agreement allows for the survey, eradication and monitoring at other waterbodies near the Delta or the State Water Project. Since the project benefits others besides the State Water Project, funding the program using Priority 4 or General Fund monies may be more appropriate. As a result, Metropolitan's transportation, East Branch Enlargement and Delta Water Charge minimum components are overstated by \$1,402,000, \$90,000 and \$35,000, respectively. (TABLE B, Item 22)
- The contractors are not liable for damage caused by project water prior to the passage through delivery structures under Article 13b of the Water Supply Contract. We noted costs charged to the contractors totaling \$31,081,000 for 2007 to 2019 that appears to meet the definition under Article 13b. Metropolitan's transportation minimum and Delta Water Charge minimum components in the 2021 Statement of Charges are overstated by \$907,000 and \$507,000, respectively. (TABLE B, Item 23)
- Costs totaling \$1.7 million for fish stocking at Pyramid, Silverwood and Castaic Lakes were improperly included in the contractors' charges, resulting in an overstatement of Metropolitan's transportation minimum component by \$1,179,000 in the 2021 Statement of Charges. (TABLE B, Item 24)
- The Department included \$1,730,000 in the 2020 variable component for the Cap and Trade emission allowances expected to be used during 2020. The cost of these emission allowances is also included in the variable component in the year they were purchased, so this results in \$1,730,000 being included in Metropolitan's variable component twice. As a result,

Metropolitan's 2020 variable component is overstated by \$876,000, which will be eliminated when the 2020 variable component is based on actual costs in the 2022 Statement of Charges. (TABLE B, Item 25)

- Consulting costs totaling \$904,000 for fish restoration projects at Lake Perris were included in the contractors' charges, when these costs should be charged to the recreation purpose, resulting in a \$827,000 overstatement to Metropolitan's transportation minimum component in the 2021 Statement of Charges. (TABLE B, Item 26)
- The Department paid \$4,233,000 from 2007 to 2019 for settlement payments and legal fees related to claims filed by employees and former employees. These costs appear to be for personnel issues and not costs necessary for the delivery of project water. As a result, Metropolitan's transportation minimum and Delta Water Charge components are overstated by \$620,000 and \$176,000, respectively, in the 2021 Statement of Charges. (TABLE B, Item 27)
- Aqueduct lining repair costs at Reach 20B totaling \$2,542,000 from 2011 through 2017 are being allocated to the minimum component when it appears that these costs meet the criteria for capitalization. This error results in an overbilling to the transportation minimum component and an underbilling to the transportation capital of \$1,345,000 and \$635,000, respectively, in Metropolitan's 2021 Statement of Charges. (TABLE B, Item 28)
- Upon conversion to the SAP system, downstream costs for January to June 1999 were transferred from the previous UCA system. The Department subsequently reversed the minimum portion of the entry totaling \$1,509,000, which we believe is incorrect. The impact to Metropolitan's 2021 Statement of Charges is an overstatement of the transportation and Delta Water Charge minimum components of \$496,000 and \$83,000, respectively. (TABLE B, Item 29)
- The Department incurred \$3.4 million of costs in 2005 through 2017 for recreation and fish and wildlife projects at Perris Reservoir that were being allocated mostly to the water supply Project purpose, rather than 100% to the recreation Project purpose. As these expenditures had no apparent transportation water supply purpose, the Department made a correction to reallocate \$2.1 million of these costs from a transportation cost center to a recreation cost center. However, not all of the costs were removed, resulting in \$471,000 of recreation-related capital costs being allocated to the contractors, which overstates Metropolitan's calculated capital component in the 2021 Statements of Charges by \$539,000 for all years, when interest is included. (TABLE B, Item 30)
- We noted that the Department made a \$500,000 payment to a reclamation district for the purchase of Chevron Point on Twitchell Island and payments in 2008 to 2018 for a subsidence reversal and carbon sequestration farm scale rice research project. In addition, expenditures totaling \$226,000 for levee and other maintenance work have also been included in the contractors' charges. It does not appear that there is any water supply purpose that supports the use of State Water Project funds for these projects. The Department has included \$5,456,000 of these costs in the 2021 Statement of Charges, resulting in an overstatement to Metropolitan's Delta Water Charge of \$265,000. (TABLE B, Item 31)

- The Devil Canyon Second Afterbay charges for debt service included in the variable component were understated by \$237,000 for 2003 to 2005 due to the use of an outdated debt service schedule. As a result, Metropolitan's variable charges in the 2021 Statement of Charges are overstated by \$190,000. (Table B, Item 32)
- The Department has made transfers of Cap and Trade emission allowance costs to the year the allowances were used for the allowances that have been surrendered but not for the estimated allowances used for historical years. Due to variations in Metropolitan's share of the variable component between the years, this results in an overstatement of Metropolitan's variable and transportation minimum components of \$18,000 and \$141,000, respectively, and an understatement of Metropolitan's Delta Water Charge of \$10,000 in the 2021 Statement of Charges. (TABLE B, Item 33)
- The Department incurred \$2,357,000 in costs, primarily at the Oroville Field Division, for restroom refurbishment, 4th of July activities, boat dock repairs, boating safety training and fishing festivals. These recreation-related costs have no water supply benefit, nor do they appear to be required by the Oroville Settlement Agreement and should not be included in the contractors' charges. The impact to Metropolitan is to overstate the Delta Water Charge by \$123,000 and overstate the transportation minimum component by \$20,000 in the 2021 Statement of Charges. (TABLE B, Item 34)
- The Coastal Branch energy charges included in the variable component were overstated by \$178,000 for 1998 through 2004 due to the use of outdated information. As a result, Metropolitan's variable charges in the 2021 Statement of Charges are overstated by \$142,000. (Table B, Item 35)
- In previous audits, we reported that the Department had recalculated the rate management credits for 1997 through 2004 because they had incorrectly used a Table B-15 that had been adjusted for the changes related to the permanent transfer of Table A water. This recalculation improperly excluded \$79,000 from the 2005 rate reduction credit due to an error in the Department's reallocation computation. (TABLE B, Item 36)
- The Department incurred \$594,000 in costs for repairs to boat ramps open to the general public, 4th of July events and work done for the Department of Parks and Recreation. We believe these costs would be more appropriately charged to recreation than included in the contractors' charges. The impact is to overstate Metropolitan's transportation minimum and Delta Water Charge minimum components by \$38,000 and \$22,000, respectively. (TABLE B, Item 37)
- We previously reported that Delta-related costs were improperly allocated statewide. The Department agreed and transferred the costs to the Delta. In reviewing the transfer of costs, we determined there to be a misposting of \$108,000 in the accounting system. The Department agreed and corrected the posting; however, the correction was double posted. As a result, Metropolitan's transportation minimum component and Delta Water Charge are overstated by \$49,000 and \$2,000, respectively, in the 2021 Statement of Charges. (Table B, Item 38)

- The Department made \$565,000 in payments to a reclamation district in 2013, 2014 and 2016 for a subsidence reversal and carbon sequestration project on Sherman Island. It does not appear that there is any water supply purpose that supports the use of State Water Project funds for this project. The error results in an overstatement to Metropolitan's Delta Water Charge of \$31,000 in the 2021 Statement of Charges. (TABLE B, Item 39)
- Integrated Regional Water Management costs for the recreation, planning and implementation program, including charges for fishing events and aquatic adventure camps totaling \$44,000 for 2006 through 2014 are charged to the contractors, result in an overstatement to Metropolitan's transportation minimum and Delta Water Charge components by \$26,000 and \$1,000, respectively, in the 2021 Statement of Charges. (TABLE B, Item 40)
- The Department used an outdated mill rate when valuing the recovery generation at the Alamo Powerplant, resulting in the value of recovery generation for the Alamo Powerplant for 2002 being overstated by \$97,000. In addition, we noted that the value of recovery generation credit for the San Luis Powerplant for 1999 was understated by \$170,000. The effect to Metropolitan of these errors was an understatement of the transportation variable component by \$1,000, an overstatement of the transportation minimum component by \$2,000 and an overstatement of the Delta Water Charge by \$9,000 in the 2021 Statement of Charges. (TABLE B, Item 41)
- Costs for 4th of July events at Lake Oroville totaling \$189,000 for 2012 to 2016 were included in the Delta Water Charge. As a result, Metropolitan's Delta Water Charge is overstated by \$9,000. (TABLE B, Item 42)
- Our audit disclosed that costs incurred in 2007 totaling \$106,000 for a 4th of July event at Lake Oroville were incorrectly assessed to the contractors, which results in a \$8,000 overstatement of Metropolitan's Delta Water Charge in the 2021 Statement of Charges. (TABLE B, Item 43)
- The costs for relicensing the southern facilities, previously considered minimum costs, were reclassified as capital costs beginning with the rebill of the 2015 Statement of Charges. Our audit disclosed that, after the adjustments were made to reclassify the relicensing costs from minimum to capital, \$9,000 of costs remained in the minimum cost centers, resulting in an overstatement to Metropolitan's transportation minimum component of \$6,000 in the 2021 Statement of Charges. (TABLE B, Item 44)
- The Department recalculated the power benefit associated with increasing the capacity of the South Bay Improvement Facilities, resulting in a \$1,000 decrease in the power valuation for 2004 to 2006. These revisions have not yet been reflected in the variable component. Metropolitan's variable component is overstated by \$1,000. (TABLE B, Item 45)
- The Tehachapi Afterbay charges for debt service included in the variable charges are understated by \$85,000 for 2004 to 2005 due to the use of an outdated debt service schedule. As a result, Metropolitan's transportation variable component in the 2021 Statement of Charges is understated by \$68,000. (Table B, Item 46)

- The Department updated the 2005 allocation factors used for power costs; however, upon conversion of these costs to the current version of SAP, not all of the 2005 power costs are being allocated using the most current factors. The effect of not completely updating the allocation of the 2005 power costs is a \$909,000 understatement and a \$16,000 overstatement to Metropolitan's variable component and Delta Water Charge component, respectively, in the 2021 Statement of Charges. (TABLE B, Item 47)
- FERC relicensing costs for 1998 through 2019 were understated by \$1,944,000 in the computation of the variable component and the credits included in the computation of the Delta Water Charge were understated by \$1,944,000 due to the use of outdated costs. As a result, Metropolitan's variable charge, including interest, is understated by \$3,148,000, and the Delta Water Charge is overstated by \$162,000 in the 2021 Statement of Charges. (TABLE B, Item 48)

Findings Resulting in Credits, Refunds and Adjustments:

Previously Reported Findings

- The WSR proceeds used to calculate the Surcharge are inconsistent with the actual capital costs incurred. Due to the Department's estimated methodology, the use of outdated WSRB proceeds and the use of inconsistent data discussed previously in this report, we estimate that Metropolitan's 2001 through 2019 Surcharge components are overstated in total by \$93 million. (TABLE C, Item 1)
- The Department's original methodology for calculating the revenue collected through the Delta Water Charge component for capital costs paid with Water System Revenue Bonds for purposes of the Surcharge calculation resulted in the understatement of the revenue leading to an over collection through the Surcharge. The Department corrected the methodology for the 2020 Surcharge calculation, but we estimate the amount over-collected from all contractors in the Surcharge component from 1989 to 2019 to be \$135 million to \$150 million. Metropolitan's share of this over-collection is estimated to be at least \$75 million. (TABLE C, Item 2)
- As a result of permanent water transfers under and outside the Monterey Agreement, the buyer may be required to purchase additional capacity in the aqueduct to transport water through reaches the seller did not participate in repayment. This situation results in the Department recovering more than the actual costs, so the excess is returned to the other contractors participating in the reaches. The excess collected for 2014 and prior, totaling \$47.5 million, was returned to the contractors in December 2015. Metropolitan's share of this refund was \$27.4 million. This refund did not include interest, which the Department has calculated for all contractors to be \$4.2 million at SMIF rates and \$18.6 million at project interest rates. Based on the return of the refund, Metropolitan's share of the interest is estimated to be \$10,755,000 at Project Interest Rates and \$2,427,000 at SMIF rates. (TABLE C, Item 3)
- The Department excluded \$19,644,000 of Coastal Branch capital costs that were recovered through the transportation variable component from the computation of the 2000 Surcharge, which results in these costs being billed to the contractors twice. As a result, Metropolitan's 2000 Surcharge is overstated by \$632,000. (TABLE C, Item 4)

- There was an inconsistency in the application of the recreation project purpose split between two components of the WSRB Surcharge computation. The error resulted in the overstatement of the WSRB Surcharge in the 1990 through 1993 Statements of Charges totaling \$933,000, of which Metropolitan's share is \$555,000. (TABLE C, Item 5)
- As noted in a prior year, certain costs totaling \$3,883,000 were excluded from the computation of the 1992 Surcharge, which results in an overstatement of Metropolitan's 1992 Surcharge of approximately \$100,000. (TABLE C, Item 6)
- In our testing of a SMIF interest refund on the debt service reserve, we noted errors in the calculation, causing Metropolitan's portion of the refund to be overstated by \$6,000. The Department has indicated that additional SMIF interest will not be returned until the allocation methodology for the Springing Amendment has been finalized. (TABLE C, Item 7)
- As part of the State of California's Cap and Trade program, the Department was required to purchase Cap and Trade emission allowances for energy generated at the Reid Gardner Powerplant in 2013 and for energy generated at the Lodi Energy Center in 2013 and after. The Department paid administrative charges related to the Cap and Trade program of \$135,000 in 2013 and \$81,000 in 2015. Previously, these amounts were included in the variable component, but the Department believes these amounts would be more appropriately billed through the Off-Aqueduct component. When these amounts are billed to the contractors, Metropolitan will be charged approximately \$150,000 through an Off-Aqueduct billing adjustment. (TABLE C, Item 8)