



THE METROPOLITAN WATER DISTRICT
OF SOUTHERN CALIFORNIA

Office of the General Manager

VIA EMAIL

January 12, 2021

Director Jerry Butkiewicz
Director Gail Goldberg
Director Michael T. Hogan
Director Tim Smith
San Diego County Water Authority
4677 Overland Avenue
San Diego, CA 92123

Dear Directors:

Re: Your letter dated January 10, 2021 regarding Draft Appendix A dated December 22, 2020

This letter addresses your comments received January 10, 2021 (SDCWA 2021 Letter), regarding the Board Distribution of the Draft Appendix A dated December 22, 2020 (Attachment 1) and Appendix A redline draft (Attachment 2).

Thank you for your review of and comments on Metropolitan's Appendix A. We have carefully reviewed and considered the comments and circulated them to our finance team, including Disclosure Counsel and our Municipal Advisor.

Before discussing specific comments, please note that Appendix A provides material financial and operating information about Metropolitan to potential investors. Disclosure Counsel prepares Appendix A with assistance and oversight from the Office of the Chief Financial Officer and the Office of General Counsel. Finance, Water Resource Management, Water System Operations, Engineering Services, Office of General Counsel, and Human Resources staffs provide the information necessary to update Appendix A. Metropolitan's Controller reviews and verifies tables, statistics and financial data. Metropolitan also works with, and receives input from, its Bond Counsel and Municipal Advisor, as well as the underwriters of the bonds and their counsel, to ensure Metropolitan meets all legal requirements in the drafting of Appendix A.

Appendix A is reviewed by Metropolitan's Board of Directors. Metropolitan's objective is to provide complete and accurate disclosure regarding the bonds being offered and their security and source of payment to potential investors. Appendix A is updated periodically to provide current information. Forward-looking statements or projections are based on current information such as

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the facts and assumptions contained within the approved biennial budget for fiscal years 2020-21 and 2021-22 and ten-year financial forecast. Revisions to current year projections may be made based on available information regarding experienced results when warranted.

In the SDCWA 2021 Letter, you incorporate by reference prior SDCWA letters regarding Appendix A, which have been addressed in Metropolitan's response letters electronically provided to all SDCWA directors and copied to Metropolitan's Board of Directors.

The following SDCWA comments and Metropolitan's responses refer to the redline draft of Appendix A dated December 22, 2020, showing changes from the draft dated April 29, 2020 (Attachment 1).

Comments Regarding Demand for and Metropolitan Water

SDCWA Comment: "Our overarching concern remains, that Appendix A as drafted and taken as a whole, does not fairly describe what is driving the reduced demand for MWD water and the financial impacts on MWD."

Metropolitan Response: Metropolitan substantively responded to these comments in its June 22, 2018, November 15, 2018, and May 16, 2019 response letters and those responses are incorporated by reference here. Appendix A notes the ongoing IRP process and planning approach being utilized. Additionally, the 2020 IRP update of water transaction forecasts, once completed and approved by the Board, will be incorporated into the subsequent Appendix A.

SDCWA Comment: "A-5. Water transactions. While the COVID-19 pandemic may very well impact MWD water sales, there is no reason to believe that MWD's delivery of the Water Authority's QSA water will be impacted by the pandemic."

Metropolitan Response: Appendix A accurately describes currently known COVID-19 possible impacts. As the COVID-19 outbreak continues, it is difficult to determine the degree of impact, if any, on Metropolitan's water transactions. As described in prior letters, pursuant to the Exchange Agreement, SDCWA makes its purchased conserved IID water and its conserved canal lining water available to Metropolitan at its intake at Lake Havasu. In exchange, Metropolitan delivers an equal volume of water from any source through its delivery system to SDCWA. The Exchange Agreement and its terms are accurately described in Appendix A, see "Quantification Settlement Agreement" and "Metropolitan and San Diego County Water Authority Exchange Agreement."

SDCWA Comment: "A-12. Local Water Supplies. The description does not account for known facts regarding development of local water supplies and includes 2015 IRP numbers and "targets" that are substantially outdated, all of which has been the subject of discussion beginning at the Board's October retreat, and reinforced during the 2020 IRP update process by many directors and member agencies."

Metropolitan Response: Metropolitan believes that all material information regarding Local Water Supplies has been disclosed in Appendix A. However, Metropolitan will include information describing local water supplies not funded by Metropolitan prior to printing.

SDCWA Comment: “A-66. Summary of Water Transactions and Revenues. The schedule improperly combines water sales and transportation services—apples and oranges—and then computes an “average dollars per 1,000 gallons,” which is a number with no meaning in the context of water or transportation cost.”

Metropolitan Response: Metropolitan clearly discloses and describes Metropolitan’s water transactions and revenues. The term “water transactions” is defined wherever it is used. “Water transactions” includes water sales, exchanges, and wheeling; exchanges and wheeling may occur with member agencies and third parties. Similarly, the term “water revenues” is clearly defined wherever it is used and expressly states that it includes revenues from water sales, exchanges, and wheeling. The table accurately reflects the revenues generated by Metropolitan for the water services it provides.

SDCWA Comment: “A-66. Ten Largest Water Customers. The schedule is misleading for the same reasons. The Water Authority is not MWD’s largest “water” customer as indicated; correctly stated, it is MWD’s largest user of MWD transportation service and its eighth largest water customer. Combining the two in a single calculation does not provide transparency of MWD’s water sales and services; at a minimum the chart should be titled Ten Largest Customers and break out water sales and transportation services provided to the Water Authority.”

Metropolitan Response: The Largest Water Customer table reflects all water transactions. As indicated above, the term “water transactions” is defined and includes water sales, exchanges, and wheeling; exchanges and wheeling may occur with member agencies and third parties. “Customer” as used in Appendix A is meant in its broadest definition as a person or organization that pays for goods or services.

SDCWA Comment: “A-67. Water Stewardship Rate. The Court of Appeal has rejected MWD’s contention that, “[a]ll users...benefit from avoided system infrastructure costs through conservation and local resources development, and from the system capacity made available by investments in demand management programs like Metropolitan’s Conservation Credits Program and Local Resources Program.” The Water Stewardship Rate was not invalidated as a charge on MWD water purchases, but was invalidated as a transportation charge. See Appendix A redline draft at p. A-79, fourth full paragraph. Reference to “transactions” again, obscures this important distinction.”

Metropolitan Response: In *SDCWA v. Metropolitan*, 12 Cal.App.5th 1124, the Court of Appeal found that the administrative record before it for the rates in CYs 2011 through 2014 did not support Metropolitan’s Water Stewardship Rate allocation to transportation rates, but the court did not address the allocation in subsequent years based on a different record. The Court of Appeal did not consider the inclusion of the Water Stewardship Rate

in Metropolitan's full service rate. Moreover, the Water Stewardship Rate has not been collected from SDCWA on its Exchange Agreement deliveries since January 1, 2018 and has not been collected from any member agency on any transactions since January 1, 2021. Therefore, there is no relevant distinction, as claimed, since that rate does not currently affect revenues.

SDCWA Comment: "A-81. Offsetting Benefits. We disagree with the statement that only the stayed 2018 case had previously included an offsetting benefits claim, however, do not dispute that this is MWD's contention in the litigation on an issue that is yet to be tried. We disagree with a number of MWD's characterizations relating to the litigation, but have only addressed here those in which the Court has already made specific rulings that are inconsistent with MWD's statements, e.g., Water Stewardship Rate, described above."

Metropolitan Response: Appendix A is not the appropriate document to include SDCWA's contentions in the ongoing rate litigation.

Other Comments in SDCWA 2021 Letter Regarding January 2021 Board Memo 7-1 (Appendix A)

SDCWA Comment: "A-6. General Manager's retirement. While the General Manager (GM)'s retirement may coincide with the hiring of a successor, there has been no board determination to that effect. The GM submitted his resignation which was accepted by the Board, scheduled to occur at the end of 2020. Due to delays in the GM search process, the timeline has been delayed; however, there has not been any determination by the Board one way or the other as to when Mr. Kightlinger will depart. Without benefit of reviewing Mr. Kightlinger's employment contract, it is unknown what impact if any might result from describing an agreement that does not exist that he will remain the GM until his successor is hired."

Metropolitan Response: The General Manager stated his intent to retire upon the hiring of his successor. As stated in the introductory paragraph of the Management section on page A-6, Appendix A clearly discloses that the General Manager serves at the pleasure of the Board.

SDCWA Comment: "A-12. Water Conservation. Please describe how this explanation incorporates the per capita reduction reported in the recent IRP Retrospective Draft, representing a 500,000 acre-foot reduction in demand."

Metropolitan Response: The discussion of "Water Conservation" on A-12 describes the stated water conservation goal set forth in the most recently adopted IRP. This section does not describe any of the preliminary findings in the IRP Retrospective Draft. All information regarding the ongoing 2020 IRP Update can be found on A-12.

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SDCWA Comment: “A-27. IID’s CEQA lawsuit. We trust you will update the language to reflect the Court’s decision on technical grounds that IID failed to exhaust its administrative remedies but that it also found that MWD’s assumption of California’s DCP obligation could not be deemed negligible so as to qualify for the CEQA exemption MWD relied on.”

Metropolitan Response: Appendix A will be updated to reflect the recent decision in IID v. MWD litigation. On January 11th, the court released a revised final order. The revised final order states that IID’s petition was denied for failure to exhaust administrative remedies, and that MWD’s assumption of California’s DCP obligation did qualify for the CEQA exemption MWD relied on.

SDCWA Comment: “A-36. Bard Water District Seasonal Fallowing Program. Please provide data for 2021 cost and acre feet in place of the 2020 data being deleted.”

Metropolitan Response: Metropolitan will be providing up to \$1.4 million for the Bard Water District Seasonal Fallowing Program’s (Program) 2021 fallowing season. This includes \$457 per acre, up to 3,000 acres, and an additional one-time payment of \$15,000 provided to Bard for an estimated unit cost of \$231 per acre-foot. Given the magnitude of this program, this additional detail is not material to investors. The number of acres and payment for the 2021 fallowing season will be finalized by March of 2021, and Metropolitan staff will be updating the Board on activities relating to the Program in the next few months.

SDCWA Comment: “A-38. Storage Capacity and Water in Storage. Staff is deleting the projected operation of storage in terms of drawing on storage in seven of about 10 years and contributing to storage in about three out of 10 years. Please provide the changed projections showing projected contributions to and drawdowns from storage based on projected demands.”

Metropolitan Response: Prior storage projections were removed because they are no longer applicable.

SDCWA Comment: “A-43. Regional Water Resources. The single greatest and most notable change in regional water resources over the past five and 10 years, having the single greatest impact on the reduced demand for MWD’s supplemental water supply, is the more than 300,000 acre feet of water supply developed by the Water Authority—both QSA and seawater desalination, neither of which is mentioned in the description of regional water supply. This supply is delivered year in and year out, unlike the LAA supply which varies, as described in detail in the draft Appendix A, from 141,866 in fiscal year 2018-19 to a high of 332,528 in fiscal year 2015-16. Other MWD agencies and sub-agencies are also reducing demand on MWD, consistent with California law and water policy, which also is not adequately addressed in the draft Appendix A.”

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Metropolitan Response: Appendix A includes all material information related to local water supplies. Metropolitan has disclosed the seawater desalination programs operating in Metropolitan’s service area, see “REGIONAL WATER RESOURCES–Local Water Supplies – Seawater Desalination”. Appendix A also contains descriptions of local water supplies that have been developed by member agencies. As noted above, Metropolitan will also be adding a description of the quantity of local water supplies not funded by Metropolitan to the various subsection in “REGIONAL WATER RESOURCES–Local Water Supplies.” With respect to conserved IID and canal lining water exchanged under the Exchange Agreement, please refer to our response to comment on A-5, above.

SDCWA Comment: “A-48. Regional Recycled Water Program (RRWP). Thank you for including disclosure that MWD’s financial projections do not include future capital costs of the RRWP. Since you have included reference to the \$6 million payment by Southern Nevada Water Authority (SNWA) for planning costs, we recommend you also include disclosure of the total estimated planning costs, estimated capital cost of the RRWP and the fact that SNWA’s payment must be refunded if the parties do not move forward with an agreement for the RRWP.”

Metropolitan Response: Anticipated costs for the full-scale Regional Recycled Water Program are not included in Appendix A because the Board has not approved the project and there are no firm financial or contractual commitments to move beyond the demonstration project at this time, except to undertake the environmental review activities as described, the budgeted costs for which are clearly disclosed. Appendix A will be revised to reflect the potential reimbursement of SNWA’s payment.

Sincerely,



Katano Kasaine
Assistant General Manager/Chief Financial
Officer/Treasurer



Marcia Scully
General Counsel

cc: J. Kightlinger
MWD Board Members
SDCWA Board of Directors and Member Agencies

Attachment 1— Board Distribution Draft Appendix A dated December 22, 2020

Attachment 2— Board Distribution Draft Appendix A dated December 22, 2020, redline draft