



THE METROPOLITAN WATER DISTRICT
OF SOUTHERN CALIFORNIA

Office of the General Manager

VIA EMAIL

May 11, 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 May 9, 2021 regarding Draft Appendix A dated April 27, 2021

This letter addresses your comments received on May 9, 2021 (SDCWA 2021 Letter), regarding the Board Distribution of the Draft Appendix A dated April 27, 2021 (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, as you know, 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

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 April 27, 2021, showing changes from the draft dated December 22, 2020 (Attachment 2).

Comments Regarding Demand for 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: "MWD's 10-year rate forecast, which staff continues to say serves as MWD's long-range financial plan, does not include the costs of the two major projects—the Delta Tunnel and Regional Recycled Water Program—MWD is counting on for long-term water supply reliability."

Metropolitan Response: Metropolitan's Ten-Year Financial Forecast is a ten-year financial projection of overall rates, determined by projected revenue requirements and expenses. Staff does not "say [it] serves as MWD's long-range financial plan." The Ten-Year Financial Forecast does not include the anticipated costs for the full-scale Regional Recycled Water Program or the Delta Conveyance Project because the Board has not approved either of these projects. Other than the respective environmental review and planning activities described in Appendix A, including the budgeted costs therefor, there are no firm financial or contractual commitments related to these two projects that can be described at this time.

SDCWA Comment: MWD’s practice of melding MWD water sales and wheeling revenues (combined and reported as “transactions”) obscures the financial and resource planning implications of MWD’s reduced water sales trend.

Metropolitan Response: As explained in several previous letters, 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.

SDCWA Comment: “A-11. Current Water Conditions. The description of MWD’s 2021 Colorado River supply is incorrectly stated as 1,008,700 acre-feet, by including the Water Authority’s independent Colorado River water and San Luis Rey Water Transfer as “MWD’s supplies.” By contrast, MWD’s Water Surplus and Drought Management (WSDM) Report dated May 11, 2021 properly accounts for the Water Authority’s Colorado River supplies and San Luis Rey Water Transfer at 283,000 acre-feet and 16,000 acre-feet, respectively, for 2021. In addition to correcting this error, we also suggest that Appendix A be updated to match the supply conditions described in the May 2021 WSDM report.”

Metropolitan Response: Pursuant to the 2003 Amended and Restated Exchange Agreement between Metropolitan and SDCWA, Colorado River water acquired by SDCWA is made available to Metropolitan’s intake on Lake Havasu, where Metropolitan takes possession of the water. In exchange, Metropolitan delivers a like-amount of its own blended water to SDCWA at the Metropolitan-SDCWA connections. Similarly, under a separate agreement, the United States delivers water allocated to the San Luis Rey Settlement Parties to Metropolitan. In exchange, Metropolitan delivers a like-amount of its own blended water to SDCWA for the San Luis Rey Settlement Parties at the Metropolitan-SDCWA connections. Accordingly, Metropolitan properly reports all Colorado River water it receives pursuant to its basic apportionment, programs, and agreements.

SDCWA Comment: “This section relies on outdated 2015 IRP data rather than referencing the updated local supply forecast included in MWD’s 2020 UWMP. Among other things, the 2020 UWMP forecasts that in 2040 there will be up to 172,000 acre-feet (or almost 7%, depending on hydrology), more in local supply production than included in MWD’s 2015 forecasts. Also, MWD is contractually bound under Section 4.1 of its Exchange Agreement with the Water Authority to report the Water Authority’s QSA exchange water as a local supply.”

Metropolitan Response: Metropolitan’s 2020 UWMP is prepared in compliance with the Urban Water Management Planning Act and by its statutorily prescribed nature, calls for assessments with standardized or mandated criteria for water supply and demand forecasts and projections. These criteria can, for some assumptions underlying the forecasting and projection process, determine how those assumptions are used. As explained in the paper titled, Impact of Local Supply Projections on Demand on Metropolitan (see 2020 UWMP Reference Documents <http://www.mwdh2o.com/AboutYourWater/Planning/Planning->

Documents/Pages/2020-Reference-Materials.aspx), a broader context of local supply projections inform other planning processes at Metropolitan, including financial projections. The IRP, which is currently being updated, is Metropolitan's long-term planning process that guides long-term financial projections. Upon completion of the 2020 IRP, Metropolitan will update its long-term financial projections to be consistent with the updates in the 2020 IRP. Metropolitan believes that all material information regarding Local Water Supplies has been disclosed in Appendix A.

With regards to the request that Metropolitan report water it receives pursuant to the Exchange Agreement with SDCWA as "local supply," please refer to Metropolitan General Counsel's letter dated April 23, 2021 fully addressing this issue.

SDCWA Comment: "A-13. 2020 IRP. As noted above, continued reference to the outdated 2015 IRP rather than to current, available information is of concern. This is especially the case considering delayed progress of the 2020 IRP, still underway (with much remaining to be done) after more than 15- months in process."

Metropolitan Response: The Integrated Water Resources Plan section in Appendix A, beginning on page A-11, accurately describes the last completed IRP and the ongoing development of the 2020 IRP. The IRP is a long-term planning process that informs many decisions at Metropolitan on a long-term basis and it is, therefore, reasonable to serve as the basis of planning processes over many years. Once the Board completes and approves the 2020 IRP, a description of the water resources planning document will be incorporated into subsequent updates of Appendix A.

SDCWA Comment: "A-17. State Water Project. The language added to the last full paragraph on page A-17 appears inconsistent with other parts of the same paragraph regarding the status of the Delta Conveyance Agreement in Principle (AIP) and proposed amendments regarding the allocation of project costs. If negotiations with DWR for the Delta Conveyance AIP are now completed (we do not recall this being reported to the MWD Board of Directors, so please advise), the paragraph should describe what the process will be if public agency boards do not subscribe to 100% of the project, especially given that the MWD board has authorized its participation in the planning phase only."

Metropolitan Response: As noted in Appendix A, negotiations on the Delta Conveyance AIP have been completed. The Delta Conveyance AIP will be the basis for amendment of the State water supply contracts that would allow for the costs related to any Delta Conveyance Project to be allocated, and collected, by DWR. The Delta Conveyance AIP also provides for the allocation of benefits for any Delta Conveyance Project in proportion to each State Water Contractor's participation.

Each State Water Contractor's level of participation will be addressed separately. As stated in Appendix A, each agency's board, including Metropolitan's, will have to authorize that agency's participation level in the Delta Conveyance Project. As no State Water Contractor has authorized participation levels, and contract amendments will not be considered until

2024, it is not known at this time what the process will be if public agency boards do not subscribe to 100% of the project.

SDCWA Comment: “A-24. Colorado River Water Apportionment and Seven-Party Agreement. MWD’s net Colorado River diversions are reported incorrectly by including the Water Authority’s independent Colorado River supplies and San Luis Rey transfer water as MWD supplies.”

Metropolitan Response: Please refer to Metropolitan’s response above regarding SDCWA Comment: “A-11. Current Water Conditions”.

Other Comments in SDCWA 2021 Letter Regarding May 2021 Board Memo 7-2 (Appendix A)

SDCWA Comment: “A-25. Quantification Settlement Agreement. Please correct to describe the project completion dates for the All-American and Coachella canal lining projects as 2010 and 2007, respectively, and that the total conserved water amount is 77,700 acre-feet annually for 110 years, plus any unused environmental mitigation water for the Coachella Canal Lining Project up to 4,850 acrefeet.”

Metropolitan Response: Metropolitan’s records show lining project completion dates of December 2006 for the Coachella Canal Lining Project and 2009 for the All-American Canal Lining Project. SDCWA’s most recent Official Statement also reports 2009 for the completion of the All-American Canal Lining Project.

The consecutive discussions under the headings “Quantification Settlement Agreement” and “Metropolitan and San Diego County Water Authority Exchange Agreement” fully disclose the volume of canal lining water allocated to SDCWA that is made available to Metropolitan at Lake Havasu, through 2112, pursuant to the 2003 Exchange Agreement.

SDCWA Comment: “A-43. Metropolitan’s Water Storage Capacity and Water In Storage. Lake Mead’s storage capacity is reported here as 1,739,000 while the May 2021 WSDM report states the storage capacity as 1,657,000. Please confirm and include the correct number.”

Metropolitan Response: The May 2021 WSDM report reflected IID’s increased storage of 32,824 AF of Extraordinary Conservation ICS and BICS in Lake Mead, and 50,000 AF of water borrowed by Arizona under the DCP, reducing Metropolitan’s available ICS storage in Lake Mead by 82,824 AF. Appendix A will be updated to reflect this more up to date accounting of Lake Mead ICS Storage Capacity.

SDCWA Comment: “A-68. Tier 1 and Tier 2 Water Supply Rates. At a minimum, the draft should be amended to include reference to the fact that no Tier 2 water rates have ever been collected by MWD and are highly unlikely to be collected in the future given reduced demand for MWD water. Given this fact, there is no logical support for the statement that “the Tier 2 Supply Rate encourages the member agencies and their customers to maintain existing local supplies and develop cost effective local supply resources and conservation.” MWD is currently purchasing water transfers from north of the Delta even though no Tier 2 revenue has ever been collected. See Appendix A language added at A-10: “On April 13, 2021, the Board authorized the General Manager to secure up to 65,000 acre-feet of additional water pursuant to one-year water transfers from water districts located north of the Sacramento-San Joaquin River Delta.”

Metropolitan Response: The statement included in Appendix A refers to the purpose and intent of the Tier 2 Supply Rate, which remains unchanged.

SDCWA Comment: “A-68-69. Water Stewardship Rate. As per our prior comments, we do not agree with the characterization of the Court of Appeal’s ruling on the Water Stewardship Rate, which clearly states that demand management costs are supply costs not transportation costs and therefore must be allocated accordingly. The Court of Appeal also expressly rejected MWD’s reliance on “avoided costs” as a basis for rate-setting. At a minimum, this section should add a disclosure that MWD is seeking by its most recently filed appeal to eliminate or revise language in the judgment and writ of mandate entered by the Court which it contends is inconsistent with the disclosures contained in Appendix A.”

Metropolitan Response: Metropolitan’s position as to the Court of Appeal decision and the status of the litigation is accurately described in Appendix A.

SDCWA Comment: “A-69-70. Member Agency Purchase Orders. We incorporate by reference our comments in prior letters stating why reference to MWD “Purchase Orders” in Appendix A is misleading, including but not limited to the fact that no Tier 2 revenue has ever been collected and is unlikely to ever be collected by MWD. See above discussion of Tier 1 and Tier 2 water supply rates.”

Metropolitan Response: Purchase Orders remain in place and effective. Therefore, the inclusion of descriptions of such agreements are accurate and appropriate. Additionally, we incorporate by reference our responses in prior letters regarding the description of voluntary water supply purchase orders in Appendix A.

SDCWA Comment: “A-78 – A-84. Litigation Challenging Rate Structure. The Water Authority disagrees with many of the characterizations in the draft Appendix A of the litigation, but limits its responses here to specific statements:

- o A-80: Final sentence of third paragraph says, “Metropolitan may raise this issue [setoff from SDCWA’s damages] again on any later appeal from the cases’ final judgment.”
- o A-80-A-81: In the paragraph describing MWD’s 998 offer, the Water Authority disagrees that MWD’s offer met the statutory criteria (additional information previously provided by the Water Authority is available if MWD has not made this information available to bond counsel).
- o A-81 (fifth full paragraph): The Water Authority filed its responding brief on appeal on May 7, 2021.
- o A-82 (third full paragraph): The stipulation and order on the amount of the Water Authority’s recoverable fees provides that SDCWA is entitled to recover post-judgment interest on the amount at 7 percent per annum.
- o A-82-A-83: The offsetting benefits theory in the 2014/2016 cases is not an “added claim.” To the contrary, *as Judge Massullo has already concluded*, the Water Authority’s “original complaint alleged that Met’s rates violate the Wheeling Statutes and are invalid because the rates Metropolitan charges for transportation . . . exceed fair compensation for use of Metropolitan’s facilities,” including the offsetting benefits requirement. (See September 9, 2020 Order Re Motion to Correct at page 2, internal quotations omitted.) The Water Authority’s amended complaint merely “reiterates Met’s alleged failure to comply with its statutory obligation, in greater detail.” (*Ibid.*)
- o A-83 (second full paragraph): The Water Authority’s answers to MWD’s cross complaint also contain affirmative defenses.”

Metropolitan Response: We will (1) delete the sentence stating Metropolitan may raise the set-off issue on any later appeal from the 2010 and 2012 cases’ final judgment, since Metropolitan opted not to do so; (2) add the May 7, 2021 filing by SDCWA; and (3) add that SDCWA’s answers to Metropolitan’s cross-complaints include affirmative defenses. We will not make other changes to the rate litigation provisions, as Appendix A accurately describes material facts relating to the rate litigation and Metropolitan does not believe Appendix A is the appropriate document to include SDCWA’s characterizations of the ongoing litigation.

SDCWA Directors

May 11, 2021

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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 April 27, 2021

Attachment 2— Board Distribution Draft Appendix A dated April 27, 2021, redline draft