



THE METROPOLITAN WATER DISTRICT
OF SOUTHERN CALIFORNIA

Office of the General Manager

February 1, 2018

Ms. Maureen Stapleton
General Manager
San Diego County Water Authority
4677 Overland Avenue
San Diego, CA 92123

Dear Ms. Stapleton:

I would like to bring your attention to Metropolitan's staff recommendation in our budget proposal for fiscal years 2018/19 and 2019/20 and how those recommendations impact the San Diego County Water Authority (SDCWA) and its member agencies with regard to the exchange agreement.

As you are aware, the exchange agreement between Metropolitan and SDCWA sets the price Metropolitan charges SDCWA for exchanging conserved water made available to SDCWA from the Imperial Irrigation District and canal lining, with water Metropolitan delivers to SDCWA, at Metropolitan's transportation rates. In the rate litigation brought by SDCWA challenging Metropolitan's transportation rates, the appellate court ruled Metropolitan may collect State Water Project transportation costs as part of Metropolitan's transportation rates. The proposed rates for 2019 and 2020 accordingly comply with that ruling and continue to collect State Water Project transportation costs in Metropolitan's transportation rates.

The appellate court also found the administrative record before it for the rates in 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. Metropolitan's policies have supported the belief that conservation and local resource development reduce the demand for imported supplies, which reduces the costs to build, expand, operate, and maintain transportation facilities. In our view, this has a regional benefit for all of Southern California. As you are aware, the issue of avoided costs and their application to transportation rates was not actively briefed or litigated in the cases.

Based on the appellate court decision, we believe this matter merits further study. Later this year, staff intends to begin an internal process with input from the member agencies to further study and determine the most appropriate cost allocation of the Demand Management cost function. This would be an open and transparent process with scheduled workshops and allow for review and comment by all member agencies and Metropolitan's Board. While this review is being conducted, staff is proposing that Metropolitan not bill any amount of the Water

Ms. Maureen Stapleton

Page 2

February 1, 2018

Stewardship Rate on exchange agreement deliveries for calendar years 2019 and 2020. The Water Stewardship Rate would continue to be a part of Metropolitan's full service water rate and the rate for wheeling service. This issue would be revisited in the next biennial budget and rate setting cycle for years 2021 and 2022 when the decision by Metropolitan's Board would be informed by the completed study of the Demand Management cost function.

As for 2018, Metropolitan's previously approved rates include the Water Stewardship Rate as a transportation cost. Staff is further recommending that Metropolitan suspend billing and collecting the current Water Stewardship Rate on exchange agreement deliveries for calendar year 2018. This recommendation cannot become effective without Board authorization, so staff will continue to bill and collect Metropolitan's adopted transportation rates at least through April 2018 when the Board considers this proposal. If the Board adopts staff's recommendation to suspend billing and collecting the Water Stewardship Rate on the exchange agreement deliveries, such monies collected through April 2018 would be refunded to SDCWA.

At this time, this is only a staff recommendation that will be included as part of the proposed biennial budget for fiscal years 2018/19 and 2019/20 to be voted on by the Board in April 2018. We do not believe this approach is mandated by the appellate court decision; rather, we believe this is the most equitable approach given our state of information at this time and the guidance we have received from the appellate court. Metropolitan's Board may very well adopt an approach to these issues other than staff's recommendation.

If you have any questions, please feel free to call me.

Sincerely,



Jeffrey Kightlinger
General Manager

cc: Metropolitan Board of Directors
San Diego County Water Authority Board of Directors