



Finance & Asset Management Committee

Historical Revenue and Expense Analysis

Item 6c

March 12, 2024

Item 6c
Historical
Revenue and
Expense
Analysis

Subject

Historical Revenue and Expense Analysis

Purpose

Follow up informational item from February 2024

Summary of the Requests

- Finance was asked to provide a 10-year historical revenue and expense analysis
 - Staff prepared and delivered this presentation to the FAM Committee at Budget Workshop #1 on February 12, 2024
- As a subsequent follow-up request, Finance was asked to provide a 10-year historical revenue and expense analysis (budget v. actual) by rate element. **The data, as requested, is not available.** Metropolitan's actual revenues and expenditures are recorded in accordance with GAAP standards; they are not recorded by rate element

MWD Water Service Rates & Charges

- Metropolitan, a wholesaler, is structured to provide for full-service **treated** or **untreated** water
 - **A single enterprise**
- Functionalization of costs must be reasonable
- Rate unbundling provides transparency to identify the costs of the operational functions corresponding to the rate elements and charges during development of the budget and the cost-of-service process

Table 1. Water Service Rates and Charges

	Effective January 1st	2023	2024
Tier 1 Supply Rate (\$/AF)		\$321	\$332
Tier 2 Supply Rate (\$/AF)		\$530	\$531
System Access Rate (\$/AF)		\$368	\$389
System Power Rate (\$/AF)		\$166	\$182
Full Service Untreated Volumetric Cost (\$/AF)			
Tier 1		\$855	\$903
Tier 2		\$1,064	\$1,102
Treatment Surcharge (\$/AF)		\$354	\$353
Full Service Treated Volumetric Cost (\$/AF)			
Tier 1		\$1,209	\$1,256
Tier 2		\$1,418	\$1,455
Readiness-to-Serve Charge (\$M)		\$154	\$167
Capacity Charge (\$/cfs)		\$10,600	\$11,200

Unrestricted Reserves

Policy Established Pursuant to the Administrative Code

§ 5202. Fund Parameters.

The minimum cash and securities to be held in the various ledger funds as of June 30 of each year shall be as follows:

(a) For the Revenue Remainder Fund cash and securities on hand of June 30 of each year shall be equal to the portion of fixed costs of the District estimated to be recovered by revenues from water transactions, including, but not limited to, sales, exchanges, and wheeling, for the eighteen months beginning with the immediately succeeding July. Such funds are to be used in the event that revenues are insufficient to pay the costs of the District.

(c) Amounts remaining in the Revenue Remainder on June 30 of each year after meeting the requirements set forth in Section 5202(a) shall be transferred to the Water Rate Stabilization Fund and to the extent required under Section 5202(d), to the Water Treatment Surcharge Stabilization Fund.

(d) After making the transfer of funds as set forth in Section 5202(c), a determination shall be made to substantially identify the portion, if any, of such transferred funds attributable to collections of treatment surcharge revenue in excess of water treatment cost and to collections of water stewardship rate revenue in excess of costs of the Conservation Credits Program, Local Resources Program seawater desalination and similar demand management programs, including the departmental operations and maintenance costs of administering these programs. Such funds shall be transferred to the Water Treatment Surcharge Stabilization Fund and the Water Stewardship Fund, respectively, to be available for the principal purpose of mitigating required increases in the treatment surcharge and water stewardship rates. If such determination indicates a deficiency in treatment surcharge or water stewardship rate revenue occurred during the fiscal year, a transfer of funds shall be made from the Water Treatment Surcharge Stabilization Fund or the Water Stewardship Fund, as needed and appropriate, to reimburse funds used for the deficiency. Notwithstanding the principal purpose of the Water Treatment Surcharge Stabilization Fund and the Water Stewardship Fund, amounts assigned to these fund shall be available for any other lawful purpose of the District.

- The Administrative Code – which was approved by the Board – establishes Metropolitan’s unrestricted reserves:
 - Calculation methodology, amounts, and uses
 - Principal purpose to maintain stable and predictable water rates and charges

(e) Amounts in the Water Rate Stabilization Fund shall be held for the principal purpose of maintaining stable and predictable water rates and charges. The amount to be held in the Water Rate Stabilization fund shall be targeted to be equal to the portion of the fixed costs of the District estimated to be recovered by revenues from water transactions, including, but not limited to, sales, exchanges, and wheeling, during the two years immediately following the eighteen-month period referenced in Section 5202(a). Funds in excess of such targeted amount shall be utilized for capital expenditures of the District in lieu of the issuance of additional debt, or for the redemption, defeasance or purchase of outstanding bonds or commercial paper of the District as determined by the Board. Provided that the District’s fixed charge coverage ratio is at or above 1.2 amounts in the Water Rate Stabilization Fund may be expended for any lawful purpose of the District, as determined by the Board of Directors, provided that any funds distributed to member agencies shall be allocated on the basis of water revenues during the previous fiscal year, such revenues to include sales under the Interim Agricultural Water Program, Replenishment Service Program and all Full Service water sales.

Key Challenges & Risks

Enterprise Fund Accounting

- Metropolitan operates as a **utility enterprise** in accordance with generally accepted accounting principles (GAAP) for proprietary funds as required by Governmental Accounting Standards Board (GASB)
- MWD's **enterprise (purpose)** under the MWD Act is to develop, store, and distribute water, at wholesale, to its member public agencies for domestic and municipal purposes. This is unlike an all-purpose city or county, that engages in various general governmental and enterprise activities and keeps separate funds for each of those activities, including utilities
- MWD's presentation of **unbundled rates does not represent a distinct activity** from an accounting perspective – they are all components of MWD's primary purpose under the MWD Act. All operating revenues and unrestricted reserves – unless restricted by Administrative Code – are available to support MWD's enterprise-wide activities
- It is uncommon to dissect an enterprise fund's unrestricted reserves

Key Challenges & Risks

Special Funds for Tracking Purposes

- This requires the creation of multiple “special funds” to record and track both the revenues and expenditures of unbundled rate elements (i.e., supply, system access, power) - **which reflects a significant structural and system change across the district**
 - Creating and tracking reserves for each unbundled rate element would be inconsistent with Metropolitan’s enterprise structure
 - Structural limitations exist that require additional analysis to evaluate costs (i.e., time-keeping, billing system, and other financial systems)
 - There is no clear methodology to allocate existing unrestricted reserves into the proposed new reserve categories

Key Challenges & Risks

No California water utility uses “special funds” within an enterprise

- There are **no enterprise funds** using this approach
- Metropolitan’s **external auditors could not find** examples of water districts in California, **including MWD’s Member Agencies**, that use multiple funds to account for the activities of their utility enterprise, particularly by unbundled rate element category
- Importantly, cities or other multi-purpose agencies, including multi-enterprise agencies, are not comparable to Metropolitan

Key Challenges & Risks

Reduced Flexibility / Greater Reserve Needs in the Aggregate

- This approach would **limit system-wide flexibility** to cover unanticipated expenditures due to changing hydrologic conditions not contemplated in the adopted biennial budget
- If the flexibility on the use of unrestricted reserves is not maintained (i.e., requiring reserves by rate element/function), it would generally **require an increase in the reserve levels within each rate element/functional category** to account for greater degree of revenue/expense volatility
- **MWD can manage the volatility in its revenues** even with a high-degree of fixed expenses, largely because of the flexibility provided by having unrestricted reserves

Key Challenges & Risks

Access to Capital Markets & Rating Agency Considerations

- Creation of additional reserve funds would reduce Metropolitan's unrestricted reserve balance that is currently available for any lawful district expense, **including for debt service payments**
- Lower unrestricted reserve balances could **require higher rate increases** within biennial budget periods to meet Metropolitan's rate covenants including Metropolitan's debt service coverage ratio
- Likely viewed as a **negative rating action**, which will increase debt service costs and/or reduce Metropolitan's access to capital markets for future bond funded capital projects. This, in turn, could negatively impact the ratings of Metropolitan's Member Agencies

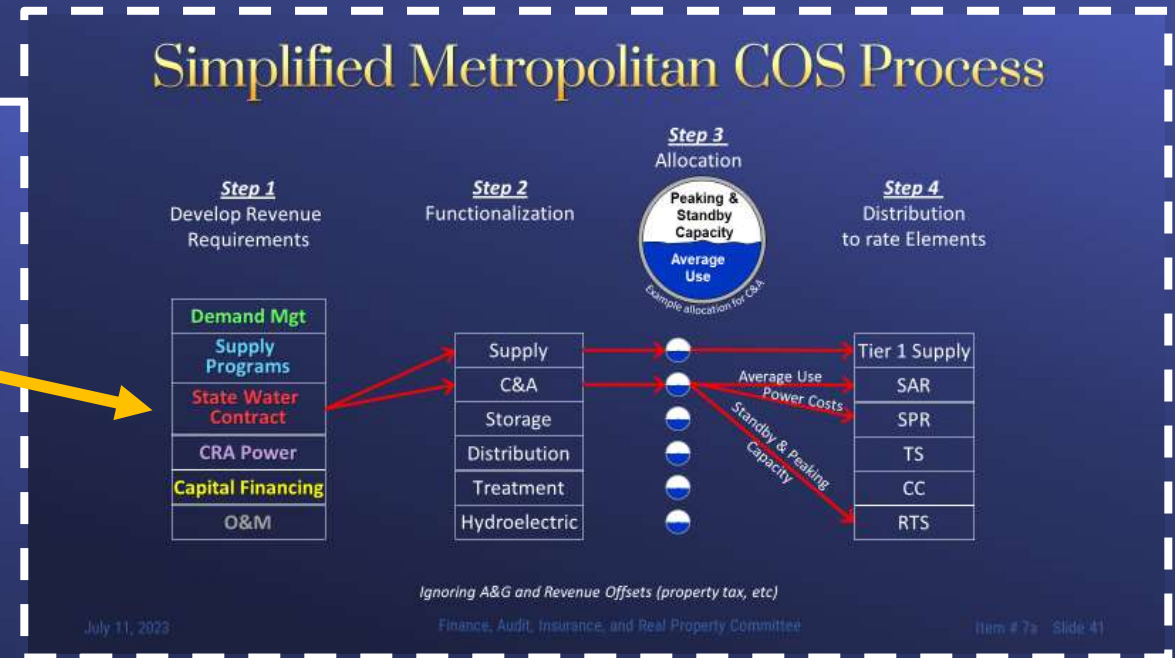
Requires a Year-End Cost-of-Service Study

Translate Actual Expenditures Back Into Rate Elements

	2022/23 Actual	2022/23 Budget	Variance
(\$ in millions)			
FY 22/23 Expenses (Cash Basis)			
<i>June 30, 2023</i>			
State Water Contract	\$ 577.5	\$ 651.7	\$ 74.2
Supply Programs	135.6	105.1	(30.5)
CRA Power Costs	161.9	105.9	(56.0)
Debt Service	300.7	288.0	(12.7)
Demand Management	59.8	68.8	9.0
Departmental O&M	556.1	586.1	30.0
PayGo	135.0	135.0	-
Delta Conveyance	34.5	34.5	-
Total Expenses	\$ 1,961.1	\$ 1,975.1	\$ (14.0)

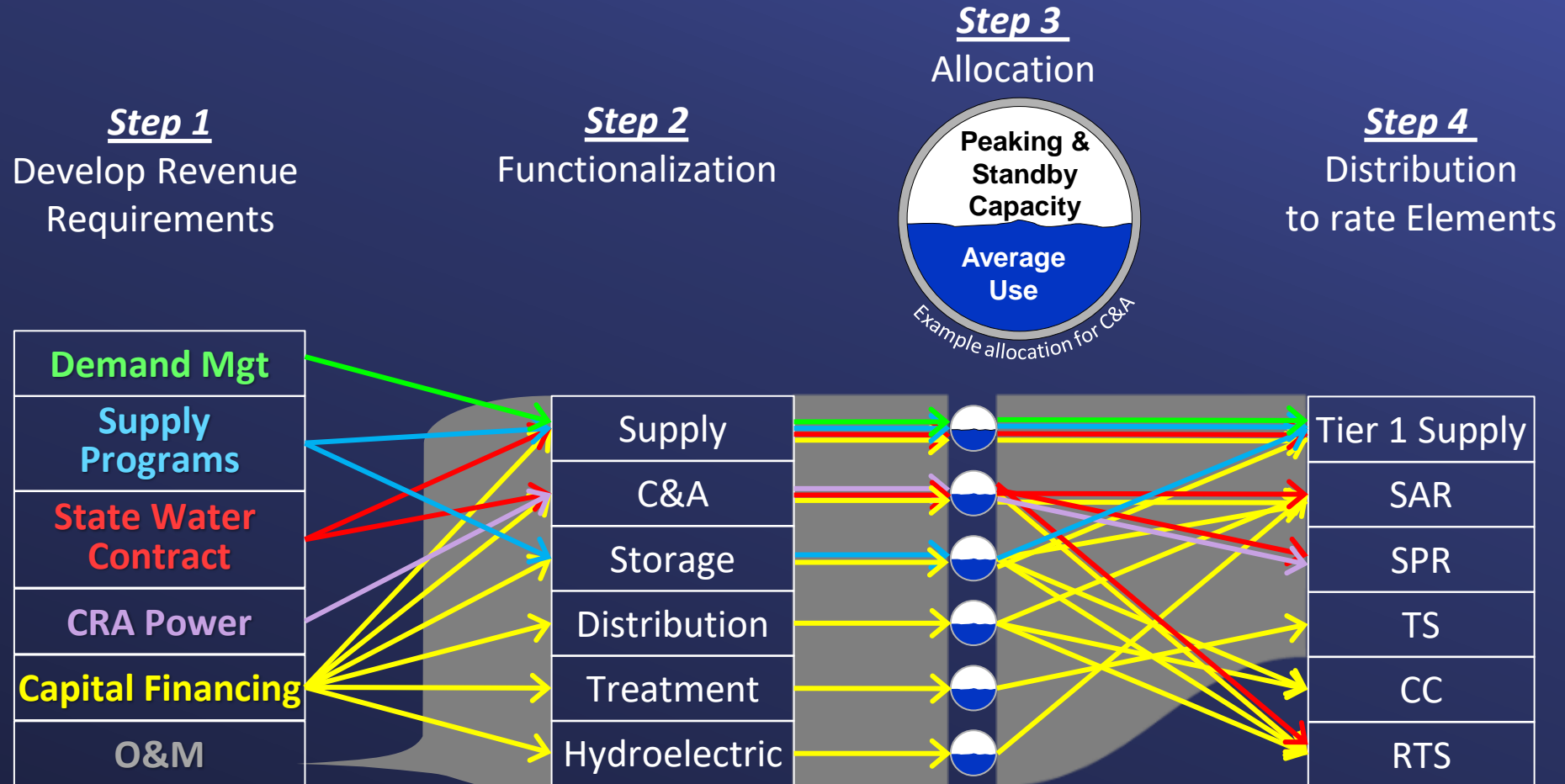
* Budget includes debt financed funding of \$4.5M from the CA WaterFix refund.

August 15, 2023 Finance, Audit, Insurance and Real Property Committee Item # 7a Slide 6



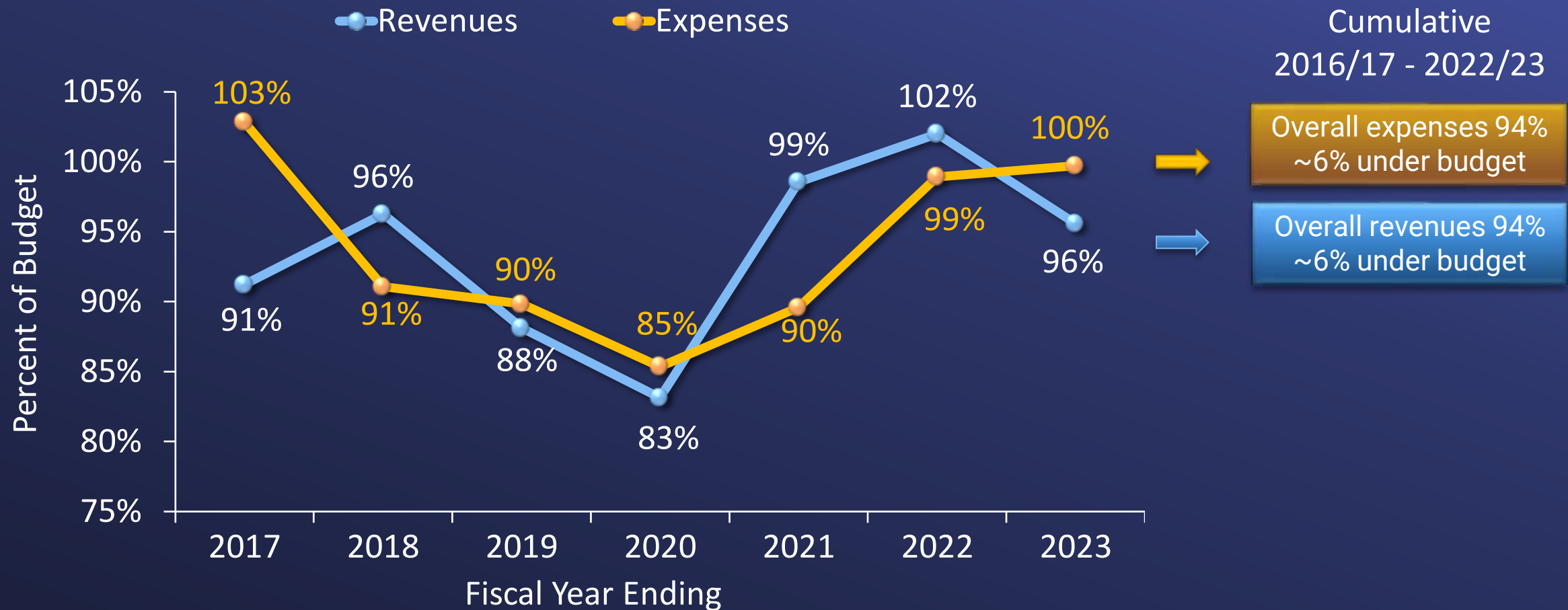
Requires evaluation each year and over a multi-year period to reverse engineer

Simplified Metropolitan COS Process



Ignoring A&G and Revenue Offsets (property tax, etc)

Actuals vs. Budget



FY2023 actuals are unaudited

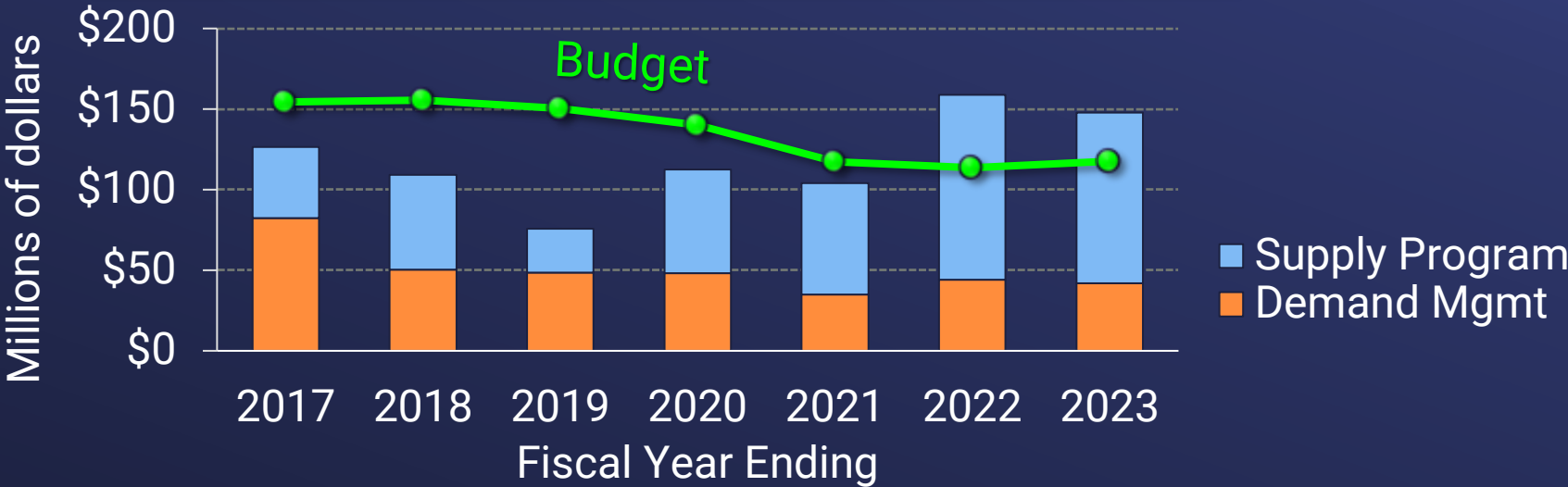
Actuals vs. Budget

Supply Programs and Demand Management

Cumulative actual supply program & DM costs from FY2017 to FY2023 were ~12% under budget.

Overall expenditures were ~6% under budget
Overall revenues were ~6% under budget

Supply programs: supplement Metropolitan’s principal sources of supply – SWP and Colorado River. Ex. PVID, AVEK High Desert Water Bank, dry Year transfers, etc.
Demand management: Conservation Program, Local Resources Program, Future Supply Actions & Stormwater Pilot



Recovered by:

Supply
SAR
SPR
TS
CC
RTS

This slide shows some of the costs that are recover by the Tier-1 Supply rate element.
Other costs include Sate Water Contract, O&M, capital financing costs.

FY2023 actuals are unaudited

Supply Revenue Requirement

Example from 2022/23 Budget/COS

SWC Delta: State Water Contract Delta
Capital and Delta OMP&R Charges

Supply programs: supplement Metropolitan's
principal sources of supply – SWP and
Colorado River. Ex. PVID, AVEK High Desert
Water Bank, dry Year transfers, etc.

Capital Financing: The portion of capital
financing costs that is attributed to Supply. Ex.
drought storage portion of DVL and PVID land
purchases

Demand management: Conservation
Program, Local Resources Program, Future
Supply Actions & Stormwater Pilot

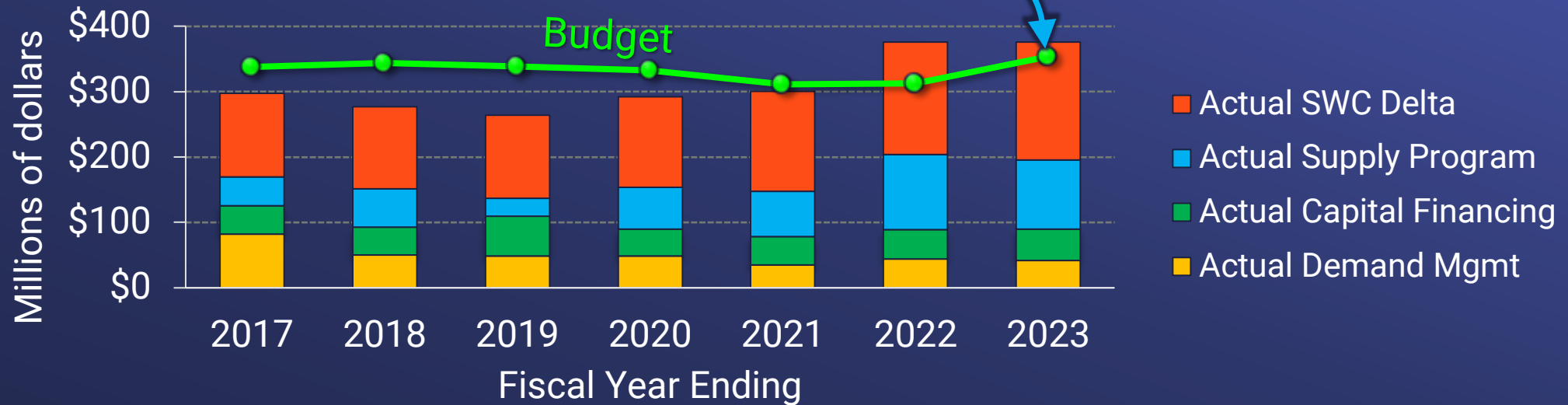
2023 Supply Revenue Requirement
in Million of dollars

SWC Delta	\$191
Supply Programs	67
Capital Financing	46
Demand Management	51
Departmental O&M	108
Total Supply Costs	462
Revenue offsets	(55)
Supply Revenue Requirement	\$407

\$354 Million
77% of the supply
expenditures.

Actuals vs. Budget

Supply Components*



Cumulative actual SWC delta, supply programs, capital financing, and demand mgmt costs from FY2017 to FY2023 were approximately 6% under budget

Overall expenditures were approximately 6% under budget
Overall revenues were approximately 6% under budget

Findings:

- Cost allocated to the supply rate element is in-line with the over/under collection for the overall expenditures and revenues
- The current COS process is reasonable at assigning costs to rate elements

*This slide shows most of the costs that are recover by the Tier-1 Supply rate element. It does not include departmental O&M costs.
FY2023 actuals are unaudited

Metropolitan Water Transactions

- SDCWA-Metropolitan Exchange Agreement contract price is equal to charges “generally applicable to the conveyance of water by Metropolitan on behalf of its member agencies”
- Under current rate structure, this is Metropolitan’s transportation rates

	Full-Service Water Service		SDCWA Exchange - Set by agreement
	Treated	Untreated	
Tier 1 Supply	✓	✓	
SAR	✓	✓	✓
SPR	✓	✓	✓
TS	✓		✓ *
CC	✓	✓	✓
RTS	✓	✓	

Wheeling and Exchanges set by agreement

* Only applicable when SDCWA takes treated water

