



STATE WATER PROJECT CONTRACT EXTENSION PROJECT

Draft Meeting Summary and Action Items

State Water Project Contract Extension Project

July 10, 2013 10:00 AM – 3:00 PM

Draft Meeting Attendance List

<p><u>California Department of Water Resources Lead Negotiators</u></p> <ul style="list-style-type: none"> • Steve Cohen, California Department of Water Resources • Rob Cooke, California Department of Water Resources • Perla Netto-Brown, California Department of Water Resources • Vera Sandronsky, California Department of Water Resources • Carl Torgersen, California Department of Water Resources • Ralph Torres, California Department of Water Resources <p><u>State Water Project Contractor Lead Negotiators</u></p> <ul style="list-style-type: none"> • Dan Flory, Antelope Valley-Eastern Kern Water Agency • Paul Gosselin, Butte County • Valerie Pryor, Castaic Lake Water Agency • Mark Krause, Desert Water Agency • Curtis Creel, Kern County Water Agency • Kathy Cortner, Mojave Water Agency • Steve Arakawa, MWD of Southern California • Deven Upadhyay, MWD of Southern California • Bob Perreault, Plumas County Flood Control & Water Conservation District • Jeff Davis, San Geronio Pass Water Agency • Ray Stokes, Santa Barbara County Flood Control and Water Conservation District / Central Coast Water Authority • David Okita, Solano County Water Agency • Mark Gilkey, Tulare Lake Water Storage District and County of Kings 	<ul style="list-style-type: none"> • Lisa Kern (by phone), Ventura County Flood Control District <p><u>California Department of Water Resources Staff</u></p> <ul style="list-style-type: none"> • Ted Alvarez, California Department of Water Resources • Terri Ely, California Department of Water Resources • Karen Enstrom, California Department of Water Resources • Jennifer Iida, California Department of Water Resources • Scott Jercich, California Department of Water Resources • Kathie Kishaba, California Department of Water Resources • Philip LeCocq, California Department of Water Resources • Chris Martin, California Department of Water Resources • Jamie Moran, California Department of Water Resources • Dave Paulson, California Department of Water Resources • Nancy Quan, California Department of Water Resources • David Sandino, California Department of Water Resources • Rita Sanko, California Department of Water Resources • Dena Uding, California Department of Water Resources • Pedro Villalobos, California Department of Water Resources
--	---

<p><u>State Water Project Contractors and SWC, Inc.</u></p> <ul style="list-style-type: none"> • Tamara Baptista, Alameda County Flood Control and Water Conservation District, Zone 7 • Josh Nelson, Best, Best & Krieger LLP/Crestline Lake Water Agency • Bruce Alpert, Butte County • Tom Glover (by phone), Dudley Ridge Water District • Gary Bucher (by phone), Kern County Water Agency • Don Marquez, Kern County Water Agency • Jaime Dalida, MWD of Southern California • Kevin Donhoff, MWD of Southern California • David Reukema, MWD of Southern California • John Schlotterbeck, MWD of Southern California • Leah Wills, Plumas County Flood Control and Water Conservation District • Matt Naftaly, Santa Barbara County Flood Control & Water Conservation District (by phone) • Lynn Hurley, Santa Clara Valley Water District • Dana Jacobson, Santa Clara Valley Water District • Eric Chapman, State Water Contractors, Inc. • Theresa Lightle, State Water Contractors, Inc. • Julie Ramsay, State Water Contractors, Inc. • Linda Standlee, State Water Contractors, Inc. 	<p><u>DWR Consultants for Contract Extension</u></p> <ul style="list-style-type: none"> • Erick Cooke, Environmental Science Associates <p style="text-align: center;"><u>Public</u></p> <ul style="list-style-type: none"> • Tina Cannon Leahy, California State Assembly Water, Parks, and Wildlife Committee (by phone) • Patricia Schifferle, Planning & Conservation League • Matt Weiser, Sacramento Bee (by phone) • Thomas Rinn, Waterworks Consulting (by phone) <p style="text-align: center;"><u>Facilitation Team</u></p> <ul style="list-style-type: none"> • Alex Braunstein, Kearns & West • Mike Harty, Kearns & West • Kelsey Rugani, Kearns & West • Anna West, Kearns & West
--	--

I. Welcome/Introductions

There were roundtable introductions of the negotiation teams and staff. Members of the public were given the opportunity to introduce themselves.

II. Meeting Overview

Anna West reviewed the Meeting Ground Rules emphasizing respect and listening. She also reviewed the process for public comment at the end of the meeting. Anna outlined the negotiation session agenda and stated that the DWR Counter Offer and BDCP Participation Options will be discussed.

Anna then reviewed the action list from the June 26, 2013 negotiation session. The group finalized the June 26 Meeting Summary, which will be posted on the website.

III. DWR Contract Extension Offer

Before reviewing the Counter Offer, Carl Torgersen thanked his staff for putting the proposal together in a short amount of time. Regarding Objective 3, Rob Cooke explained that a Freeze-Go system will apply to all costs incurred prior to January 1, 2016. After that date, all payments will shift to a Pay-As-You-Go billing method. Rob stated that Article 22 through 29 would need to be amended and the WSRB surcharge would only apply to costs incurred prior to January 1, 2016. Rob outlined a new piece of DWR's Objective 3 proposal related to variable costs. While under the current system the Department is constantly waiting for actuals to come in. DWR proposes that Contractors pay projected variable costs up-front, on a monthly basis. Rob clarified that DWR would estimate what the cost would be based on monthly water deliveries.

Perla Netto-Brown provided an overview of DWR's Counter Offer on Objective 2a. The purpose of this Objective is to implement and develop a General Operating Account (GOA) that meets the Department's needs. The Department proposes funding the account equivalent to 90 days, which today would be \$150 million. The current balance of the GOA is \$27.4 million. The GOA can be used towards supporting the normal peaks and valleys of cash flow during the year, supplying cash flow to cover shortages due to the two-year billing cycle, and providing immediate cash to meet all State Water Project obligations, including costs that are not anticipated and emergencies for any State Water Resources Development System (SWRDS) purpose. Replenishment of the GOA will occur within the normal two-year billing process to the Contractors or in an expedited manner mutually agreed upon by DWR and the SWP Contractors. The Department proposes eliminating the 30-day grace period, resulting, by DWR's estimate, in approximately \$30 million, and that the GOA is reviewed every five years, in consultation with the Contractors. Increases to the GOA after 2035 would come from direct billings to the Contractors. Like the SWP Contractors Offer, DWR proposes eliminating the Replacement Accounting System (RAS) for transportation and conservation facilities. DWR proposes to transfer \$20 million into the GOA bringing its total up to \$170 million including the \$150 million from the 90-day reserve. Regarding financial management, the Department is interested in implementing what they can on improved reporting and management tools.

Perla further explained that there could be emergencies or other situations where the GOA would be used for non-reimbursable costs. The intent is not to deplete the GOA or lead to a permanent reduction, but to provide cash until the beneficiaries are billed and have paid.

Deven Upadhyay sought clarification on the difference between the Department's initial offer and this most recent one. Is this current offer asking for more or trying to reach middle ground? Perla stated that the difference is a movement to a middle ground in that DWR had incorporated concepts from the Contractors, including eliminating the grace period and the RAS. She noted that the Department's revised offer is for 90 days down from the original offer which had 120 days.

Lisa Kern asked what approximately would be in the RAS before 2016. Perla clarified that there is currently a cash balance of \$32 million not taking into account encumbrances. DWR proposes to retain \$20 million for the GOA account, and then the remainder would be available for return to the Contractors.

Steve Cohen clarified that when the GOA is used for an emergency where the purpose is for water supply, the Contractors would pay those costs. If the funds are for non-water supply or both non-water

supply and water supply, then the interest that accumulates could be used toward non-water supply costs. DWR would look to Davis-Dolwig or the legislature if there are recreation costs to be reimbursed. Carl Torgersen added that emergency costs involving non-water supply purposes would likely be relatively small and that in a disaster scenario, there would likely be other funding available.

Steve Cohen then reviewed Objective 2b stating that DWR wants to be confident that there are sufficient revenues for cash flow coverage, emergencies, and non-water supply purposes or water supply with no water contractor. Under the current system, DWR has a revenue stream for covering these purposes, and the Department wants to assure they have the ability to cover those costs after 2035.

The proposed SWRDS Support Account would go into effect after 2035 when 51(e) revenues are no longer available. The purpose of the account is to pay for costs where no funds or no revenue sources are available, and DWR would consult with the Contractors on how to use the fund. The target amount for the account is \$60 million, and DWR is proposing that 51(e) revenues would be used to initially fund the account. When 51(e) funds are no longer available then the Contractors would be billed the lesser of 1) 1% of the Contractors' annual charges for the billing year, or 2) a percentage (if less than 1%) of the Contractors' annual charges.

Paul Gosselin asked if these funds could go towards projects that are reimbursable by the legislature and if DWR would need legislative authority before carrying out the transaction. Steve clarified that DWR is looking into ways to fund projects in ways that are permissible under current law. Steve also reiterated that the Department would initially fund the account with system revenues.

Jeff Davis asked if this fund would be used to fund a project where 95% of its purpose is for water supply and 5% is not. Steve stated that the Department wants to have flexibility in a situation where there isn't available funding otherwise. Currently, the Department does not see this fund being used very often, but in an emergency situation where not all of the project is for water supply, this account would be used to pay for some of those costs.

Deven Upadhyay asked why the term "good faith efforts" was used when describing that 51(e) revenues would fund Objective 2b whereas "proposes to use" 51(e) revenues was used for Objective 2a? Steve answered that DWR wants to ensure that if they are offering to fund these accounts, that they have the money available to do so. He clarified that the intent is to have initial funding for 2b using system revenues. Deven also asked if costs are not initially funded by a source and SWP Contractors pay the costs, but a source eventually becomes available, will the Contractors be reimbursed? This is an item to be discussed within a Technical Team, but DWR affirmed it would replenish the GOA account once paid by the beneficiary.

IV. BDCP Draft Offer

Paul Gosselin reviewed the revised Objective 4 on BDCP participation options. He stated that the Objective makes participation in BDCP voluntary, allowing Contractors who are not receiving benefits from BDCP, such as Butte County and Plumas County Flood Control and Conservation District, to voluntarily opt-out of paying for costs related to the BDCP. David Okita and Curtis Creel shared that they had assisted Paul and Bob Perreault in drafting the Objective language and clarified that while they agree in concept, that all 29 SWP Contractors have not discussed this issue at length. Bob Perreault

stated his support of the Objective, and Carl Torgersen stated that DWR is not prepared to provide comments at this time.

V. Contract Extension Offers Continued

Ray Stokes addressed a concern about 51(e) revenues potentially being distributed disproportionately amongst the Contractors. He also asked for clarification on if the billing system moves to Pay-As-You-Go and the Contractors would pay 100% cost recovery as they do currently, then SWP Contractors believe that there will be 51(e) revenues available post-2035. Ray gave the example of a \$100 million dollar project with 75% funded through 30-year bonds and 25% funded through 51(e) revenues where Contractors are billed directly with interest charges and therefore 51(e) revenues exist after 2035. Assuming 100 percent cost recovery for all projects, then SWP Contractors believe that there will be 51(e) revenues after 2035. If this is the case, then it has significant consequences for the counterproposals, including Objective 2b and funding for non-reimbursable costs.

DWR responded that this discussion should continue at the Technical Team level, and should address likelihood, permissibility, and consequences. Ray stated that having 51(e) revenues post-2035 is a foundational issue for Contract Extension, suggesting that Contract Extension negotiations had assumed that 51(e) revenues would go away post-2035, and that may not be the case.

SWP Contractors Feedback on DWR's Counter Offers

David Okita then walked through DWR's Counter Offer and identified items where we can "park" the language because the individual item looks close, understanding that all parties need the full package to determine if it can be agreed to.

Objective 2a

Regarding **Objective 2a**, the Contractors stated that we can "park" the following language:

1. Funding the GOA, last sentence:

DWR would change the priorities set forth in Article 51(e) making the increase to the GOA first priority after rate management credits and eliminate the GOA rate of funding per year (\$2 million) to any amount of Systems Revenue cash flow until the proposed level is achieved.

2. Uses of the GOA

- a. The State Water Project (SWP) experiences peaks and valleys in its cash flow cycle similar to any other business. Some months, "cash in" will exceed "cash out" and other months the reverse may occur. The GOA will help to ensure there is sufficient cash available during the low points in the cash cycle to meet all the SWP obligations.
- b. The GOA will provide cash flow to cover shortages due to the two-year billing cycle of the Statements of Charges. Under the current SWP contracts, the contractors are billed based on actual costs and projections. The projections are "trued-up" in the next full billing cycle which occurs two years later. This can cause a cash flow shortage for the SWP.

3. Replenishment of the GOA

Replenishment of the GOA reserve account, depending on the amount of the draw, will occur through the normal, two year billing process to the State Water Contractors (SWCs) or in an expedited manner as mutually agreed upon between DWR and the SWCs. Emergency draws will be billed to the SWCs and other project beneficiaries.

The Contractors stated that the following statements on Objective 2a need more discussion:

1. Funding the GOA

The balance in the GOA is \$27.4 million as of January 2013. In order to bring the GOA to the 90 days or \$150 million level, DWR proposes to use available Systems Revenue cash flow. After 2035, any increases to the 90 days level would come from billings to the water contractors under the Conservation Minimum component of their bills based on Table A.

2. Uses of the GOA

- c. The State Water Project (SWP) experiences peaks and valleys in its cash flow cycle similar to any other business. Some months, “cash in” will exceed “cash out” and other months the reverse may occur. The GOA will help to ensure there is sufficient cash available during the low points in the cash cycle to meet all the SWP obligations.
- d. The GOA will provide cash flow to cover shortages due to the two-year billing cycle of the Statements of Charges. Under the current SWP contracts, the contractors are billed based on actual costs and projections. The projections are “trued-up” in the next full billing cycle which occurs two years later. This can cause a cash flow shortage for the SWP.
- e. The GOA will provide immediate cash for costs that are not anticipated or cannot be billed in accordance with need, due to contract language.
- f. Emergencies for any State Water Resources Development System (SWRDS) purpose.

4. Elimination of Grace Period

All billing components to the annual Statements of Charges shall be due on the invoice due date with no 30 day grace period; effectively eliminating the 30 day grace period.

5. Supplemental Billings

DWR shall have the ability to issue “revised” SWC billings in the event of a significant cash flow shortage caused by an emergency or crisis.

6. Periodic Review and Adjustment

Every five years, DWR will prepare an analysis, in consultation with the SWCs, to determine the appropriate level of the GOA. After 2035, increases to the GOA will come from direct billings to the SWCs as described above in Item No. 1. Decreases to the account will result in direct refunds to the SWCs.

7. Elimination of the Replacement Accounting System (RAS)

The GOA will eliminate the RAS for Transportation and Conservation Facilities with the intent to have replacement costs treated as a current minimum or capital cost. A portion of the current RAS cash balance (\$20 million) will be transferred to the GOA to increase the account to \$170 million.

The \$20 million is in addition to the 90 day level to be maintained per item 1 above. The balance in the RAS account will be returned to the SWCs.

8. Interest Earnings on GOA

Interest Earnings on the GOA shall be retained in the account or used to meet other lawful SWRDS purposes, including transfer to the SWRDS Support Account per objective 2b, as determined by the Director of DWR.

9. Financial Management

The SWP Contractors' Offer included a proposal of 90 days, but that item was not included in the areas where the language can be "parked." David clarified that the 90 days is linked to the \$150 million proposed in DWR's Counter Offer and that more discussion is needed. David also mentioned that the Contractors view the elimination of the 30-day grace period as a potential tool for reducing DWR's cash flow needs.

Objective 2b

Regarding Objective 2b, the Contractors are not willing to accept any facet of 2b at this time.

Objective 3

Regarding Objective 3, the Contractors suggest we can "park" the following:

Implement Freeze – Go*

Concept - Amend the existing contract to establish a "Freeze – Go" Billing System.

- For all costs incurred prior to January 1, 2016, continue repayment consistent with current contract terms
- For all costs incurred after December 31, 2015, convert repayment to a Pay-As-You-Go methodology.

1. Project Repayment Period

Amend the definition of the Project Repayment Period to apply only to those costs incurred prior to January 1, 2016. The term of the Project Repayment Period will remain the same (e.g. January 1, 1961 through December 31, 2035). Retain the condition that if any bonds for the purposes of the State Water Project are sold past the termination date of the extended contracts, the contract termination date will be extended until the bonds are fully repaid.

2. Project Interest Rate

Amend the definition of the Project Interest Rate to apply only to those costs incurred prior to January 1, 2016. The Project Interest Rate will remain 4.610%

3. Amend Articles 22 – 29 and 50 (WSRB Surcharge) to add reimbursement of costs using a Freeze – Go methodology

All costs incurred prior January 1, 2016 will be allocated and repaid the same way it has been done historically. For costs incurred after December 31, 2015, amend the contract to recover Capital and Minimum cost based on actual debt service, not DWR costs. Article 50 will be amended so the WSRB Surcharge will only apply to costs incurred prior to January 1, 2016.

The Contractors would like to further discuss the DWR proposal on variable costs.

Ray asked if the rate management credits increase to \$48 million was left out intentionally. Carl responded that the Department is not ready to increase the credits at this time and credits will be addressed during the five year reviews. Steve stated that 1HH was raised within a Technical Team and more discussion is needed; this is why the Department did not include a 1HH proposal within their Counter Offer.

David Okita then stated that SWP Contractors omitted Objective 2b from their last offer because they assumed if that it could be dealt with at a later date. If DWR needs Objective 2b addressed in the current process, then it could be that there are other issues that the Contractors would like to address concurrently.

Deven Upadhyay shared his perception that the DWR Counter Offer included more money than originally offered by the Department, and asked how the Counter Offer could be viewed as a step towards middle ground. Perla Netto-Brown indicated that DWR had started at a 120 days or \$200 million in the GOA account for reserves and had come down to 90 days or \$150 million. Perla clarified that DWR's original offer did not include a value for 2b, so this additional offer was always anticipated, but this is the first time it was shared. She also indicated that the DWR Counter Offer had incorporated concepts from SWP Contractor proposals. Carl Torgersen added that it was not DWR's intention to increase the overall dollar amount asked for in the Counter Offer, but to offer new ideas to be discussed. Curtis Creel suggested that the financial viability of the State Water Project is a shared interest of both parties and further discussion needs to occur in a Technical Team to flesh out which tools, whether it's the elimination of the grace period, elimination of RAS and/or other tools, are appropriate to execute within this process.

Jeff Davis stated that financial management concepts are important because all of the Contractors report to an elected body and they need to be able to share insight on DWR's finances and what happens to their money. It was decided that the financial management concepts will be discussed further in a financial management Technical Team. Curtis Creel asked if the Department is open to considering financial management in the Contract Extension process. Carl conveyed that the Department is open to considering options that could include something in Contract Extension, or addressing it outside of Contract Extension.

VI. Next Steps

Anna reviewed the Contract Extension Process through July. Since issues including 51(e) revenues beyond 2035, variable billing, 1HH, RAS, and financial management need to be discussed further in

Technical Teams, the next two negotiation sessions will be Technical Team meetings. The next negotiation session will be Wednesday, July 31st at the Library Galleria. Anna reviewed the other action items.

VII. Public Comment

Patricia Schifferle from the Planning & Conservation League provided oral comment.

VIII. Adjourn

The meeting was adjourned.

	Action Items	Responsibility Due Date
1.	June 26 Negotiation Session Meeting Summary to be finalized and posted on the website.	Kearns & West ASAP
2.	Technical teams to meet July 17 at Resources Building 9:00 - 11:00am: 2a issues including 51(e) revenues beyond 2035, Variable billing value, 1HH, RAS and \$20 million 11:00 – 1:00pm: Financial management	Perla Netto Brown, Rob Cooke, Steve Cohen and Ray Stokes July 17 th Carl Torgersen and Curtis Creel Prior to July 10 th
3.	July 24 to be technical team meeting(s) and not a negotiation session.	All July 24th
4.	July 31 to be the next negotiation session in public.	All July 31st
5.	An Administration Committee Call to be scheduled.	Kearns & West ASAP
6.	Email and calendar requests to be sent for negotiation sessions through September.	Kearns & West ASAP
7.	July 10 Negotiation Session Meeting Summary to be prepared.	Kearns & West ASAP