DWR 10/23/13

DWR Tentative Offer: Reserves and Flow of Funds

I. GOA, SSA, SRA, State Water Facilities Capital Account

A. General Operating Account (GOA)

1. Uses – Cash flow deficiencies resulting from chargeable water supply purposes and during a SWRDS emergency for any SWRDS purpose.

2. Initial Cap - $150 million. Initial funding will come from 51(e) revenues and $20 million from RAS. (See “E. Flow of Funds” below)

3. Cap Adjustment – Modeled after the formula in the Monterey Amendment. Every five years, adjust the cap by the percentage change in O & M charges (not including power charges) to the water contractors for the previous five year period, but limit any change in any five year period to no more than 35% of the then existing cap. All funding for any increase would come from Article 51(e) revenues, interest and investment earnings in the GOA and from SRA funds, as determined by the Director. If there is a decrease in the cap (but the cap shall not be lower than $150 million), the excess funds would be transferred to the SRA. The cap would be eliminated on January 1, 2036.

4. Replenishment of the use of GOA funds will come from charges to the water contractors to the extent the expended funds were spent on chargeable water supply purposes and from the SSA, SRA, or other sources for GOA funds spent on non-water supply purposes.

B. SWRDS Support Account (SSA)

1. Uses – pay for costs of the system where there are currently no funds or revenue sources available to pay for such costs. It is expected that these costs would be for non-water supply purposes and not for costs chargeable to the water contractors. The contractors are to be consulted about the projects and activities to be funded from the SSA.

2. Cap - $60 million with no adjustment through December 31, 2035. On January 1, 2036 the cap would be eliminated. Initial funding will come from 51(e) revenues. (See “E. Flow of Funds” below)

3. Replenishment of the SSA shall be accomplished through 1) reimbursements received for expenditures made from the SSA; 2) transfers, in the discretion of the Director, from the SRA; 3) transfers, in the discretion of the Director, of investment earnings from the GOA; 4) deposits in the discretion of the Director, from other available system revenues; and 5) interest and other investment income retained in the SSA.

C. SWRDS Reinvestment Account (SRA)

1. Use – the primary purpose is to provide a SWRDS revenue stream by investing funds in the SRA in facilities and programs that benefit SWRDS and are chargeable to the water contractors.

2. Investments – At the discretion of the Director, authorized SRA investments shall be as follows: 1) investment in SWRDS capital facilities, recovered at the prevailing tax-free municipal bond market rates corresponding to the SWRDS bond rating at the time of financing, in maturity ranges that may extend 10 to 50 years; 2) temporary financing in lieu of the SWRDS commercial paper program; and 3) any other legally permissible investment for the SWRDS.

3. Use of investment earnings generated by the SRA and other available (but not yet invested) funds in the SRA will, at the discretion of the Director, 1) provide the source of replenishment funds to the SSA; 2) for funds not transferred to the SSA, be accumulated in the SRA and held in the SRA for investment purposes; and 3) provide a funding source for funding level adjustments to the GOA.

D. State Water Facilities Capital Account (FCA)

1. The FCA shall continue as described in the Monterey Amendment (Article 51(b)) through December 31, 2035 and on January 1, 2036 the FCA will be closed and the funds in the FCA will be transferred to the SSA, provided that the Director will have the discretion to close the account and transfer the funds sooner than January 1, 2036.

E. The Flow of Funds

1. Initial funding of the increase in the GOA and the initial funding of the SSA and SRA shall come from 51(e) revenues, as the Director determines. The intent is to use available 51(e) revenues (plus $20 million from RAS, which will be returned to the contractors when the GOA is fully funded) to increase the GOA, as the highest priority, but also to retain the Director's

discretion to begin funding the SSA and SRA and to use available 51(e) revenues for any other SWRDS purpose prior to fully funding the GOA. The Director will retain the discretion to use available 51(e) revenues for additional SWRDS purposes as he currently has under the Monterey amendment.

2. The limitation on the amount ($2 million per year) and timing of additional contributions to the GOA contained in Article 51(e)(v) will be deleted, so that DWR will be able to use any amount of available 51(e) revenues to increase funds in the GOA, but such use shall be subordinate to the annual rate management reductions to the water contractors.

3. Flexibility in the event of an unforeseen funding issue – if any of the three accounts experiences a significant funding issue, as determined by the Director, the Director may transfer, on a temporary basis until the significant funding issue is resolved, funds from either of the other two accounts to the account experiencing the significant funding issue. Repayment of the transferred money shall come from the appropriate sources for the account receiving the transferred money.

4. DWR will prepare regular reports on the three accounts, which will be shared with the water contractors.

5. Backstop in the event the SRA or SSA fails to function as envisioned: DWR will eliminate the backstop if upon DWR's evaluation, a high degree of confidence exists that the arrangements for funding the new accounts will provide the revenue stream needed by SWRDS post 2035.

II Rate Management Reductions

A. Any consideration by DWR to amend Article 51 to provide for an increase in the annual rate management reductions is heavily dependent on the water contractors' acceptance of the terms and conditions for the accounts discussed in Section I above and the conditions specified in this Section II. Therefore, for discussion purposes only, the following conditions and consideration, among others, may be required before DWR will agree to embody in the contract a permanent increase in rate management reductions up to $48 million per year (still subject to availability in any year as in the current Monterey amendment).

B.

1. The contract will make clear that with the increase in the rate management reductions up to $48 million, the water contractors will not be entitled to receive any further rate management reductions – including no additional rate management reductions to make up for deficiencies in past projected

rate management reductions or to provide any additional rate management reductions above $48 million annually in the future.

2. DWR-State Water Contractors Financial Committee: DWR and the water contractors will be members of the committee, the primary function of which will be to make recommendations to the DWR director regarding certain financial aspects of SWRDS. The scope of the financial committee's responsibilities will be described in a charter mutually agreeable to DWR and the contractors.

3. The contractors shall agree to waive and release certain claims that were reserved in the Tolling and Waiver Agreement executed in 2007 relating to (1) the use of bond proceeds to pay for recreation costs and the related adjustments made to the contractors bills, (2) accounting for the costs of the San Joaquin Drainage Program and (3) the adjustment of water supply responsibility for certain Delta Facilities (see Section 1(b)(2), (3), (4) and (5)of the Tolling and Waiver Agreement). Other issues to be released and waived relate to DWR's recent adjustment of the water contractors' responsibility for facilities south of Dos Amigos and DWR's treatment of energy from off-aqueduct power facilities. Such releases and waivers could be addressed in an amendment to the Tolling and Waiver Agreement.

III. Emergency Bills

A. In lieu of supplemental billing and effective with the new amended contract, DWR shall have the ability to issue "emergency" Contractor billings up to 10% of the Contractors' current statement of charges for that calendar year in the event of a significant cash flow shortage caused by an emergency or crisis, where the GOA does not have sufficient funds available or where use of the GOA would deplete the fund (after taking into account temporary transfers of money from the SRA and SSA) and put the State Water Resources Development System water deliveries at risk.