



CITY OF SAN DIEGO

JAY GOLDSTONE
CHIEF OPERATING OFFICER

September 15, 2021

General Manager Sandy Kerl
San Diego County Water Authority
4677 Overland Avenue
San Diego, CA 92123

Dear General Manager Kerl:

Thank you for the time you and your staff have spent with the City of San Diego (City) team over the past few weeks. We've greatly appreciated further explanation of the information contained in the 2021 Long-Range Financing Plan (LRFP).

The City serves 1.4 million ratepayers, making it the largest member agency of the San Diego County Water Authority (SDCWA), and decisions made at SDCWA significantly impact our customers. Water purchased from SDCWA, like other member agencies, is the largest annual non-personnel expense for the City.

Given the declining water sales environment facing SDCWA due to local supply development and conservation by customers throughout the County, it is not only a worthwhile exercise, but incredibly important to the City that each and every rate driver be thoroughly analyzed to ensure rates are not escalating to a more unaffordable point on behalf of San Diegans. The LRFP presents an opportunity for the SDCWA Board of Directors to determine key policies that will govern financial decisions that ultimately impact our ratepayers. As such, I'm writing to formally request the following amendments to the LRFP and associated actions to be taken by SDCWA.

Incorporate Affordability in General Budgeting and Debt Policymaking

Southern California has some of the highest water rates in the country. What is outlined in the high/low projections show that by 2031, SDCWA rates could increase by up to 66%. Given the affordability challenges that exist throughout the County, the LRFP cannot be silent on its impact to individual ratepayers and SDCWA must provide a plan for reviewing its expenditures and resources with the goal of mitigating rate increases as much as possible. This will not only ensure the fiscal sustainability of SDCWA, it will also ensure affordable access to clean and safe drinking water for all San Diegans.

Maintain Existing Policies with Respect to its Debt Service Coverage Ratio ("DSCR")

In June 2021, SDCWA's Board approved a policy with a minimum DSCR of 1.2x and target level of 1.5x. However, the LRFP includes a proposal to treat the 1.5x target as the minimum target. The City recommends the LRFP remain consistent with the recently approved Statement of Debt Management and Disclosure Policy.

Increase Reporting to Determine Capital Funding Mix

The LRFP proposes an inversion of the debt/cash funding mix from the existing policy of 70% debt/ 30% cash to 35% debt/ 65% cash for the next ten years. The last LRFP update was in 2015 and staff stated that SDCWA has not maintained the funding mix targets set forth; rather SDCWA has been operating at a funding mix of approximately 20% debt/80% cash; vastly different than the plan identified in the 2015 LRFP.

Instead of setting a target mix for the next ten years through the LRFP, the City recommends that SDCWA prepare Five-Year Financial Projection Reports on a biannual basis that provide more frequent monitoring and opportunities for transparent adjustment to the projected debt/cash funding mix of the CIP program. Further supporting the need for increased monitoring of the debt/cash mix, is the planned issuance of \$170 million in new debt to fund CIP program expenditures in the coming months that will result in a much higher percentage of debt funding versus cash funding than the mix proposed in this LRFP; making the plan already out of date for the next two to three fiscal years as the new debt proceeds are spent down.

A clear and transparent understanding by the SDCWA Board on the funding mix is incredibly important as cash funding of the CIP program would likely require more immediate cash availability, posing concerns surrounding intergenerational equity, and could result in rate spikes for member agencies, which are ultimately passed on to San Diegans.

Additionally, the City recommends preparation of the recommended Five-Year Financial Projection Reports to be provided during the mid-term budget cycle to serve as the framework for the following year's budget development and rate setting processes. These new reports would serve as a planning tool in assisting budget decisions by assessing impacts to revenues and expenditures, and by exploring strategies to fund capital needs.

Third-Party Review and Timelines for Board Consideration

The City recommends that SDCWA retain as-needed, third-party consultant(s) to review cost of service studies, rate designs, and the CIP planning and prioritization. The results of this review will provide insight and additional information for the SDCWA Board of Directors, member agencies, and the public. Additionally, the City recommends extending the period of review for future financial planning documents, including the recommended Five-Year Financial Projection Reports, budgets, and cost of service studies to allow for meaningful engagement as was discussed during SDCWA's June Board meeting.

Explore Opportunities to Benefit from Take-or-Pay Contracts

Throughout the late 1990s and early 2000s, SDCWA was a pioneer in ensuring a reliable water supply portfolio was developed for the County. These investments have greatly benefited the region, but the future of our region's water demand looks very different today. Given that water sales and water supply contracts account for 60% of SDCWA expenditures, the City recommends SDCWA pursue opportunities to leverage the existing take-or-pay contracts. Identifying transfer opportunities for these contracted supplies could result in rate-relief for CWA member agencies, especially given the decline in both current and projected water sales compared to the anticipated future water sales at the time the contracts were executed decades ago.

Provide Comprehensive Options for Addressing Expenditures

As SDCWA continues in its transition from an organization focused on constructing new facilities to an organization focused on the operations and maintenance of existing facilities (as noted in the LRFPP) within an environment of declining sales, the City believes it is critical to monitor both revenues and expenditures (operating and capital). Effective scrutiny of both is a necessary exercise in ensuring the long-term financial sustainability of SDCWA, and in ensuring the organization is meeting the needs of the member agencies it serves. The overall intention of this recommendation to provide comprehensive options for addressing expenditures is to ensure that public resources are planned, managed, and used as effectively and efficiently as possible to preserve affordability for San Diegans.

Impacts of the LRFPP by Rate Category

In addition to the recommended amendments to the LRFPP outlined in this letter, the City recommends that SDCWA provide an excel version of the rate model spreadsheet used in the preparation of the LRFPP that includes the projected impact to each rate category to all member agencies and the Board of Directors.

Thank you for your time and attention to this important issue. Please reach out with any questions you may have.

Sincerely,



Jay Goldstone
Chief Operating Officer
City of San Diego

cc: Honorable Mayor Todd Gloria
San Diego County Water Authority Board of Directors & General Managers
Matthew Vespi, Chief Financial Officer
Alia Khouri, Deputy Chief Operating Officer
Lakshmi Kommi, Director, Debt Management Department
Shauna Lorange, Director, Public Utilities Department
Ally Berenter, Senior Manager, External Affairs & Water Policy