

MEMBER AGENCIES

Carlsbad  
Municipal Water District

City of Del Mar

City of Escondido

City of National City

City of Oceanside

City of Poway

City of San Diego

Fallbrook  
Public Utility District

Helix Water District

Lakeside Water District

Olivenhain  
Municipal Water District

Otay Water District

Padre Dam  
Municipal Water District

Camp Pendleton  
Marine Corps Base

Rainbow  
Municipal Water District

Ramona  
Municipal Water District

Rincon del Diablo  
Municipal Water District

San Dieguito Water District

Santa Fe Irrigation District

South Bay Irrigation District

Vallecitos Water District

Valley Center  
Municipal Water District

Vista Irrigation District

Yuima  
Municipal Water District

**OTHER  
REPRESENTATIVE**

County of San Diego

October 25, 2018

**VIA U.S. MAIL AND EMAIL**

**Board Members**  
Metropolitan Water District of Southern California  
P.O. Box 54153  
Los Angeles, CA 90054-0154

**RE: Potential Settlement of Litigation**

Dear Metropolitan Board Members:

As the Water Authority's new Chair of the Board, I write to you as a continuation of the effort and two-year commitment of our prior Chair, Mark Muir, to try to resolve the disputes between our agencies in a mutual dialogue with Metropolitan. While that process did not result in settlement, it has been the impetus for our Board leadership, staff and counsel to work on developing a settlement approach that we believe takes into account Metropolitan's stated needs, and that we are prepared to recommend to the Water Authority's Board of Directors. Separate and apart from litigation specifics and the myriad issues and details that must necessarily be addressed in formal settlement meetings that hopefully will be forthcoming, I want to share the broad outline of, and rationale for, our approach.

First, the Water Authority's approach is based on the premise that ***neither party should be expected to give up anything it has already won.*** As a result, Metropolitan's allocation of historic State Water Project costs is included in the proposed Exchange Agreement price discussed below, while the Water Stewardship Rate (WSR) is not. The Water Authority would also retain the benefit of court decisions in its favor on preferential rights, the ruling that Metropolitan's Rate Structure Integrity (RSI) clause is unenforceable and unconstitutional, and the damages and interest on unlawful Exchange Agreement WSR charges. A final judgment in the 2010-2012 cases would be entered accordingly.

Second, the Exchange Agreement price would be set as a ***price certain of \$369 per acre-foot***, starting January 1, 2019, for delivered water (including power), with annual adjustments every January 1 tied to the Gross Domestic Product-Implicit Price Deflator index. This price is derived from the 2003 Exchange Agreement price set by Metropolitan, less the WSR component ruled by the court to be invalid, escalated by 3 percent per year. In other words, ***this is the exact charge Metropolitan itself set, except for the portion found to be invalid.*** This price would govern the entire term of the Exchange Agreement through 2047 for the IID transfer water and for the remaining portion of the 110-year term of the canal lining water transfer.

Third, ***the Water Authority's approach would be to dismiss, without prejudice, all of its Water Stewardship Rate on supply claims in all pending litigation based on Metropolitan's agreement to fund the Water Authority's LRP applications, including the Carlsbad project and all pending LRP agreements with our member agencies,<sup>1</sup> and a negotiated amount of restitution for years in which Metropolitan barred the Water Authority and its member agencies from participating in its LRP and Conservation Credits Program.*** Metropolitan has already included the Water Authority's current member agency projects in its planned LRP funding, but has not yet included Carlsbad for funding, apparently on the basis it is already operational. However, the only reason the project became operational before LRP funding would have been considered and approved is because Metropolitan imposed the unlawful RSI clause and enforced it against the Water Authority and our member agencies.

Fourth, consistent with its 2007 Memorandum of Agreement with the Water Authority, Metropolitan would immediately implement a ***200,000 acre-foot Colorado River Intentionally Created Surplus (ICS) sub-account and delivery flexibility under the Exchange Agreement*** to allow for the maximum amount of storage of the Water Authority's ICS-qualified water in Lake Mead. This action would not only fulfill a longstanding promise by Metropolitan, but greatly benefit Metropolitan, its member agencies and Colorado River Basin States. Further, Metropolitan would support the Water Authority's efforts to secure its own ICS account. Under our approach, Metropolitan would also receive ICS credit for its proportionate share of costs paid toward Water Authority ICS-eligible projects via LRP subsidies, thus allowing Metropolitan to secure ICS water at a competitive, if not lower, cost than other alternatives, such as the Yuma Desalter. The sub-account would remain in place until the Water Authority obtains its own ICS account with the Secretary of the Interior.

Finally, this approach is designed to ***resolve all pending litigation between our agencies***, even though all of the issues presented in the litigation have not yet been addressed or finally resolved through the court process. Our approach is designed to "clear the deck" by ending all current litigation and allowing us to work together on the 2020 rate-setting process, based on Metropolitan's agreement that the Water Authority (and other member agencies as they wish) will as part of that process, be provided a fully functional rate model on reasonable, agreed-upon terms. The Water Authority would accept \$5 million in full and complete satisfaction of all attorneys' fees and costs, which represents a significant compromise from the \$8.9 million the trial court awarded to the Water Authority.

At a high level, we believe this approach provides substantial benefits to both of our agencies, including: a) Metropolitan may continue funding LRP projects through its WSR charge on supply, while the Water Authority is assured of receiving LRP benefits in a more reasonable ratio to the amount of WSR charges it has paid and will pay; b) the Water Authority's remedy for Metropolitan's imposition of the RSI clause is limited to an amount

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<sup>1</sup> City of San Diego Pure Water Project, Padre Dam-East County Advanced Water Purification Project; Fallbrook PUD GWRP, Vallecitos WD and Carlsbad MWD Carlsbad Desalination Project.

of agreed-upon restitution and reinstatement of the Carlsbad project, which is no more than any other Metropolitan member agency would have received, and merely puts the Water Authority in the position it would have been in had the unconstitutional RSI provision never been created and enforced; c) the Water Authority's member agency requests for LRP funding (e.g., Pure Water) are already being processed under current Metropolitan board policy applicable to all member agencies; d) creation of the ICS sub-account will not only fulfill a promise Metropolitan made to the Water Authority more than 10 years ago, but greatly benefit both agencies, as Lake Mead levels will be materially increased without Metropolitan having to borrow or buy additional water supplies in order to meet its Drought Contingency Plan commitment; e) all disputes over water rates and charges through the 2018 rate-setting process and for access to the rate models that established them are fully resolved; and f) establishing a fixed Exchange Agreement price will eliminate the need for extended continued litigation over the offsetting benefits of the Water Authority's QSA supplies, and will also avoid future litigation resulting from the price being tied to Metropolitan rates. Finally, and at the highest level, both agencies will benefit from avoiding the time, expense and controversy of continued litigation, based on a principled and reasoned approach to compromise.

Of course, each of these issues must be reviewed and considered in detail by our agencies, in order to conclude and document a settlement. No double recovery by the Water Authority is intended through any of these provisions. This approach assumes continuation of Metropolitan's current general rate structure, including its policy preference to recover its costs via volumetric rates. Our approach has not been to "start high" and bargain; instead, we have taken a practical approach that includes substantial concessions on the part of the Water Authority, not the least of which is the extent of the benefits the Water Authority's Colorado River water has provided, and will continue to provide to Metropolitan and its member agencies. We hope that you will agree that both the structure and terms of this settlement approach demonstrate an appreciation of Metropolitan's perspectives and our willingness to compromise.

I look forward to working closely with Metropolitan leadership over the next two years.

Sincerely,



Jim Madaffer  
Chair

Cc (via e-mail): Water Authority Board of Directors  
Maureen Stapleton  
Jeffrey Kightlinger  
Mark Hattam, Esq.  
Marcia Scully, Esq.