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TECHNICAL MEMORANDUM

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RICK ARAGON, COACHELLA VALLEY WATER DISTRICT

FROM: ALLAN HIGHSTREET, NBS, PRINCIPAL CONSULTANT

SUBJECT: SWP 2024 PROPERTY TAX JUSTIFICATION

DATE: JUNE 11, 2023

INTRODUCTION

CVWD annually prepares a justification for setting the State Water Project (SWP) Property Tax rate. The property tax is set to recover State Water Project related costs and is the primary revenue source of the SWP enterprise fund. This memorandum describes the justification for setting the property tax rate for fiscal year 2024. Also, the District asked NBS to evaluate the impact of recovering these charges through water rates versus property taxes, specifically the groundwater replenishment rates, to assist it in determining whether the tax is necessary.

BACKGROUND

In 1963, CVWD entered into a State Water Project (SWP) Water Supply Contract with the Department of Water Resources for additional imported water (23,100 acre-feet) to supplement its Colorado River supply for groundwater recharge. In subsequent years, CWD acquired an additional 115,250 acre-feet in transfers from other State Water Contractors, for a total maximum SWP supply of 138,350 acre-feet. The amount of water available each year depends on hydrologic conditions and reservoir storage levels.

Under the Burns-Porter Act, approved by voters in a statewide election in 1960, the State of California and thirty water agencies signed binding water delivery contracts. The state contracts were considered long term debts under Proposition 13, permitting the agencies to levy separate property taxes. Over time, the courts held that the indebtedness also included the cost of maintaining and operating the State Water Project. The Burns-Porter Act and water contracts under that act do contemplate that local taxes may be required to pay for obligations to the state and authorize such taxation when necessary. While exempt from Proposition 13's one-percent tax limit, local districts should explore making state water contract payments from water charges rather than taxes if possible.

Because CVWD does not have a physical connection to SWP facilities (which terminate at Lake Perris in Southern California), and MWD and CVWD have access to both SWP water and Colorado River water, an

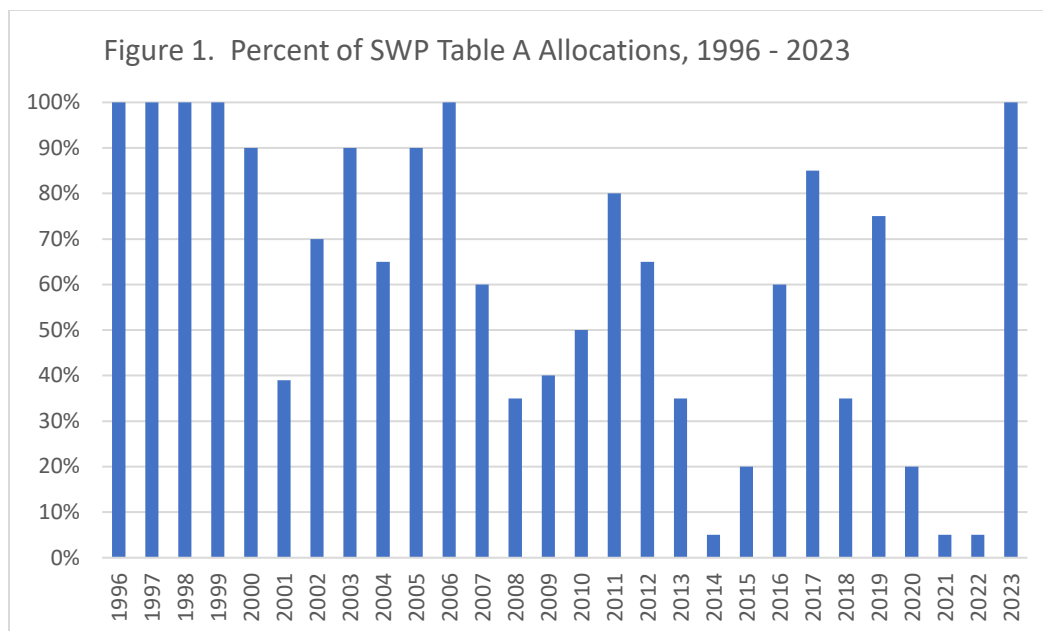
agreement was reached to allow CVWD to exchange with MWD its SWP water for an equivalent amount of Colorado River water. This exchange water is delivered to MWD's Colorado River Aqueduct to the turnout on Whitewater River. The exchange water is then delivered to both the Mission Creek Groundwater Replenishment Facility and the Whitewater Groundwater Replenishment Facility for direct groundwater recharge, helping eliminate groundwater overdraft in these areas of the Coachella Valley Groundwater Basin.

SWP FUND PLANNED EXPENDITURES

The District tracks revenues and expenditures related to the State Water Project in the State Water Project Enterprise Fund. In fiscal year 2014 this fund was combined with the Groundwater Replenishment Fund, but the State Water Project Enterprise Fund was reinstated in Fiscal Year 2020. The majority of these costs are paid directly to the California Department of Water Resources for the SWP Water Supply Contract Table A water and delivery, but also include payments to the Department of Water Resources for delivery of other water via the State Water Project system, payments to others to store the District's Table A water to ensure eventual delivery, for the cost of others' Table A water and related State Water Project delivery expenses, for supplemental Yuba water contracted and invoiced by the Department of Water Resources and delivered via the State Water Project system, and for costs necessary to administer the District SWP Water Supply Contract such as necessary staff time or membership dues to the State Water Contractor's Association, which plays a vital role in managing the DWR – State Contractor relationship.

The SWP Water Supply Contract has two main cost components, a Delta Charge which pays for costs for storage and conserving available supply, and a transportation charge that is based on transporting the available supply. The Delta Charge costs are allocated to contractors based on their Table A amounts (without respect to actual deliveries – i.e., this is a “take-or-pay” charge), while the transportation charges are based on the proportional use of facilities for deliveries in a given year. There are also additional charges for facilities constructed after 1987, which are negotiated separately (such as East Branch extension). Each of these charges includes capital, maintenance, operation, and replacement components.

Water purchases are highly variable based on weather conditions (which determine the amount of water available from the SWP as well as supplemental supplies when they are available). Figure 1 shows the State Water Project final percentage allocation of the Table A amounts for each year from 1996 to 2023.



Because of the uncertainty of the water deliveries and amounts ultimately invoiced by the Department of Water invoices as shown in Figure 1, the amount spent on water varies significantly from year to year. Because of this, the SWP Enterprise Fund has a significant reserve fund to smooth the cost to tax- and ratepayers of funding this supply and to ensure the District can purchase supplies when they are available. This reserve can only be used for financial obligations not anticipated during the normal budgeting process, such as if there were additional water available for purchase or if the Department of Water Resources invoiced for more expenses passed through to the District than forecasted, as sometimes occurs. The reserve fund was previously set at \$26.4 million based on hydrology patterns and expenses for the calendar years 2002 through 2007. The District reviewed actual expenses and SWP water allocations from 2007 to 2020 and reduced this reserve to \$20 million. Given the volatility of water purchases expenditures, the District is considering increasing the reserve target level to an amount closer to the annual water purchases when there are full deliveries. As the purpose of the reserve is to ensure the District can fund its whole allocation when it is available, this is a reasonable measure of the need for reserve funds.

Table 1 shows the District's SWP Fund Budget for FY 2022 (actual) through FY 2024 (estimated). The major cost of the fund is water purchases, approximately 98 percent of the costs in each year. This explains the variability of the Fund's cost, dependent on the SWP Table A allocations which, as noted above, vary with the weather. With a full allocation projected for FY 2024, the water purchases cost is projected to be significantly higher than typical. Given the increase in costs, the District anticipates having to draw down reserves to pay all these costs. Because the SWP Fund expects a reserve of close to \$50 million at the beginning of FY 24, the District will not make an adjustment to the SWP Property Tax rate for FY 24 to offset these increased costs. The District will wait until its Board establishes a new reserve fund target before taking steps to achieve it over a reasonable time.

Table 1. State Water Project Fund Budget, FY 2022 to FY 2024

Description	FY 2022	FY 2023	FY 2023	FY 2024
	Actual	Projected	Budget	Estimated Budget
Revenues				
Water Sales				
Drought Penalties				
Sanitation Service Fees				
Service Charges				
Availability Charges				
Replenish Charges				
Surcharges				
Property Tax-General				
Property Tax-SWP	\$ 79,688,626	\$ 86,063,716	\$ 82,079,284	\$ 90,254,230
Charges for Services				
Intergovernmental				
Investment Income	\$ 101,412	\$ 356,106	\$ 251,247	\$ 980,505
Other Revenue				
Total Revenues	\$ 79,790,038	\$ 86,419,822	\$ 82,330,531	\$ 91,234,735
Expenses				
Salaries and Benefits	\$ 281,087	\$ 306,555	\$ 306,555	\$ 615,525
<i>Capitalized Labor</i>				
Salaries and Benefits (Net of Capitalized Labor)	\$ 281,087	\$ 306,555	\$ 306,555	\$ 615,525
Supplies and Services	\$ 1,124,540	\$ 981,841	\$ 606,301	\$ 773,516
Utilities			\$ 75	\$ 50
Replenishment				
Water Purchases	\$ 60,131,882	\$ 72,245,957	\$ 72,245,957	\$ 92,623,919
QSA Mitigation Costs				
Pass-Through (Contra Expense)				
Capital Outlay			\$ 500	
Total Expenses	\$ 61,537,509	\$ 73,534,353	\$ 73,159,388	\$ 94,013,010
Operating Income (Loss)	\$ 18,252,529	\$ 12,885,469	\$ 9,171,143	\$ (2,778,275)
Nonoperating Revenues (Expenses)				
Interfund Transfers				
Interfund Revenues				
Debt Service - Interfund				
Sources				
Loan Proceeds				
Loan Forgiveness				
Interim Financing				
Capital Improvement Reimbursements				
Use of Restricted Funds				
Grant Revenue				
Uses				
Debt Service-External				
Capital Improvement Budget				
Contribution to Motorpool CIP				
Pending Litigation Accrual				
Other Revenue (Expenses)	\$ 209,023			
Total Nonoperating Revenue (Expenses)	\$ 209,023	\$ -	\$ -	\$ -
Total Expenses	\$ 61,746,532	\$ 73,534,353	\$ 73,159,388	\$ 94,013,010
Increase (Decrease) in Cash Flow	\$ 18,461,552	\$ 12,885,469	\$ 9,171,143	\$ (2,778,275)
Beginning Reserve	\$ 17,678,247	\$ 36,139,799	\$ 36,139,799	\$ 49,025,268
Ending Reserve	\$ 36,139,799	\$ 49,025,268	\$ 45,310,942	\$ 46,246,993
Assigned Reserve	\$ 20,000,000	\$ 20,000,000	\$ 20,000,000	\$ 20,000,000
Unassigned Reserve	\$ 16,139,799	\$ 29,025,268	\$ 25,310,942	\$ 26,246,993
Note: For FY 2022, the costs represent actual expenditures in FY 2022. For FY 2023, two figures are shown; the budget estimate for FY 2023 adopted at the start of the fiscal year and where the costs are expected to end up based on knowing the first 10 months of expenditures (projected). FY 2024 costs are the estimated budget.				
Source: FY24 SWP Fund Budget.xlsx from CVWD, May 25, 2023.				

GROUNDWATER PRODUCTION BY AREA OF BENEFIT

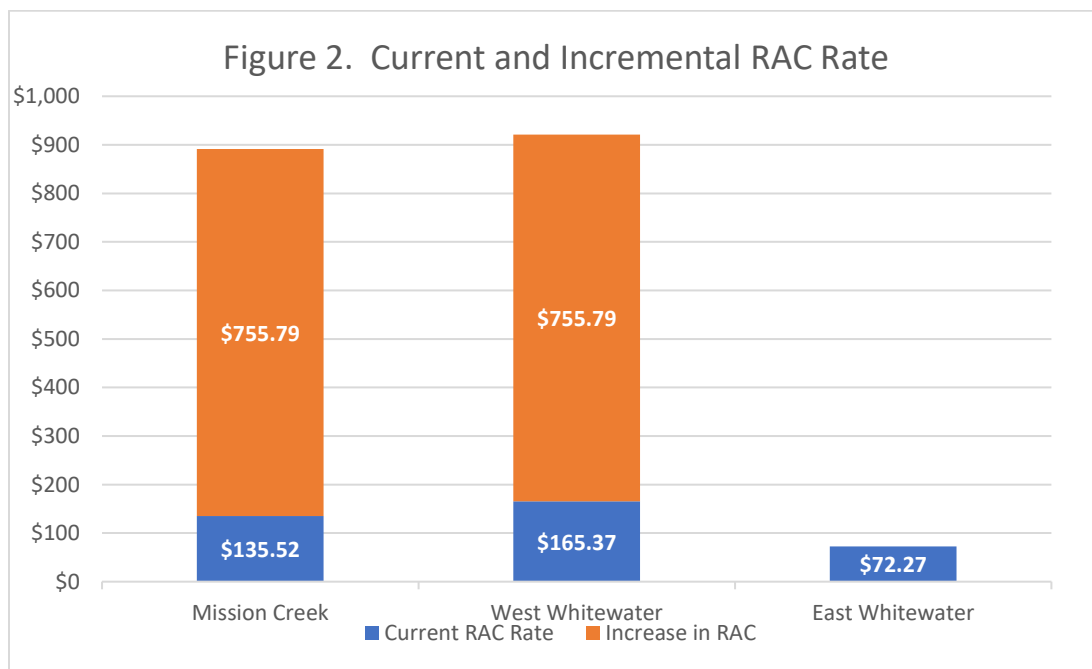
If property tax revenue was not used for SWP expenses, those charges would be allocated to the West Whitewater and Mission Creek groundwater replenishment areas of benefit, as SWP supplies are used to recharge those sub-basins. These costs would be allocated by groundwater production in each area. This production does not include production by minimal pumpers who extract 25-acre feet or less per year and others exempt from the RAC (Water Code section 31633.5 allows minimal pumpers to be excluded from the engineering survey and report of water production, and they are exempt from any replenishment assessments). Table 2 shows the groundwater production by area of benefit.

Table 2. Groundwater Production by Area of Benefit					
Area of Benefit	CY 2020 (a)	CY 2021 (a)	CY 2022 (a)	CY 2023 (b)	CY 2024 (b)
	Actual	Actual	Actual	Estimated	Estimated
Mission Creek	4,655	4,582	4,390	4,358	4,390
West Whitewater	117,770	122,413	122,060	122,123	120,000
East Whitewater	117,925	119,700	118,609	114,162	105,000
Total Production	240,350	246,695	245,059	240,643	229,390
Source: 2023-2024 Engineer's Report on Water Supply and Replenishment Assessment, Coachella Valley Water District, April 2023					
(a) From Tables 3-1, 4-1, and 5-1 from the Engineer's Report.					
(b) Calculated by dividing Replenishment Assessment Revenue by RAC rate, from Tables 3-3, 4-3, and 5-3 of the Engineer's Report.					

SWP 2024 EXPENSES ALLOCATED TO AREA OF BENEFIT

FY 2024 SWP Expenses from Table 1 were allocated to the West Whitewater and Mission Creek areas of benefit based on their proportional share of groundwater production (from Table 2). Table 3 shows the incremental RAC increase if SWP expenses were allocated to each area of benefit. Figure 2 also shows this graphically.

Table 3. SWP Expenses Allocated to Area of Benefit, Incremental RAC Increase					
Projected FY 2024 SWP Expenditures		\$94,013,010			
Area of Benefit	Current RAC Rate	Groundwater Production	Allocated SWP Cost	Increase in RAC	Total RAC
Mission Creek	\$135.52	4,390	\$3,317,928	\$755.79	\$891.31
West Whitewater	\$165.37	120,000	\$90,695,082	\$755.79	\$921.16
East Whitewater	\$72.27				\$72.27
		124,390	\$94,013,010		



KEY ASSUMPTIONS

1. This analysis focused on the SWP fund expenses. The analysis was based on the reserve fund already having been funded. If additional reserve funds were required, the incremental increase would be larger.
2. This analysis did not address the certainty of the revenue stream moving from property taxes, which are very stable, and the District has the power to collect, to a replenishment assessment charge, where collections would be more problematic.
3. These proposed charges are, in our professional opinion, impractical as they would incur rate shock and would lead water users to seek alternatives to groundwater. We leave the economic consequences of such a dramatic increase in replenishment charges to the District's economic advisors.