August 26, 2005
Meeting Summary of the
Financial Affairs Committee

Participants

Larry Bauman – Bureau of Reclamation
Kristy Dickhaut – Westlands Water District
Lee Emrick, Colusa County Water District
Anthea Hansen – Del Puerto Water District
Mike Hagman – Friant Water Authority
Russ Harrington – CVP Water Association
Lynn Hurley – Santa Clara Valley Water District
Kathy Kitchell – City of Roseville
Eric Limas, Lower Tule River Irrigation District (by telephone)
John Pelley – Bureau of Reclamation
Donna Tegelman – Bureau of Reclamation
Jesus Reynoso – Bureau of Reclamation
Ed Roman -- SMUD
Les Ross – Bureau of Reclamation
Alan Thompson – East Bay MUD
Kathryn Thompson – Bureau of Reclamation
Jerry Toenyes – Northern California Power Agency

1. Opening Business

This August 26th meeting was held at Mid-Pacific Regional Office of the Bureau of Reclamation in Sacramento. The meeting notes from the July 29 FAC meeting were approved without change. Item 3 on the Agenda – Review of PUE Issues with Bureau of Reclamation staff – was postponed until the September FAC meeting because Barry Mortimeyer was unable to attend this August meeting. There were no additions to the Agenda. The next FAC meeting is scheduled to begin at 9:30 on September 23 at the Mid-Pacific Regional Office, 2800 Cottage Way, Sacramento. Note that the September meeting will be in the main building, and not in one of the Cafeteria Conference Rooms.

2. 2005 FAC Issues Matrix

A. **Budget Workshops – Refining Customer Participation**. Russ spoke to Craig Muehlberg, who said that the following dates have been finalized for the annual activity plan reviews:

Mid-Pacific Regional Office	October 5th
Folsom Area Office	October 6th
Shasta Area Office	October 12th
Fresno Area Office	October 19th

Regarding the request for the ability to review the upcoming year's budget plans, Russ has been advised that the CVPWA should send Reclamation a letter to the MP Region Office (with copies to the Area Offices and Donna Tegelman, because she is in charge of miscellaneous items and RAX) requesting this 2006 budget review at the respective October meetings.

Regarding the pre-year budget reviews that Russ has been pursuing, Craig said that the President's Budget emerges from Embargo each year on the first Tuesday in February. This gives a time frame from the emergence of the President's budget until the start of the fiscal year in October to conduct a review of the upcoming year's budget. Craig said that there was the possibility that Congress may adjust the President's Budget, but that this is typically only a couple of dozen items; this is a relatively small amount, given the size of the Mid-Pacific Regional budget. For the upcoming year, most of the Congressional adjustments pertained to CalFed.

Action Items – Russ to co-ordinate letter to appropriate Reclamation staff regarding the implementation of a current year (FY 06) budget review to be held on the same day of the reviews for the FY 09 activity plans that are already scheduled. Russ to also follow-up with Craig Muehlberg regarding the ability to hold one or more "Pre-Year" meetings for FY 07, which may be held subsequent to the release of the President's Budget next February.

B. **BOR-WORKS Water Accounting Program Development**. Larry stated that the one-year contracts for the two independent Oracle contractors that Reclamation had hired had expired in July. He said that the Contractors had made satisfactory performance on these contracts, but that there was still additional work for them to do. As a result, one of the independent Oracle contractors is currently working on an interim contract from August through October. The other Oracle contractor is currently on emergency (family) leave out of the country, but will be back and working by the end of September. Larry said that they had obtained a temporary fill-in for the Oracle contractor who was on leave, but they didn't like the quality of work from this contractor, who was discharged. The two original Oracle contractors will be offered another long-term contract with multiple extensions for continued work as needed. Performance for these two contractors has been satisfactory, and Reclamation staff stated that it is difficult to find competent Oracle contractors. Reclamation staff also noted that they have two in-house Oracle programmers in addition to the two consultants. Contractors requested a workshop to get training on the new system. The response from Reclamation staff was that they still aren't ready to provide system access to the outside world.

In the annual CFO Audit (contracted to KPMG, which is a private accounting firm), the auditors had findings relative to the system controls of BOR-WORKS. One finding dealt with the testing of new releases. Mid-Pacific Region staff is modifying its change management process to address this issue, which relates to "non-destructive program changes.

Regarding the entry of transfer rates into the BOR-WORKS system, the system needs to have prior entries for each transfer before any adjustments can be made. Part of the problem with transfer rate entries is that the Area Offices are responsible for entering adjustments into the WORKS system, and in a number of cases the Area Offices are not doing this. Regarding the incorrect assessments of Tiered Pricing to water deliveries of several contractors, this problem is being addressed, but it is still occurring. Only a few Contractors have been subject to tiered-pricing provisions, in part because Contractors are only subject to these provisions after they have renewed their Contracts.

Regarding Monthly Water Statements and Water User Reports, some Contractors are receiving monthly data from the WORKS system and some are not. This data should be available going back to October 2004 for Contractors who request this information (as a few Contractors have already done). Reclamation staff members were asked to provide output to Contractors through the WORKS system that is in the same format as the prior reports that they received under the old system. They responded that this isn't possible at the current time because they need to get the data integrity issues resolved before looking at output formats. They also said that they have prohibited Area Offices from providing this information to Contractors, because the information that the Area Offices have been providing to Contractors outside the WORKS system don't contain the same data as the WORKS system, which represents the official data record. Contractors were informed that they may need to keep internal records to replace data which was formerly sent to them by Area Office staff from a data source outside the WORKS system. Reclamation staff members were asked to develop a procedure through which the MP Region would have a monthly or even weekly recurring meeting to make sure that data is properly entered into the WORKS system. In addition, Reclamation staff members were asked to provide reports to Contractors in a shorter timeframe; one estimate was that Contractors don't receive water delivery and payment data regarding a given month for four months.

Action Items – Russ to follow-up on possibility of developing a weekly conference call between MP Region staff and Area Office to ensure that accurate data is input into the WORKS system, and that all necessary data is entered. Each Contractor representative should request monthly water statements from the BOR-WORKS system dating back to October 2004, and should verify the accuracy of this data. Russ to follow-up on the possibility of a Contractor WORKS workshop at some point in the future.

C. **Water Transfer Rate Policy Development**. Larry referenced a conference call with several FAC members (Russ, Ara, Anthea, Charlotte Dahl) regarding outstanding transfer rate issues, including a revenue crediting methodology and the need to complete a procedures manual for calculating transfer rates. Subsequently, Ara started a first draft of this procedures manual, which has been distributed to Reclamation staff members and the FAC members for review and comment.

The problem with incorrect and inconsistent interpretations of the transfer rate policy by Area Office staff was raised again. Larry reiterated his position that once Reclamation signs a transfer agreement, the transfer rate embedded in that agreement is final, and specifically not subject to change to correct an inappropriately-applied transfer rate. However, Reclamation staff are still working through this issue internally.

Regarding revenue crediting, Donna Tegelman stated that she still believes that a notification letter to Contractors is necessary, and she has received support of this position from MP Region management. However, she has also stated that the tasking of preparing this letter was assigned to Larry, and that Larry has been working predominantly on the capital ratesetting revisions and power issues. Russ volunteered to draft the revenue crediting letter, which Larry said would be acceptable.

Action Items – Interested Contractor and Reclamation representatives are to provide comments on the Procedures Manual for transfer rates which was drafted by Ara. Russ will draft the revenue crediting notification letter on behalf of Reclamation staff.

D. **Historical Advance Payment Reconciliations**. Larry said that the independent Contractor who had been working on this project has been diverted to another activity. This individual won't be returning to work on the Historical Advance Payment Reconciliations until October at the earliest. Although approximately 2/3 of the total water service contracts are completed, some of the largest contracts have yet to be started. The Friant Contractors may be reconciled next.

E. **Security Cost Reimbursability**. Larry stated that the cost split between Water and Power in the May 1st report was only an example, and was not intended to be the final cost distribution recommendation. In this report, the cost allocation was divided 50% to Power and 50% to Water. While the water cost allocation was subdivided among the project purposes, the power cost allocation was allocated 100% directly to Power Contractors. This has prompted a number of complaints from Power Contractors, and as a result Reclamation has been holding internal discussions on an appropriate allocation methodology for these costs.

Reclamation staff were asked why it was appropriate for Water and Power contractors to pay to protect part of the national infrastructure. The comment was made that the purpose of a terrorist attack would be to inflict casualties, not to disrupt water and power. The comment was made that of the Shasta security costs, 20% was allocated to Keswick; Jerry Toenyes asked whether this was an excessive allocation.

Larry said that his most recent instructions are that the 2005 Security costs are completely non-reimbursable. He also added that the non-reimbursability provision by the Senate, which is in effect at least until another report is completed in 2007, is still in effect to the best of his knowledge. However, he added that if he is so instructed, a reimbursability adjustment could be made such that the costs are never included in the rates, but are simply dropped into the final accountings for cost recovery. Larry said that he would keep Russ informed regarding any

developments pertaining to Security Cost reimbursability. Larry said that Reclamation staff has some idea of how these costs might be allocated, but that no final determination has been made.

Action Item – Larry to inform Russ of any potential or impending changes in reimbursability status.

3. Review of PUE Issues. Discussion of this agenda item was postponed until the September FAC meeting, when Barry Mortimeyer from the Reclamation Operations office would be available to provide more information.

4. CVPIA / AFRP Status Update.

Contractors asked about the annual year-over-year increase in the inflation rate by 3.9%, when prevailing CPI data sources indicated that inflation for the current year was between 2.5% and 3.0%. Reclamation staff asked FAC representatives to provide the sources of their CPI data, which the respective Contractors agreed to do. Reclamation staff stated that their CPI data was obtained from the Office of Management and Budget (OMB) CPI calculations. Les Ross said that the inflation rate includes actual data through 2005, but also includes a guesstimate for 2006 data. The reason that this guesstimate is necessary is that Restoration Fund budget data must be derived from the Restoration Fund rate, which is in turn derived from this CPI forecast. Part of the reason that the increase is 3.9% this year is that the guesstimate for last year was too low, and part of this year's increase is intended to recover the deficiency in last year's estimate. FAC members also noted that CVPIA does not specify a specific inflation index, and the question was raised of the accuracy of the OMB data which Reclamation has been using since CVPIA inception. Less Ross noted that the annual Restoration Fund inflation rate is based on an October-to-October point estimate, and is reported to Congress each year. He added that a mid-year adjustment is not feasible due to the impacts that the rate change would have on the budgeting processes. Katherine Thompson asked whether the OMB directs the use of the CPI-Urban for determining the annual Restoration Fund increase.

Action Items – Russ to provide Katherine Thompson with the CPI data sources which have been referenced by FAC members in their comparisons to the inflation rate of the Restoration Fund. Reclamation staff to determine whether the Restoration Fund inflation rate must be based on the CPI-Urban data provided by the OMB

Regarding Restoration Fund payment crediting data, Les Ross made the comment that he only sends Restoration Fund payment crediting data for individual Contractors to those Contractors who specifically request this data. The only Contractor representative who has actively requested this data in the past is Anthea, who said that she has found some discrepancies in the past. One mistake that she has found is that some Restoration Fund payments have been mis-applied against another Contractor payment obligation. The comment was made that at least some of the data discrepancies in the Historical Advance Payment Reconciliations may be due to these mis-allocations of Restoration Fund payments. The comment was made that any mis-applied Restoration Fund payments would impact the Restoration Fund rate calculation for both Water and Power Contractors.

Action Items – Les Ross to provide Mike Hagman with the Friant Restoration Fund payment data from 2003 forward. Interested Contractors should request Restoration Fund crediting data from Les Ross to reconcile against their internal records.

Reclamation staff was also asked whether the CVPIA expenditures for 2004 were now available. Each year, Reclamation staff prepares an offsets report, which lists CVPIA expenditures by activity. This report also segregates the funding sources for these expenditures among the Restoration Fund, Federal Energy and Water Appropriations, and State of California funding sources. Katherine Thompson said that this document was still under internal review, but that it should be available for distribution soon.

5. Technical Service Center Costs. Mike Hagman reported that this report has been submitted, and that there have been no new developments since the last FAC meeting.

6. Folsom Dam Costs. This topic has been the subject of extensive discussion over the last few weeks. At the Congressional level, Congressman Doolittle has presented language to a House Conference Committee that may mandate a 52% allocation to Flood Control and a 48% allocation to Safety of Dams all Folsom Dam Modifications listed in a 2002 report cited by the legislation. Russ has been in contact with the Corps of Engineers (Corps) and the Sacramento Area Flood Control Agency (SAFCA) regarding this project and the reimbursability issue, as well as with Reclamation staff at the Folsom Area Office. Note that Reclamation staff members have taken the position that none of the Folsom Dam Modifications costs should be reimbursable to Contractors, and have provided supporting information to Contractors to justify non-reimbursability. Reclamation staff members have indicated that they support non-reimbursability for these projects from the Commissioner's level down.

At this time, most of the Folsom Dam Modifications projects are on hold because bids from private Contractors to complete the work have been significantly higher than the Corps authorized budgets. As a result, the Corps has gone back to the drawing board for most projects, which will require as long as 18 months to review. The one Folsom Dam Modifications project that is proceeding on the fast track is the Folsom Bridge. Russ expects continue to engage extensively on this issue as new developments occur.

Action Items – Russ to prepare a letter to the Corps of Engineers regarding Folsom Dam Modifications and involvement of CVP Contractors in decision-making process. Russ also to prepare White Paper to brief Contractor representatives on current status of Folsom Dam Modifications. Russ to meet with Deputy Folsom Area Office Manager Rick Johnson to obtain briefing on 2002 report that is referenced in Congressman Doolittle's proposed legislative language.

7. Klamath Water Purchase – Funding Sources & Reimbursability. Per a request from the last FAC meeting, Jesus provided the cost code for the Klamath Water Purchase, which is 0416-6000. Note that this a Trinity cost code number. Jesus said that it was linked to a non-reimbursable cost center, which is based on non-reimbursable Trinity Fish and Wildlife legislation.

Power Contractors stated that the lost power impact was $1.4 million, and asked that Water Users discourage Reclamation from making these purchases in the future. Power Contractors also asked whether they should be made whole from their increased cost due to this foregone power. Water Contractors responded that this was mandated by Reclamation as opposed to Contractors, and that Water Contractors were given very little notice that this would occur. Jerry Toenyes made the statement that although this water has already been purchased, it still hasn't been released.

Donna Tegelman suggested that both Water and Power Contractors should meet with Kirk Rodgers and front office staff in an effort to resolve this issue.

8. Capital / Deficit Rate Development. Larry announced that a meeting with the MP Region front office has occurred, and a decision has been made regarding a new methodology. The results of this meeting will be provided at the end of September. Larry said that a notification letter regarding the change will be sent to Contractors, and that Contractors will be allowed an opportunity to provide comments. This notification letter will be sent prior to the completion of the 2006 draft water rates, and will include Reclamation's rationale for implementing the change. These draft water rates, which will be published by no later than September 30th, will include capital rates that are calculated using the new methodology. Larry stated that Contractors will have the opportunity to comment on the new capital rates as part of the annual comment period on draft water rates, because this will allow Contractors to comment after they've seen the effects of the new methodology.

Action Item – Reclamation staff to provide Contractors with notification letter regarding change in capital rate methodology during the month of September.

The mechanism for adjusting the capital rates will be an adjustment to the delivery projections through 2030, which are utilized in deriving each Contractor's capital rate. The new methodology for prorating capital among Contractors will be based on delivery projections per Reclamation's Operations and Criteria Plan (OCAP), which provides average water delivery projections for each region. Larry added that the OCAP may be replaced in the future with a new hydrology study if that study provides updated information. Larry confirmed that the denominator of the capital rate equation will be based on the Cumulative average from 1994 through the current year for which data is available, to reflect water delivery projections in the post-CVPIA operating environment. One thing that Larry did note is that Reclamation will be making unspecified adjustments to the OCAP data; Russ asked Larry to provide specific details regarding these adjustments as well as the pre-adjustment and post-adjustment OCAP data.

Action Item – Larry to provide Russ with detailed list of all deviations from OCAP data that are proposed for incorporation into the capital rate methodology.

Regarding outstanding M&I deficits remaining after the negotiated M&I Settlement, Reclamation staff noted that Contractors have a one-time opportunity to repay their outstanding M&I O&M Deficit balances. The deadline for this repayment, per notification letter that has alredy been sent by Reclamation, is September 15th. After this time, the Capital Interest Deficit and O&M Deficits for all M&I Contractors will be melded into a single rate, and it will be

impossible to segregate a higher-interest portion of the deficit against which to apply deficit payments. This blending of the capital and O&M M&I deficit balances and interest rates is a provision of the M&I settlement.

Action Item – Contractors who want to retire their higher-rate O&M deficit balances need to have payment received by Reclamation by Thursday, September 15th.