



*November 18, 2005
Meeting Summary of the
Financial Affairs Committee*

Participants

Larry Bauman – Bureau of Reclamation
David Bird – Tehama Colusa Canal Authority (by telephone)
Brice Bledsoe – Contra Costa WD (by telephone)
Kristy Dickhaut – Westlands Water District
Lee Emrick – Colusa County WD
Anthea Hansen – Del Puerto Water District
Mike Hagman – Friant Water Authority
Russ Harrington – CVP Water Association
Henry McLaughlin – City of Fresno (by telephone)
Kay Moore – Bureau of Reclamation
Erma Leal – Bureau of Reclamation, Fresno Area Office (by telephone)
Paul Olmstead – SMUD
John Pelley – Bureau of Reclamation
Jesus Reynoso – Bureau of Reclamation
Ed Roman – SMUD
Dick Stevenson – Bureau of Reclamation
Craig Stroh – Bureau of Reclamation
Judy Tapia – Bureau of Reclamation (by telephone)
Alan Thompson – East Bay MUD

1. Opening Business

The November 18th FAC meeting was held at Mid-Pacific Regional Office of the Bureau of Reclamation in Sacramento. Larry Bauman mentioned that some of the changes that he'd requested were not included in the final version of the October FAC meeting notes. Russ Harrington responded that any of Larry's requested changes that he didn't include in the original October FAC meeting notes would be listed in the November FAC meeting notes. Kristy Dickhaut requested that the agenda be adjusted to include an item for Monthly Water Statements, and Larry Bauman requested that an agenda item be added for Trinity PUD. Both of these items were added to the agenda. The FAC was asked whether they would be interested in having a December FAC meeting on December 16th. It was decided to schedule this meeting to provide the FAC with an opportunity to begin discussion regarding the 2006 Issues Matrix. The

December 16th FAC meeting will be held at the same time and location as the November FAC meeting. Reclamation staff indicated that their participation in this meeting may be relatively low due to the proximity to Christmas and the end of the year. The date and location of the January 2006 FAC meeting was also discussed. The proposed meeting date for the January FAC meeting is at the Water Users Conference in Reno on Tuesday, January 17th (the day before the Water Users Conference formally begins). Reclamation staff requested that due to an impending project deadline, that the FAC meeting (or at least the portion that requires Reclamation's participation) be concluded as soon as possible.

2. 2005 FAC Issues Matrix

A. Budget Workshops – Refining Customer Participation. Due to a scheduling conflict with another meeting, Regional Budget Officer Craig Muehlberg was unable to attend the FAC meeting. At this time, the Area Office Managers have been asked to provide their input regarding the customer budget summary by December 16th. These comments are now in the Embargo period, but will be made available on Reclamation's website when the budget is released from Embargo during February 2007.

B. BOR-WORKS Water Accounting Program Development. Larry Bauman reported that the annual audit by KPMG has led to a requirement that Water Contractors' payments must now be segregated into water payments and power (PUE) payments. Larry said that facilitating this new requirement will require substantial modifications to the WORKS system. At this time, Reclamation is looking at several alternative remedies for this problem. One of the potential solutions under consideration is to direct bill PUE expenses. Larry also noted that both capital and O&M expenses are included in the KPMG requirement. He added that he doesn't want to have to re-open the ratesetting policy to resolve the issue of splitting water user payments between PUE payments and water cost payments. This KPMG finding is the result of an audit of the WAPA financial statements. Larry stated that the payment application priority will not change; payments will be allocated to O&M expenses first, then Deficits, and then Capital. However, Larry said that this would not be the case if Reclamation was forced to Direct Bill PUE expenses. Larry emphasized that Reclamation would prefer to leave the ratesetting policy alone and address this issue solely within the Financial Statements. As a side note, Ed Roman asked how the \$345 thousand payment by Water Users for Power Purchases through the Power O&M Cost Allocation agreement was being included in the rates, and Jesus Reynoso replied that this is probably handled ahead of time. Returning to the primary topic, Larry said that if the Direct Pumping rate component were to be Direct Billed, then this component may be removed from the water rates. Larry reiterated that the core problem as stated by the KPMG auditors is that the PUE component of water payments are being treated as water revenue, but according to the auditors these components of the payment should be treated as Power Revenue. Larry was requested to provide more information regarding this issue. Larry said that if this issue is resolved, then Larry will discuss the solution that was selected.

C. Water Transfer Rate Policy Development. Russ Harrington stated that the Contractors' draft of the Transfer Rate Procedures Implementation Guide has been submitted by the CVPWA to Reclamation staff on November 1st. Russ added that after Reclamation has had a chance to review this document and develop some edits to this document, Contractors would like

to have a meeting with Reclamation staff to discuss these edits. Larry Bauman responded that Reclamation staff hasn't had time to address this Implementation Guide. Larry added that this is an important issue to Reclamation and that they want to resolve this before the beginning of the 2006 water year. Regarding the Revenue Crediting Notification letter that CVPWA staff drafted and submitted to Reclamation, Larry said that he forwarded this draft to Donna, but hasn't heard anything since then regarding the status of this letter. It was tentatively proposed that the policy guide be reviewed at the Water Users Conference in Reno.

D. Historical Advance Payment Reconciliations. Larry Bauman announced that the Fiscal Year 2006 budget has provided for two additional independent contractors to be hired to work on the Historical Advance Payment Reconciliations. Larry said that one of these two additions is already working, and that final applicants will be reviewed in the near future to choose the second independent contractor. Larry confirmed that these two new hires are in addition to the independent contractor and Reclamation staffmembers who are already working on this project. He said that these new contractors will both be familiar with the Reclamation accountings, and will be able to "hit the ground running". Larry said that Reclamation's goal is to finish these Reconciliations by the end of this Fiscal Year, but that he thought that this timeline may be a little optimistic. He reiterated that Contractors are always given 30 days to respond to Reclamation after they send a given Contractors' its completed reconciliation for verification against the Contractor's internal records. He said that in each case, the Contractor has asked for and received an extension of this 30 day time limit. Part of the problem is that it takes Contractors time to dig the historical payment records from the 1980s and 1990s from their storage facilities. Larry added that if any Contractor fails to respond, then Reclamation will treat the Reclamation Reconciliation as final; however, all Contractors that Reclamation has contacted this far have responded with a request for the time extension.

E. Security Cost Reimbursability. Larry Bauman stated that the Continuing Resolution under which operations are being extended includes an Energy and Water Appropriations bill that contains language pertaining to Security costs. This language instructs Reclamation to provide a report within 60 days regarding how the Security costs would be recovered by Reclamation. In response to this language, Reclamation is now developing alternative recovery mechanisms for internal review. Reclamation staff wants to be ready in the event that these costs are declared reimbursable. These alternatives will specifically address Security costs at both Folsom and Shasta. Larry acknowledged that the language doesn't explicitly declare these costs reimbursable, but asks how these costs would be recovered if determined to be reimbursable. Craig Stroh mentioned that in one section of this Energy and Appropriations bill, the reimbursable cost base (Reclamation-wide) was projected to be \$10 million, and in another place this bill mentions reimbursement to additional beneficiaries, which may be interpreted to include non-reimbursable project purposes. Larry said that a Reclamation report is being prepared that will be completed through the Denver Office by a workgroup that is run by Kathy Norris.

F. Draft 2006 Water Rates. Larry Bauman stated that he hasn't yet received Contractor comments on the draft 2006 water rates. Russ Harrington responded that he has responses prepared, but he gave Contractors until after this FAC meeting to provide internal comments regarding his responses. Russ told Larry that he would be sending the comments immediately after this FAC meeting (which Russ has now done). Jesus Reynoso stated that there would be

two changes to the 2006 water rates based on the comments that have been received regarding the capital rate methodology change. The first is that the pro-ration of capital to the Cross Valley Canal (CVC) Contractors would be adjusted to reflect the State-side capacity limitations, and the second is that the denominator in the capital rate calculation for Settlement Contractors will be adjusted to reflect the 75% minimum (to be consistent with the 75% of entitlement minimum used in pro-rating capital to Settlement Contractors). Jesus said that ratesetting staff is still determining the final percentage that will be used in the CVC capital pro-ration. Kristy Dickhaut asked that Contractors be notified of any adjustments to the draft 2006 rates before these adjustments are finalized.

Larry said that some non-CVP Contractors wanted to be given the opportunity to participate in certain meetings held between the FAC and Reclamation. Alan Thompson stated that the FAC tries to speak for everyone's interests, but that the FAC doesn't include representation from all Contractors. Russ said that he and Bob Stackhouse have discussed this issue, and Russ will need to consult with Bob and the CVPWA board regarding this matter. Larry and Jesus asked whether it would be acceptable to the FAC for Reclamation to issue a single response to the 2006 draft rate comments, which would give all Contractors who provided comments the answers to the questions from all Contractors who submitted comments. Russ said that this would actually be preferred by the FAC.

G. CVP Safety of Dams Contractor Notification and Repayment Issues. Kay Moore reiterated her position that the ratesetting policy may not be in compliance with the Safety of Dams repayment requirements based on the application of revenues. However, she added that it is not necessary that payment begin immediately upon completion of the Safety of Dams project even though repayment must be completed within 50 years of the original finish date for the project. The response to Kay's comment began with the statement that the CVP is unique, and that most of the other Reclamation projects are based on repayment contracts with only a few Contractors. Brice Bledsoe asked whether a separate provision can be established to provide for Safety of Dams repayment within the framework of the ratesetting policy. He mentioned that Contra Costa WD water payments have included a \$2.00 per AF administrative payment, and that Reclamation has taken an incremental \$2.50 per AF from Contra Costa's annual water payments and applied this portion of the payment toward Contra Costa's capital obligation. Brice added that Reclamation could also bill a Safety of Dams component through the water rates if necessary. Brice concluded that Contractors need to go into discovery mode regarding this issue, and that Contractors haven't found any legislation that requires a fixed annual Safety of Dams repayment requirement. Brice asked Reclamation to provide the FAC with the legislative language that requires fixed annual repayments for Safety of Dams costs. Contractors also expressed concern over the repayment period itself. The ratesetting policy provides that significant new additions to the project could have a repayment period extended beyond the 2030 deadline for pre-existing capital facilities. The Safety of Dams legislation providing for a repayment period of up to 50 years is not sufficiently specific, and Contractors would like more information from Reclamation regarding the repayment period for these CVP Safety of Dams projects. The FAC indicated that Contractors would prefer not to have separate repayment contracts for the Safety of Dams project costs. The FAC also indicated that they would like to maintain repayment flexibility and asked Reclamation to identify the Safety of Dams repayment costs. Attached are the current Safety of Dams costs, which are currently included in the capital

rate/repayment base. Reclamation stated that these current totals may increase substantially due to potential Safety of Dams projects at Folsom by both Reclamation and the Corps of Engineers.

Dick Stevenson stated that it was the Solicitor's Office in Washington, DC that determined the separate repayment requirement for Safety of Dams projects. He said that Reclamation is now composing a White Paper for submission to the DC Office, and that Reclamation needs approval from DC to include the Safety of Dams repayment in the ratesetting structure instead of creating separate repayment contracts. He said that at this time, the DC Office is leaning towards allowing the Safety of Dams repayment to be conducted within the ratesetting policy. Reclamation is currently having internal meetings to resolve this issue, and Dick noted that he will be meeting after this FAC meeting with Accounting Services Manager Laura Close to discuss this issue. The costs from the pre-existing Safety of Dams work at Mormon Island (conducted through the early 1990s) are now being declared "substantially complete" so that Reclamation can include these costs in the Safety of Dams cost base. Dick stated that Reclamation was originally required to have a repayment contract in place for any Safety of Dams work prior to completion. However, there were times when Reclamation was unable to implement this requirement. As a result, the new policy is that the repayment contract must be in place prior to "substantial completion" of the Safety of Dams project being declared; however, the Secretary is authorized to extend the due date for the repayment contract if it is apparent that the repayment contract will not be completed within 30 days of substantial completion of the project. However, this new policy hasn't yet been signed by the Commissioner of Reclamation. Although the pre-existing work at Mormon Island has been declared complete, Reclamation is now preparing for a new phase of Safety of Dams work. Reclamation staff asked Contractors for enough time to allow for completion of the White Paper, and will keep us posted on progress. In response to Contractors' questions, Dick noted that the Safety of Dams repayment requirement is not related to capital repayment as provided in article 9D. Regarding the project repayment period for each Safety of Dams project, Larry Bauman stated that the repayment period is decided on a case-by-case basis. The latest Safety of Dams legislation, which was enacted during December 2004, included a provision that beneficiaries must be included in Safety of Dams projects from the planning stage through completion. The repayment period will be discussed during this planning phase. Reclamation staff also noted that all Safety of Dams projects must go to the Secretary for approval before the fix is completed. As a closing note, Reclamation confirmed that at Folsom Dam, Reclamation may be looking at some of the Dikes to the north of the Folsom Dam as well as the Mormon Island facility.

H. Monthly Water Statements. Kristi Dickhaut told Larry Bauman that Westlands Water District had been getting water statements each month through the summer, but that Westlands has not received a statement since August. Kristi said this has caused problems at Westlands because Westlands accounting staff has nothing from Reclamation against which to reconcile their internal records. Judi Tapia said that the Fresno Area Office made an internal decision not to send these statements because the September Water Statements contained year-end estimates instead of actual delivery data. The Fresno Area Office didn't want to create confusion with these statements. Judi indicated that they have the actual data for September, October, and November now, and that as soon as the WORKS system is available they will send the water statements for all three months to Contractors. Judi indicated that the Fresno Area Office may also wait to release the September and October monthly water statements next year.

Contractors indicated that they would prefer to have the September and October monthly water statements on a more timely basis, even if the data was based on estimated as opposed to actual water deliveries.

I. Trinity PUD. Larry Bauman stated that in each year prior to 2005 the annual assessment for Trinity PUD was included in the Water Marketing rate. Larry said that this cost was removed from the 2005 rate to be separately billed, but that this billing hasn't yet been sent. Larry said that in 2006 these costs will be billed by the Mid-Pacific Accounting Services group. Larry said that the Foreward to the ratebooks will include the statement that these costs will be removed from the rates and billed separately. Larry said that Laura Close (Accounting Services Manager) informed him that any bill for less than \$50 will not be billed, but will be added into the Contractor's annual accountings as a PUE assessment. For 2005, these costs will not be billed. Instead, these costs will be included in the final accountings, which may include this cost as a separate line-item. The reason that these costs are being removed from the Water Marketing cost base is that the Business Resources Manager and the Accounting Services group are concerned that legislation may require that these payments must be made specifically. The total annual assessment is approximately \$180 thousand per year. Contractors were concerned that these billings might not go to the appropriate personnel within their department, and asked to notify Laura Close regarding the appropriate destination for these bills. Larry indicated that the allocation of these costs may change from prior years, and that his staff is still working on this. As a side note, it was mentioned that the original destination of the diverted Trinity River water was intended to be the West Sacramento Valley.

3. Review of PUE Issues. There was nothing substantially new to report. Per Reclamation's time constraints, this item was tabled until the next meeting.

4. CVPIA / AFRP Status Update. There was nothing substantially new to report. Per Reclamation's time constraints, this item was tabled until the next meeting.

5. Folsom Safety of Dams Costs. Reclamation staff reported that they didn't have any new information regarding the reimbursability language that Congressman Doolittle inserted into the 2005 WRDA bill. Contractors didn't have any definitive information to provide during this meeting. Shortly after the FAC meeting, Ed Roman sent Russ Harrington an e-mail indicating that Jason Larrabee (Congressman Doolittle's staffer) told SMUD representatives that the language pertaining to the 51.1% / 48.9% cost split did not survive.

Regarding the Reclamation Safety of Dams work that will commence on the Mormon Island levee (and possibly other levees as well), during the October FAC meeting Reclamation staff had requested that the FAC identify 3 representatives to represent the CVP on the financial issues for this project and 3 representatives to represent the CVP on the engineering/technical issues. On the financial side, Russ Harrington, Mike Hagman, and Kristy Dickhaut volunteered. On the technical side, Ed Roman and Bob Martin (with the San Luis Delta Mendota Water Authority) volunteered. There is one remaining position available for an engineering/operations representative.

6. Capital Ratesetting. Reclamation was asked to confirm that the denominator in the capital ratesetting equation would be based on cumulative average deliveries as opposed to a 10-year rolling average. Reclamation staff confirmed that this is definitely the case, and that this will be stated in the Forward to the ratebooks. Contractors said that they didn't object to using 1995 as the starting point, so long as the cumulative average is employed from 1995 forward.

Contractors also noted that the A-13 schedules for Irrigation and M&I that are used to determine the denominator in the capital ratesetting formula did not accurately reflect the average historical delivery base from 1995 through 2004 in the A-14 schedule. Reclamation staff had indicated that the discrepancy was because unused water was removed from the delivery base to determine the A-13 amounts. Contractors asked whether the unused water would be added during the following year if this unused water was rescheduled, and Reclamation staff confirmed that this would be the case. Rescheduled water would be included in the year when this water was delivered. Reclamation staff indicated that the only adjustment to the historical A-14 data before calculation for the A-13 annual delivery base was that unused water was removed, and that no other adjustments have been made. Contractors have been asked to check their water delivery records for the 1995 through 2004 time period regarding the unused and rescheduled water adjustments.

7. FAC Chair and Vice Chair positions. The two-year terms of the current FAC chair and vice chair positions end at the conclusion of calendar 2005. Nominations and a vote were held for the next two-year term. The unanimous vote was that Brice Bledsoe would remain the Chairman and that the Vice Chair positions would be Mike Hagman for Irrigation, Lynn Hurley for M&I, and Ed Roman for Power.

Requested Amendments to Notes from October 2005 FAC Meeting

Larry Bauman's amendments to the October 2005 FAC Meeting Notes are as follows:

B. BOR-WORKS Water Accounting Program Development. Larry Bauman stated that program development was continuing. The tiered pricing, current and prior year adjustments, and transfer issues continue to be the main focus and are all on track to be resolved. These features are currently in system test, and are expected to go to user test (Reclamation staff) at the end of October.

C. Water Transfer Rate Policy Development. Larry Bauman stated that he and Jesus Reynoso had met with Donna Tegelman a few days before the FAC meeting to discuss the Transfer Rate Policy and any issues that may still be unclear. Larry said that they had the mutual understanding that the policy is a living document, and can be adjusted if there are some items that are still unclear. Responses were also provided to four questions that Russ had sent to Larry earlier in the week:

1. The full cost incremental rate component would normally be the difference between the transferee's full cost rate and the sum of the transferor's COS and any incremental rate components. However, interest issues involving transfer with the Exchange Contractors remains unresolved at this time.

2. The “COS plus incremental facilities/services” policy only applies to transfers where the transferor has renewed its contract.
3. The pricing of transfers that involves Ability to Pay Contractors still needs to be clarified by Reclamation staff.
4. The notification letter for the revenue crediting methodology is expected to be sent to all CVP Contractors during mid-November.

E. Security Cost Reimbursability. Although this item isn’t currently as active as some of the other FAC agenda items, it was determined that Security Costs should remain on the Agenda at least as a tracking item. Larry Bauman announced that Reclamation has been working on a revision to the May 1st hypothetical cost split of Security Costs between Water and Power Contractors. This revision will be shared with the Contractors upon completion and approval by Reclamation management.

F. Draft 2006 Water Rates. Larry Bauman announced that the 2006 draft water rates were posted on September 30th. After the FAC meeting, Larry confirmed that the comment period for the 2006 draft rates is 60 days after the date of the letter (September 30, 2005). He asked that comments on the 2006 draft rates not include comments pertaining to the capital and deficit rate methodology change. He added that there is a separate forum specifically for the comments on the capital ratesetting methodology and that these comments are due to Reclamation by November 4, 2005.

Questions were raised regarding the Folsom South Canal costs, and the impact that these costs would have on O&M rates. Larry was asked whether he could extend the repayment period for the Folsom South Canal costs, which have more than doubled in 2006 due to a \$640 thousand cost projection to perform access road maintenance sealing work. The answer was that in accordance with current Reclamation policy, these costs become due and payable in the year in which they are incurred. He distinguished these Folsom South Canal costs from the CFO Audit costs (with the five year repayment option) by stating that the Contractors never had the option to pay the CFO Audit costs when they were originally incurred because they were incorrectly classified as capital costs. These types of extraordinary maintenance with their high costs and immediate repayment period are becoming a Reclamation-wide problem and concern. At one point in time, Reclamation had a program (Rehabilitation and Betterment) for extraordinary maintenance which provided for a longer repayment period, but that program has been discontinued. Discussions have taken place at the Reclamation Denver Office to consider having this program (note that you have “problem”; should be “program”) reinstated or an alternative considered.

A. Providing Comments in Response to Notification Letter. Larry Bauman stated that he hasn’t received many responses yet to the notification letter. He reminded the FAC that the comment deadline is November 4th. Reclamation staff was asked about the delivery projections for the Cross Valley Canal Contractors. Mike Hagman stated that the delivery projections for the Cross Valley Canal Contractors are too high, because these Contractors have additional capacity restrictions in addition to the hydrology constraints faced by the other CVP South of Delta Contractors. (Note for Russ: can we put this in the notes when this discussion occurred after the meeting?)

Action Item – For any consolidated comments on the 2006 capital and deficit rates that Contractors would like to submit through the CVPWA, please send these comments to Russ by no later than October 28th.