

POTENTIAL MESSAGING REGARDING THE OVERDRAFT
FROM THE PERSPECTIVE OF DISTRICT RATEPAYERS

- [Slide 1] The answer to: “Will rates increase for FY 2014?” is “Yes, unfortunately.” How much will they increase? The Board does not yet know, as the FY 2014 budget is still being worked on. A 20% increase is the maximum they can be raised under the District’s authority to raise rates from the June 2011 Proposition 218 process. The Board should know by May. But, here’s why they will probably rise for FY 2014 beginning in the August billing (the District’s new FY begins on each July 1st):
- [Slide 2] Majority of the cash outflow during FY 2009 - 2011, before the present Board took over, was to “do something about the overdraft.”
- Since 1982 when the USGS produced definitive evidence that the Borrego Valley Groundwater Basin was being overdrafted to the extent that serious economic, social, and environmental harms were likely to occur, the District, assisted with grants from federal, state, and local agencies has spent approximately \$5 million (on a Present Value [PV] basis) primarily to study the physical parameters of the overdraft, to fallow a few hundred acres of farmland, to identify potential alternative sources of supply, and the costs to build a pipeline to the Valley.
- Yet, according to a USGS preliminary report due out in final form this year, the net result has been that the overdraft has more than doubled since 1982; rising from about 6,000 AFY to about 15,000 AFY.
- One of the reasons that the District has been able to limit potential revenue increases to no more than 80% through FY 2016 from rates in effect in FY 2011 was to stop spending more money to “do something about the overdraft.”
- In both FY 2011 & FY 2012, all available cash flow has gone to keep up with current period operating and maintenance (O&M) costs for providing reliable potable water service, replacing aging infrastructure (the District operates infrastructure with a replacement cost of around \$62.5 million) and building reserves necessary to regain the District’s credit rating it lost in December 2010. This Board’s desire is to establish sufficient cash flow so that the District is able to borrow from the bond markets again by FY 2016/FY2017.
- The water business is extremely capital intensive. Attempting to fund Repair and Replacement (R&R) of aging infrastructure out of current revenues is not feasible. This would require periodic multimillion dollar assessments for the 2,000+ customers of the District. Something no ratepayer could afford to pay. Thus, the need to long-term financing to spread out the payments for R&R.

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- It is important for the District to keep its physical infrastructure in good shape. Deferring maintenance and repairs and replacement too long, thinking one is saving money, costs more. An analogy is avoiding oil changes on your car, thinking you are saving money. Neglecting regular oil changes is expensive and so is deferring maintenance and repairs and replacement of aging infrastructure too long.
- But presently, the big ticket cost-driver for District customers and all pumpers in the Valley is the overdraft.
- Last year, the District hoped that DWR would award funding through its Integrated Regional Water Management (IRWM) grant program to help establish the economic cost to all parties in the Valley for not resolving the overdraft in a timely fashion. Unfortunately, DWR denied this planning grant request.
- [Slide 3] One reason for little action in the past for not resolving the overdraft has been the question of urgency; “why should we invest funds to resolve the overdraft today rather than tomorrow?” The question still remains: “where are we on the cost curve of Option A - an unmanaged basin?” and “How can we drop to the Option B cost curve in an economically timely fashion?”
- Overdrafting a basin is expensive:
 - As water levels decline, more electricity is required to pump this water to the surface. Water is heavy and pumping it from 8 feet in the past rather than about 400-feet or more today costs more.
 - As water levels decline, existing wells fail and no longer can pump adequate water to the surface. Wells need to be drilled deeper or relocated, which requires the construction of new distribution lines. These improvements will increase delivered water costs.
 - As water levels decline, water quality often decreases. To make this deeper water potable may require much more expensive treatment. This increases water costs.
 - Gradual compaction of the aquifer and subsidence can occur over time. Compaction of the aquifer is the loss of space where groundwater can reside. Subsidence is a sinking or downward settling of the earth's surface due to the excessive withdrawals of groundwater. Both compaction and subsidence is human-caused and is typically irreversible if and when it occurs.

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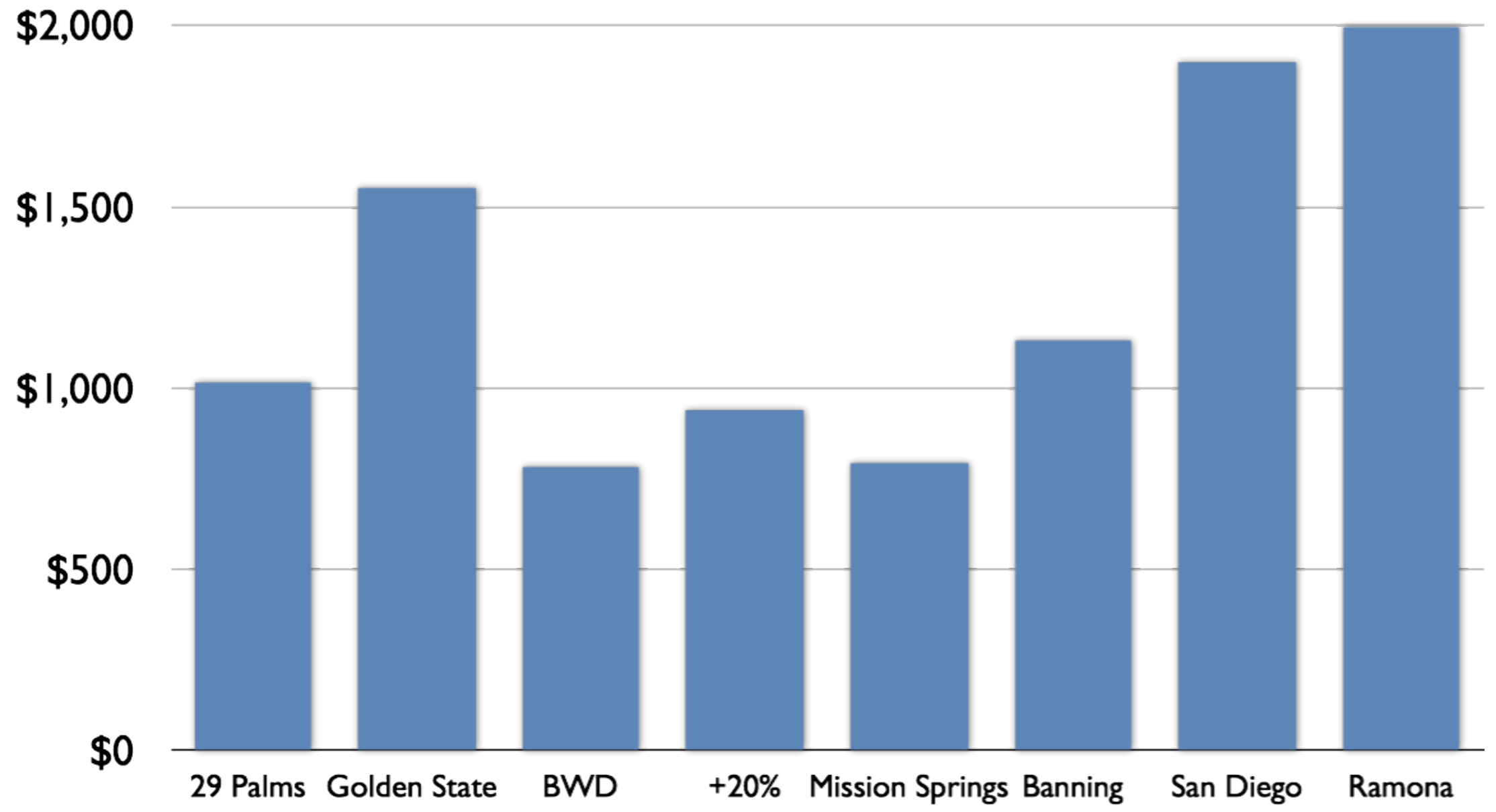
- If the overdraft continues at its present rate, it is certain that some or all of these increases in water costs will occur.
- Today's nominal cost of delivered groundwater (not the *economic* cost) from the basin is about \$200/AF for irrigation-quality water (water one does not want to drink) and about \$760/AF for potable water.
- Some have promoted the use of imported water to address the overdraft. Reclamation presented some of the difficulties and uncertainties regarding this option. There is no free lunch. No one will provide free water to the Valley and pay all the costs to construct a pipeline to transport this water to the Valley anytime soon. That is a pipe dream.
- Some have suggested tapping the Clark Dry Lake aquifer as a source. However, Clark Lake aquifer is useful only if a sustainable source of water exists there sufficient to pay for a pipeline and treatment plant. That is, withdrawals that do not exceed the safe yield on a continuing basis. To do the necessary studies could potentially cost around \$1 million. And, **IF** a sustainable supply was determined, it appears that the cost of this water to District's customer's could be about \$1,400/AF. This cost is almost twice the present cost of water from the BVGB.
- Some have recommended adjudicating the basin as a solution. Twenty-two basins in southern California have chosen this option to resolve their communities' overdraft situation.
- Some have even suggested to do nothing about the overdraft; just let free market forces work. This was what was proposed back in 1982. This option did not work between 1982 and today. It is unlikely to work going forward from today. There is no evidence that overdrafts have been able to be resolved in an economically timely fashion using market forces alone.
- A basin planning authority, in combination with market forces, is typically required to resolve an overdraft in an economically timely fashion. In California, a basin planning authority can be established through negotiated plan agreed to by pumpers that are then stipulated by the courts or legislatively enacted. If negotiations stall or fail entirely, then an adjudication may be the only means to resolve the overdraft.
- The District's Board believes that bringing an over-drafted groundwater basin back into balance is a difficult task and is optimally done by cooperation among all affected parties. The District believes that the best solutions rely on a combination of market forces, legal

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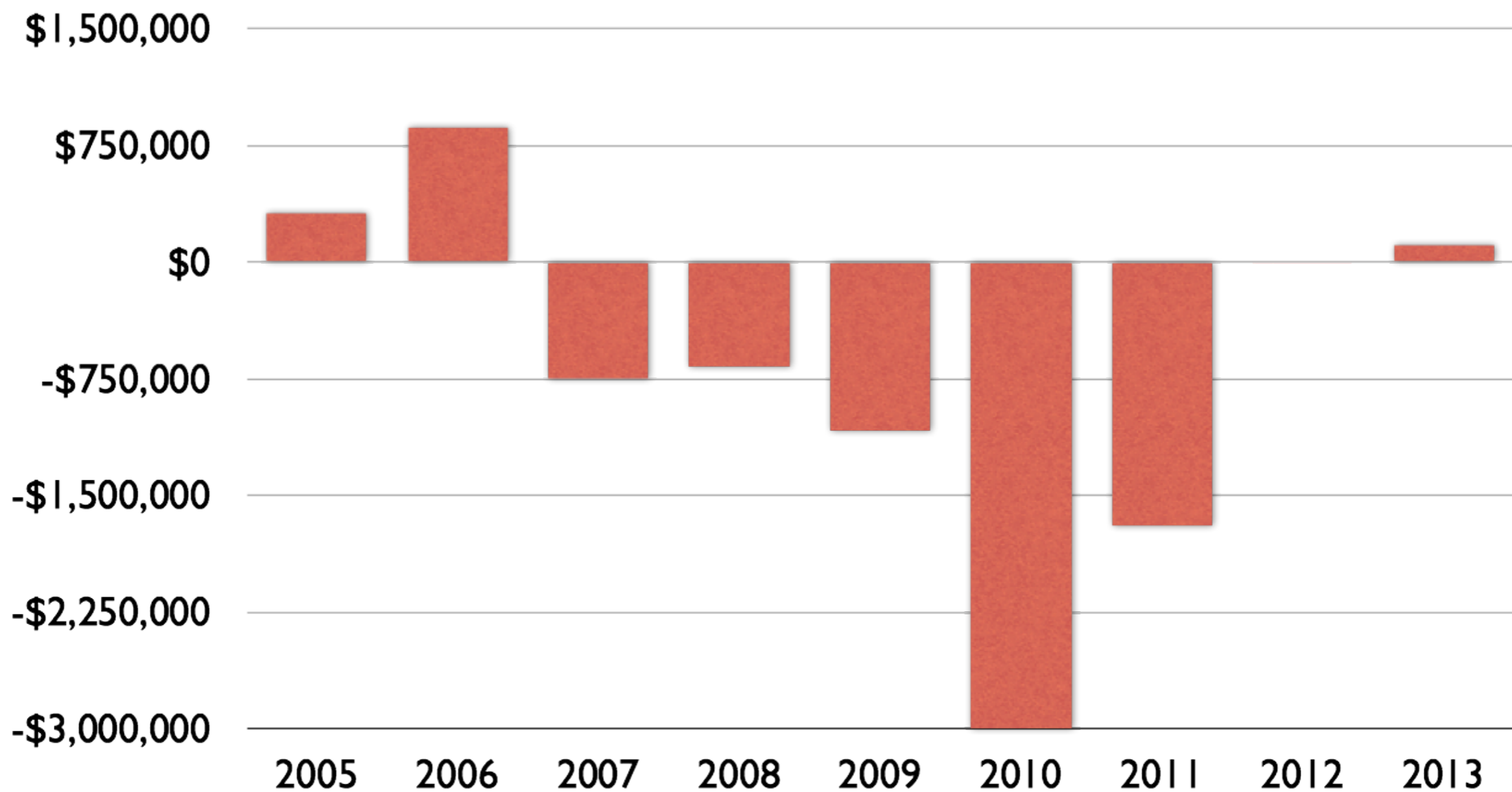
requirements and good old-fashioned cooperation. The District is looking for that type of solution to solve our common problem.

- Last fall, staff from the Department of Water Resources (DWR) met with a number of significant water users in Borrego Valley and encouraged the groups to meet to determine whether a coalition could be formed to find common ground to address the overdraft. The message from DWR was clear - in order to maintain local control of the basin, all major stakeholder groups must participate in a collaborative process or there would be little hope for federal, state, or local assistance to reverse the declining trend of the groundwater basin.
- Local leaders from the Chamber of Commerce, agriculture, Borrego Water District, education, golf, lodging, State Park, and recreation agreed to participate in an open and nonjudgmental dialog with the goal of finding common ground toward sustaining the valley's water supply.
- The newly named Borrego Water Coalition (BWC) is motivated by an agreement that an overdraft exists. The goal of the group is to work together to manage the basin to resolve the overdraft and provide water for the future. Their findings and recommendations will be provided to other potential stakeholders and interested parties in the near future.

■ Dollars per acre-foot (326,000 gallons) of water purchased



■ Net Increase (Decrease) In Cash & Cash Equivalents



Option A - Unmanaged Option B - Managed
Economics of Unmanaged vs Managed Basin

