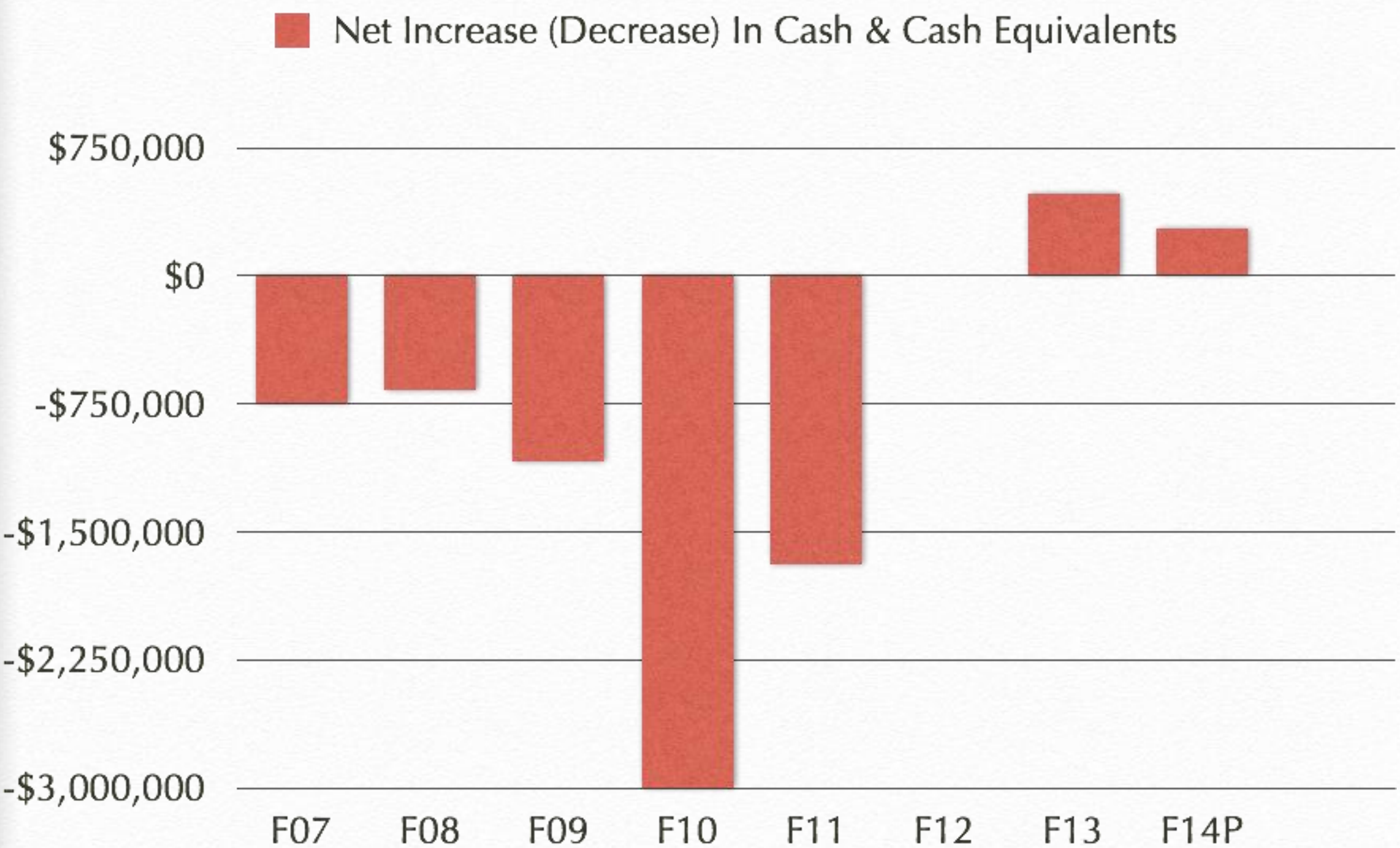
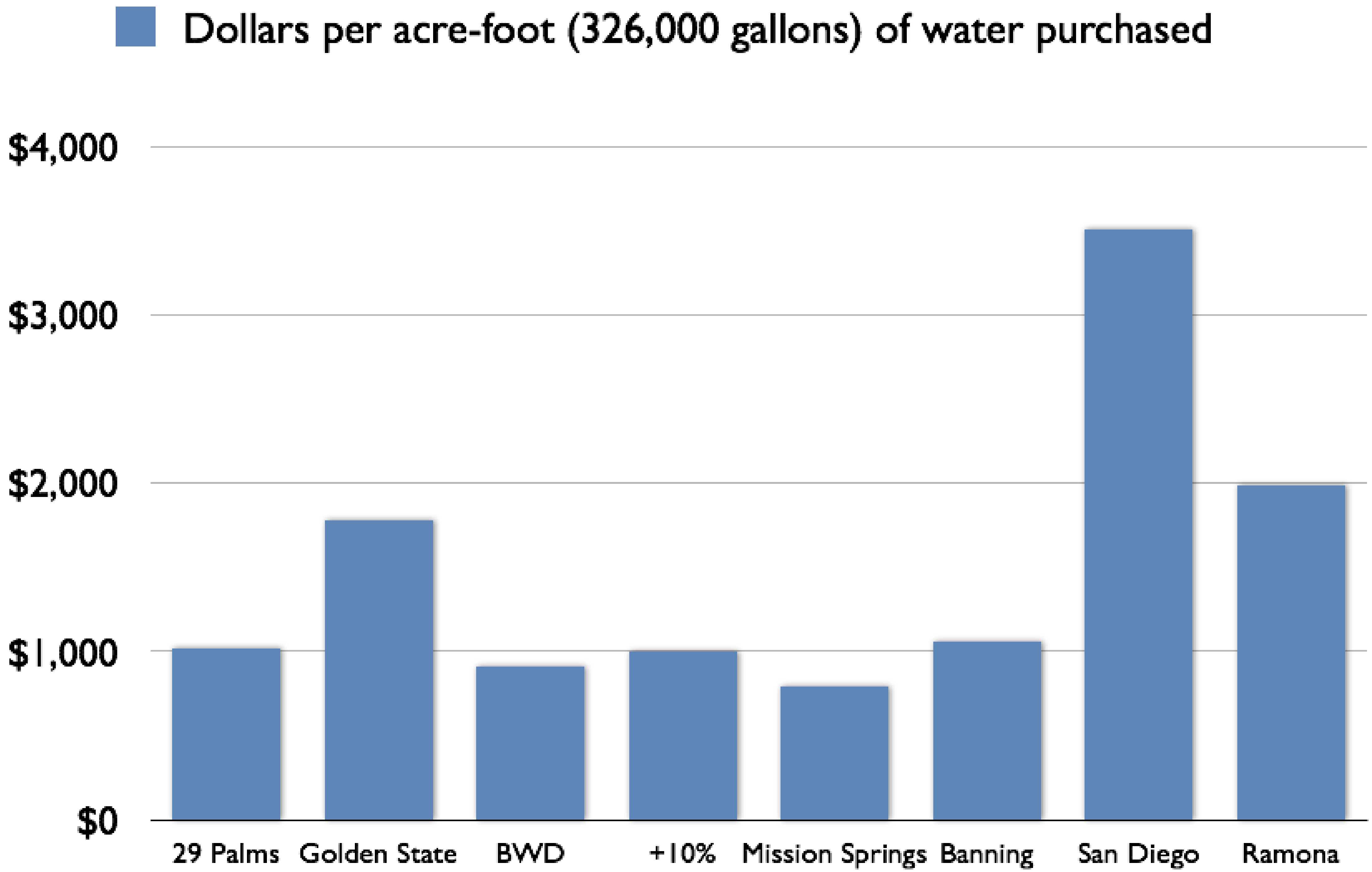

Net Increase (Decrease) In Cash & Cash Equivalents
$750,000
$0
-$750,000
-$1,500,000
-$2,250,000
-$3,000,000
F07
F08
F09
F10
F11
F12
F13
F14P


Dollars per acre-foot (326,000 gallons) of water purchased
$4,000
$3,000
$2,000
$1,000
$0
29 Palms
Golden State
BWD
+10%
Mission Springs
Banning
San Diego
Ramona

- [Slide 1] describes where the Board believes the District ended up in terms of cash-on-hand at the end of FY 2013 (June 30, 2013) and where we are projected to be at the end of FY 2014 (June 30, 2014).
- [Slide 2] describes how the District's current rates compare with other nearby water districts and how the District's rates will compare if the Board raises rates 10% for FY 2015.
- This is my 4th and final presentation about District finances during my term in office that ends in December. In my first year in office, I had the distinctly unpleasant task of explaining the dire state of the District's finances inherited from the prior board - as the previous board and its general manager had:
  - spent $5.7M of the $6.5M in cash reserves the District had accumulated over the past 20 years; obligated the District to pay $660,000 more by June 30, 2011 of that year; and promised to spend an additional $7.5M in District revenues over the next 30-years.
- The end result of this profligate spending and overdraft policy that assumed that “everything could stay the same”; that there would be no real cost to resolving the overdraft situation was that:
  - the District lost its credit worthiness. A disaster for a capital intensive business like a water district. And, to keep potable water delivery to your homes and businesses; the District was forced to raise rates as much as 100% (compounded) over FY 2011 levels through FY 2016 just to keep the lights on and the water flowing, assuming that:
    - the $1.1M this Board took out of annual operating and maintenance (O&M) expenses from FY 2011 levels;
    - the reduction of employees from 17 in FY 2011 to today's level of 10-employees;
    - eliminating all non-O&M expenses related to the overdraft (now zero dollars), and:

        - deferring about $400,000 each year of repair and replacement (R&R) of infrastructure costs until the District could assume new debt when it was creditworthy again;

    - was enough to generate free cash flow and accumulate cash reserves fast enough to return the District to creditworthiness sufficient to approach the bond markets again for reasonably-priced debt by FY 2016 or FY 2017.

    - Otherwise, the District would continue in a downward spiral where deferred R&R would eat up any cost savings and we would be in a race to raise rates fast enough to pay for deferred R&R costs out of operations cash flow.

    - This is a race that few water utilities can ever win. The current replacement cost of the District's infrastructure is approximately $62.5M. An appropriate amount of R&R dollars must be spent each year to keep the District on a lowest-operating cost basis. R&R can be deferred for only so long before the deferral becomes dis-economic (wealth-destroying).

- Maybe the hardest decision this Board has had to make during the past 4-years was to curtail any spending towards "fixing" the overdraft.

    - The overdraft today is more than twice the amount of the overdraft in 1982. This is the case even as the District and its ratepayers, along with help from some federal and state agencies spent more than $5.645M on understanding and "fixing" the overdraft since 1982. Clearly, spending more money on more of the same activities did not appeal to this Board.

    - But, the overdraft itself, if not resolved, will continue to drive rates higher - potentially much higher - as withdrawals may require additional advanced treatment to render this water from deeper levels in the Basin potable or even useful for irrigation purposes.

- The consequential risks of dewatering of the basin's upper aquifer may include:

- additional deleterious impacts to the Anza-Borrego State Park's ("the Park") desert ecosystem;
- loss of commercial development and economic growth opportunities in the Valley;
- reduction of recreational alternatives;
- rising water-related costs that hurt the poor and force some on fixed incomes to leave the Valley;
- collapse of real estate values (the County estimates the value of property in the Valley at ~$300M today); and
- loss of agricultural productivity in the Valley.

- Without substantive and timely mitigation steps to resolve the overdraft of the Basin's groundwater supply, the estimated economic cost to the Valley may be many millions of dollars in:
  - lost economic value of investments in property,
  - increased pumping costs as the water table falls,
  - land subsidence that destroys physical public infrastructure, and
  - other unwanted and costly changes to life in Borrego.
- Remember the saying: "Make lemonade out of lemons." That is what this Board has attempted to do related to the overdraft:
  - Without the finances, the District's ratepayers could no longer be on the hook to cover all the costs of "fixing" the overdraft as before;
  - Potential sources of public financing to address the overdraft declined to help until the major water pumpers and users in the Valley were willing to work together;

- Potential sources of private financing said the same thing - organize the pumpers and users in the Valley to see if everyone can get on the same page;
- this Board also consulted some of the top water law attorney's in the state who said the same thing: get the major water pumpers and users together and see if you can work out a plan to bring the Basin into balance.
- [To be perfectly clear, none of the expert advice we received advocated that the District embark on an adversarial adjudication. They indicated that this may be warranted IF the parties could not agree on a plan, but to presume that a plan would not and could not be negotiated was the height of irresponsibility and willful negligence.]

- Thus, in December 2012, the District supported DWR's efforts to establish a forum where all the major pumpers and water users in the Valley could meet and talk frankly with one another. This group is what has become the Borrego Water Coalition whose mission is to develop a plan to manage the Borrego Valley Basin. Such a plan includes:
  - Goal 1: To develop recommendations for managing the Borrego Valley Groundwater Basin including: what needs to be done, by when, by who, for what cost and what benefits, under what authority, how will results be measured, and what will be the consequences for not achieving these results.
  - Goal 2: To make certain the analytical basis for choosing basin management strategies to achieve basin management objectives meet the reasonable business person test. (That is, do we understand in sufficient detail the economic costs and benefits of a particular strategy and are these strategies prioritized as to expected costs and benefits?.)
  - Goal 3: To recommend the means for paying for the implementation of the managed basin plan.
  - Goal 4: To recommend the best authority to enforce the basin management plan.

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

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In June 2011, as a result of the 218 process, revenue increases were approved for FY 2012-2016 of 30%, 30%, 10%, 10%, 5% for each of these fiscal years. These revenue increases were analytically determined to provide the cash flow and reserves (savings) necessary to return the District to creditworthiness, defined as the ability to borrow approximately $6-$7M for repair and replacement of infrastructure, by FY 2016/2017:

- less than 8 cents of each dollar of revenue increase through FY 2016 will go to pay increases in O&M expenses (mostly electricity costs, but also about $300,000 in expected pension increase costs that the District is legally obligated to pay as a result of decisions made by the prior Board in 2010);
- about 24 cents will go for capital improvements and groundwater management. The pay-as-you go repair and replacement of infrastructure from the current year's revenues as neither cash savings nor new public debt is available to fund these costs as in the past;
- the remaining 68 cents will go to replenish savings (cash reserves). This is a requirement that the public bond market credit rating agencies have for reestablishing credit and the ability to borrow by FY 2016/2017.

Some of you have been critical of this Board for raising rates. Here are some facts concerning our decisions. Much more is available on the District's web site under "Rate Increase."

We are told that Operations & Maintenance (O&M) expenses are too high.

> The District has made significant cuts to the FY 2011 O&M budget.

The District really doesn't need reserves.

> Reserves are our savings accounts. Without them, we would have no viable method to ensure continuous water service during emergencies. Cash reserves are required for

the District to return to fiscal stability, to borrow money for capital improvements; and to enable the District to operate in an efficient manner. It is irresponsible to risk the economic well-being of this community by failing to fully fund reserves.

If the District would just eliminate all the studies, it would not need a rate increase.

I hope that the presentations today will obliterate this myth. If this community wants to resolve the overdraft, not only is the work discussed today necessary, it must be done right and in a timely fashion.

Rates are too high.

Yes and no. Yes they are higher than in the past, but as compared to other Districts, even if revenue requirements increase through FY 2016 as presently forecast, the District's rates will still be near the median for groundwater dependent water districts located in Southern California's desert communities. Currently, we are among the least expensive for water rates in San Diego County.

To put this in perspective, by FY 2016, if all the proposed revenue increase goes into effect, it will cost about the same amount for 250 gallons of water from the District as it costs today for 1 gallon of bottled water purchased from Costco. But, the water from the District is regulated and regularly tested, unlike the bottled water. Water from the District is also likely to be as good or better quality than the bottled water you can buy. That is, even at its potentially most expensive, potable water from the District is about 250 times less expensive on a fully costed basis than the best alternative - without the added cost of recycling the plastic bottle.

All of this is to say that, regrettably, the Board sees no other responsible option but to raise revenues as recommended by the District's financial advisors. If we are to return the district to fiscal stability and move toward a solution of the overdraft, we must have a source of income to cover those expenses.

It would be disingenuous and irresponsible to hold out false hope that we will be able to modify the five-year revenue increase schedule and reduce rates below those designed by a highly-regarded financial consulting firm which based its analysis on a thorough examination of the District's financial situation.