

*In the opinion of Orrick, Herrington & Sutcliffe LLP, Bond Counsel to the Department, based upon an analysis of existing laws, regulations, rulings and court decisions, and assuming, among other matters, the accuracy of certain representations and compliance with certain covenants described herein, interest on the Series AM Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986 and is exempt from State of California personal income taxes. In the further opinion of Bond Counsel, interest on the Series AM Bonds is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although Bond Counsel observes that such interest is included in adjusted current earnings when calculating corporate alternative minimum taxable income. Bond Counsel expresses no opinion regarding any other tax consequences related to the ownership or disposition of, or the accrual or receipt of interest on, the Series AM Bonds. (See “TAX MATTERS” herein.)*

**\$183,960,000**

**STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES  
Central Valley Project Water System Revenue Bonds  
Series AM**

**Dated: Date of Delivery**

**Due: December 1, as shown on Maturity Schedule**

The State of California Department of Water Resources (the “Department”) is issuing its \$183,960,000 Central Valley Project Water System Revenue Bonds, Series AM (the “Series AM Bonds”), for the purpose of refunding a portion of the Department’s outstanding Bonds and paying costs of issuance of the Series AM Bonds.

The Series AM Bonds will be issued in fully registered form in denominations of \$5,000 or any integral multiple thereof, and will be delivered in book-entry form, without coupons, registered in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York (“DTC.”) Purchasers of the Series AM Bonds will not receive physical certificates representing their interests in the Series AM Bonds. DTC will act as securities depository for the Series AM Bonds. The principal of and interest on the Series AM Bonds are payable directly to DTC by the Treasurer of the State of California. Interest is payable semiannually on June 1 and December 1 of each year, commencing on June 1, 2013. Upon receipt of payments of such principal and interest, DTC will in turn remit such principal and interest to the participants in DTC (as described herein) for subsequent disbursement to the beneficial owners of the Series AM Bonds. (See APPENDIX G – “DTC AND BOOK-ENTRY.”)

The Series AM Bonds are subject to redemption prior to maturity as described herein. (See “DESCRIPTION OF THE SERIES AM BONDS – Redemption.”)

Payment of the scheduled principal of and interest on the Series AM Bonds is secured by a pledge of Revenues under the Resolution.

**THE SERIES AM BONDS ARE SPECIAL, LIMITED OBLIGATIONS OF THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES. THE SERIES AM BONDS DO NOT CONSTITUTE A DEBT, LIABILITY, OR OBLIGATION OF THE STATE OF CALIFORNIA. NEITHER THE FAITH AND CREDIT NOR THE TAXING POWER OF THE STATE OF CALIFORNIA IS PLEDGED TO THE PAYMENT OF THE PRINCIPAL OF, OR PREMIUM, IF ANY, OR INTEREST ON THE SERIES AM BONDS.**

**Maturity Schedule  
(See Inside Cover)**

*This cover page contains certain information for quick reference only. It is not intended to be a summary of the security or terms of the bond issue. Investors must read the entire Official Statement to obtain information essential to the making of an informed investment decision.*

*The Series AM Bonds are offered when, as and if issued and received by the Underwriters subject to approval of validity by The Honorable Kamala D. Harris, the Attorney General of the State of California, and by Orrick, Herrington & Sutcliffe LLP, Bond Counsel to the Department, and certain other matters. Certain legal matters are also subject to the approval of Stradling Yocca Carlson & Rauth, a Professional Corporation, counsel to the Underwriters. It is expected that the Series AM Bonds in book-entry form will be available for delivery to DTC on or about March 5, 2013.*

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***Honorable Bill Lockyer***  
***Treasurer of the State of California***

---

**RBC Capital Markets**

**BMO Capital Markets**

**Barclays Capital**

**Citigroup**

**Drexel Hamilton, LLC**

**Hutchinson Shockey Erley & Co.**

**Morgan Keegan**

**Stone & Youngberg, a Division of Stifel Nicolaus**

**Wulff, Hansen & Co.**

**Blaylock Robert Van, LLC**

**De La Rosa & Co.**

**Great Pacific Securities**

**Jefferies**

**Morgan Stanley**

**US Bancorp**

**MATURITY SCHEDULE**  
relating to

**\$183,960,000**

**State of California Department of Water Resources  
Central Valley Project Water System Revenue Bonds  
Series AM  
(Base CUSIP<sup>†</sup> 13066K)**

<b><u>Maturity Date</u></b> <b><u>(December 1)</u></b>	<b><u>Principal</u></b> <b><u>Amount</u></b>	<b><u>Interest</u></b> <b><u>Rate</u></b>	<b><u>Yield</u></b>	<b><u>CUSIP<sup>†</sup></u></b> <b><u>Suffix</u></b>
2013	\$12,320,000	5.000%	0.900%	U31
2014	14,070,000	5.000	1.000	U49
2015	1,525,000	5.000	1.160	U56
2016	10,215,000	5.000	1.250	U64
2017	11,595,000	5.000	1.460	U72
2018	9,665,000	5.000	1.760	U80
2019	20,015,000	5.000	2.030	U98
2020	11,310,000	5.000	2.320	V22
2021	10,715,000	5.000	2.510	V30
2022	19,880,000	5.000	2.670	V48
2023	17,405,000	5.000	2.790 <sup>c</sup>	V55
2024	18,745,000	5.000	2.900 <sup>c</sup>	V63
2025	26,500,000	5.000	2.980 <sup>c</sup>	V71

<sup>†</sup> Copyright 2013, American Bankers Association. CUSIP® is a registered trademark of the American Bankers Association. CUSIP data herein is provided by the CUSIP Service Bureau, operated by Standard & Poor's. This data is not intended to create a database and does not serve in any way as a substitute for the CUSIP Services Bureau. CUSIP numbers have been assigned by an independent company not affiliated with the Department and are included solely for the convenience of the registered owners of the Series AM Bonds. Neither the Department nor the Underwriters assume responsibility for the accuracy of such numbers.

<sup>c</sup> Priced to the earliest permitted call date of June 1, 2023 at par.

T H E C A L I F O R N I A

STATE  
WATER  
PROJECT



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No dealer, broker, salesperson or other person has been authorized to give or to make any representations other than those contained herein and, if given or made, such other information or representation must not be relied upon as having been authorized. This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy nor shall there be any sale of the Series AM Bonds by a person in any jurisdiction in which it is unlawful for such person to make such an offer, solicitation or sale. This Official Statement is not a contract with the purchasers of the Series AM Bonds. Statements contained in this Official Statement that involve estimates, projections, forecasts or matters of opinion, whether or not expressly so described herein, are intended to be solely as such and are not to be construed as representation of fact. The information set forth herein other than that provided by the Department, although obtained from sources which are believed to be reliable, is not guaranteed as to the accuracy or completeness.

The Underwriters have provided the following sentence for inclusion in this Official Statement. The Underwriters have reviewed the information in this Official Statement in accordance with, and as part of, their respective responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriters do not guarantee the accuracy or completeness of such information.

THE UNDERWRITERS MAY OVER-ALLOT OR EFFECT TRANSACTIONS THAT MAY STABILIZE OR MAINTAIN THE MARKET PRICE OF THE SERIES AM BONDS AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

The information and expression of opinions herein are subject to change without notice and neither delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the State of California, the Contractors or the Department since the date hereof.

This Official Statement is delivered for use in connection with the issuance, sale and delivery of the Series AM Bonds.

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**CAUTIONARY STATEMENTS REGARDING  
FORWARD-LOOKING STATEMENTS IN  
THIS OFFICIAL STATEMENT**

Certain statements included or incorporated by reference in this Official Statement constitute forward-looking statements. Such statements generally are identifiable by the terminology used, such as “plan,” “expect,” “estimate,” “budget” or other similar words. Such forward-looking statements include but are not limited to certain statements contained in the information under the captions “Summary Statement,” “Introduction,” “Plan of Refunding,” “California State Water Project,” “Water System Projects,” “Estimated Capital Financing From Water System Revenue Bonds for Existing Water System Projects,” “Power Operations of the State Water Project,” “The Water Supply Contracts,” “The Contractors” and “Litigation.”

The achievement of certain results or other expectations contained in such forward-looking statements involves known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. The Department does not plan to issue any updates or revisions to those forward-looking statements if or when its expectations or events, conditions or circumstances on which such statements are based occur or do not occur, except as described under the caption “CONTINUING DISCLOSURE” and in APPENDIX D.

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## SUMMARY STATEMENT

*This Summary Statement is subject in all respects to the more complete information and definitions contained elsewhere in this Official Statement, including the Appendices attached hereto. Capitalized terms used in this Official Statement without definition have the respective meanings set forth in the Central Valley Project Water System Revenue Bonds, General Bond Resolution, No. DWR-WS-1 of the State of California Department of Water Resources, adopted as of July 1, 1986, and resolutions supplemental thereto, including the supplemental resolution authorizing the Series AM Bonds (the "Resolution.")*

### **The Department**

The State of California Department of Water Resources is a department within the California Natural Resources Agency of the State of California. The Department is responsible for, among other things, the planning, construction and operation of the State Water Project, the operation of programs for the safety of dams, flood management, local assistance and subventions, other water-related matters and the operation of the Power Supply Program. Unless otherwise expressly noted, the term "Department," as used in this Official Statement, means the State of California Department of Water Resources solely in its capacity with respect to the State Water Project, and not in any other capacity mentioned herein.

### **Authorization of the Series AM Bonds**

The Department will issue the Series AM Bonds pursuant to the provisions of Part 3 (commencing with Section 11100) of Division 6 of the Water Code of the State of California (referred to as the "Central Valley Project Act") and the Resolution.

The Series AM Bonds constitute a series of the Department's Central Valley Project Water System Revenue Bonds issued under the Resolution (all bonds issued under the Resolution, collectively, the "Bonds").

### **Purpose of the Series AM Bonds**

The Series AM Bonds are being issued to (1) refund certain of the Department's outstanding Water System Revenue Bonds and (2) pay costs of issuance of the Series AM Bonds. (See "PLAN OF REFUNDING.")

### **Security for the Bonds; Limited Obligations**

The payment of the scheduled principal of and interest on all Bonds, including the Series AM Bonds, is secured by a pledge of the Revenues under the Resolution, which are the portion of the receipts of the Department under the Water Supply Contracts resulting from the construction, acquisition or operation of Water System Projects (but only in the amounts required to meet the rate covenant of the Resolution), income from the investment of moneys held in the Revenue Fund pursuant to the Resolution and certain other moneys received by the Department under the Water Supply Contracts, which the Department in its discretion determines to be Revenues. The Department estimates that payments from The Metropolitan Water District of Southern California will account for approximately 46 percent of the Revenues to be derived from Water Supply Contract payments through the final maturity of the Bonds. However, that percentage may change over time. The balance of such Revenues will be receivable from the other Contractors. (See "SECURITY FOR THE BONDS" and "THE WATER SUPPLY CONTRACTS.")

**THE SERIES AM BONDS ARE SPECIAL, LIMITED OBLIGATIONS OF THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES. THE SERIES AM BONDS DO**

**NOT CONSTITUTE A DEBT, LIABILITY, OR OBLIGATION OF THE STATE OF CALIFORNIA. NEITHER THE FAITH AND THE CREDIT NOR THE TAXING POWER OF THE STATE OF CALIFORNIA IS PLEDGED TO THE PAYMENT OF THE PRINCIPAL OF, OR PREMIUM, IF ANY, OR INTEREST ON THE SERIES AM BONDS.**

### **Rate Covenant**

The Department has covenanted in the Resolution to charge and collect amounts under the Water Supply Contracts sufficient to return the costs of all Water System Projects without regard to whether or not the Department is able to construct, acquire or operate any such Water System Project and that Revenues receivable under all Water Supply Contracts in any year shall be the sum of 1.25 times the aggregate debt service payable from Revenues on all Bonds outstanding in such year, plus the amount estimated by the Department to be sufficient to provide for the costs of operation and maintenance of all Water System Projects, plus the amount, if any, required by a supplemental resolution authorizing a series of Bonds in order to deposit moneys in the Debt Service Reserve Account to meet the requirements of the Resolution for the issuance of additional Bonds. (See “SECURITY FOR THE BONDS – Rate Covenant.”)

### **Debt Service Reserve Account**

The Resolution provides that on the issuance of each series of Bonds, provision must be made for placing moneys in the Debt Service Reserve Account, so that on the first interest payment date when interest on the Bonds of that series is to be paid from Revenues, there will be on deposit in the Debt Service Reserve Account an amount equal to, for any date of calculation, for all Series of Bonds outstanding for which interest is then payable in whole or in part from Revenues, one-half of the maximum Annual Debt Service for the then current Year or any Year after such date of calculation.

Upon the issuance of the Series AM Bonds the amount on deposit in the Debt Service Reserve Account will be equal to or exceed the Reserve Account Requirement for the outstanding Bonds as of such issuance. (See APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE RESOLUTION – Debt Service Reserve Account.”)

### **The State Water Project**

The State Water Project is a complex of dams, water storage facilities, aqueducts, pumping stations and electric generation facilities, which have been constructed by the Department for the purposes of developing a water supply and conveying water to areas in need within the State of California (the “State”) and providing flood control, recreation, fish and wildlife enhancement, hydroelectric power and other benefits. All 647 miles of the initially planned aqueduct system have been completed. With the addition of the Grizzly Valley pipeline, the Thermalito Powerplant power canal and tail channel, and the extension of the East Branch aqueduct, the entire aqueduct system totals 705 miles. The 443-mile main stem California Aqueduct runs from a point near Stockton southward to a terminus in Riverside County. The dependable annual water supply available for delivery by the existing State Water Project will vary yearly depending on hydrologic conditions and regulatory mandates. (See “STATE WATER PROJECT WATER SUPPLY.”)

Under the Water Supply Contracts presently in effect, the Contractors may request from the State Water Project maximum annual delivery amounts totaling 4,172,786 acre-feet. Payments by the 29 participating local public agencies under the Water Supply Contracts provide for the operation, maintenance, planning and capital costs, including interest, of the State Water Project. (See “CALIFORNIA STATE WATER PROJECT,” “THE CONTRACTORS” and “THE WATER SUPPLY CONTRACTS.”)

## **Financing of the State Water Project**

A large portion of the State Water Project has been financed from the issuance of \$1,582,400,000 in aggregate principal amount of State general obligation bonds, of which \$326,990,000 in aggregate principal amount are outstanding. The Department has also issued \$1,526,155,000 in aggregate principal amount of revenue bonds for certain power facilities of the State Water Project, of which \$68,070,000 in aggregate principal amount are outstanding. Such revenue bonds are secured by revenues of the Department other than those that are pledged to secure the Bonds and were and are issued under and secured by resolutions separate and apart from the Resolution authorizing and securing the Bonds. (See “FINANCIAL OPERATIONS – Financing of the State Water Project.”)

The Department has previously issued forty series of Bonds totaling \$7,476,100,000 in aggregate principal amount, of which \$2,203,240,000 in aggregate principal amount are outstanding under the Resolution. The Series AM Bonds offered hereby are the forty-first series of Bonds to be issued pursuant to the Resolution and secured by the Revenues pledged under, and the funds and accounts established by, the Resolution. The Department may from time to time issue additional Bonds secured by a lien on Revenues under the Resolution equally and ratably with the payment of scheduled principal of and interest on the Series AM Bonds and the currently outstanding Bonds. (See “INTRODUCTION,” “PLAN OF REFUNDING,” “SECURITY FOR THE BONDS – Outstanding Bonds; Additional Bonds,” “FINANCIAL OPERATIONS – Outstanding Revenue Obligations of the Department for the State Water Project.”)

The Department has authorized the issuance of Notes in a principal amount outstanding at any one time not to exceed the lesser of \$150,000,000 or the principal amount of Notes supported by the credit agreement then in effect (currently \$139,668,367). Proceeds from the sale of Notes are used to finance Water System Projects prior to permanent financing from the sale of Bonds. The Department’s obligation to make debt service payments on the Notes is subordinate to its payment obligations with respect to the Bonds. As of the date of delivery of the Series AM Bonds, the Department will have approximately \$50,000,000 principal amount of Notes outstanding. (See “PLAN OF REFUNDING – Proposed Issuance of Series AP Bonds to Refund Outstanding Notes.”)

### **Additional Bonds**

The Department may issue, under certain conditions, additional Bonds to provide funds for the cost of any Water System Project or for refunding purposes. Such additional Bonds will be on a parity with outstanding Bonds and secured by an equal lien on the Revenues under the Resolution. (See “PLAN OF REFUNDING,” “SECURITY FOR THE BONDS – Outstanding Bonds; Additional Bonds” and APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE RESOLUTION – Issuance of Bonds.”)

### **The Contractors**

The 29 Contractors are principally located in the San Francisco Bay Area, the Central Coast, the Central Valley and Southern California and their service areas encompass approximately 25 percent of the State’s land area and approximately 71 percent of its population. Each Contractor has entered into a Water Supply Contract with the Department, acting on behalf of the State. Certain of the Contractors receive a major portion of their income from *ad valorem* taxes. The ability of Contractors to tax for general purposes and to appropriate tax revenue for general purposes is limited under California law. (See “THE WATER SUPPLY CONTRACTS” and “CERTAIN LIMITATIONS ON CONTRACTOR REVENUE SOURCES.”)

## **The Water Supply Contracts**

The Water Supply Contracts are to remain in effect until 2035 or until all bonds issued to finance construction costs of State Water Project facilities have been repaid, whichever period is longer. As of the date of issuance of the Series AM Bonds, the final maturity of the Bonds to be outstanding upon the issuance of the Series AM Bonds will occur in 2035. Under its Water Supply Contract, each Contractor may request water deliveries from the State Water Project up to a maximum specified annual amount, and agrees to pay its allocated share of the costs of gathering, storing, conveying and delivering water. Generally, the Department's costs, including interest, of providing the facilities of the State Water Project, including the Water System Projects, are payable by the Contractors whether or not water is delivered. If a Contractor defaults under its Water Supply Contract, the Department may, upon six months' notice, suspend water deliveries to that Contractor. During such period, the Contractor remains obligated to make all payments required by the Water Supply Contract. If a Contractor fails or is unable to raise sufficient funds by other means to make Water Supply Contract payments, the Contractor is required by the Water Supply Contract to levy a tax or assessment sufficient for such purpose.

The Department and the various subsets of Contractors ("affected Contractors") have entered into an Off-Aqueduct Power Facilities Amendment, an East Branch Enlargement Amendment, a Water System Revenue Bond Amendment, a Coastal Branch Extension Amendment, an East Branch Extension Amendment and a South Bay Aqueduct Enlargement Amendment to the Water Supply Contracts for the purpose of financing certain of the Water System Projects. These amendments establish procedures to provide for the payment of construction costs financed with Bonds by establishing separate subcategories of charges to produce the revenues required to pay all of the annual financing costs, including coverage, of the Bonds allocable to such Water System Projects. If any affected Contractor defaults on payment under certain of such amendments other than the Coastal Branch Extension Amendment, the East Branch Extension Amendment and the South Bay Aqueduct Enlargement Amendment, the shortfall may be collected from nondefaulting affected Contractors, subject to certain limitations. (See "SECURITY FOR THE BONDS" and "THE WATER SUPPLY CONTRACTS.")

In December 1994, representatives of the Department and certain Contractors adopted a set of principles pursuant to which additional amendments to the Water Supply Contracts have since been negotiated (the "Monterey Amendment.") The Department has covenanted in the Resolution not to amend the Water Supply Contracts in any manner that would materially adversely affect the security for the Bonds, and the Department believes that the Monterey Amendment complies with that covenant. (See "WATER SUPPLY CONTRACT RELATED LITIGATION – Monterey Amendment Litigation," for a description of certain litigation and the implementation of the settlement thereof that could affect the Monterey Amendment. See also "WATER SUPPLY CONTRACT RELATED LITIGATION – Claims Relating to the Use of Bond Proceeds to Pay Costs Allocable to Recreation and Fish and Wildlife Enhancement.")

### **Continuing Disclosure**

The Department will covenant for the benefit of the holders and beneficial owners of the Series AM Bonds to provide certain financial information and operating data relating to the Department not later than 270 days following the end of each Department fiscal year (the "Annual Report"), commencing with the report containing 2012-2013 Fiscal Year financial information and to provide notices of the occurrence of certain enumerated events ("Event Notices"). The specific nature of the information expected to be contained in the Annual Report or the Event Notices and certain other terms of this continuing disclosure obligation are set forth in APPENDIX D – "SUMMARY OF CONTINUING DISCLOSURE CERTIFICATE." Within the past five years the Department has not failed to comply, in all material respects, with all previous similar undertakings under continuing disclosure certificates.

## **No Relationship to Power Supply Revenue Bonds**

The Department's Central Valley Project Water System Revenue Bonds are not secured by the same sources of repayment as, and otherwise bear no material relationship to, bonds issued by the Department to finance and refinance the State of California's Power Supply Program (the "Power Supply Revenue Bonds.") **The State Water Project and the Power Supply Program are separate and distinct enterprises, and have separate and distinct sources and uses of funds. Revenues pledged to secure payment of the Bonds may not be used to pay the Power Supply Revenue Bonds or any other expenses of the Power Supply Program, and resources pledged to secure the payment of the Power Supply Revenue Bonds may not be used to pay the Bonds or any other expenses of the State Water Project.**

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**STATE OF CALIFORNIA  
DEPARTMENT OF WATER RESOURCES  
OFFICIAL STATEMENT**

**Relating to its**

**\$183,960,000  
Central Valley Project  
Water System Revenue Bonds,  
Series AM**

**INTRODUCTION**

This Official Statement is furnished by the State of California Department of Water Resources, in its capacity as operator of the State Water Project (the "Department"), for the purpose of setting forth information concerning its Central Valley Project Water System Revenue Bonds (the "Bonds" or the "Water System Revenue Bonds"), particularly the \$183,960,000 Central Valley Project Water System Revenue Bonds, Series AM (the "Series AM Bonds").

The Department will issue the Series AM Bonds pursuant to the provisions of Part 3 (commencing with Section 11100) of Division 6 of the Water Code of the State of California (referred to as the Central Valley Project Act and herein referred to as the "CVP Act") and the Central Valley Project Water System Revenue Bonds, General Bond Resolution, No. DWR-WS-1 of the Department, adopted as of July 1, 1986, and resolutions supplemental thereto, including the supplemental resolution authorizing the Series AM Bonds (such resolutions being herein, except as the context otherwise indicates, collectively called the "Resolution"). All capitalized terms used in this Official Statement and not defined herein have the same meanings as in the Resolution. (See APPENDIX C – "SUMMARY OF CERTAIN PROVISIONS OF THE RESOLUTION.")

This Official Statement also contains certain information with respect to the California State Water Project, the projects financed with the Bonds (the "Water System Projects") and the contracts for a supply of water from the State Water Project (the "Water Supply Contracts") between the Department on behalf of the State of California and 29 California public agencies (the "Contractors"). Contractor payments for water pursuant to the Water Supply Contracts are the principal component of the Revenues, as hereinafter defined, pledged for the payment of the interest on and the principal of the Series AM Bonds.

**Purpose of the Series AM Bonds**

The Series AM Bonds are being issued to (1) refund certain of the Department's outstanding Water System Revenue Bonds and (2) pay costs of issuance of the Series AM Bonds. (See "PLAN OF REFUNDING.")

## PLAN OF REFUNDING

On the date of delivery of the Series AM Bonds, the Department will apply a portion of the proceeds of the Series AM Bonds to provide for the defeasance of a portion of the outstanding Bonds of Series Y and all of the outstanding Bonds of Series AA in the aggregate principal amount of \$211,840,000 as set forth below (the “Series AM Refunded Bonds”). The following table sets forth certain pertinent information with respect to the Series AM Refunded Bonds:

### Bonds to be Refunded by the Series AM Bonds

<u>Revenue Bond Series</u>	<u>Year of Issuance</u>	<u>Outstanding Principal Amount</u>	<u>Principal Amount to be Refunded</u>	<u>Interest Rate</u>	<u>Maturity Date (December 1)</u>	<u>Redemption Date (June 1)</u>	<u>Redemption Price</u>
Y	2003	\$14,355,000	\$14,355,000	5.250%	2013	2013	100%
Y	2003	15,940,000	15,940,000	5.250	2014	2013	100
Y	2003	1,620,000	1,620,000	5.250	2015	2013	100
Y	2003	11,555,000	11,555,000	5.250	2016	2013	100
Y	2003	13,160,000	13,160,000	5.250	2017	2013	100
Y	2003	10,980,000	10,980,000	5.250	2018	2013	100
Y	2003	22,840,000	22,840,000	5.250	2019	2013	100
Y	2003	51,760,000	51,760,000	5.000	2025	2013	100
AA	2003	13,275,000	13,275,000	5.000	2020	2013	100
AA	2003	12,580,000	12,580,000	5.000	2021	2013	100
AA	2003	23,340,000	23,340,000	5.000	2022	2013	100
AA	2003	20,435,000	20,435,000	5.000	2023	2013	100

On the date of delivery of the Series AM Bonds, the Department will cause a portion of the proceeds of the Series AM Bonds, together with other available moneys, to be applied to the purchase of obligations of the United States of America or certain of its agencies or certain other securities permitted under the Resolution (the “Government Obligations”), which will be deposited, together with certain uninvested cash, if any, in an irrevocable trust (the “Escrow Account”) to be held by the Treasurer of the State of California (the “State Treasurer”) as security solely for the Series AM Refunded Bonds. The Government Obligations in the Escrow Account will mature at such times and in such amounts, and will bear interest payable at such times and in such amounts that, together with the uninvested cash on deposit in the Escrow Account, if any, sufficient moneys will be available to pay, when due or called for redemption, all principal of and interest and premium on the Series AM Refunded Bonds. (See “VERIFICATION.”) Concurrently with the issuance of the Series AM Bonds, irrevocable instructions will be given to the State Treasurer, as Trustee for the Series AM Refunded Bonds, to mail a timely notice of redemption with respect to the Series AM Refunded Bonds. Accordingly, upon issuance of the Series AM Bonds, adequate and complete provision will be made for the full and timely payment of the principal or redemption price of and interest on the Series AM Refunded Bonds when due, and the Series AM Refunded Bonds will be payable solely from the Government Obligations and uninvested cash, if any, on deposit in the Escrow Account. Once the deposit to the Escrow Account is made as described above, the Series AM Refunded Bonds will not be payable from Revenues as hereinafter defined nor from any other source of revenues.

### **Application of Escrow Account**

The uninvested cash, and the maturing principal of, and the investment income to be derived from, the Government Obligations held by the State Treasurer in trust in the Escrow Account is solely for payment of principal or redemption price of and interest on the Series AM Refunded Bonds as provided in the Escrow Agreement and will not be available to pay principal of, or premium or interest on, any Bonds other than the Series AM Refunded Bonds.



**Proposed Issuance of Series AP Bonds to Refund Notes**

In addition to the Series AM Bonds, the Department expects to issue its Central Valley Project Water System Revenue Bonds, Series AP (the “Series AP Bonds”) in the aggregate principal amount of approximately \$50,000,000 on or about March 26, 2013, to provide long term financing for Water System Projects financed with Notes.

**ESTIMATED APPLICATION OF SERIES AM BOND PROCEEDS**

The following table sets forth the estimated application of the proceeds of the Series AM Bonds:

Deposit in Escrow Account to Refund Series AM Refunded Bonds <sup>(1)</sup> .....	\$212,867,573.64
Cost of Issuance of Series AM Bonds <sup>(2)</sup> .....	1,009,557.36
Total Proceeds of the Series AM Bonds	<u>\$213,877,131.00</u>
Original Issue Premium .....	<u>(29,917,131.00)</u>
Principal Amount of Series AM Bonds.....	<u>\$183,960,000.00</u>

<sup>(1)</sup> Simultaneous with the delivery of the Series AM Bonds, \$1,675,397.92 will be released from the Debt Service Reserve Account and \$2,706,110.94 will be released from the Revenue Fund, in each case, representing an amount associated with the Series AM Refunded Bonds. This amount will be deposited in the Escrow Account providing for the payment of the Series AM Refunded Bonds to and including their call date.

<sup>(2)</sup> Includes underwriting discount, legal fees, financial advisory fees, printing expenses and other costs.

**DESCRIPTION OF THE SERIES AM BONDS**

**General**

The Series AM Bonds will be dated the date of delivery thereof, expected to be on or about March 5, 2013, will be issued in fully registered form without coupons, will be in denominations of \$5,000 principal amount or any integral multiple thereof, and will bear interest payable semiannually on June 1 and December 1 of each year, commencing on June 1, 2013 (each, an “interest payment date”). The Series AM Bonds will mature (subject to the right of prior redemption discussed below) on December 1 in each of the years and in the respective principal amounts, and will bear interest at the respective rates (calculated on the basis of a 360-day year composed of twelve 30-day months), as shown on the Maturity Schedule immediately following the cover page of this Official Statement.

Interest on the Series AM Bonds is payable to the person whose name appears on the Bond registration books of the State Treasurer as the owner as of the close of business on the fifteenth day of the month immediately preceding an interest payment date, whether or not the day is a business day.

**THE SERIES AM BONDS ARE SPECIAL, LIMITED OBLIGATIONS OF THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES. THE SERIES AM BONDS DO NOT CONSTITUTE A DEBT, LIABILITY, OR OBLIGATION OF THE STATE OF CALIFORNIA. NEITHER THE FAITH AND THE CREDIT NOR THE TAXING POWER OF THE STATE OF CALIFORNIA IS PLEDGED TO THE PAYMENT OF THE PRINCIPAL OF, OR PREMIUM, IF ANY, OR INTEREST ON THE SERIES AM BONDS.**

**Book-Entry Only**

The Series AM Bonds will be issued as fully registered bonds and registered in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York (“DTC.”) DTC will act as securities depository for the Series AM Bonds. Purchasers will not receive certificates representing Series AM Bonds

purchased by them. The State Treasurer will pay principal of and interest on the Series AM Bonds directly to DTC. Upon receipt of payment of principal and interest DTC is obligated to remit such payments of principal and interest to the DTC Participants for subsequent disbursement to the Beneficial Owners of the Series AM Bonds. (See APPENDIX G – “DTC BOOK ENTRY.”)

## **Redemption**

*Optional Redemption.* The Series AM Bonds maturing on or after December 1, 2023 are subject to redemption prior to their respective stated maturities, at the option of the Department from any source of available funds, as a whole, or in part by such maturities as the Department may designate (and by lot within any maturity), on any date on or after June 1, 2023, upon payment of a redemption price equal to the principal amount of the Series AM Bonds to be redeemed, plus accrued interest to the date fixed for redemption, without premium.

*Selection of Bonds for Redemption.* Whenever less than all the outstanding Bonds of any maturity of Series AM Bonds are to be redeemed on any one date, the State Treasurer shall select the Series AM Bonds of such maturity to be redeemed by lot in any manner the State Treasurer deems fair.

*Notice of Redemption.* So long as DTC is acting as securities depository for the Series AM Bonds, notice of redemption with respect to the Series AM Bonds will be given by mailing copies of such notice to DTC, not to the beneficial owners (as defined in APPENDIX G – “DTC AND BOOK-ENTRY” herein) of any Series AM Bonds designated for redemption, at least 20 days but not more than 60 days prior to the redemption date. The Resolution provides that if notice of redemption has been duly given and moneys for the payment of the redemption price of the Series AM Bonds called for redemption are held by the State Treasurer, then on the redemption date designated in such notice the Series AM Bonds so called for redemption will become due and payable, and from and after the redemption date, interest on the Series AM Bonds so called for redemption will cease to accrue and the holders of such Series AM Bonds will have no rights in respect thereof except to receive payment of the redemption price thereof.

The receipt of such a notice shall not be a condition precedent to such redemption and the failure to so receive any such notice shall not affect the validity of the proceedings for the redemption of Series AM Bonds for which notice of redemption was given.

*Right to Cancel Notice of Redemption.* Upon the written request of the Department, any notice of redemption may be cancelled by giving notice of such cancellation, in the same manner as for giving notices of redemption, at any time prior to the date fixed for redemption designated in such notice of redemption.

*Effect of Redemption.* If, on the date fixed for redemption, moneys equal to the redemption price of Series AM Bonds or portions thereof designated for redemption, together with interest accrued thereon to the date fixed for redemption, shall be held by the State Treasurer for such Bonds so as to be available for payment of such redemption price and interest on such date, and if notice of redemption shall have been mailed as provided in the Resolution, then such Bonds or portions thereof, whether or not presented for redemption, shall cease to be entitled to any benefit under the Resolution other than the right to receive payment of the redemption price together with accrued interest to the date fixed for redemption, no interest shall accrue on such Bonds or portions thereof after the date fixed for redemption, and, except as to the portion not designated for redemption of any Bond designated for redemption only in part, the redemption price of and accrued interest on such Bonds shall be payable only from the moneys held by the State Treasurer for such Bonds for that purpose.

## **Defeasance**

The obligations of the Department and the pledge, lien, covenants and agreements of the Department made or provided for in the Resolution will be fully discharged and satisfied as to any Series AM Bond and such

Bond shall no longer be deemed to be outstanding thereunder if certain conditions set forth in the Resolution are satisfied. (See APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE RESOLUTION – Discharge of Obligations Under the Resolution.”)

## **SECURITY FOR THE BONDS**

### **Sources of Revenues**

Under the Water Supply Contracts, the Contractors are required to pay to the Department amounts calculated by Department and to be sufficient to return to the Department its annual costs of the State Water Project allocated to water and power supply. The revenues pledged to the payment of the scheduled principal of and interest on all Bonds (the “Revenues”) are the portion of the receipts of the Department under the Water Supply Contracts resulting from the construction, acquisition or operation of Water System Projects (but only in the amounts required to meet the rate covenant of the Resolution), income from the investment of moneys held in the Revenue Fund pursuant to the Resolution and certain other moneys received by the Department under the Water Supply Contracts, which the Department in its discretion determines to be Revenues. Revenues do not include any other income or receipts resulting from the construction, acquisition or operation of a Water System Project other than the income and receipts specified in the immediately preceding sentence. Revenues from facilities constructed or acquired with the proceeds of CVP Act revenue bonds, including the Bonds, are not subject to the provisions of the Burns-Porter Act pledging other Water Supply Contract revenues to the payment of State general obligation bonds issued under the Burns-Porter Act. (See “FINANCIAL OPERATIONS – Allocation of State Water Project Revenues.”)

Under the Resolution, the Department is required to charge the Contractors amounts under the Water Supply Contracts sufficient to repay the costs of all Water System Projects, whether or not the Department is able to construct or operate the Water System Projects or to produce, make available or deliver water from the Water System Projects. The terms of the Water Supply Contracts provide for such charges. The Resolution requires that the Revenues receivable in each year, after deduction of the costs of maintenance and operation (excluding depreciation but including appropriate amounts for operating and replacement reserves) of the Water System Projects for such year (the “Water System Operating Expenses”) shall be at least equal to the sum of 1.25 times the debt service payable from Revenues on all Bonds outstanding in such year and the amount, if any, required by a supplemental resolution authorizing a series of Bonds in order to deposit moneys in the debt service reserve account established under the Resolution (the “Debt Service Reserve Account”) to meet the requirements of the Resolution for the issuance of additional Bonds. Amounts received in excess of maintenance, operation and debt service needs are held by the Department and refunded to Contractors approximately one year following receipt. Under the CVP Act, the payment of debt service has priority over the payment of operating expenses. Under current law, the charges of the Department under the Water Supply Contracts are not subject to regulation by any state or federal regulatory authority. (See “THE WATER SUPPLY CONTRACTS – Amendments Providing Certain Revenues to Pay Water System Revenue Bonds.”)

The Department estimates that upon issuance of the Series AM Bonds, payments from The Metropolitan Water District of Southern California (“Metropolitan”) will account for approximately 46 percent of the Revenues to be derived from Water Supply Contract payments. (See “THE CONTRACTORS – Selected Contractor Financial Information.”) However, that percentage may change over time.

### **Pledge of Revenues**

The principal of, and premium, if any, and interest on the Bonds are payable from and secured by a lien upon and pledge of the Revenues. The Bonds are also payable from Bond proceeds and other available funds (except amounts, if any, in any Rebate Account) to the extent provided in the Resolution.

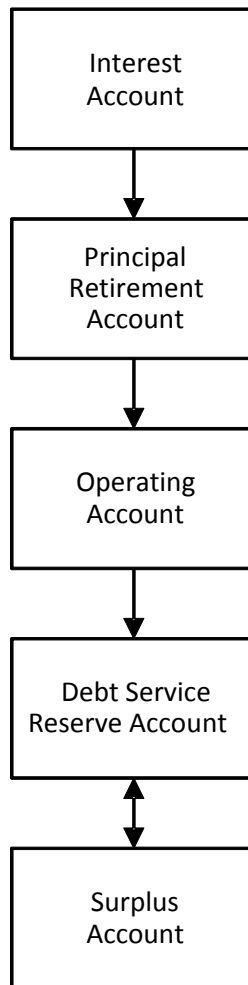
THE SERIES AM BONDS ARE SPECIAL, LIMITED OBLIGATIONS OF THE DEPARTMENT. THE SERIES AM BONDS DO NOT CONSTITUTE A DEBT, LIABILITY, OR OBLIGATION OF THE STATE OF CALIFORNIA. NEITHER THE FAITH AND CREDIT NOR THE TAXING POWER OF THE STATE OF CALIFORNIA IS PLEDGED TO THE PAYMENT OF THE PRINCIPAL OF, OR PREMIUM, IF ANY, OR INTEREST ON THE SERIES AM BONDS.

**Flow of Funds**

The portion of each Contractor’s payments under its Water Supply Contract attributable to the Water System Projects will be deposited in the Revenue Fund.

The diagram below illustrates the priority of allocations to various accounts within the Revenue Fund. (See APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE RESOLUTION – Disposition of Revenues.”)

**Priority of Allocation of Revenues**



Moneys in the Debt Service Reserve Account may be used only to make up any deficiency in the Interest Account or Principal Retirement Account, in that priority.

Moneys in the Surplus Account are available for any lawful purpose, including transfer to funds not subject to the pledge of the Resolution.

### **Rate Covenant**

The Department has covenanted in the Resolution to charge and collect amounts under the Water Supply Contracts sufficient to return the costs of all Water System Projects without regard to whether or not the Department is able to construct, acquire or operate any such Water System Project and that Revenues receivable under all Water Supply Contracts in any year shall be the sum of 1.25 times the aggregate debt service payable from Revenues on all Bonds outstanding in such year, plus the amount estimated by the Department to be sufficient to provide for the costs of operation and maintenance of all Water System Projects, plus the amount, if any, required by a supplemental resolution authorizing a series of Bonds in order to deposit moneys in the Debt Service Reserve Account to meet requirements of the Resolution for the issuance of additional Bonds. Amounts received in excess of maintenance, operation and debt service needs are held by the Department and refunded to Contractors approximately one year following receipt. The manner in which charges under the Water Supply Contracts are established and collected is described under “THE WATER SUPPLY CONTRACTS – Basic Contract – Water Charges” and “– Payment of Water Charges.”

### **Debt Service Reserve Account**

The Resolution provides that on the issuance of each series of Bonds, provision must be made for placing moneys in the Debt Service Reserve Account, so that on the first interest payment date when interest on the Bonds of that series is to be paid from Revenues, there will be on deposit in the Debt Service Reserve Account an amount equal to, for any date of calculation, for all Series of Bonds outstanding for which interest is then payable in whole or in part from Revenues, one-half of the maximum Annual Debt Service for the then current Year or any Year after such date of calculation.

Upon the issuance of the Series AM Bonds the amount on deposit in the Debt Service Reserve Account will be equal to or exceed the Reserve Account Requirement for the outstanding Bonds as of such issuance date. (See APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE RESOLUTION – Debt Service Reserve Account.”)

Upon the issuance of the Series AM Bonds, the amount of the Reserve Account Requirement for the outstanding Bonds will be approximately \$104,546,570. The Department anticipates that approximately 53 percent of the amount held in the Debt Service Reserve Account on the date of issuance of the Series AM Bonds will be invested in the State Treasurer’s Pooled Money Investment Account, with the balance invested directly in U.S. Government securities. (See “THE DEPARTMENT – Investments of Department Moneys”). This percentage may change. (See APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE RESOLUTION – Debt Service Reserve Account.”)

### **Outstanding Bonds; Additional Bonds**

Bonds in an aggregate principal amount of \$2,203,240,000 are currently Outstanding and all Outstanding Bonds (including any additional Bonds) are secured equally and ratably with the Series AM Bonds. (See “PLAN OF REFUNDING” and “FINANCIAL OPERATIONS – Outstanding Revenue Obligations of the Department for the State Water Project” and “– Estimated Annual Debt Service.”)

The Department may issue additional Bonds on a parity basis with outstanding Bonds to finance the costs allocated to any Water System Project, including the cost of planning, construction or acquisition, or to refund bonds if, among other things, the Department certifies that (a) after the issuance of such Bonds, estimated Revenues in each year will not be less than the sum of (i) 1.25 times debt service to be paid from Revenues, plus (ii) estimated Water System Operating Expenses, (b) the Debt Service Reserve Account established pursuant to

the Resolution is projected to contain on the first interest payment date on which interest for such additional Bonds is payable from Revenues, an amount equal to the Reserve Account Requirement, and (c) the State Treasurer must have received evidence that the issuance of the additional Bonds will not result in the lowering of any rating then assigned to any then outstanding Bonds by any nationally recognized rating agency. (See “PLAN OF REFUNDING – Proposed Issuance of Series AP Bonds to Refund Outstanding Notes” and see also APPENDIX C – “SUMMARY OF CERTAIN PROVISIONS OF THE RESOLUTION – Issuance of Bonds.”)

Pursuant to Section 11731 and 11751 of the CVP Act, the Department may issue revenue bonds bearing interest at a rate not exceeding 12 percent per annum and may sell revenue bonds at a price of not less than 94 percent. If the Department determines that interest on revenue bonds will be subject to federal income taxation and to the extent permitted by applicable law, such bonds may bear interest at such rate or rates, and may be sold at such price or prices, as the Department may determine.

## **THE DEPARTMENT**

### **Introduction**

The Department is a department within the California Natural Resources Agency of the State and is responsible for the planning, construction and operation of the State Water Project. The Department is also responsible for, among other things, the operation of programs for the safety of dams, flood management, local assistance and subventions and other water-related matters, and the operation of the Power Supply Program. The Department was established in 1956 by an act of the State Legislature that combined the functions of the Water Project Authority and certain responsibilities of the Department of Public Works’ former Division of Water Resources. At present, the Department employs approximately 3,294 full-time staff throughout the State.

### **Management**

The Director of Water Resources oversees the Department’s activities, with the assistance of a Chief Deputy Director and five Deputy Directors. The Director and Chief Deputy Director are appointed by the Governor and report to the Governor through the Secretary of the California Natural Resources Agency. Biographical information for the management officials of the Department currently responsible for the State Water Project is as follows.

*Mark W. Cowin* has served as Director of the Department since February 2010. He has worked for the Department for over 30 years. Prior to his appointment as Director, Mr. Cowin served as Deputy Director of Integrated Water Management for the Department. In previous assignments with the Department Mr. Cowin served for five years as Chief of the Department’s Division of Planning and Local Assistance and as an Assistant Director for the CALFED Bay-Delta Program.

*Dale K. Hoffman-Floerke* was appointed Chief Deputy Director of the Department in July 2012. Ms. Hoffman-Floerke is responsible for many of the Department’s administrative and water management policy issues. Prior to her appointment as Chief Deputy Director, she served since 2010 as acting Deputy Director for Delta and Statewide Water Management, which included program manager responsibilities for the Department’s participation in the Bay Delta Conservation Plan. Ms. Hoffman-Floerke has also served as Deputy Director for Integrated Water Management and in other managerial and staff positions since joining the Department in 1979.

*Carl A. Torgersen* was appointed Deputy Director for the State Water Project in April 2012, after serving as Acting Deputy Director for the State Water Project since September 2011. Mr. Torgersen is responsible for directing the activities of the Division of Engineering, Division of Operations and Maintenance, the State Water Project Analysis Office, the State Water Project Power and Risk Office, and the Hydropower License Planning and Compliance Office. Prior to this assignment, he was Chief of the Division of Operations and Maintenance since 2006. He has worked for the Department for more than 30 years. He is a licensed Professional Mechanical Engineer.

*Cathy Crothers* has served as Chief Counsel of the Department since April 2011, and was Acting Chief Counsel of the Department since May 2010. She oversees a staff of 40 attorneys working on the Department's varied and complex legal issues. She joined the Department in 1990 and prior to serving as Acting Chief Counsel she served as the Assistant Chief Counsel responsible for water rights, environmental compliance, energy planning, and local project financing since 2007.

*Perla Netto-Brown* has served as the Chief of the Division of Fiscal Services since May 2000 and as such is the chief financial officer of the Department. She joined the Department in 1986 and has served in various accounting positions in the Division of Fiscal Services prior to her appointment as Chief of the Division of Fiscal Services. Prior to joining the Department, Ms. Netto-Brown was an auditor with the California Auditor General.

## **Fund Accounting**

The Department's operations with respect to the State Water Project are accounted for and conducted under special funds established by the California Water Code, principally the State Water Resources Development Bond Fund, the Central Valley Project Construction Fund (the "Construction Fund") and the Central Valley Project Revenue Fund (the "Revenue Fund.") The Department's operations with respect to the State Water Project are separate and apart from the Department's operations that are primarily funded by State General Fund appropriations and from the Department's Power Supply Program. (See "FINANCIAL OPERATIONS – Allocation of State Water Project Revenues.")

## **Employee Relations**

The Ralph C. Dills Act, enacted in 1977, provides that State employees have a right to form, join, and participate in the activities of employee organizations for the purpose of representation on all matters of employer-employee relations. However, once an employee organization is recognized as the exclusive representative of a bargaining unit, only that organization may represent the bargaining unit employees. The Department has approximately 3,294 full-time employees of whom approximately 2,381 are represented in 10 of the 21 statewide bargaining units adopted by the Public Employment Relations Board ("PERB") for collective bargaining purposes. The remainder of the Department's employees are not covered by collective bargaining agreements because of their managerial, supervisory or confidential status.

The scope of representation is limited to wages, hours, and other terms and conditions of employment. Representatives of the Governor are required to meet and confer in good faith and endeavor to reach agreement with the employee organization, and, if agreements are reached, to prepare a memoranda of understanding and present them to the Legislature for approval. In cases where the parties are unable to reach agreement, either party may request the PERB to appoint a mediator to assist them in reconciling a dispute.

Ten bargaining units represent employees of the Department. Currently, none of the ten memoranda of understanding (each an "MOU" and collectively, the "MOUs") in effect with respect to these bargaining units has expired. If a MOU expires without a successor MOU in place, as provided by State law the current MOU remains in effect until the successor MOU or an extension of the current MOU is negotiated and approved by the respective bargaining unit and the Legislature. Most of the MOUs expire on July 1, 2013.

The Department is also currently working with the California Department of Human Resources to improve its ability to recruit and retain qualified personnel who are critical to the operation and maintenance of the State Water Project.

As part of the 2012 – 2013 fiscal year State budget, Governor Brown directed that State employee compensation be reduced by five percent. All bargaining units represented at the Department, with one exception, agreed to a personal leave program for this fiscal year, involving a slightly less than five percent pay

reduction in exchange for eight hours of leave credits monthly. Employees represented by the union that did not agree to the reduction, have had the same pay reduction-leave credit terms applied to them.

### **Pension Obligations**

State departments and agencies, including the Department, participate in the California Public Employees' Retirement System ("PERS"), an agent multiple-employer pension system that provides a contributory defined-benefit pension for substantially all State employees. PERS has unfunded liabilities in the tens of billions of dollars. The Department is required to contribute the actuarially determined remaining amounts necessary to fund benefits for its employees, using actuarial methods and assumptions adopted by the PERS Board of Administration. For the years ended June 30, 2012 and June 30, 2011, the Department paid approximately \$25.0 million and \$23.0 million, respectively, in annual pension contributions in respect of the State Water Project. The level of future required annual pension contributions by the Department depends on a variety of factors, including future investment portfolio performance, actuarial assumptions and additional potential changes in retirement benefits. There can be no assurances that the Department's required annual contribution to PERS will not significantly increase.

Additional information concerning State Water Project pension obligations, including a description of the actuarial assumptions and methods used to determine required contributions, are set forth in Note 8 of the financial statements of the State Water Resources Development System appearing in APPENDIX B. Such information is reported in part on the basis of State Miscellaneous Category Tier I and Tier II employees, of which State Water Project employees represent only a portion. For the years ended June 30, 2012 and June 30, 2011, Department contributions with respect to the State Water Project represented approximately 1.3 percent and 1.1 percent, respectively, of contributions for all of State Miscellaneous Category Tier I and Tier II.

### **Post-employment Benefits Other Than Pensions**

In addition to the pension benefits provided by the State, the State also provides post-retirement health care benefits, in accordance with California Government Code section 22760(g), to all employees who retire from the State on or after attaining certain age and length of service requirements. The post-retirement health care benefits are funded by the State General Fund on a pay-as-you-go basis. Expenses for health care benefits for the Department's active employees and retirees for the years ended June 30, 2012 and 2011 were approximately \$31,091,000 and \$41,382,000, respectively. Post-retirement health care data for the Department's retirees alone are not available.

### **Investments of Department Moneys**

The Department uses the State's Centralized Treasury System. Moneys on deposit in the State's Centralized Treasury System are invested by the State Treasurer in the Pooled Money Investment Account (the "PMIA"). As of January 31, 2013, the PMIA held approximately \$39.9 billion of State moneys, and approximately \$21.5 billion invested for about 2,660 local governmental entities through the Local Agency Investment Fund (the "LAIF"). The assets of the PMIA as of January 31, 2013 are shown in the following table:



**Analysis of the Pooled Money Investment Account Portfolio**

<u>Type of Security</u>	<u>Amount (in thousands)</u>	<u>Percent of Total <sup>(1)</sup></u>
U.S. Treasury Bills and Notes .....	\$37,894,255	61.67%
Federal Agency Debentures	1,520,704	2.47
Certificates of Deposit .....	6,850,002	11.15
Bank Notes	0	0.00
Federal Agency Discount Notes	5,094,093	8.29
Time Deposits .....	4,153,640	6.76
GNMAs	3	0.00
Commercial Paper .....	4,099,200	6.67
FHLMC/REMICs	242,733	0.39
AB 55 Loans	232,676	0.38
Loans per Government Code .....	964,400	1.57
Other (International Bank for Reconstruction and Development Bonds) .....	399,962	0.65
Total	<u>\$61,451,668</u>	<u>100.00%</u>

(1) May not sum due to rounding.

Source: State of California, Office of the State Treasurer.

The State's treasury operations are managed in compliance with the California Government Code and according to a statement of investment policy that sets forth permitted investment vehicles, liquidity parameters and maximum maturity of investments. The PMIA operates with the oversight of the Pooled Money Investment Board (consisting of the State Treasurer, the State Controller and the Director of Finance). The LAIF portion of the PMIA operates with the oversight of the Local Agency Investment Advisory Board (consisting of the State Treasurer and four other appointed members).

The PMIA is not now invested, nor has it ever been invested, in structured investment vehicles or collateralized debt obligations. The PMIA Portfolio performance and the PMIA's holdings are displayed quarterly on the State Treasurer's website and may be accessed under PMIB Quarterly Reports. The PMIA does not currently invest in auction rate securities.

The State Treasurer does not invest in leveraged products or inverse floating rate securities. The investment policy permits the use of reverse repurchase agreements subject to limits of no more than 10 percent of the total amount in the PMIA. All reverse repurchase agreements are cash matched either to the maturity of the reinvestment or an adequately positive cash management date which is approximate to the maturity of the reinvestment.

The average life of the investment portfolio of the PMIA as of January 31, 2013 was 226 days.

As of January 31, 2013, the Department had approximately \$487,087,000 invested in the PMIA. The moneys consist of Contractor payments to the Department, which are invested on a short-term basis until they are expended for their designated purpose, replacement reserves, construction funds and debt service reserves.

# CALIFORNIA STATE WATER PROJECT

## Introduction

The State Water Project is one of the largest water supply projects undertaken in the history of water development and encompasses a complex of dams, reservoirs, pumping plants, powerplants, aqueducts and pipelines owned and operated by the State. The Department is responsible for the planning, construction and operation of the State Water Project. After a construction program that commenced in 1957, the project is now providing water to all 29 Contractors. Under the Water Supply Contracts presently in effect, the Contractors may request from the State Water Project maximum annual delivery amounts totaling 4,172,786 acre-feet. (See "THE WATER SUPPLY CONTRACTS.") An acre-foot is the amount of water that will cover one acre of land to a depth of one foot, and is equivalent to 325,900 gallons. However, the amount of water that may be made available for delivery by the State Water Project in any year will depend on various factors, and the Water Supply Contracts provide for reductions in water deliveries if the total amount available for delivery is insufficient to satisfy all Contractor requests. (See "STATE WATER PROJECT WATER SUPPLY.")

More than two-thirds of California's natural water supply originates in the northern third of the State, but more than three-quarters of the demand for water is in the southern two-thirds, which includes the San Francisco Bay area, the San Joaquin Valley, the central California coast and Southern California. The State Water Project was developed in order to deliver water to areas of need throughout the State for domestic, industrial and agricultural purposes, as well as to provide flood control, recreation, fish and wildlife enhancement, hydroelectric power and other benefits.

The State Water Project includes aqueducts, dams and reservoirs, pumping plants, hydroelectric generating facilities and other power plants. The State Water Project does not include any water treatment facilities or any desalination or other facilities for the production of water.

Portions of the State Water Project system consist of facilities developed and used jointly with the federal Central Valley Project operated by the U.S. Bureau of Reclamation (the "Bureau.") In addition, both projects have primary sources of water north of the Delta, transport water across the Delta, and draw water from the southern edge of the Delta. The federal Central Valley Project, like the State Water Project, provides water for irrigation in the Central Valley, urban water supply, water quality, flood control, power, recreation, and fish and wildlife enhancement. Costs for the jointly developed facilities are shared, with approximately 55 percent being paid by the State and 45 percent being paid by the federal government. In 1986, the Department and the Bureau entered into a Coordinated Operation Agreement (the "COA") under which the State Water Project and the federal Central Valley Project coordinate operations, including releases from upstream reservoirs and pumping from the Delta. The COA permits increased operational efficiency for both projects, ensures that each project receives an equitable share of available surplus water, and provides for sharing responsibilities in meeting certain Delta water quality standards.

## Aqueduct System; Pumping Facilities

All 647 miles of the initially planned aqueduct system have been completed. With the addition of the Grizzly Valley pipeline, the Thermalito Powerplant power canal and tail channel, and the extension of the East Branch aqueduct, the entire aqueduct system totals 705 miles. The main stem of the aqueduct system, the California Aqueduct, is 443 miles in length and transports water from the delta formed by the confluence of the Sacramento and San Joaquin Rivers (the "Delta") through the Central Valley of California, over the Tehachapi Mountains and then into Southern California. Major branch aqueducts include the 28-mile North Bay Aqueduct north of the San Francisco Bay, the 45-mile South Bay Aqueduct in the southern San Francisco Bay area, the 116-mile Coastal Branch aqueduct from the southern San Joaquin Valley over the coastal mountains to the central California coast north of Los Angeles, the 32-mile West Branch aqueduct in Southern California and the 33-mile extension of the East Branch aqueduct in Southern California. Aqueducts consist primarily of open

concrete lined canals, siphons and underground pipelines. The main stem of the California Aqueduct has 381 miles of canals and siphons, 49 miles of pipelines or tunnels and 13 miles of channels and reservoirs. The branch aqueducts are mostly pipelines and tunnels rather than canals.

State Water Project facilities also include 20 pumping plants and stations, four pumping-generating plants, and five hydroelectric powerplants.

See the fold-out entitled “State Water Project Facilities” at the end of this Official Statement.

### **Storage Facilities**

State Water Project facilities include 34 storage facilities of which 21 are primary reservoirs and lakes. Reservoirs are used to provide long term water storage, manage State Water Project water flows, provide recreation, and generate power.

See the fold-out entitled “State Water Project Facilities” at the end of this Official Statement.

The Department’s Division of Dam Safety routinely inspects operating dams and may impose operating restrictions on dams and reservoirs that could adversely affect the operation of the State Water Project. One State Water Project dam, Perris Dam, is subject to a Division of Dam Safety order. (See APPENDIX I – “WATER SYSTEM PROJECTS – Project Descriptions – *Perris Dam Remediation Program.*”)

### **Power Resources**

State Water Project facilities include a number of power generation and transmission resources. (See “POWER OPERATIONS OF THE STATE WATER PROJECT.”)

### **Operational Control**

The Department schedules and controls the operation of the State Water Project from a central operations center. This central operations center uses the communication and Supervisory Control and Data Acquisition (“SCADA”) systems to monitor and control the water and power movements in the aqueducts, pipelines and tunnels of the State Water Project in addition to the 29 pumping and generating plants of the State Water Project. Both the SCADA and communication systems are currently being upgraded and such upgrading is expected to be completed over the next five years. When complete the central operations center will continuously monitor and have remote control capability for all State Water Project facilities. Remote operations include start-up and shut down of pumping and generating units and opening or closing of gates and valves which control the flow of water throughout the State Water Project. However, under emergency or back-up operation mode, the operations of each field division are handled at the local field division level.

### **Seismic Considerations**

State Water Project facilities are designed to withstand earthquakes without major damage, in accordance with State Division of Safety of Dams criteria. Dams, for example, are designed to accommodate movement along their foundations and to resist earthquake forces on their embankments. Earthquake loads have been taken into consideration in the design of project facilities such as pumping plants and powerplants.

Major portions of the California Aqueduct are located parallel to and near the San Andreas Fault and other faults. All major faults are crossed either by canal at ground level or by pipeline at very shallow depths, to ease repair in case of damage from movement along a fault. The location of check structures on the canal allows for hydraulic isolation of any fault crossing repair.

Since the Loma Prieta earthquake of October 1989, eight earthquakes of Richter-scale magnitude of 6.5 or greater have occurred in or near California. Other than slight damage caused by the 6.7 Richter-scale magnitude Northridge earthquake of January 1994, no known damage to the State Water Project has been caused by an earthquake. Under the Water Supply Contracts, the Contractors are required to continue making all payments to the Department when due despite any interruption in water supply due to an earthquake.

A major seismic event causing damage to State Water Project facilities could disrupt the operation of the State Water Project or require significant unexpected capital expenditures. Central Valley and Delta levees could also be impacted by such an event. (See “STATE WATER PROJECT WATER SUPPLY – Central Valley and Delta Levees.”)

### **Self-Insurance; Financing of Emergency Repairs**

The State does not maintain commercial insurance for the State Water Project other than a portion of its Reid Gardner Project, nor does it maintain a funded insurance reserve. However, the Department maintains a replacement reserve, currently in the approximate amount of \$35.15 million, which it uses to replace certain equipment periodically. The Department is authorized to issue bonds, payable from available revenues or federal reimbursements under the National Disaster Act, for the purpose of providing funds for emergency repairs to power projects or State Water Project facilities necessitated by natural disasters, provided that certain conditions can be met and certain certifications can be made.

### **Security Efforts; Emergency Preparedness**

Department operations staff and security personnel undertake security efforts to safeguard the infrastructure, key facilities, information technology systems, personnel and the water supply of the State Water Project. Security measures include restrictions on public access to recreational and other State Water Project facilities, monitoring of State Water Project facilities, aerial surveillance of the aqueduct system, a comprehensive security assessment and a State Water Project-wide security plan.

The Department coordinates its security efforts with the California Emergency Management Agency and various State and federal law enforcement agencies as a matter of routine security procedure, and coordinates with other water, health, environmental and public safety agencies as needed. In addition, the Department is a participant on various California Emergency Management Agency committees.

Although the Department has undertaken many emergency preparedness and security improvements, a terrorist attack or significant natural disaster could materially impair system operations and water deliveries.

### **Environmental Considerations**

Projects undertaken by the Department are generally subject to the California Environmental Quality Act (“CEQA”) and certain projects involving the participation of the Bureau or other federal agencies are also subject to the National Environmental Policy Act of 1969, as amended (42 U.S.C. Section 4321).

Under CEQA, a project that may have a significant effect on the environment and is to be carried out or approved by a public agency must comply with a comprehensive environmental review process, including the preparation of an Environmental Impact Report (“EIR”). The EIR reflects not only an independent technical analysis of the project’s potential impacts, but also the comments of other agencies with some form of jurisdiction over the project and the comments of interested members of the public. Contents of the EIR include a detailed statement of the project’s significant environmental effects; any such effects that cannot be avoided if the project is implemented; mitigation measures proposed to minimize such effects; alternatives to the proposed project; the relationship between local and short-term uses and long-term productivity; any significant

irreversible environmental changes that would result from the project; the project's growth-inducing impacts; and a brief statement setting forth the agency's reasons for determining that certain effects are not significant and hence do not require discussion in the EIR. Before approving a project the agency must make findings on whether or how it can mitigate the significant environmental effects of the project. If the agency requires mitigation, the agency must adopt a mitigation monitoring plan to determine whether the mitigation is carried out during project implementation. If the agency determines that the project itself will not have a significant effect on the environment, it may adopt a written statement (called a negative declaration) to that effect and need not prepare an EIR. After deciding to approve or carry out a project, either following the EIR process or after adopting a negative declaration, the agency must file notice of such determination. Any action or proceeding challenging the agency's determination must be brought within 30 days following the filing of such notice. Actions have been, and in the future may be, filed against the Department challenging the Department's compliance with CEQA, including the adequacy of the EIR or other environmental documents, for a particular project. If the action is successful, the particular project could be delayed, revised, suspended or canceled. CEQA also contains a number of exemptions, which the Department uses for its projects when appropriate.

As part of its regular planning and budgetary process, the Department gives careful attention to environmental considerations. All projects are evaluated under the Department's environmental impact review procedures, developed in compliance with federal and State laws and regulations.

## **STATE WATER PROJECT WATER SUPPLY**

### **General**

Under the Water Supply Contracts, the charges payable by the Contractors are generally computed to enable the Department to recover its costs, including debt service on the Bonds when due. Such charges will vary with the amount of water delivered only to the extent that the amount of water delivered has an effect on the variable operation and maintenance costs of the State Water Project. The Contractors' obligations to make payments in amounts sufficient to pay debt service on the Bonds is not conditioned on the amount of water delivered. (See "SECURITY FOR THE BONDS – Sources of Revenues" and "THE WATER SUPPLY CONTRACTS.") However, the Department is obligated under its Water Supply Contracts, subject to the availability of funds, to make all reasonable efforts, consistent with sound fiscal policies, reasonable construction schedules and proper operating procedures, to complete the project facilities necessary to make water deliveries at the time and in the amounts specified in the Water Supply Contracts. This section describes the historical water supply available for delivery by the State Water Project and certain factors that have had or may in the future have an effect on the availability of such water supply. The Department can give no assurances that future legislation or regulation in any of the areas discussed in this section will not affect State Water Project operations including, but not limited to, reductions in the water supply available to the State Water Project.

### **Annual Water Deliveries**

The annual water supply available for delivery by the State Water Project will vary from year to year depending on many factors including hydrologic conditions. The Department's annual determination of the State Water Project's delivery capability is based on extensive and ongoing analyses of operational capability taking into account (i) storage levels at the beginning of the year, (ii) target storage levels at the end of the year, (iii) the actual amount of snow and rainfall that has occurred to date in the year and a conservative estimate of the amount of snow and rainfall that may occur over the remainder of the year, (iv) the operational capacity of State Water Project facilities, and (v) operational mandates for in-stream water requirements and environmental protection of the Delta as imposed by federal and state regulatory agencies. Using this procedure, the Department has been able to meet the following percentages of Contractor requests for each of the last ten years:

**Annual Water Deliveries of the State Water Project  
as a Percentage of Contractor Requests**

Year	Percentage of Contractor Requests Delivered <sup>(1)</sup>
2003	90%
2004	65
2005	90
2006	100
2007	60
2008	35
2009	40
2010	50
2011	80
2012	65

<sup>(1)</sup> The annual water delivery for each calendar year is determined in the Spring of that year and based on hydrological conditions at the time of determination and other factors as described in the preceding paragraph.

The delivery of less than 100 percent of Contractor requests in nine of the ten years listed in the preceding table reflect the impact of one or more of the factors listed in the preceding paragraph affecting the Department’s annual determination of the State Water Project’s delivery capability in each such year.

According to the State Water Project Delivery Reliability Report 2011, dated June 2011, the Department estimates that if annual precipitation conditions vary in the same manner as they have over the eighty-two year period of analysis (water-years 1922-2003, a water-year consists of twelve consecutive calendar months beginning with the month of October), the State Water Project would be capable of delivering at least 2,400,000 acre-feet of water in approximately 75 percent of the water-years, at least 2,700,000 acre-feet of water in approximately 50 percent of the water-years, and at least 2,900,000 acre-feet of water in approximately 25 percent of the water-years. Under the Water Supply Contracts presently in effect, the Contractors may request from the State Water Project maximum annual delivery amounts totaling 4,172,786 acre-feet. The maximum annual delivery amounts were established when the Water Supply Contracts were executed and delivered, prior to the final determination of the scope of the State Water Project.

**State and Federal Regulations Affecting the State Water Project**

The following subsections describe certain state and federal regulation of the State Water Project and related litigation that could impact the ability of the Department to deliver water to the Contractors. The Contractors’ obligations to make payments in amounts sufficient to pay debt service on the Bonds is not conditioned on the amount of water delivered. (See “SECURITY FOR THE BONDS – Source of Revenues” and “THE WATER SUPPLY CONTRACTS” and “STATE WATER PROJECT WATER SUPPLY– General.”)

*Bay-Delta Water Rights and Water Quality Regulation.* The State Water Project diverts unregulated flow, and rediverts water it has stored upstream and later released into the Feather River, from the Delta. The Delta is also the source of water for local agricultural, municipal and industrial needs, and, in addition, supports significant resident and anadromous fish and wildlife resources and important recreational uses of water. Both the State Water Project’s upstream reservoir operations and its Delta diversions can at times affect these other uses of Delta water directly, or indirectly, through impacts on Delta water quality.

The State Water Resources Control Board (the “SWRCB”) has historically been responsible for regulating the State Water Project (along with the federal Central Valley Project operated by the Bureau) under the SWRCB’s water quality and water rights authorities to protect the reasonable needs of all uses of Delta waters. In this regard, in 1995, the SWRCB adopted a Water Quality Control Plan for the Bay-Delta estuary and in March 2000, the SWRCB implemented the 1995 Water Quality Control Plan through a water rights decision known as “D 1641.” D 1641 requires the State Water Project and the federal Central Valley Project to meet the 1995 Water Quality Control Plan’s numeric objectives for maintaining water quality. In addition, D 1641 recognizes a settlement (known as the “Sacramento Valley Water Management Program”) among the Department, Bureau, export contractors and upstream Sacramento Valley water users under which the parties have agreed to develop additional supplies of water for local use, for Delta protection, and for State Water Project and federal Central Valley Project use. The Department and the Bureau are responsible for preparing a draft Environmental Impact Report/Environmental Impact Statement that is required before approving actions to implement the settlement. However, work on the environmental document is on hold pending discussions among the various parties regarding how to proceed. In December 2006, the SWRCB approved a 2006 Bay-Delta Water Quality Control Plan (the “2006 Plan”), which supersedes the 1995 Water Quality Control Plan. The SWRCB is currently in the process of updating the 2006 Plan as described herein.

In February 2006, the SWRCB ordered the Department and the Bureau to take corrective actions to address threatened violations of their respective water rights permits implementing the southern Delta summer water quality objective for agricultural uses. Under this action, the Department and Bureau were to provide a schedule to the SWRCB of the proposed construction and operation of permanent operable gates in the southern Delta to help improve water quality. Other requirements of the enforcement action addressed the extent of the obligations of the State Water Project and federal Central Valley Project to protect water quality in the southern Delta. In response to a lawsuit filed against the SWRCB by the Bureau, certain Contractors and certain federal water contractors, the SWRCB clarified the enforcement order and the parties to the lawsuit entered into a stipulation for dismissal without prejudice and a tolling agreement, which extends to April 30, 2014. In addition, a June 2009 federal biological opinion for salmon, steelhead trout and green sturgeon states that DWR shall not implement the permanent operable gates because that project would adversely modify critical habitat. As a result, in January, 2010, the SWRCB issued an order that modified its February, 2006 enforcement order by, among other things, allowing the Department and the Bureau to defer the construction of the permanent operable gates and requiring the Department and the Bureau to conduct studies and consider other measures to address water quality in the southern Delta until the SWRCB issues a new water quality control plan and related water rights decision for the Delta.

In December 2007, the SWRCB adopted a resolution setting out a process for the review of beneficial uses in the Delta in response to scientific studies showing a decline in native species and in support of the current efforts of the Bay-Delta Conservation Plan Steering Committee and Delta Vision Task Force to develop plans to improve the Delta ecosystem. (See “STATE WATER PROJECT WATER SUPPLY – Long Term Planning Efforts for the Delta,” “– *The Delta Vision*” and “– *Bay Delta Conservation Plan*.”) In accordance with the resolution, in July 2008 the SWRCB adopted the Strategic Workplan for Activities in the San Francisco Bay/Sacramento-San Joaquin Delta Estuary (the “Strategic Workplan”) that describes a number of activities the SWRCB and Regional Water Quality Control Boards intend to pursue to address the water supply and environmental situation in the Bay-Delta. The Strategic Workplan activities are responsive to priorities identified by the Delta Vision Task Force, build on existing processes, such as the Bay-Delta Conservation Plan, and identify a wide range of flow-related and water quality actions to better protect the Bay-Delta. The Strategic Workplan includes plans to review and update the 2006 Plan and to review the Bay-Delta Conservation Plan, water rights, and other requirements to protect fish and wildlife beneficial uses. In February 2009, in furtherance of the Strategic Workplan, the SWRCB began the process to review and update the southern Delta salinity and San Joaquin River flow objectives, and their program of implementation. As part of this process, the SWRCB is preparing environmental documents to evaluate the effects of potential modifications to the southern Delta salinity and San Joaquin River flow objectives and is considering adopting

related amendments to the 2006 Plan. In January 2012, also in furtherance of the Strategic Workplan, the SWRCB began the process to review and update the other aspects of the 2006 Plan, which will include an environmental review of the effects of any proposed changes to the 2006 Plan.

In September 2010, three environmental groups filed a lawsuit against the SWRCB and the Department in State court, challenging the Department's operations in the Delta on a variety of theories, including alleged violations of the public trust doctrine, D 1641 and the State Constitutional provision regarding reasonable use of water. The complaint claims that these violations have led to the recent decline of certain Delta fish species. The plaintiffs are asking the Court to declare that the SWRCB and the Department have violated the provisions and doctrine cited in the complaint and to enjoin the Department from diverting water from the Delta while these alleged violations persist. This lawsuit is in the pre-trial stage.

In July 2011, an organization representing twenty-seven Contractors filed a lawsuit against the State Water Resources Control Board and the Central Valley Regional Water Quality Control Board challenging an amendment to the Sacramento-San Joaquin Delta Basin Plan regarding the control in the Delta of methylmercury, a chemical which can be harmful to fish. The amendment, among other things, assigns certain responsibilities jointly to the Department (with regard to both the State Water Project and the Department's flood management programs), the Central Valley Flood Protection Board and the State Lands Commission to control methylmercury in the open waters of the Delta in two phases. Phase I, which lasts for up to nine years, emphasizes studies and pilot projects to control methylmercury and Phase II requires implementation of measures to achieve required methylmercury levels by 2030. The Department was named as a real party in interest in the lawsuit. The Contractors contend that since the Department's State Water Project activities do not add or introduce methylmercury into the open waters of the Delta, there is no basis in law for assigning such responsibility to the Department in its capacity as operator of the State Water Project. This lawsuit is in the pre-trial stage.

*Federal Endangered Species Act: General.* The Department joins the Bureau in consultations with the US Fish and Wildlife Service ("USFWS") and the National Oceanic and Atmospheric Administration-Fisheries ("NOAA") regarding the impacts to endangered fish species from the operations of the State Water Project and federal Central Valley Project. This process results in the issuance of biological opinions pursuant to the Endangered Species Act ("ESA"). These biological opinions update, extend, and consolidate prior opinions and authorize the incidental taking of the listed species of fish by the two projects. Biological opinions are generally valid until changed conditions or new listings of species would require re-initiation of consultation.

*Federal Endangered Species Act: Delta Smelt.* In December 2008, the USFWS issued a Biological Opinion for Delta smelt and related water projects operations ("2008 Biological Opinion"), which superseded a previously issued Delta smelt biological opinion. The issuance of the 2008 Biological Opinion is now the operation-criteria for the federal Central Valley Project and State Water Project. The 2008 Biological Opinion requires operational measures to protect Delta smelt and, in addition, includes a measure specifying certain water flow requirements in the Delta during the fall season in wet years. This fall measure requires the two water projects to control salinity incursion in the Delta through increased water releases from water storage and fewer water diversions during wet years.

In March 2009, two water agencies that receive water from the federal Central Valley Project and an organization representing 27 State Water Project Contractors filed separate lawsuits against the USFWS challenging the 2008 Delta smelt Biological Opinion as being too restrictive regarding pumping water from the Delta. The Department has intervened as a plaintiff in these cases, which have been consolidated and are now called the "Delta Smelt Cases." In October 2009, a hearing was held on plaintiffs' summary judgment motions challenging the validity of the 2008 Biological Opinion. In November 2009, the Court ruled in favor of plaintiffs on one issue in their summary judgment motion that the 2008 Biological Opinion requires compliance with the National Environmental Policy Act ("NEPA") and that the Bureau is the appropriate federal agency to



prepare the environmental documentation. In December 2010, the court issued a decision that remanded the 2008 Biological Opinion to the USFWS to explain its scientific conclusions that the Court found to be arbitrary. These items included river flow issues. Both the November 2009 and December 2010 Court decisions have been appealed by parties on both sides of the lawsuits, and the hearing on these appeals was held in September 2012, but no decision has yet been issued. The USFWS issued a new draft Biological Opinion for Delta smelt in November 2011 and will conduct an environmental review under NEPA in the next two years. A new final Biological Opinion will be issued after the NEPA process has concluded.

*Federal Endangered Species Act: Salmon, Steelhead Trout and Green Sturgeon.* In June 2009, following consultation with the Department and Bureau, NOAAF issued a new salmon, steelhead trout and green sturgeon Biological Opinion (“2009 Biological Opinion”), which superseded a previously issued biological opinion for these fish species. The 2009 Biological Opinion imposes restrictions on the Department’s pumping and operational activities in the Delta based upon the level of flows from the San Joaquin River and the presence of salmon and steelhead trout in the vicinity of the Delta pumping plant.

Six separate lawsuits were filed in federal court against NOAAF challenging the 2009 Biological Opinion as being too restrictive on the grounds that the measures to protect the fish are not supported by the best available science. State Water Contractors, federal water contractors and local water districts were among the plaintiff’s filing the lawsuits. The Department intervened as a plaintiff in these cases which were consolidated. In May, 2010, the Court ruled in favor of plaintiffs’ motion for a preliminary injunction that sought to enjoin two operational constraints limiting Delta pumping in 2010. The Court enjoined the two constraints, which allowed an increase in Delta pumping during May and June 2010. The Court also ruled in favor of plaintiffs that the 2009 Biological Opinion requires compliance with the National Environmental Policy Act and that the Bureau is the appropriate federal agency to prepare the environmental documentation. In December 2011, the Court issued its judgment regarding plaintiffs’ and Department’s summary judgment motions which challenged the 2009 Biological Opinion. The Court, having found that the biological opinion was not adequately supported in certain respects, remanded the opinion back to NOAAF and ordered the agency to issue a new final biological opinion by February 2016. NOAAF is expected to issue a revised draft biological opinion as the next step in response to the Court’s order and to conduct an environmental review under NEPA thereafter. In the meantime, the 2009 Biological Opinion remains in effect, although in January and February 2012 parties on both sides of the lawsuits appealed the Court’s decisions. A hearing on these appeals is expected to be set after briefing is completed in April 2013. There are also certain seasonal export restrictions in the 2009 Biological Opinion that become operative at various times from January through June each year, and therefore there may be a hearing or other proceeding regarding permissible interim operations during the period that NOAAF is redrafting the opinion and during the pendency of the appeals.

*Federal Endangered Species Act: Longfin Smelt.* In April 2012, the USFWS found that the longfin smelt warrants consideration for protection under the ESA, but that it is currently precluded from listing the species because of the need to address other higher priority species. As a result, the USFWS has added the longfin smelt to the list of candidates for ESA protection, where the status will be reviewed annually. In the meantime there will be no requirements or restrictions regarding the longfin smelt imposed under the ESA. The longfin smelt is listed as threatened under the California Endangered Species Act (“CESA”) and the Department is already taking actions to protect the longfin smelt consistent with the take permit the Department received from the California Department of Fish and Wildlife (formerly known as California Department of Fish and Game) (“DFW”). (See “STATE WATER PROJECT WATER SUPPLY – State and Federal Regulations Affecting the State Water Project – *State Endangered Species Act.*”)

*State Endangered Species Act.* To obtain the authority under the CESA to “take” Delta smelt and salmon, the Department requested a “consistency determination” from DFW for the federal Delta smelt Biological Opinion and for the federal salmon Biological Opinion. In July 2009, DFW issued its determination that the federal Delta smelt Biological Opinion was consistent with CESA and in September 2009, that the

federal salmon Biological Opinion was consistent with CESA. In late 2009, various Contractors filed three lawsuits regarding DFW's consistency determinations issued to the Department. These lawsuits challenge the need for the Department to obtain any authorization from DFW under CESA and challenge the consistency determinations as containing overly restrictive conditions pertaining to State Water Project operations in the Delta. The consistency determination cases have been stayed pending the outcome of lawsuits challenging the federal Delta smelt Biological Opinion and the federal salmon Biological Opinion (See "STATE WATER PROJECT WATER SUPPLY – State and Federal Regulations Affecting the State Water Project – *Federal Endangered Species Act: Delta Smelt*" and "– *Federal Endangered Species Act: Salmon, Steelhead Trout and Green Sturgeon.*")

In March 2009, the Commission also formally listed the longfin smelt, which resides in the Delta, as a threatened species under CESA. The DFW has granted the Department an incidental "take" permit for longfin smelt under CESA, which will continue in effect through December 2018. The permit incorporates the 2008 Biological Opinion for Delta smelt as an element of the take permit for longfin smelt. As a result, under most conditions, when certain flow restrictions for the protection of Delta smelt are being implemented, the permit imposes no additional requirements for the protection of adult longfin smelt. However, under the permit, the presence of adult or larval longfin smelt at certain locations during certain times of the year could cause a reduction in State Water Project water deliveries.

Both the consistency determinations for Delta smelt and salmon and the incidental take permit for longfin smelt incorporate conditions from the federal Biological Opinions for Delta smelt and salmon. The Department monitors activities in the federal cases and works with DFW to assure that the Department retains CESA compliance for its State Water Project operations. (See "STATE WATER PROJECT WATER SUPPLY – State and Federal Regulations Affecting the State Water Project – *Federal Endangered Species Act: Delta Smelt*" and "– *Federal Endangered Species Act: Salmon, Steelhead Trout and Green Sturgeon.*")

### **Long-Term Planning Efforts for the Delta**

The activities and programs described in this section "Long-Term Planning Efforts for the Delta" build on prior activities and programs, including the CALFED Bay-Delta Program begun in 1995 with the participation of various State and federal agencies, as well as California's environmental, urban and agricultural communities, to develop long-term, collectively-negotiated solutions to the environmental and water management issues concerning the Delta.

*The Delta Vision.* In 2006 Governor Arnold Schwarzenegger established a task force to develop a long-term sustainable vision for the Delta. The task force issued a Delta Vision strategic plan in November 2008 and an implementation report for the strategic plan in January 2009, which included specific recommendations to the Governor. Fundamental actions in the plan include developing a new system of dual water conveyance through and around the Delta, additional water storage projects, an emergency preparedness strategy and water conservation goals, restoring the ecosystem and establishing a Delta governance structure. The task force also created a non-profit organization, the Delta Vision Foundation, following the conclusion of their recommendations to the Governor. The new organization provides updates to the public on its view of the progress of the Delta Vision's implementation.

*Delta Stewardship Council and Related Legislation.* The Delta Stewardship Council was created as part of a special legislative package, enacted in November 2009. The legislative package addressed California's statewide water situation, with particular emphasis on the Delta. The package included an \$11.1 billion general obligation bond measure. See "STATE WATER PROJECT WATER SUPPLY – Statewide Water Considerations – *Sources of Funding for Water Related Improvements*" below. The Delta Stewardship Council is charged with developing and implementing a Delta Plan, which will include the BDCP (defined in the next paragraph) once the BDCP is approved as meeting federal and State ESA requirements. The Delta Protection

Commission, which is a State agency with certain land use responsibilities in the Delta, was directed in the same legislation to prepare an economic sustainability plan for the Delta and to provide information and recommendations to the Delta Stewardship Council. In 2012, the Delta Protection Commission completed the economic sustainability plan and provided its recommendations to the Council. The Council has developed and circulated drafts of the Delta Plan for public comment and is now conducting environmental review for the Delta Plan. The Delta Plan is currently scheduled to be adopted in late 2013. In January 2013, the Council held a hearing on proposed regulations related to the Delta Plan. The Sacramento-San Joaquin Delta Conservancy, which was also established through the legislative package, will be implementing ecosystem restoration activities in the Delta based on a strategic plan that it has adopted. In addition, the package included separate bills that address groundwater, water conservation and unauthorized Delta water diversions.

*Bay Delta Conservation Plan.* An approach, known as the Bay Delta Conservation Plan (“BDCP”), is being developed to promote the recovery of endangered, threatened and sensitive fish and wildlife species and their habitats in the Delta in a way that will also protect and restore water supplies and address water conveyance through the Delta. The BDCP is intended to establish long-term regulatory coverage for up to 50 years for the State Water Project and federal Central Valley Project through permits issued under section 10 of the ESA, known as a Habitat Conservation Plan.

As part of the information gathering process for the BDCP, the Department sought permission to access Delta properties for the purposes of environmental surveys and geotechnical exploration. Beginning in 2008, the Department filed petitions in court to gain access to the property of owners who had not granted permission. In early 2011, the trial court allowed access for Department environmental surveys, but denied access for the geotechnical exploration, which includes drilling activities. The property owners have appealed the order allowing environmental surveys on their property and the Department has appealed the order denying access for geological exploration. Both appeals are pending before a State appellate court. In October 2010, a lawsuit was filed challenging the Department’s environmental compliance and seeking to enjoin certain of the Department’s geologic activities in the Delta. After holding a hearing on the merits, the trial court ruled in November 2011 in favor of the Department and rejected the plaintiffs’ challenge. As a result, the Department has continued to conduct geologic activities in water and on properties to which the Department has access.

In October 2010, the Department entered into an agreement with DFW to coordinate efforts regarding the Department’s expenditure of approximately \$188 million over ten years for certain habitat restoration activities. These activities are intended to satisfy State and federal ESA habitat restoration requirements, as well as the restoration component for the proposed BDCP.

In December 2010, (after three years of collaboration meetings) the California Natural Resources Agency published a document describing a conceptual BDCP for further evaluation during 2011, as well as a draft BDCP. A refined draft BDCP based on further modeling and analysis was then developed. The plan and environmental review will include analysis of strategies and measures to promote and improve the overall ecological health of the Delta and the species that inhabit the Delta and the analysis of water conveyance options including conveyance through Delta channels and/or new alternative conveyance, such as a canal or tunnel. On July 25, 2012, Governor Jerry Brown and U.S. Secretary of Interior Ken Salazar announced State and federal government support of a proposed project involving a tunnel conveyance system to be analyzed along with other alternatives in the environmental review process. The costs of any conveyance system, if ultimately approved and constructed through the BDCP process, could be substantial. Such conveyance system costs would be expected to be paid by users and beneficiaries of the conveyance system, but no determination has been made as to the method of financing or the allocation of responsibility for such costs. A public review process of the draft BDCP and EIR/EIS is scheduled for mid-2013.

## **Central Valley and Delta Levees**

*General.* Water delivered to Southern California through the State Water Project must traverse the Delta through channels protected by levees that are susceptible to major failures due to flood and seismic events. If a major levee failure were to occur in the Delta or on the Sacramento River flood control system, it could adversely affect the ability of the Department to deliver State Water Project water through the Delta. In the event of such a failure, the quality of the Delta's water could be compromised from an increase in salinity and other adverse water quality conditions caused by an influx of water from the San Francisco Bay and could result in curtailing pumping of State Water Project water from the Delta southward to the Central Valley and Southern California. After Governor Arnold Schwarzenegger declared an emergency in 2006 for California's Central Valley levee system, including the Delta and Sacramento River flood control systems, the Department and U.S. Army Corps of Engineers repaired over 100 critical erosion sites. The Department has continued to evaluate and, as necessary, take action to repair other sites. In 2006, California voters approved Proposition 1E (the Disaster Preparedness and Flood Prevention Bond Act of 2006) and Proposition 84 (the Safe Drinking Water, Water Quality and Supply, Flood Control, River and Coastal Protection Bond Act of 2006), which together provide funding through the issuance of general obligation bonds to improve the State's flood management programs and infrastructure, including levees in the Delta and levees and structures of the Sacramento River flood control system. In addition, the Department, through the Delta Flood Control Program, has funded significant repairs and improvements to the Delta levee system. In December 2011, the Department, as required by statute with regard to its flood management responsibilities, completed a Central Valley Flood Protection Plan that analyzes flood risks and potential measures to address those risks in the Delta and in certain other areas of the California Central Valley. The Central Valley Flood Protection Board adopted the Central Valley Flood Protection Plan in June 2012.

*Lawsuits Regarding 2004 Delta Levee Failure.* Four lawsuits have been filed to recover damages caused when a Delta levee failed and flooded the Upper Jones Tract and Lower Jones Tract in June 2004. Three of the lawsuits name as defendants a local Delta reclamation district, the State Reclamation Board and the Department. A cause of action in each of these three lawsuits alleges that the State Water Project's operations and activities in the Delta were a cause of the damage. All four lawsuits were consolidated for trial and after completion of the trial, the trial judge issued a decision in August 2012 in favor of the Department. In October 2012, the plaintiffs, with the exception of two insurance companies, appealed the decision. The Department does not believe that an adverse court decision in any of these consolidated cases would have a material adverse impact on State Water Project finances or operations.

*Lawsuit Regarding North Delta/Mokelumne River Sedimentation.* In February 2008, a local reclamation district and a large landowner with property bordering the Mokelumne River in the North Delta brought suit against three State agencies with flood management responsibilities in the Delta, including the Department. The suit alleges that sedimentation has been allowed to build up in the Mokelumne River and in adjacent channels due to a lack of dredging by the defendant State agencies and to State Water Project water conveyance operations in the Delta and that such buildup presents an unreasonable risk of flooding to the landowner's property and other property in the North Delta. The lawsuit also alleges that the Department is breaching its contract with the North Delta Water Agency regarding State Water Project water flows through the North Delta. The suit seeks injunctive and declaratory relief to require remedial actions to be taken. The trial in the case began in January 2013. The Department believes that even if the lawsuit is successful, it will not have a material adverse impact on State Water Project finances or operations.

## **Statewide Water Considerations**

*Sources of Funding for Water Related Improvements.* In 1992, Congress enacted the Central Valley Project Improvement Act (the "CVPIA"), which required, among other things, many environmental restoration studies and projects, the cost of which is to be shared by the federal government and the State. In 1994, the

Department entered into a cost sharing agreement with DFW, the Bureau and the USFWS (the “Cost Sharing Agreement”) for those projects. The State’s cost share is approximately \$175 million and is funded by general fund appropriations, general obligation bond financing and other sources. The Department does not expect State Water Project funds to be used for such purpose.

In addition to the CVPIA, California voter-approved measures such as Proposition 13 (the Safe Drinking Water, Clean Water, Watershed Protection and Flood Protection Act, approved in 2000), Proposition 50 (the Water Security, Clean Drinking Water, Coastal and Beach Protection Act of 2002), Proposition 84 (the Safe Drinking Water, Water Quality and Supply, Flood Control, River and Coastal Protection Bond Act of 2006) and Proposition 1E (the Disaster Preparedness and Flood Prevention Bond Act of 2006) have or will require the State to undertake a variety of projects for environmental restoration, water use efficiency and conservation, water supply enhancement and reliability, ecosystem restoration, watershed protection, water conveyance, delta levee restoration and water storage planning and studies. These measures authorize the issuance of State general obligation bonds to fund such projects. In 2009, the California legislature enacted the Safe, Clean, and Reliable Drinking Water Supply Act of 2010, which, if approved by the voters in its current form, would authorize \$11.14 billion in general obligation bonds to fund various water projects and programs. These include projects and programs designed to address regional water supply reliability, Delta ecosystem sustainability, conservation and watershed protection, groundwater and water quality protection, water recycling and statewide water system operational improvements, including surface and groundwater storage projects. This bond measure is currently scheduled to be presented to the voters for their approval in November 2014.

*Programmatic Considerations.* To achieve additional capability of supplying State Water Project water to the Contractors on a dependable basis at levels of acceptable water quality, the Department is considering additional water facilities and additional programs for reservoir and ground water storage, waste water reclamation, and conservation. Alternatives under consideration include (1) new reservoir storage north and south of the Sacramento-San Joaquin Delta, (2) Delta conveyance, (3) conjunctive operation with ground water storage in State Water Project service areas, (4) purchase of water from federal or local developments, and (5) construction of local water supply developments within State Water Project service areas.

*Future Mandates Relating to the Delta.* Water rights issues and environmental regulation with respect to the Delta have been an active area in recent decades. See “State and Federal Regulations Affecting the State Water Project” and “Long Term Planning Efforts for the Delta.”

*Invasive Species.* Zebra and Quagga Mussels are established in the Eastern United States and moved West, establishing in the Colorado River system and an isolated reservoir in Central California. Quagga mussels now infest Metropolitan Water District of Southern California’s Colorado River Aqueduct and associated delivery system in southern California. A population of zebra mussels is established in San Justo Reservoir in central California. Quagga and zebra mussels are now within 25 miles of the State Water Project. The mussels can clog water intakes, trash racks and other protective screens. Once established, the mussels cannot be easily eradicated using current technologies. Mussel management will result in a significant increase in the cost of operation and maintenance of water delivery systems. In addition, there can also be adverse ecological impacts. To prevent the spread of the mussels into the State Water Project, the Delta and other bodies of water and water systems, the Department has joined with DFW, as the lead agency, and other state and federal agencies on a number of activities. These include boat inspections, monitoring of water bodies and water systems and education of the public, especially boat owners and operators. In addition, the Department has developed a Rapid Response Plan and a Vector Management Plan as mandated by the California Fish and Game Code. Lastly, the Department is currently developing a mussel management and control program for the State Water Project.

*Climate Change.* Climate change is likely to impact California water resources. Rising temperatures are, for example, expected to result in more precipitation falling as rain instead of snow resulting in a reduction in the Sierra snowpack. The impact of climate change, along with other potential impacts, could affect the timing and/or amount of annual water supply available for delivery by the State Water Project, increase flood risk and cause other challenges related to delivery and storage of water by the State Water Project. The Department considers the potential impacts of climate change, including greenhouse gas emissions, in its long-term planning efforts and has been working to develop measures to mitigate the potential adverse impact of climate change. The impact of climate change on the operation of the State Water Project and the extent to which the Department will need to take additional actions to address the effects of climate change are uncertain.

## **POWER OPERATIONS OF THE STATE WATER PROJECT**

The State Water Project is one of the largest consumers and suppliers of electric power in the western United States. This section describes the State Water Project's power-related activities. Revenues from the State Water Project's power related activities are not pledged to the payment of the Bonds.

The activities and responsibilities of the California Energy Resources Scheduling Division of the Department (the "CERS Division") in connection with the State's program of supplying electricity to retail customers are separate and distinct from the activities and responsibilities of the Department in connection with the State Water Project. This section describes the CERS Division's power supply activities and historical or recent events concerning those activities only to the extent they affect the State Water Project.

### **Historic Involvement of State Water Project in Power Markets**

Since the commencement of the major facilities of the State Water Project in the 1960's, the Department has been an active participant in the power markets of California and the western United States. The Department currently owns and operates eight power facilities with a total generating capacity of approximately 1,800 MW and with total annual energy generation in recent years ranging between approximately 3,100 and 7,500 GWh. (See "POWER OPERATIONS OF THE STATE WATER PROJECT – Power Generation.") The Department also owns and operates 23 pumping plants with a total load, if all were operational simultaneously, of approximately 2,000 MW and total annual energy consumption in recent years ranging between 5,300 and 10,000 GWh. By way of comparison, the average load for all electricity users in California is approximately 30,000 MW and total 2011 consumption in California, according to the California Energy Commission, is approximately 273,000 GWh.

The pumping plants, which are the State Water Project's major power-consuming components, can be operated principally during the off-peak portion of the daily electricity consumption cycle due to their large pumping capacity. Similarly, the designed capacity of most of the Department's hydroelectric generation facilities permits those facilities to be operated at 100 percent of generation capacity during on-peak hours and generally held idle during off-peak hours. This flexibility in the scheduling of the Department's generation and load enables the Department to sell relatively high value power during on-peak hours and buy less expensive power during off-peak hours, or to do the functional equivalent by entering into contracts to deliver power on demand during on-peak hours in exchange for substantially larger amounts of power delivered to the Department during off-peak hours.

In addition to the eight powerplants it owns, the Department also has long-term contracts for the purchase of power from Pine Flat Powerplant, which is owned and operated by Kings River Conservation District, and five small hydroelectric powerplants, which are owned and operated by the Metropolitan Water District of Southern California.

## Power Generation

The Department has provided for the financing, construction and operation of a variety of power projects including hydroelectric, geothermal and coal-fired electric generating facilities and facilities to transmit electric energy. The table below summarizes current megawatt hour generation, construction costs and completion date for the Department’s power projects.

	<b>Capacity (MW)</b>	<b>Expected Annual Generation (MWh)</b>	<b>Construction Cost in Millions</b>	<b>Completion Date</b>
Alamo Project Powerplant .....	17	114,000	\$ 49.4	1986
Castaic Powerplant.....	214	719,000 <sup>(a)</sup>	82.0	1978
Devil Canyon Powerplant .....	280	1,770,000	198.4	1993
Mojave Siphon Powerplant.....	29	96,000	65.6	1996
Hyatt-Thermalito Complex (Oroville) .....	762	2,202,000	282.0	1987
William E. Warne Powerplant (Pyramid) .....	74	472,000	80.0	1983
Reid Gardner Project <sup>(b)</sup> .....	245	1,280,000 <sup>(a)</sup>	252.8	1983
Gianelli (San Luis) Pumping-Generating Plant.....	222	188,000 <sup>(a)</sup>	47.2	1967

<sup>(a)</sup> State Water Project share.

<sup>(b)</sup> The Reid Gardner Power Plant is operated by NV Energy. The Participation Agreement between the Department and NV Energy for coal-fired energy will not be renewed after it terminates in July 2013. The Department intends to replace a portion of the energy lost by termination of this agreement with energy provided to the Department from the Lodi Energy Center. (See “POWER OPERATIONS OF THE STATE WATER PROJECT – Lodi Energy Center Project.”)

See the fold out entitled “State Water Project Facilities” at the end of this Official Statement.

## Power Sales and Purchases

Periodically, the Department enters into long-term and mid-term energy sales agreements and energy exchange agreements with municipal utilities, private utilities, and other entities that buy or sell energy in California and neighboring states. The Department also transacts with the California Independent System Operator (“CAISO”) in its markets for day-ahead and real-time energy purchases and sales. In addition, the Department sells ancillary services from its generating facilities to the CAISO and buys ancillary services from the CAISO to meet the requirements for its State Water Project pumping plants. These agreements and arrangements with utilities, entities that buy or sell energy, and the CAISO allow the State Water Project to manage its power operations. The table below provides the Department’s historical revenues from power sales and costs of power purchases on an annual basis over the past five calendar years.

<b>Year</b>	<b>Costs of Power Purchases (in millions)</b>	<b>Revenues from Power Sales (in millions)</b>
2008	\$249	\$199
2009	162	110
2010	267	154
2011	271	110
2012	265	81

Because the Department procures significant amounts of electric power for State Water Project operations in the short-term markets for power, it has some exposure to volatility in the electric power market. This exposure is mitigated by the fact that the bulk of the State Water Project’s power needs can be met through Department-owned generation, long term and mid-term power purchase contracts and energy exchange

arrangements. (See “POWER OPERATIONS OF THE STATE WATER PROJECT – Historical Sources of Power for State Water Project Operations.”) It is further mitigated by the fact that the majority of the State Water Project’s power needs are during off-peak periods on the daily energy consumption cycle, when the demand for and the cost of energy are generally lower. (See “POWER OPERATIONS OF THE STATE WATER PROJECT – Historic Involvement of State Water Project in Power Markets.”)

The cost of power for State Water Project operations is paid out of the California Water Resources Development Bond Fund. (See “FINANCIAL OPERATIONS – Allocation of State Water Project Revenues.”) Power costs for State Water Project operations allocable to water supply to the Contractors are passed on to Contractors under the Water Supply Contracts through the variable operation cost component of the Transportation Charge. (See “THE WATER SUPPLY CONTRACTS – Basic Contract – *Water Charges*.”) The Department’s exposure to any volatility in short-term power costs is aggravated by the fact that the variable operation cost component of the Transportation Charge is paid on an estimated basis subject to “true up” approximately two years later. If the Department underestimates power costs in assessing the variable operation cost component, it will typically not recover the difference between actual and estimated costs for approximately two years. (See “THE WATER SUPPLY CONTRACTS – Basic Contract – *Payment of Water Charges*.”) Under the Water Supply Contracts, however, the Department has the option under certain circumstances to revise its billings, and it has exercised that option in the past.

The Department regularly solicits energy purchase, sale and exchange proposals from electric utilities and energy supply companies to address the need for a reliable supply of its Water System Project energy requirements. In addition, the Department has entered into a Power Sales Agreement with Northern California Power Agency and other project participants, reflecting the Department’s participation in the Lodi Energy Center Project to assist it in meeting its power needs. The Department completed an integrated resource plan in 2009 that identified additional strategies to meet its future power needs. (See “POWER OPERATIONS OF THE STATE WATER PROJECT – Lodi Energy Center Project.”)

On balance, the Department does not expect the cost of power to have a material adverse effect on its ability to continue to operate and maintain the State Water Project or on the security for, or the Department’s ability to repay, the Bonds. However, no assurance can be given that the Department will not experience disruptions in State Water Project operations due to future deterioration in the California energy markets.



## Historical Sources of Power for State Water Project Operations

The historical sources of power for operating the State Water Project on a calendar year basis for the years 2008 through 2012 are set forth in the table below. The Department has satisfied its power load through its own resources, long-term purchase and exchange contracts and short-term and spot market purchases, as needed.

	Electrical Energy (millions of kilowatt hours)				
	2008	2009	2010	2011	2012
State Water Project Hydroelectric Plants					
Gianelli (San Luis) .....	140	56	87	74	143
Castaic .....	577	606	442	417	609
Devil Canyon.....	679	554	991	1,291	941
William E. Warne (Pyramid).....	310	280	266	243	355
Hyatt-Thermalito Complex (Oroville)	975	1,427	1,534	2,194	1,622
Alamo .....	65	55	79	105	30
Thermalito Diversion Dam.....	13	23	10	12	21
Mojave Siphon .....	40	30	60	84	58
Subtotal SWP Sources .....	2,799	3,031	3,468	4,420	3,778
State Water Project Thermal Plant (Reid Gardner Project) <sup>(a)</sup> .....	1,127	1,224	901	843	1,029
Power Purchases .....	4,100	3,300	4,031	3,604	2,320
Energy via Exchanges .....	161	106	0	0	0
Total Sources.....	8,187	7,661	8,400	8,867	7,127
Power Sales (Excess Sources) .....	2,334	2,223	1,814	1,192	533

<sup>(a)</sup> The Reid Gardner Power Plant is operated by NV Energy. The Participation Agreement between the Department and NV Energy for coal-fired energy will not be renewed after it terminates in July 2013. The Department intends to replace a portion of the energy lost by termination of this agreement with energy provided to the Department from the Lodi Energy Center. (See "POWER OPERATIONS OF THE STATE WATER PROJECT – Lodi Energy Center Project.")

## Power Transmission

State Water Project power transmission needs are presently served through transmission service contracts and transmission ownership.

*Transmission Service Contracts.* The Department obtains 78 percent of the High Voltage transmission service used by the State Water Project from the CAISO under a Scheduling Coordinator Agreement with the CAISO. Included in this transmission service is access to CAISO trading hubs. The Department also has a major transmission service contract with PG&E that provides 22 percent of the High Voltage transmission service used by the State Water Project.

The Comprehensive Agreement with PG&E, dated April 22, 1982 (the “PG&E Transmission Contract”), provides High Voltage and Low Voltage transmission service throughout Northern and Central California. The PG&E Transmission Contract expires on December 31, 2014. Under the PG&E Transmission Contract, PG&E, at the Department’s request, built transmission reinforcements, which consisted of a series of capacitor bank installations at each substation, between the Table Mountain and Tesla substations to increase transmission reliability. Under the PG&E Transmission Contract, the Department also had the option of having PG&E construct transmission reinforcements between the Los Banos and Midway substations to further increase transmission reliability. Instead of building the Los Banos-Midway reinforcements, the Department and PG&E entered into an agreement that allows PG&E to drop Department pump load and generation automatically when certain emergency conditions occur on the PG&E transmission system. The agreement provides the Department with increased transmission service reliability during non-emergency periods at a lower cost than the reinforcements. In addition, the PG&E transmission contract provides for the connection of State Water Project facilities in PG&E’s Service Area to the transmission grid.

The Department also has several transmission agreements with Edison that provide for the connection of State Water Project facilities in Edison’s service area to the transmission grid.

*Transmission Ownership.* The Department also either solely or partially owns several transmission lines that interconnect State Water Project facilities with PG&E’s transmission system. The following is a summary of the transmission lines owned by the Department:

The 10 mile Oroville Complex-Table Mountain 230 kilovolt line is solely owned by the Department. The triple-circuit line connects the Hyatt and Thermalito Powerplants to PG&E’s Table Mountain substation.

The Castle Rock-Lakeville 38-mile 230 kilovolt double-circuit line is co-owned with PG&E and others. The Department owns a 165 megawatt entitlement in this line, but has leased 55 megawatts to other public utilities. The remaining 110 megawatt entitlement has been retained by the Department.

The one mile Pine Flat 230 kilovolt transmission line is solely owned by the Department. This transmission line emanates from the Pine Flat Powerplant and interconnects with PG&E’s system.

The Department owns 75 percent of the 230 kilovolt double-circuit transmission line between Midway substation and Wheeler Ridge substation; the other 25 percent is owned by PG&E. The transmission line connects the Buena Vista, Wheeler Ridge and Wind Gap pumping plants to the PG&E Midway substation. Each pumping plant’s tie line is solely owned by the Department.

### **Federal Energy Regulatory Commission Proceedings**

A number of proceedings are pending before FERC relating to the Department as operator of the State Water Project. Some of these proceedings address requests from the CAISO, investor-owned utilities, and others to increase or adjust rates or allocate responsibility for costs for transmission and other services provided to the Department and other entities in California. The Department is participating in these proceedings because the outcome of these proceedings has the potential to increase the Department’s annual power costs. However, the Department does not believe that any increased charges arising from these proceedings will materially impact the Department’s operations or ability to pay debt service on the Bonds. Any increased charges will be passed through to the Contractors under the Water Supply Contracts in the form of higher operating charges.

## **California Energy Crisis and Claims for Partial Energy Purchase Refunds**

The California energy crisis of 2000-01 adversely impacted the financial condition of some market participants, including the State Water Project. As a supplier of energy, the Department received increased market prices for energy sales in late 2000 and in 2001. Some of the proceeds of such sales may be subject to refund.

FERC proceedings were instituted to address power purchaser requests for partial refunds from sellers of energy and related services in 2000 and 2001, including the Department. However, in September 2005, the United States Ninth Circuit Court of Appeals ruled that FERC lacked jurisdiction under the Federal Power Act to order governmental entities, such as the Department, to provide refunds in these types of proceedings. As a result of this Ninth Circuit Court of Appeals' ruling, a group of California entities filed similar claims for partial energy purchase refunds with the California Victim Compensation and Government Claims Board against the governmental entity sellers, including the Department. The Claims Board has denied the claim made against the Department, which now allows the claimants to file a lawsuit against the Department. The Department and the claimants have entered into a tolling agreement that is scheduled to expire on February 28, 2014. The costs of refunds, if any, will be passed through to Contractors and, therefore, are not expected to have a materially adverse effect on the ability of the Department to pay its obligations when due or its ability to operate and maintain the State Water Project.

## **Reid Gardner Termination, Groundwater Contamination Cleanup and Environmental Lawsuit**

The Department's Reid Gardner Project consists of the Department's interest in a 260 megawatt coal-fired steam electric generating unit in Nevada constructed by NV Energy ("NVE"). The Department's ownership interest in the project is scheduled to terminate in July 2013. (See APPENDIX I – "WATER SYSTEM PROJECTS – Project Descriptions – *Reid Gardner Project*.")

In February 2008, NVE entered into an Administrative Order on Consent with the Nevada Division of Environmental Protection, pursuant to which NVE agreed to undertake investigatory activities and remediate the soil and groundwater contamination attributable to the Reid Gardner Generating Station. NVE operates the Reid Gardner Generating Station, which houses four coal-fired generating units. The Department owns 67.8 percent and NVE owns 32.2 percent of Unit 4 as tenants in common and the other three generating units are owned by NVE. The Department also has a 29.2 percent share of the common facilities at the site. The Department is participating in NVE's soil and groundwater remediation activities. However, the Department believes that its participation in these remediation activities will not have a material adverse impact on State Water Project finances or operations.

In February 2012, an environmental organization and band of Native Americans in Nevada served a notice on NVE and the Department that they intend to file a lawsuit under the federal Resource Conservation and Recovery Act and the Clean Water Act related to operations of the Reid Gardner Generating Station, which includes the unit in which the Department has an ownership interest. The notice asserts, among other things, violations arising from coal operations, groundwater contamination and discharge of pollutants into the nearby river. However, the Department believes that this lawsuit, if successful, would not have a material adverse impact on State Water Project finances or operations.

## **Oroville Facilities Relicensing Program**

In January 2005, the Department filed its application with FERC for a new license for its Hyatt-Thermalito hydroelectric generation facilities, which are referred to by FERC as the Oroville Facilities (Project No. 2100) ("Oroville Facilities.") The existing FERC license, granted in 1957, expired on January 31, 2007. The Department's application requested a new 50-year license and was filed with a comprehensive settlement

agreement for the relicensing of the Oroville Facilities (the “Settlement Agreement”) with 51 stakeholders including federal, state and local agencies, and individuals. FERC issued an annual license effective February 1, 2007, with provisions for automatic annual renewals until a new long term license is issued. The Department has used a collaborative approach to relicensing (referred to as “Alternative Licensing Procedures”) that involves working cooperatively with federal and State resource agencies, Indian tribes, local public agencies, non-governmental organizations and other interested parties to achieve consensus on the FERC license application and environmental documentation.

In March 2006, the Department and 51 settling parties signed the Settlement Agreement. The Settlement Agreement covers the protection, mitigation, and enhancement measures that will be implemented over the term of a new license to balance the Oroville Facilities operations with the environment and other project resources such as recreation, cultural, land use, and aesthetics. The Settlement Agreement has been submitted to FERC with the settling parties requesting FERC to adopt only the agreed-upon provisions as the terms and conditions of the new FERC license, so as not to jeopardize settlement. Other parties, that were not parties to the Settlement Agreement, have also intervened in the relicensing proceeding with various requests for additional conditions to be included in the new license. These parties include Butte and Plumas Counties, several Indian tribes, and other interest groups and individuals. The Department has responded in opposition to the inclusion of the proposed additional conditions.

FERC published its Final Environmental Impact Statement (“FEIS”) in May 2007, which completed the federal environmental documentation process. The FEIS included the majority of the Settlement Agreement terms that come under FERC jurisdiction. The Department issued the final EIR in July 2008. Butte and Plumas Counties filed lawsuits challenging the adequacy of the final EIR. After holding a hearing on the merits, the court issued its decision in favor of the Department in 2012 and the county plaintiffs have appealed the court’s decision. Notwithstanding the lawsuits, in January 2010 the State Water Resources Control Board, using the Final EIR, issued the required Clean Water Act Section 401 Water Quality Certification for the Oroville Facilities. FERC and the Department are awaiting the issuance of a final Biological Opinion for the project from the NOAAAF. The Department expects that the new FERC license would be for a term of 30 to 50 years. In the meantime, FERC is expected to continue issuing annual licenses for the Oroville Facilities.

### **Lodi Energy Center Project**

The Department entered into a Power Sales Agreement with the Northern California Power Agency (“NCPA”) and other project participants in May 2010, reflecting the Department’s participation in the Lodi Energy Center Project (the “LEC Project.”) The LEC Project will consist of a 280 megawatt natural gas-fired combined cycle powerplant to be constructed by NCPA in Lodi, California. The terms of the Power Sales Agreement provide that the Department will be entitled to receive 33.5 percent of the output, and be responsible for its share of the construction and operation costs, of the LEC Project. The power received by the Department pursuant to its participation in the LEC Project will assist the Department in meeting future State Water Project energy requirements, including the replacement of energy currently provided by the Reid Gardner Project. (See APPENDIX I – “WATER SYSTEM PROJECTS – Project Descriptions – *Reid Gardner Project*.”) Construction of the LEC Project has been completed and operation began in November 2012.

### **Thermalito Powerplant Fire**

On November 22, 2012, a major fire occurred at the Thermalito Powerplant, which is part of the Hyatt-Thermalito hydroelectric generation facilities located on the Feather River near Oroville. The fire caused substantial damage to the plant rendering the plant inoperable. Until the plant is repaired and placed back in service, the electrical generation from the Hyatt-Thermalito facilities will be reduced. The Department is in the process of investigating the cause of the fire and cleaning up the plant. Thereafter, the Department will consider the feasibility of repairing and reconstructing the plant and equipment and make a determination regarding

further actions. The Department does not believe that this event will have a material adverse impact on the Department's aggregate power cost or on the ability of the Department to operate and maintain the State Water Project. If a determination is made to repair and/or reconstruct the Thermalito Powerplant the associated costs are likely to be financed with Bonds. (See APPENDIX I – "WATER SYSTEM PROJECTS – Capital Expenditures for Capital Projects).

### **No Relationship to Power Supply Revenue Bonds**

In response to the California energy crisis of 2000-01, the Department created the separate CERS Division to perform its function as supplier of energy to retail customers under its Power Supply Program, and to distinguish and keep that program separate and distinct from its power activities in connection with the State Water Project. The Department has issued Power Supply Revenue Bonds to finance and refinance a portion of the costs of the Power Supply Program. \$7.127 billion of Power Supply Revenue Bonds are currently outstanding.

**The State Water Project and the Power Supply Program are separate and distinct enterprises, and have separate and distinct sources and uses of funds. None of the power generated by the State Water Project is being or will be sold to the Power Supply Program. Revenues pledged to secure payment of the Bonds may not be used to pay the Power Supply Revenue Bonds or any other expenses of the Power Supply Program, and resources pledged to secure the payment of the Power Supply Revenue Bonds may not be used to pay the Bonds or any other expenses of the State Water Project.**

## **FINANCIAL OPERATIONS**

### **Financing of the State Water Project**

In addition to the revenue bond obligations described under "FINANCIAL OPERATIONS- Outstanding Revenue Obligations of the Department for the State Water Project" below, a large portion of the State Water Project has been financed by the sale of general obligation bonds of the State pursuant to the provisions of the Burns-Porter Act, which authorized the issuance of \$1,750,000,000 in aggregate principal amount of such bonds for the construction of the State Water Project. The Burns-Porter Act was adopted by the voters at the State's general election of November 8, 1960. Of that authorization, \$1,582,400,000 in aggregate principal amount (including the entire amount available for construction of the initial components of the State Water Project) has been issued, of which \$326,990,000 in aggregate principal amount are outstanding. The unissued \$167,600,000 of the authorization is available only to provide funds for the construction of certain additional water conservation facilities.

Certain other moneys have been made available to the Department to pay the cost of construction of the State Water Project, including the proceeds of the sale of revenue bonds pursuant to the CVP Act (see "FINANCIAL OPERATIONS – Outstanding Revenue Obligations of the Department for the State Water Project"), a portion of the moneys from State offshore oil royalties, other State appropriations, the PMIA Loan (defined below), and federal reimbursements for project costs allocated to flood control.

After the issuance of the Series AM Bonds, the Department anticipates issuing approximately \$1,549.4 million of additional Bonds to finance completion of existing Water System Projects. (See APPENDIX I – "WATER SYSTEM PROJECT – Capital Expenditures for Water System Projects.") In addition, the Department could issue additional Bonds to finance all or a portion of the settlement agreement costs of Federal Energy Regulatory Commission ("FERC") relicensing of its power, water storage and associated facilities at Oroville. Such costs could total \$86 million or more. The Department may also undertake additional capital projects in the future, which could result in the issuance of additional Bonds or other obligations in substantial amounts. (See "SECURITY FOR THE BONDS – Outstanding Bonds; Additional Bonds" for a description of certain limitations on the issuance of additional Bonds).

## **Fish and Wildlife Enhancement and Recreation Costs**

The Department is required under the Davis-Dolwig Act, enacted by the Legislature in 1961, to incorporate recreation and fish and wildlife enhancement features in the planning and construction of the State Water Project. The Davis-Dolwig Act provides, in California Water Code section 11913, that it is the intent of the Legislature that there shall be included in the budget for the Department for each fiscal year, and in the State's budget act for each fiscal year, an appropriation from the General Fund of the funds necessary for enhancement of fish and wildlife and for recreation in connection with state water projects (including the State Water Project). Between 1998 and 2011, no appropriation from the General Fund was made to the Department for these purposes. However, effective with the 2012-2013 fiscal year, legislation was enacted that provides for a continuous annual appropriation of \$10 million from the General Fund portion of the Harbors and Watercraft Revolving Fund to the Department for Davis-Dolwig Act purposes. Seven and one half million dollars of this amount is continuously appropriated each fiscal year for current fish and wildlife enhancement and recreation costs and the other \$2.5 million of this amount is continuously appropriated each fiscal year to reimburse the Department for fish and wildlife enhancement and recreation costs incurred prior to 2012. If additional funding is required for these purposes, the Department will be required to seek additional appropriations.

In 2006, California voters approved Proposition 84 (the Safe Drinking Water, Water Quality and Supply, Flood Control, River and Coastal Protection Bond Act of 2006), which, among other things, authorized the sale of \$54 million in State general obligation bonds for State Water Project recreation and fish and wildlife enhancement purposes. To the extent that sufficient moneys for the enhancement of fish and wildlife and for recreation in connection with state water projects are not made available to the Department through appropriations or the sale of general obligation bonds, costs allocated by the Department to the development of public recreation or fish and wildlife enhancement are expected to be paid by the Department on an on-going basis with State Water Resources Development System revenues available after the payment of operation and maintenance costs, Bond debt service and the PMIA Loan. (See "THE WATER SUPPLY CONTRACTS – Monterey Amendment" and "WATER SUPPLY CONTRACT RELATED LITIGATION – Claims Relating to the Use of Bond Proceeds to Pay Capital Costs Allocable to Recreation and Fish and Wildlife Enhancement.")

## **Allocation of State Water Project Revenues**

Under the California Water Code, State Water Project revenues are allocated between two funds, depending on the source of the revenues.

State Water Project revenues from Water System Projects financed by Bonds are, to the extent allocated to the Bonds, deposited in the Central Valley Project Revenue Fund and pledged to the repayment of Bonds.

State Water Project revenues from the Devil Canyon Castaic Facility are deposited in the Central Valley Project Revenue Fund and pledged to the payment of the Devil Canyon Castaic Bonds. State Water Project revenues from the Water System Projects financed by Notes are, to the extent allocated to the Notes, deposited in the Central Valley Project Revenue Fund and pledged to the payment of the Notes.

All other State Water Project revenues are deposited in the California Water Resources Development Bond Fund and used first to pay the reasonable operating and maintenance costs of the State Water Resources Development System (which includes the State Water Project); second, to reimburse the General Fund of the State for the payment of the general obligation bonds issued to finance a portion of the capital costs of the State Water Project; and thereafter to the payment of the costs of the acquisition and construction of the State Water Resources Development System.

## Outstanding Revenue Obligations of the Department for the State Water Project

The Department has previously issued forty series of Water System Revenue Bonds totaling \$7,476,100,000 in aggregate principal amount, of which \$2,203,240,000 in aggregate principal amount are Outstanding. All of such Bonds are fixed rate bonds and are secured equally and ratably with the Series AM Bonds. (See “PLAN OF REFUNDING.”)

The Department has also issued \$1,526,155,000 in aggregate principal amount of revenue bonds secured by three separate bond resolutions to finance certain power facilities of which \$68,070,000 in aggregate principal amount are outstanding. All bonds issued under two of these resolutions have been fully retired. The outstanding revenue bonds issued under the third resolution are referred to as Devil Canyon-Castaic Bonds. Funds to be available to pay interest on and principal of the Devil Canyon-Castaic Bonds will not constitute Revenues under the Resolution and will not be available to pay interest on or principal of the Bonds. At no time will Revenues be available to pay interest on or principal of the Devil Canyon-Castaic Bonds.

The table below summarizes certain information for the Department’s outstanding long-term revenue bond programs.

	<b>When Issued</b>	<b>Final Maturity</b>	<b>No. of Series</b>	<b>Original Principal Amount in Millions</b>	<b>Outstanding Principal Amount in Millions<sup>(1)</sup></b>
Devil Canyon-Castaic Bonds <sup>(2)</sup> .....	1972	2022	1	\$ 139	\$ 68
Water System Revenue Bonds <sup>(3)</sup> .....	1986-2012	2035	40	7,476	2,203
Total <sup>(4)</sup> .....				<u>\$7,615</u>	<u>\$2,271</u>

(1) Previously refunded bonds, the Series AM Bonds and the Series AP Bonds are not included in these totals.

(2) Not secured by the Revenues securing the Bonds.

(3) Does not reflect the issuance of the Series AM Bonds or the Series AP Bonds. The Series AM Bonds will be issued in the aggregate principal amount of \$183,960,000 and will refund \$211,840,000 in aggregate principal amount of outstanding Bonds and the Series AP Bonds are expected to be issued in the aggregate principal amount of approximately \$50,000,000. (See “PLAN OF REFUNDING.”)

(4) Totals may not sum due to rounding.

The Department has authorized the issuance of the Notes in a principal amount outstanding at any one time not to exceed the lesser of \$150,000,000 or the principal amount of Notes supported by the credit agreement then in effect (currently \$139,668,367). The Note program is designed to be an ongoing source of interim financing for Water System Projects prior to permanent financing from the sale of Bonds. The Department currently has approximately \$50,000,000 aggregate principal amount of Notes outstanding. It is anticipated that Notes issued in the future will be refunded periodically by other long-term Bonds. (See “PLAN OF REFUNDING – Proposed Issuance of Series AP Bonds to Refund Outstanding Notes.”) Pursuant to a Revolving Credit Agreement that extends through October 24, 2014, Bank of Montreal, acting through its Chicago Branch has agreed to make advances to the Department, if necessary and subject to certain conditions, to provide moneys for the payment of the Notes when due. The Department may replace the existing revolving credit agreement under the conditions provided by the Note resolution and the agreement. The Notes are payable from the Central Valley Project Revenue Fund and from payments under the Water Supply Contracts. In the event that amounts received by the Department under the Water Supply Contracts are insufficient to pay all amounts due under the Notes, the Bonds and the State’s general obligation bonds issued for the State Water Project, such moneys are to be allocated first to the payment of amounts due under the Bonds and such general obligation bonds.

On April 1, 2008, the Pooled Money Investment Board of the State made a \$29,600,000 loan from the Pooled Money Investment Account to the Department (the “PMIA Loan”) in accordance with California

Government Code section 16313, which authorizes the Board to make a loan, on such terms and conditions as the Board may determine, from the Pooled Money Investment Account to any state agency in order to prepay or replace existing financing when the Board determines it is in the best interest of the State to do so. The proceeds of the PMIA Loan together with certain other available funds of the Department were used to retire or provide for the defeasance of approximately \$28.2 million principal amount of certain Bonds and Notes, the proceeds of which were used to pay capital costs allocated to the purposes of fish and wildlife enhancement and the development of public recreation. (See also “WATER SUPPLY CONTRACT RELATED LITIGATION – Claims Relating to the Use of Bond Proceeds to Pay Capital Costs Allocable to Recreation and Fish and Wildlife Enhancement.”) The Department expects to pay the PMIA Loan solely from “surplus revenues” as defined in California Water Code section 12937(b)(4). None of such surplus revenues are pledged to secure the Bonds, and none of the Revenues pledged to secure the Bonds are available to pay the PMIA Loan. The current balance of the PMIA Loan is approximately \$16,494,016.

The Department currently has no interest rate swaps, caps or hedges or other contingent payment obligations payable from Revenues.

### Estimated Annual Debt Service

The following table sets forth the estimated annual debt service for all Bonds that will remain outstanding after giving effect to the issuance of the Series AM Bonds and the application of the proceeds thereof as described in this Official Statement and assuming no additional Bonds are issued prior to the issuance of the Series AM Bonds. (See “PLAN OF REFUNDING” and “SECURITY FOR THE BONDS – Outstanding Bonds; Additional Bonds.”)

Year Ending (December 1)	Outstanding Bonds Total Debt Service <sup>(1)</sup>	Series AM Bonds			Grand Total <sup>(2)(3)</sup>
		Principal	Interest	Debt Service	
2013	\$ 186,086,754	\$ 12,320,000	\$ 6,796,218	\$ 19,116,218	\$ 205,202,972
2014	178,945,984	14,070,000	8,582,000	22,652,000	201,597,984
2015	199,689,640	1,525,000	7,878,500	9,403,500	209,093,140
2016	190,447,230	10,215,000	7,802,250	18,017,250	208,464,480
2017	189,241,041	11,595,000	7,291,500	18,886,500	208,127,541
2018	170,422,362	9,665,000	6,711,750	16,376,750	186,799,112
2019	165,423,898	20,015,000	6,228,500	26,243,500	191,667,398
2020	170,127,488	11,310,000	5,227,750	16,537,750	186,665,238
2021	169,093,125	10,715,000	4,662,250	15,377,250	184,470,375
2022	159,580,496	19,880,000	4,126,500	24,006,500	183,586,996
2023	150,222,925	17,405,000	3,132,500	20,537,500	170,760,425
2024	146,458,682	18,745,000	2,262,250	21,007,250	167,465,932
2025	130,620,062	26,500,000	1,325,000	27,825,000	158,445,062
2026	142,883,467	--	--	--	142,883,467
2027	155,561,761	--	--	--	155,561,761
2028	138,162,066	--	--	--	138,162,066
2029	144,299,850	--	--	--	144,299,850
2030	17,422,450	--	--	--	17,422,450
2031	17,433,125	--	--	--	17,433,125
2032	17,427,300	--	--	--	17,427,300
2033	14,883,225	--	--	--	14,883,225
2034	14,881,150	--	--	--	14,881,150
2035	14,900,988	--	--	--	14,900,988
<b>Total<sup>(2)(3)</sup></b>	<b>\$2,884,215,068</b>	<b>\$183,960,000</b>	<b>\$72,026,968</b>	<b>\$255,986,968</b>	<b>\$3,140,202,036</b>

<sup>(1)</sup> Excludes debt service on previously refunded Bonds and the Series AM Refunded Bonds.

<sup>(2)</sup> Totals may not sum due to rounding.

<sup>(3)</sup> After the issuance of the Series AM Bonds and the refunding of the Series AM Refunded Bonds, and without giving effect to the proposed issuance of the Series AP Bonds and the application of the proceeds thereof, the Department anticipates it will have \$2,175,360,000 aggregate principal amount of Bonds outstanding. (See “PLAN OF REFUNDING.”)



## **Article XIII B of the Constitution**

Article XIII B of the California Constitution (“Article XIII B”) establishes limits on certain annual appropriations of state and local entities. See “CERTAIN LIMITATIONS ON CONTRACTOR REVENUE SOURCES – Article XIII B of the Constitution.” The Department’s experience is that Article XIII B has not significantly impaired the State’s ability to appropriate funds for the State Water Project.

Article XIII B was adopted pursuant to California’s constitutional initiative process. From time to time other initiatives could be adopted by California voters, placing additional limitations upon the State or the Department.

## **THE WATER SUPPLY CONTRACTS**

The Water Supply Contracts between the State, acting by and through the Department, and the 29 Contractors are substantially uniform with respect to basic terms except with respect to certain payments by Contractors for agricultural water as noted below. Copies of the Water Supply Contracts between the State and the 29 Contractors are on file at the offices of the Department and of the State Treasurer in Sacramento, and reference is made thereto for information with respect to all of the terms and conditions thereof. The following discussion, except as noted, is applicable to each of the 29 Water Supply Contracts, and assumes the effectiveness of the amendments described below under the heading “Monterey Amendment.” All but two of the Contractors (Plumas County Flood Control and Water Conservation District and Empire West Side Irrigation District) have signed the Monterey Amendment.

### **Basic Contract**

*Term.* The Water Supply Contracts are to remain in effect until 2035, or until all bonds issued to finance construction costs of State Water Project facilities have been repaid, whichever period is longer. The final maturity of the Bonds to be outstanding upon the issuance of the Series AM Bonds will be in 2035. (See “SECURITY FOR THE BONDS – Outstanding Bonds; Additional Bonds.”)

*Annual Table A Amounts.* The year of initial water delivery is estimated in each Water Supply Contract and a schedule in each of the Water Supply Contracts sets forth the maximum annual amounts of water the Contractor may request to be delivered (“Annual Table A Amount”) commencing in the initial year. These scheduled amounts increase yearly and reach the maximum Annual Table A Amount in a specified year, which for all but five of the smaller Contractors was reached by January 1, 1997. Those five Contractors will reach their respective maximum Annual Table A Amounts on or before 2016. The Annual Table A Amounts schedule may be changed upon request by the Contractor and approval by the State, but no such change may be made if it would impair the financial feasibility of the State Water Project.

The maximum Annual Table A Amounts of all 29 Contractors presently total 4,172,786 acre-feet of water. (See “STATE WATER PROJECT WATER SUPPLY.”) Water delivered to a Contractor may not be disposed of by the Contractor for use outside the Contractor’s territory, subject to certain limited exceptions, without the State’s consent. Restrictions are imposed on changes in the corporate organization of the Contractor.

*Water Supply.* Subject to the availability of funds, the State is required to make all reasonable efforts consistent with sound fiscal policies, reasonable construction schedules, and proper operating procedures to complete the facilities necessary for water deliveries at the time and in the amounts specified.

The State must make all reasonable efforts to perfect and protect necessary water rights and must report at least every five years on its ability to meet future water demands.

If the State cannot complete construction of the aqueducts necessary to deliver water to the Contractor, the Contractor may, under specified circumstances, provide money to the State necessary to enable the State to complete construction. In such case, the State will own and operate the aqueducts, and the amount provided by the Contractor will be credited by the State against the Contractor's payment obligation under the Water Supply Contracts. Alternatively, the Contractor may connect, at its own expense, to the portion of the aqueduct completed by the State to receive water to which it is entitled under the Water Supply Contract.

The State is required to take all reasonable measures to make available water that meets the water quality objectives set forth in the Water Supply Contract.

*Allocation of Water Surpluses and Deficiencies.* If there is a supply of water in excess of (i) the scheduled deliveries under Table A for all Contractors and (ii) the operational requirements of the State Water Project, Contractors may purchase such surplus water on an interruptible basis. The price of this interruptible water is the incremental cost of delivery.

The Water Supply Contracts also contain provisions for the allocation of water in the event of shortages in water supply. For Contractors that have accepted the Monterey Amendment, the available supply is to be allocated in proportion to Annual Table A Amounts, with reductions for agricultural Contractors and urban Contractors being made on the same basis. Contractors that have accepted the Monterey Amendment as of the date of this Official Statement have over 99 percent of the total Annual Table A Amounts of all Contractors. (See "WATER SUPPLY CONTRACT RELATED LITIGATION – Monterey Amendment Litigation.")

For Contractors that have not accepted the Monterey Amendment, there will be a reduction first in the delivery of water for agricultural purposes by an amount not to exceed 50 percent in any one year or a total of 100 percent of the maximum annual request for agricultural water in any seven consecutive years. Any additional reductions required will be apportioned among all Contractors irrespective of use. In the event of a permanent shortage there will be a proportionate reduction of the Contractors' maximum annual request for water.

Contractors may use aqueduct capacity not used for State water to transport other water procured by them. The State is not liable for damage arising from shortages due to causes beyond its control. The total amount of Revenues required to be paid under the provisions of the Water Supply Contracts for the payment of debt service on the Bonds is not dependent on the amount of water available to be delivered.

*Water Charges.* The Water Supply Contracts in their original form provide for two charges to the Contractor: (a) a Delta Water Charge and (b) a Transportation Charge. The Off-Aqueduct Power Facilities Amendment, East Branch Enlargement Amendment, Water System Revenue Bond Amendment, Coastal Branch Extension Amendment, East Branch Extension Amendment and South Bay Aqueduct Amendment described below (collectively, the "Revenue Bond Amendments") modify the manner of calculating the charges with respect to certain facilities, including certain of the Water System Projects. (See "THE WATER SUPPLY CONTRACTS – Amendments Providing Certain Revenues to Pay Water System Revenue Bonds.")

The original Delta Water Charge and Transportation Charge each consist of three components: (a) a capital cost component; (b) a minimum operation cost component (operation costs that do not vary with water deliveries); and (c) a variable operation cost component (operation costs that vary with water deliveries). Project Planning Costs are charged under the component to which the costs of the potential project being studied would be charged if such project were constructed or acquired.

The original Delta Water Charge is a charge for each acre-foot of maximum Annual Table A Amount. It is computed so as to return to the State generally during the term of the Water Supply Contract all "reimbursable" costs of the "project conservation facilities," together with interest thereon. The "project

conservation facilities” are defined as certain categories of facilities that conserve water. Such facilities now include the Oroville facilities, the Delta facilities, the San Luis facilities and a portion of the aqueduct leading to the San Luis facilities from the Delta. “Reimbursable” costs are those costs determined by the State to be allocable to the purposes of water conservation (or, in the case of the Transportation Charge, to water transportation). The costs and revenues of powerplants that are part of the “project conservation facilities” (including the Oroville Power Facilities) are included in the determination of the Delta Water Charge.

The original Transportation Charge is computed so as to return to the State during the term of the contract the “reimbursable” costs of the facilities necessary to deliver water to a Contractor, together with interest thereon. Such facilities include facilities such as aqueducts, pumping plants and on-aqueduct power facilities, but do not include any of the facilities designated by the Resolution as Water System Projects, except for the Alamo Project, Small Hydro Project and Pyramid Hydroelectric Project (which are on-aqueduct power facilities) and except as the Transportation Charge is incorporated by reference in the Water System Revenue Bond Amendment. The costs of the facilities relating to each reach of aqueduct are allocated among all Contractors receiving water through that reach. Each year’s capital expenditures are allocated among the Contractors and the allocated amount is required to be paid by each Contractor, together with interest, in not more than 50 equal annual installments within the capital cost component of the Transportation Charge. (In contracts with agricultural water Contractors, these capital costs are repaid by a uniform charge per acre-foot of the maximum annual amount of agricultural water that may be requested, which charge is computed so as to return to the State generally during the Water Supply Contract term such costs with interest.)

The capital cost component of the Transportation Charge and all components of the Delta Water Charge are to be repaid with interest at the weighted average of the rates paid on securities issued to finance the State Water Project (except the Department’s commercial paper, the Oroville Bonds and Water System Revenue Bonds) and certain other moneys used to finance the State Water Project. The minimum and variable operation, maintenance, power and replacement cost components (the “operation cost components”) of the Transportation Charge are paid currently.

The annual net value of power produced by any powerplant located on a State Water Project aqueduct is credited to all Contractors receiving water flowing through that powerplant in proportion to each Contractor’s portion of the total water flowing through the plant during the year. The credit is given in the form of a reduction in the variable operation cost component of each such Contractor’s Transportation Charge.

*Payment of Water Charges.* On or before July 1 of each year, the State furnishes each Contractor with a statement of estimated charges for the capital cost components (including charges under the Revenue Bond Amendments) and the minimum operation cost components of the Delta Water Charge and Transportation Charge for the following calendar year. The original Delta Water Charge and Transportation Charge capital cost component payments, the East Branch Enlargement Amendment, Coastal Branch Extension Amendment, East Branch Extension Amendment and South Bay Aqueduct Enlargement Amendment revenue bond charges and the Water System Revenue Bond Amendment revenue bond surcharge are due semiannually, on January 1 and July 1 of the year following receipt of the statement of charges. The minimum operation cost component payments and the Off-Aqueduct Power Facilities Amendment payments are due in twelve monthly installments commencing on January 1 of the year following receipt of the statement of charges.

On or about July 1 of each year, the State determines the rate (per acre-foot) to be charged each Contractor in the following calendar year for the variable operation cost components of the Delta Water Charge and the Transportation Charge. The variable operation cost components in such calendar year are calculated and billed monthly based on metered water deliveries for the preceding month and the rate determined on July 1 of the prior year. Payment of the variable operation cost components is due on the sixteenth day of the month following receipt of the monthly statement of charges, which results in an approximately two-month delay between delivery of water and payment of the variable operation cost components.

On July 1 of each year, the State furnishes each Contractor with a statement showing the difference between the estimated water charges paid and the actual costs incurred in the prior calendar year. The difference is paid by or credited to each Contractor, as applicable, in equal monthly installments commencing on January 1 of the year following the “true-up” calculation. This process results in an approximately two-year delay in the reconciliation of estimated charges paid and actual costs reimbursed to the Department.

Interest from the due date at the interest rate earned by the State’s Pooled Money Investment Account must be paid on any payment received more than 30 days after the due date. A Contractor’s failure or refusal to accept delivery of water does not relieve the Contractor of its payment obligations. A Contractor is obligated to make payments to the State notwithstanding any individual default by its constituents, assignees or others in the payment to the Contractor of charges levied by the Contractor. In accordance with a statutory requirement, each Water Supply Contract requires that whenever the Contractor fails or is unable to raise sufficient funds by other means the Contractor must levy upon all taxable property in the Contractor’s service area a tax or assessment sufficient (with other available moneys) to provide for all payments under the Water Supply Contract. (See “CERTAIN LIMITATIONS ON CONTRACTOR REVENUE SOURCES.”)

If the Contractor defaults in payment, the State may, and under certain conditions is required to, upon six months’ notice, suspend water deliveries during the period of default. During such period the Contractor remains obligated to make all payments required by the Water Supply Contract and the State is not deprived of any other remedy under the Water Supply Contract or law.

### **Revenues from Bond Financed Facilities**

Revenues received under the Water Supply Contracts from facilities financed with the Bonds are available to be pledged to the payment of the Bonds. (See “SECURITY FOR THE BONDS.”) Other income and revenues derived from the Water Supply Contracts are pledged to the purposes and priorities set forth in the Burns-Porter Act, including the payment of certain operation, maintenance and replacement costs of the State Water Project, the payment of debt service on the State general obligation bonds issued under the Burns-Porter Act, the repayment of certain State moneys used for construction, and the payment of costs of acquisition and construction of the State Water Resources Development System (which includes the State Water Project).

The components of the State Water Project financed with Bonds are described in APPENDIX I – “WATER SYSTEM PROJECTS.”

### **Amendments Providing Certain Revenues to Pay Water System Revenue Bonds**

The costs of certain Water System Projects, as that term is defined by the Resolution, are recovered under one of the Water Supply Contract amendments described below.

*Off-Aqueduct Power Facilities Amendment.* In 1982, the State, acting by and through the Department, and the 29 Contractors entered into a Water Supply Contract amendment, which (a) establishes a separate subcategory of Transportation Charge for Off-Aqueduct Power Facilities, such as the Reid Gardner Project, the Bottle Rock Project and the South Geysers Project, and changes the method of allocation and payment of costs of such power facilities; (b) authorizes the State, subject to certain conditions, to include “local water projects” such as ground water storage projects, surface storage projects, wastewater reclamation projects and conservation programs, as projects of the State Water Project with the costs of such projects to be allocated under the Delta Water Charge; (c) changes the interest rate for the penalty for late payments from 6 percent to the interest rate earned by the State’s Pooled Money Investment Account; and (d) specifies that the State may, subject to certain conditions, charge the Contractors under the Delta Water Charge for water purchased by the State for delivery through the State Water Project.

Under the Off-Aqueduct Power Facilities portion of the amendment, the annual costs for such facilities financed by Bonds are allocated among the Contractors based upon power consumed in such year in delivering State Water Project water to each Contractor. Such costs include, but are not limited to, debt service, including coverage requirements (such as the requirement of the Resolution that Revenues receivable under the Water Supply Contracts after deduction of the costs of maintenance and operation be at least 1.25 times debt service on the Bonds), deposits to reserves (including the Debt Service Reserve Account) and operation and maintenance expenses, less any credits, interest earnings or other moneys received by the State in connection with the facility. If the State determines that the amount received from the Contractors in any year is less than the amount required for such Off-Aqueduct Power Facilities costs, the State may allocate the deficiency among the Contractors in the same manner as costs are allocated using the original capital cost component of the Transportation Charge.

*East Branch Enlargement Amendment.* In 1986, the State, acting by and through the Department, entered into a Water Supply Contract amendment with Metropolitan, Antelope Valley-East Kern Water Agency, Coachella, Desert Water Agency, Mojave Water Agency, Palmdale Water District and San Bernardino Valley Municipal Water District (the “Participating Contractors”), for the purpose, among others, of financing the enlargement of the East Branch of the California Aqueduct. The amendment establishes a separate subcategory of Transportation Charge for the East Branch Enlargement and provides for the payment of costs associated with financing and operating the East Branch Enlargement.

Under the East Branch Enlargement Amendment, the annual financing costs for such facilities financed by Bonds are allocated among the Participating Contractors based upon delivery capacity increase allocable to each Participating Contractor. Such costs include, but are not limited to, debt service, including coverage requirements (such as the requirement of the Resolution that Revenues receivable under the Water Supply Contracts after deduction of the costs of maintenance and operation be at least 1.25 times debt service on the Bonds), deposits to reserves (including the Debt Service Reserve Account) and operation and maintenance expenses, less any credits, interest earnings or other moneys received by the Department in connection with the facility. If any Participating Contractor defaults on payment of its allocable charges under the East Branch Enlargement amendment, among other remedies available to the State, the non-defaulting Participating Contractors may assume responsibility for such charges and receive delivery capability that would otherwise be available to the defaulting Participating Contractor in proportion to the non-defaulting Participating Contractor’s participation in the East Branch Enlargement. If Participating Contractors fail to cure the default, Metropolitan shall, in exchange for the delivery capability that would otherwise be available to the defaulting Participating Contractor, assume responsibility for the capital charges of the defaulting Participating Contractor.

Each Participating Contractor may elect to pay a portion or all of its share of capital costs by advance payment in lieu of participating in revenue bond financing. In an agreement dated June 1, 1987, the San Bernardino Valley Municipal Water District elected to pay a portion of its allocated costs in advance rather than participate in the Bonds issued to finance the East Branch Enlargement-First Stage. No other Participating Contractor has elected to use this advance payment option.

*Water System Revenue Bond Amendment.* As of 1987, the State, acting by and through the Department, and the 29 Contractors entered into a Water Supply Contract amendment for the purpose of financing facilities, including presently all Water System Projects (as that term is defined under the Resolution) other than Off-Aqueduct Power Facilities, the Alamo Project, the Small Hydro Project, the Pyramid Hydroelectric Project, the East Branch Enlargement – First Stage, the Coastal Branch Extension – Phase II, the East Branch Extension – Phase I and the South Bay Aqueduct Enlargement. The amendment establishes a separate subcategory of Delta Water Charge and Transportation Charge for projects financed with Bonds. This subcategory of charge provides the revenues required to pay the annual financing costs of the Bonds, and consists of two elements. The first element is an annual charge to each Contractor for repayment of capital costs of such projects under the original Water Supply Contract provisions for the Delta Water Charge and the Transportation Charge. The

second element is a Bond surcharge to pay the difference between the total annual charges under the first element and the annual financing costs, including coverage and reserves, of the Bonds issued for such projects.

If any Contractor defaults on payment of its allocable charges under this Amendment, the State must allocate a portion of the default to each of the nondefaulting Contractors, subject to certain limitations, including a provision that no nondefaulting Contractor may be charged more than 125 percent of the amount of its annual payment in the absence of any such default. Under certain circumstances the nondefaulting Contractors would be entitled to receive an allocation of the water supply of the defaulting Contractor.

*Coastal Branch Extension Amendment.* In 1994, the State, acting by and through the Department, entered into a Water Supply Contract amendment with Santa Barbara County Flood Control and Water Conservation District (“Santa Barbara County FCWCD”), for the purposes, among others, of financing the construction of an extension of the Coastal Branch Aqueduct from the Santa Maria River to the current terminus at Tank 5 near the town of Casmalia. The amendment establishes a separate subcategory of Transportation Charge for the Coastal Branch Extension and provides for the payment of costs associated with financing the Coastal Branch Extension.

Under the Coastal Branch Extension Amendment, the annual financing costs for such facilities are charged to Santa Barbara County FCWCD. Such costs include, but are not limited to, debt service, including coverage requirements (such as the requirement of the Resolution that Revenues receivable under the Water Supply Contracts after deduction of the costs of maintenance and operation be at least 1.25 times debt service on the Bonds) and deposits to reserves (including the Debt Service Reserve Account), less any credits, interest earnings or other moneys received by the Department in connection with the facility.

Santa Barbara County FCWCD had the option to elect to pay a portion of or all of the capital costs of the Coastal Branch Extension by advance payment in lieu of participating in revenue bond financing. Santa Barbara County FCWCD did not use this advance payment option.

Maintenance and operation expenses incurred in connection with the Coastal Branch Extension are included in the minimum operation cost component of the original Transportation Charge. There is no separate minimum operation cost component of the Coastal Branch Extension Transportation Charge.

The Department entered into a joint powers agreement, dated October 1, 1996, with the Central Coast Water Authority to allow the Central Coast Water Authority to perform both maintenance and operations work on the Coastal Branch – Phase II, from the Polonio Pass Water Treatment Plant to the pipeline terminus. The Central Coast Water Authority represents a consortium of thirteen local agencies in Santa Barbara County participating in the Coastal Branch. In 1991, the Authority entered into an agreement with Santa Barbara County FCWCD, which specifies the Authority’s responsibility for implementing the State Water Project in Santa Barbara County.

*East Branch Extension Amendment.* In March 1997, the Department entered into a Water Supply Contract amendment with San Bernardino Valley Municipal Water District and San Gorgonio Pass Water Agency, for the purposes, among others, of financing the extension of the East Branch of the California Aqueduct. The amendment establishes a separate subcategory of Transportation Charge for the East Branch Extension and provides for the payment of costs associated with financing the East Branch Extension.

Under the East Branch Extension Amendment, the annual financing costs for such facilities financed by bonds will be allocated between San Bernardino Valley Municipal Water District and San Gorgonio Pass Water Agency based upon the delivery capacity allocable to each. Such costs include, but are not limited to, debt service, including coverage requirements (such as the requirement of the Resolution that Revenues receivable under the Water Supply Contracts after deduction of the costs of maintenance and operation be at least 1.25

times Bond Debt Service) and deposits to reserves (including the Debt Service Reserve Account), less any credits, interest earnings or other moneys received by the Department in connection with the facility.

Under the East Branch Extension Amendment, each participating Contractor has the option to elect to pay a portion of or all of the capital costs of the East Branch Extension by advance payment in lieu of participating in revenue bond financing. Neither participating Contractor has elected to use this advance payment option.

Maintenance and operation expenses incurred in connection with the East Branch Extension will be included in the minimum operation cost component of the original Transportation Charge. There will be no separate minimum operation cost component of the East Branch Extension Transportation Charge.

In July 2005, the Department and the participating Contractors entered into a Joint Powers Agreement for the coordinated operation and maintenance of the Phase I facilities of the East Branch Extension. That agreement allows the participating Contractors to operate the East Branch Extension and perform some of the required maintenance work.

*South Bay Aqueduct Enlargement Amendment.* On November 7, 2003, the Department and Alameda County Flood Control and Water Conservation District, Zone 7 (“Zone 7”) entered into a South Bay Aqueduct Enlargement Amendment to their Water Supply Contract for the purpose of financing the enlargement of the South Bay Aqueduct. This amendment established a separate subcategory of Transportation Charge for the South Bay Aqueduct Enlargement and provides for the payment of costs associated with financing and operating the South Bay Aqueduct Enlargement facilities. The annual costs for such facilities are borne exclusively by Zone 7 including debt service, deposits to reserves and operation and maintenance expenses, less any credits, interest earnings or other moneys received by the Department in connection with such facilities. Under the South Bay Aqueduct Enlargement Amendment, Zone 7 may elect to pay a portion of its entire share of capital costs by advance payment in lieu of participating in revenue bond financing. Operation and maintenance expenses incurred in connection with the South Bay Aqueduct Enlargement will be included in the minimum component of the South Bay Aqueduct Enlargement Transportation Charge.

### **Monterey Amendment**

In December 1994, the Department and representatives of certain of the Contractors reached an agreement on comprehensive principles that served as the basis for negotiating amendments to the Water Supply Contracts. These amendments are collectively known as the “Monterey Amendment.” The Monterey Amendment was negotiated subject to the provision of the Resolution that the Department shall not agree to any amendment to the Water Supply Contracts that would materially adversely affect the security of the Bonds.

Water Supply Contract provisions that have been amended or added by the Monterey Amendment include provisions relating to the allocation of water (both in the event of a shortage and in the event of surplus), the transfer of the land and related assets of the Kern Fan Element of the Kern Water Bank to Kern County Water Agency (“KCWA”), the operation of certain State Water Project reservoirs, transfers of State Water Project Annual Table A Amounts (including certain transfers from agricultural Contractors to urban Contractors), other water transfers, the creation of and limitations on a Department reserve for operation, maintenance and replacement costs, and the description of facilities that may be financed with revenue bonds (adding a corporation yard and an operations center).

In addition, the Monterey Amendment provides for the reduction of annual Water Supply Contract charges in a manner such that Water Supply Contract revenues (taking into account other revenues and credits) are at levels calculated to meet (but not exceed) the following “revenue needs”: (1) annual financing requirements (including debt service and coverage) for revenue bonds, including the Bonds, issued for State

Water Project facilities, (2) maintenance and operation expenses of the State Water Resources Development System (which includes the State Water Project, the Davis-Grunsky Act Program and the San Joaquin Drainage Program), (3) debt service on general obligation bonds issued under the Burns-Porter Act, (4) \$4.5 million per year for capital costs of the State Water Project and the San Joaquin Drainage Program for which neither general obligation bond nor revenue bond proceeds are available, and (5) after the provision of at least \$40.5 million per year of reductions in charges to the Contractors, the amounts available and needed for certain “additional State Water Resources Development System purposes.”

The Monterey Amendment has been executed by the Department and 27 of the Contractors. The Contractors that have signed the Monterey Amendment have approximately 99 percent of the maximum Annual Table A Amounts and make approximately 99 percent of the annual Water Supply Contract payments. The Department believes that it can administer the State Water Project in a manner such that both the Contractors that have not signed the Monterey Amendment and the Contractors that have signed the Monterey Amendment will receive the benefits and have the obligations provided in their respective Water Supply Contracts, amended or not as the case may be.

Pending litigation relating to the Monterey Amendment is described under “WATER SUPPLY CONTRACT RELATED LITIGATION – Monterey Amendment Litigation.”

### **Obligation to Levy Taxes or Assessments**

The Water Supply Contracts, in accordance with a statutory requirement, provide that whenever a Contractor fails or is unable to raise sufficient funds by other means, the Contractor must levy on all property in the Contractor’s territory not exempt from taxation a tax or assessment sufficient to provide for all payments under the Water Supply Contract.

Although Article XIII A of the California Constitution, added to the California Constitution in 1978, limits the imposition of *ad valorem* property taxes. (See “CERTAIN LIMITATIONS ON CONTRACTOR REVENUE SOURCES”), the California Court of Appeal concluded that taxes levied by the Contractors to make payments under the Water Supply Contracts come within the Section 1(b) exception [in Article XIII A for] “*ad valorem* taxes or special assessments to pay the interest and redemption charges on . . . any indebtedness approved by the voters prior to July 1, 1978” to the general taxing limitation imposed by Article XIII A. (*Goodman v. County of Riverside*, 140 Cal. App. 3d 900 (1983)). As a result of this finding, the Court determined there was no need to address the issue of whether the application of Article XIII A to limit the levying of taxes to make payments under the Water Supply contracts would constitute an unconstitutional impairment of contract. The Court stated:

“. . . [W]e conclude, when the state’s voters approved the Act, that they approved an indebtedness in the amount necessary for building, operating, maintaining, and replacing the Project, and that they intended that the costs were to be met by payments from local agencies with water contracts. Further, we conclude that the voters necessarily approved the use of local property taxes whenever the boards of directors of the agencies determined such use to be necessary to fund their water contract obligations, and that the *ad valorem* taxes levied by [Desert Water Agency] fall within the exception of section 1, subdivision (b) [of Article XIII A].

Our conclusion here does away with the necessity to address the issue of impairment of contractual obligations.”

The California Supreme Court denied a petition for hearing on July 14, 1983.



## WATER SUPPLY CONTRACT RELATED LITIGATION

The Department is a party to several lawsuits respecting the Water Supply Contracts as described below.

### **Monterey Amendment Litigation**

In May 2003, the trial court approved a settlement agreement among the Department and the other parties in *Planning and Conservation League, et al. vs. Department of Water Resources and Central Coast Water Authority*, a lawsuit that challenged the Monterey Amendment. Under the settlement agreement, the Department agreed, among other things, to act as lead agency in the preparation of a new EIR for the Monterey Amendment. During the preparation and processing of the new EIR, the Department was permitted under the settlement agreement to continue to operate the State Water Project in accordance with the provisions of the Monterey Amendment, including the provisions pertaining to the transfer of land and related assets of the Kern Fan Element of the Kern Water Bank to KCWA. The Department also agreed to pay for certain watershed improvements in Plumas County and to pay the plaintiffs certain amounts for use in implementing the settlement agreement. The plaintiffs agreed to limit the grounds upon which they could challenge the new EIR after it is completed.

The parties to the lawsuit had engaged in settlement discussions after the Court of Appeal, in September 2000, reversed an earlier trial court ruling on the Monterey Amendment EIR. The trial court had found that the designation of the Central Coast Water Authority (“CCWA”), rather than the Department, as the lead agency for the Monterey Amendment EIR, violated the California Environmental Quality Act, but that the Monterey Amendment EIR was adequate, and the error as to the lead agency was harmless. As a result of the trial court’s ruling, the Department had proceeded to implement the Monterey Amendment, including transferring the Kern Fan Element property to KCWA. The Court of Appeal found that the Monterey Amendment EIR was inadequate because it failed to address all of the impacts of deleting a contract provision that would allow the Department to declare a permanent water shortage on the State Water Project and reduce the maximum annual amounts of water that may be requested. The California Supreme Court declined to review the case. The Court of Appeal remanded the case to the trial court to oversee the Department’s preparation of a new EIR and to consider whether the Monterey Amendment may continue to be implemented while the new EIR is being prepared. The May 2003 settlement agreement described in the immediately preceding paragraph addressed these issues.

In accordance with the Court of Appeal’s determination, the Department undertook preparation of the EIR in January 2003 and completed the Final EIR in February 2010. The Department filed its Notice of Determination in May 2010. In June 2010, two Delta water agencies and several environmental organizations and individuals filed a lawsuit in Sacramento Superior Court challenging the Department’s CEQA compliance and the validity of the Monterey Amendment, including the Department’s transfer of the Kern Fan Element to the KCWA. In July 2010, the same plaintiffs in the Sacramento Superior Court case filed a lawsuit in Kern County Superior Court challenging the transfer of the Kern Fan Element from KCWA to the Kern Water Bank Authority, a local joint powers agency which now has responsibility for the management of the Kern Fan Element and the Kern Water Bank. In addition, in June 2010, two water districts in Kern County filed a separate lawsuit in Kern County Superior Court, challenging primarily the Department’s CEQA compliance with respect to the Kern Fan Element transfer from the Department to KCWA. The two lawsuits filed in Kern County Superior Court have been transferred to the Sacramento Superior Court. In December 2012, the Department prevailed on its challenge to the plaintiffs’ validation causes of action (including the validity of Kern Fan Element transfer) on the grounds that they were not timely filed. This leaves only the plaintiffs’ CEQA compliance challenge, unless the plaintiffs appeal and are successful in their appeal to reinstate the validation causes of action. All three cases are in the pre-trial stage. The Department, however, does not expect that there would be any material adverse impact on the ability of the Department to meet its payment obligations, including those with respect to the Bonds, even if these lawsuits are successful.

## **Contractor Lawsuit Regarding Oroville Power Credits**

On April 25, 2005, fourteen Contractors filed a lawsuit against the Department in Sacramento County Superior Court for declaratory relief and breach of contract. The complaint alleges that pursuant to the Water Supply Contracts, the Department is required, but has failed, to credit all revenues from power generated by certain State Water Project conservation facilities (primarily the Hyatt and Thermalito Powerplants) to the Delta Water Charge, and, as a result, has overcharged the Contractor plaintiffs. The fourteen Contractors are: Alameda County Flood Control and Water Conservation District, Zone 7; Alameda County Water District; City of Yuba City; County of Butte; County of Kings; Dudley Ridge Water District; Empire West Side Irrigation District; KCWA; Napa County Flood Control and Water Conservation District; Oak Flat Water District; Plumas County Flood Control and Water Conservation District; Santa Clara Valley Water District; Solano County Water Agency; and Tulare Lake Basin Water Storage District. The complaint seeks a declaration that all “benefits” derived from the sale or other disposal of power from State Water Project conservation facilities be credited “in conformity with the terms of the Water Supply Contracts” and damages and costs in an unspecified amount. In December 2005, entities representing thirteen other Contractors intervened in the lawsuit in opposition to the claims of the plaintiffs. The remaining two Contractors were joined as indispensable parties. The trial in this case took place before a judge in November and December 2008. In May 2010, the Court entered its judgment in favor of the Department and the intervening Contractors, finding that the Department’s determinations and administration of the provisions regarding the Delta Water Charge power revenue credits were consistent with the Water Supply Contracts. The Contractor plaintiffs appealed the lower court’s decision to the Court of Appeal and in February 2013 the Court of Appeal issued its decision upholding the judgment of the trial court in favor of the Department and the intervening Contractors. If the Contractor plaintiffs seek review in the California Supreme Court and are ultimately successful in their efforts to reverse the lower court’s decisions, the Department believes Contractors requiring the most pumping for delivery of their State Water Project water would pay more to the Department under the Water Supply Contracts, while those requiring less pumping would pay less. The Department believes that this Contractor cost shifting would not materially adversely impact the Department’s ability to pay its obligations, including debt service on the Bonds.

## **Claims Relating to the Use of Bond Proceeds to Pay Capital Costs Allocable to Recreation and Fish and Wildlife Enhancement**

The State Water Project has multiple purposes, including water conservation, water transportation, power generation, flood control, public recreation, and fish and wildlife enhancement. California Water Code Section 11912 provides that costs incurred for the enhancement of fish and wildlife or for the development of public recreation may not be included in the Department’s prices, rates and charges for water and power. Under the terms of the Water Supply Contracts, the Department may only charge amounts that recover costs allocable to water conservation and water transportation (including the costs of mitigation of the fish and wildlife impacts arising from water conservation and transportation activities).

In December 2005, Metropolitan filed a “Notice of Contest” with the Department, challenging various charges in the Department’s billings. Based on its Notice of Contest, Metropolitan also filed a claim with the Victim Compensation and Government Claims Board, which claim was denied by the Board in March 2006. The Department and Metropolitan entered into a tolling agreement extending Metropolitan’s time to file a lawsuit on the denied claim until March 31, 2007. The tolling of Metropolitan’s time to file a lawsuit has been extended to December 31, 2015 in connection with the broader Tolling and Waiver Agreement described below.

One of the claims made by Metropolitan was that (1) Bond proceeds had been spent on the capital costs of certain recreation and fish and wildlife enhancement facilities that are a part of or are related to certain water system projects, (2) the Contractors had been charged under the Water Supply Contracts for costs relating to such recreation and fish and wildlife enhancement facilities (the “Recreation Costs”), and (3) such charges are not authorized by State law.

In the course of its investigation of Metropolitan's claims, the Department determined that it had spent approximately \$26.3 million of Bond proceeds and \$2.7 million of commercial paper proceeds on capital costs allocated by the Department to the purposes of recreation and fish and wildlife enhancement, had charged the Contractors approximately \$9.5 million for Bond debt service allocated to recreation and fish and wildlife enhancement and had paid approximately \$15.1 million of such financing costs with other revenues. The Department has issued restated bills to the Contractors for the years 1988 through 2007. This restatement has, among other things, credited back the \$9.5 million, plus interest, and restated the amount of "reductions in charges" made and to be made available to the Contractors under the Monterey Amendment to reflect the use of other revenues that are permitted to be used to pay financing costs of the Bonds allocable to recreation and fish and wildlife enhancement. (See "THE WATER SUPPLY CONTRACTS – Monterey Amendment.") One of the effects of such credits and restatements was to shift aggregate Water Supply Contract charges for the years 1997 through 2006 in the amount of approximately \$5 million among the Contractors, with some Contractors' aggregate Water Supply Contract charges being increased and other Contractors' aggregate Water Supply Contract charges being decreased. The Department has also filed with the State Treasurer, as trustee under the Resolution, a supplemental resolution (and an amendment to such supplemental resolution) determining and designating that the other revenues used to pay Bond debt service are Revenues under the Resolution.

The Department also negotiated with the Contractors who signed the Monterey Amendment, a Tolling and Waiver Agreement (as amended), under which each signing Contractor agrees that in order to facilitate Department financing transactions or other transactions that are to be secured by the revenues available to the Department under the Water Supply Contracts, and without establishing any precedent for interpretation of the Water Supply Contracts or the Davis-Dolwig Act, (California Water Code sections 11900-11925), each Contractor signing the agreement waives and releases any "Claims" based on or asserting the following:

(a) That the Department is not in compliance with its Resolution covenants or that the Contractor has any right to recover anything of value from Bondholders in their capacities as Bondholders arising out of or related to any "Claims" (defined as claims arising out of or related to (1) the Metropolitan claims; (2) the use, prior to July 1, 2006, of Bond proceeds or commercial paper proceeds to pay costs incurred for the enhancement of fish and wildlife or for the development of public recreation; (3) the related establishment, restatement or adjustment of charges and rate reductions under the Water Supply Contracts; (4) the accounting for the costs of the San Joaquin Drainage Program; (5) the allocation of certain costs in the Delta to the purposes of the development of public recreation and the enhancement of fish and wildlife; or (6) the Department's bills to the Contractors for 2007 through 2011, to the extent related to the foregoing); and

(b) That, so long as Water Supply Contract charges are properly based (without regard to Article 51 of the Water Supply Contracts (the "rate reductions" portion of the Monterey Amendment)) solely on water conservation and water transportation costs,

(i) the use of "System Revenues" (defined below) to satisfy the rate covenant of the Resolution or the commercial paper note resolution with respect to Bonds and commercial paper issued prior to July 1, 2006 (or obligations issued to refund such Bonds and commercial paper, but not including amounts needed for the payment of any "Defeasance Loan" (defined below)) (A) is not a "revenue need" under the Monterey Amendment, (B) is a violation of California Water Code Section 11912, or (C) is a breach of Water Supply Contracts; or

(ii) the use of System Revenues to pay a Defeasance Loan (A) is not an "additional State Water Resources Development System purpose" under the Monterey Amendment, (B) is a violation of California Water Code section 11912, or (C) is a breach of the Water Supply Contracts.

“System Revenues” is defined by the Tolling and Waiver Agreement to mean all revenues derived from the sale, delivery or use of water or power, and all other income or revenue derived by the Department from the State Water Resources Development System (which includes the State Water Project).

“Defeasance Loan” is defined by the Tolling and Waiver Agreement to mean any loan from the State General Fund, the Pooled Money Investment Account or other appropriate source obtained for the purpose of the retirement or defeasance of the Department’s commercial paper and/or revenue bonds outstanding as of July 1, 2006, the proceeds of which were used to pay capital costs of development of public recreation or fish and wildlife enhancement (or which refunded commercial paper and/or revenue bonds, the proceeds of which were used to pay capital costs of development of public recreation or fish and wildlife enhancement).

The Tolling and Waiver Agreement, as amended, also tolls (i.e., suspends) until December 31, 2015, the running of the time period and statute of limitations for filing by the Contractors of (1) protests regarding the Department’s bills to the Contractors for 2007 through 2013, (2) claims arising from the Department’s revisions to prior year invoices that were made to adjust for improper charges to the Contractors for recreation and fish and wildlife enhancement costs, and (3) certain other specified claims.

All 27 of the Contractors who signed the Monterey Amendment and one other Contractor have signed the Tolling and Waiver Agreement. The Contractors that have signed the Tolling and Waiver Agreement have more than 99 percent of the maximum Annual Table A Amounts and make more than 99 percent of the annual Water Supply Contract payments. The one non-signing Contractor was not asked to sign the Tolling and Waiver Agreement because the Tolling and Waiver Agreement deals primarily with issues arising under the Monterey Amendment.

No assurance can be given that Contractors will not file additional Notices of Contest, claims and/or lawsuits with respect to such restatements of the amount of reductions in charges under the Monterey Amendment. If successful, such claims may reduce the amount of Revenues available under the Resolution.

The proceeds of the PMIA Loan in the amount of \$29,600,000 together with certain other available funds of the Department were used to retire or provide for the defeasance of approximately \$28.2 million principal amount of Bonds and Notes, the proceeds of which were used to pay costs allocated by the Department to the development of public recreation or fish and wildlife enhancement (or which refunded commercial paper and/or revenue bonds, the proceeds of which were used to pay capital costs of development of public recreation or fish and wildlife enhancement). The Department no longer allocates proceeds of Notes or Bonds to the development of public recreation or fish and wildlife enhancement and, accordingly, neither the Bonds remaining outstanding nor any additional Bonds will be treated by the Department as Notes or Bonds, the proceeds of which were used to pay, directly or indirectly, costs allocable to the development of public recreation or fish and wildlife enhancement.

### **Contractor Area of Origin Claims**

In July 2008, Contractors Solano County Water Agency, Napa County Flood Control & Water Conservation District, Butte County and Yuba City filed a lawsuit against the Department in State court alleging that they have area of origin rights under California Water Code section 11460 and that they are therefore entitled to their full water supply under their respective Water Supply Contracts during periods of water shortage, as long as the State Water Project is exporting water. These Contractors claim that the deficiency provisions of the long-term Water Supply Contracts, which specify the manner in which the Department is required to allocate shortages of water among all Contractors, do not apply to them. If the Contractors prevail in their area of origin claim, there will be less water to allocate to other Contractors during periods of water shortages. The case is currently in the pre-trial stage. However, even if these Contractors prevail, the

Department believes that it will not materially affect State Water Project finances or the ability of the Department to pay debt service on the Bonds.

## **THE CONTRACTORS**

The 29 Contractors are principally located in the San Francisco Bay area, the Central Coast, the Central Valley and Southern California and their service areas encompass approximately 39,200 square miles, approximately 25 percent of the State's land area, with a population of approximately 26 million, or about 71 percent of the State's population.

With three exceptions, the Contractors are established as districts under various State statutes providing for the formation of districts for water-related purposes. One Contractor is a city and two are counties. Of the 29 Contractors, 24 provide water primarily for municipal and industrial purposes and five provide water primarily for agricultural purposes.

The State Water Project was designed to be a supplemental source of water for Contractors, not an exclusive source, and Contractors have various other sources of water supply.

Certain of the Contractors also provide other services, including flood control, ground water replenishment, sewage collection and disposal, solid waste and trash collection and disposal, hydroelectric power generation and first aid, ambulance and paramedical services.

### **Governing Bodies**

Eight of the Contractors are governed by county boards of supervisors, 19 by elected boards of directors, and one by its city council. Metropolitan's board of directors consists of representatives appointed by the governing bodies of its constituent public agencies. Boards of supervisors generally include five members who are elected by popular vote. Specially elected governing boards generally include between five and eleven members and are elected by registered voters except for a few districts in agricultural areas, where the vote is based upon ownership of land in the district.

### **Water Rates and Taxation**

Rates and charges of the Contractors are generally set by each Contractor's governing body and are not presently subject to any state or federal regulatory agency.

Many Contractors receive a major portion of their income from *ad valorem* taxes on property and some make all payments under their Water Supply Contracts from *ad valorem* taxes. The ability of Contractors to tax for general purposes and to appropriate for general purposes from tax revenue is limited under California law. (See "CERTAIN LIMITATIONS ON CONTRACTOR REVENUE SOURCES.")

### **Selected Contractor Data**

The table entitled "Selected Data on the Contractors" sets forth for each Contractor the year in which it was established, its estimated population and principal water-related activities.

## SELECTED DATA ON THE CONTRACTORS

Contractor	Year Established	Estimated December 31, 2009 Population	Principal Water Related Activities
Alameda County Flood Control and Water Conservation District, Zone 7	1967	216,000	Treats, distributes, and stores State water for municipal and agricultural purposes.
Alameda County Water District	1913	323,000	Treats and distributes State water for municipal purposes. Uses State water to replenish ground water basins for municipal and agricultural purposes as well as for salt water barrier protection for ground water basins.
Antelope Valley-East Kern Water Agency	1959	282,698	Distributes State water for agricultural purposes. Treats and distributes State water for municipal purposes.
Castaic Lake Water Agency	1962	259,200	Treats and distributes State water for municipal purposes.
City of Yuba City	1908	63,338	Treats and distributes State water for municipal purposes.
Coachella Valley Water District	1918	283,529	Exchanges State water for water from Metropolitan for storage in underground basins and for distribution for agricultural purposes.
County of Butte	1850	219,335	Distributes State water for municipal purposes.
County of Kings	1893	154,743	Exchanges State water for water from the Tulare Lake Basin Water Storage District for recreational purposes.
Crestline-Lake Arrowhead Water Agency	1962	29,959	Treats and distributes State water for municipal purposes.
Desert Water Agency	1961	71,715	Exchanges State water for water from Metropolitan for storage in underground basins and distribution for municipal purposes.
Dudley Ridge Water District	1963	36	Distributes State water for agricultural purposes.
Empire West Side Irrigation District	1931	11	Distributes State water for agricultural purposes. Exercises surface water rights.
Kern County Water Agency	1961	770,300	Distributes State water to 16 districts for agricultural and municipal use. Replenishes ground water basins with State water for municipal and agricultural use. Exercises flood control functions.
Littlerock Creek Irrigation District	1892	2,900	Distributes State water for agricultural purposes.
The Metropolitan Water District of Southern California	1928	18,559,751	Transmits and distributes State water and water from the Colorado River to 27 public agencies for municipal, agricultural and ground water replenishment purposes.
Mojave Water Agency	1960	453,297	Distributes State water for municipal purposes and uses State water to replenish ground water basins.
Napa County Flood Control and Water Conservation District	1951	136,704	Distributes water for municipal purposes. Exercises flood control functions.
Oak Flat Water District	1964	10	Distributes State water for agricultural purposes.
Palmdale Water District	1918	102,025	Treats and distributes State water for municipal purposes.
Plumas County Flood Control and Water Conservation District	1967	21,200	Distributes State water. Exercises flood control functions.
San Bernardino Valley Municipal Water District	1954	657,722	Uses State water to replenish ground water basins and for municipal purposes.
San Gabriel Valley Municipal Water District	1959	210,145	Uses State water to replenish ground water basins.
San Geronio Pass Water Agency	1961	75,000	Uses State water to replenish ground water basins and for municipal purposes.
San Luis Obispo County Flood Control and Water Conservation District	1945	265,182	Has contracted for State water. Exercises flood control functions.

<b>Contractor</b>	<b>Year Established</b>	<b>Estimated December 31, 2009 Population</b>	<b>Principal Water Related Activities</b>
Santa Barbara County Flood Control and Water Conservation District	1956	421,625	Has transferred its rights under its Water Supply Contract to the Central Coast Water Authority, which will distribute State water for municipal purposes. Exercises flood control functions.
Santa Clara Valley Water District	1951	1,764,499	Treats and distributes State water for municipal purposes. Distributes State water for agricultural purposes and for replenishment of ground water basins. Exercises flood control functions.
Solano County Water Agency	1958	412,488	Distributes State water for municipal purposes. Exercises flood control functions.
Tulare Lake Basin Water Storage District	1926	23	Distributes State water for agricultural purposes. Exercises surface water rights.
Ventura County Flood Control District	1944	460,000	Purchases State water and sub-contracts the entire amount to Casitas Municipal Water District. While Casitas manages the facility, Ventura County has primary responsibility for payment for State water. Exercises flood control functions.
<b>Total</b>		<b>26,216,435</b>	

Source: Department of Water Resources, State Water Project Analysis Office.

### **Water Deliveries and Contractor Payments**

The tables on the following pages show, for the last five calendar years, historical water deliveries from the State Water Project to each Contractor and historical payments under the Water Supply Contracts and under the Devil Canyon Castaic Contract by each Contractor.

**Historical Deliveries of Water from the State Water Project to the Contractors <sup>(1)</sup>  
(in acre-feet)**

<b>Contractor</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>Maximum Annual Table A Amount<sup>(2)</sup></b>
Alameda County Flood Control and Water Conservation District, Zone 7 .....	41,186	31,044	47,343	52,972	55,240	80,619
Alameda County Water District.....	22,902	19,452	22,571	36,610	20,831	42,000
Antelope Valley-East Kern Water Agency .....	47,758	45,747	58,489	94,046	108,548	141,400
Castaic Lake Water Agency.....	42,878	42,085	56,033	39,241	45,724	95,200
City of Yuba City.....	1,933	2,114	2,331	2,297	2,695	9,600
Coachella Valley Water District .....	46,791	46,022	85,592	79,464	118,516	138,350
County of Butte.....	9,201	581	807	1,092	1,374	27,500
County of Kings.....	3,851	3,391	4,679	6,556	7,556	9,305
Crestline-Lake Arrowhead Water Agency .....	689	865	357	192	483	5,800
Desert Water Agency.....	26,428	18,263	31,183	32,021	43,117	55,750
Dudley Ridge Water District.....	39,566	21,237	27,967	60,074	42,586	50,343
Empire West Side Irrigation District.....	947	1,034	3,259	1,915	2,242	3,000
Kern County Water Agency.....	532,343	759,025	697,958	1,200,563	976,956	982,730
Littlerock Creek Irrigation District.....	830	42	-	-	-	2,300
The Metropolitan Water District of Southern California .....	894,313	929,667	1,416,045	1,700,473	1,238,565	1,911,500
Mojave Water Agency .....	17,901	29,067	38,152	5,099	11,244	82,800
Napa County Flood Control and Water Conservation District.....	13,292	10,904	12,417	11,275	9,860	29,025
Oak Flat Water District.....	1,985	1,993	2,906	2,715	3,208	5,700
Palmdale Water District .....	5,506	15,339	10,969	17,313	19,056	21,300
Plumas Co. Flood Control and Water Conservation District.....	243	200	243	98	79	2,700
San Bernardino Valley Municipal Water District .....	38,145	38,304	49,379	30,060	113,002	102,600
San Gabriel Valley Municipal Water District .....	10,080	11,520	19,180	23,591	22,058	28,800
San Geronio Pass Water Agency .....	5,905	6,397	8,240	10,503	11,010	17,300
San Luis Obispo Co. Flood Control and Water Conserv. Dist. ....	8,426	3,801	3,757	4,631	3,944	25,000
Santa Barbara Co. Flood Control and Water Conserv. Dist. <sup>(3)</sup> .....	13,969	15,452	17,775	22,786	19,474	45,486
Santa Clara Valley Water District.....	59,160	68,194	107,871	131,237	80,794	100,000
Solano County Water Agency.....	40,320	30,950	30,816	28,034	29,394	47,756
Tulare Lake Basin Water Storage District.....	33,891	36,846	70,238	63,141	105,083	88,922
Ventura County Flood Control District.....	3,798	3,891	4,075	4,000	1,203	20,000
<b>TOTAL.....</b>	<b>1,964,237</b>	<b>2,193,427</b>	<b>2,830,632</b>	<b>3,661,999</b>	<b>3,093,842</b>	<b>4,172,786</b>

<sup>(1)</sup> Historical deliveries reflect changes resulting from the reclassification of State Water Project (SWP) water to or from these water types: flexible withdrawal, Non-SWP local water rights, or Non-SWP water.

<sup>(2)</sup> Reflects permanent transfers of Table A Amounts through December 31, 2012. For an explanation of Table A Amounts see “THE WATER SUPPLY CONTRACTS– Basic Contract– Annual Table A Amounts.”

<sup>(3)</sup> As of July 1, 1989, Santa Barbara County FCWCD transferred certain of its rights under its Water Supply Contract to certain local water purveyors and users within Santa Barbara County. Thereafter, on September 26, 1991, the local water purveyors and users transferred those rights to the Central Coast Water Authority in consideration for its agreement to provide for the delivery of State Water Project water to the local water purveyors and users. Although the Department did not object to these transfers, the Department considers Santa Barbara County FCWCD to be the party to which the Department is obligated under the Water Supply Contract, and the Department did not release Santa Barbara County FCWCD from its Water Supply Contract obligations.

Source: Department of Water Resources, State Water Project Analysis Office.



**Historical Payments to the Department from the Contractors<sup>(1)</sup>**  
(in thousands)

Contractor	2008	2009	2010	2011	2012
Alameda County Flood Control and Water Conservation District, Zone 7 .....	\$ 15,825	\$ 23,143	\$ 25,842	\$ 26,969	\$ 32,995
Alameda County Water District.....	6,910	6,549	6,233	6,244	8,981
Antelope Valley-East Kern Water Agency .....	27,963	29,559	27,781	27,238	31,090
Castaic Lake Water Agency .....	21,973	22,255	19,117	19,814	25,540
City of Yuba City.....	331	357	428	498	497
Coachella Valley Water District .....	60,129	57,555	48,405	35,892	56,834
County of Butte.....	811	864	1,072	1,264	1,423
County of Kings.....	764	743	729	797	829
Crestline-Lake Arrowhead Water Agency .....	1,830	1,731	1,332	1,668	1,718
Desert Water Agency.....	22,650	21,222	17,328	10,898	22,608
Dudley Ridge Water District.....	4,918	4,978	3,840	4,295	4,595
Empire West Side Irrigation District <sup>(3)</sup> .....	327	207	226	200	259
Kern County Water Agency.....	93,065	97,825	98,494	97,983	112,068
Littlerock Creek Irrigation District .....	738	738	398	711	563
The Metropolitan Water District of Southern California ....	594,504	667,895	540,116	619,293	555,505
Mojave Water Agency .....	18,108	24,906	22,812	32,331	23,528
Napa County Flood Control and Water Conservation District .....	5,581	5,729	6,713	8,896	8,894
Oak Flat Water District.....	341	348	358	409	334
Palmdale Water District.....	6,610	6,566	5,492	5,606	5,425
Plumas County Flood Control and Water Conservation District <sup>(3)</sup> .....	89	97	120	130	141
San Bernardino Valley Municipal Water District .....	38,557	54,741	39,054	47,372	43,642
San Gabriel Valley Municipal Water District .....	10,824	11,923	9,284	7,902	9,332
San Geronio Pass Water Agency .....	11,015	20,198	14,933	14,324	14,676
San Luis Obispo Co. Flood Control and Water Conservation District. ....	4,767	8,565	5,701	5,931	6,966
Santa Barbara Co. Flood Control and Water Conservation District <sup>(2)</sup> .....	39,743	44,303	41,264	46,884	37,531
Santa Clara Valley Water District.....	18,156	17,036	17,213	17,718	23,489
Solano County Water Agency.....	6,724	8,017	7,657	9,384	10,328
Tulare Lake Basin Water Storage District .....	8,204	8,206	7,910	7,303	8,480
Ventura County Flood Control District.....	6,314	6,690	4,158	6,052	5,103
<b>TOTAL<sup>(4)</sup> .....</b>	<b>\$1,027,771</b>	<b>\$1,152,948</b>	<b>\$974,010</b>	<b>\$1,064,006</b>	<b>\$1,053,374</b>

<sup>(1)</sup> Contractor payments made in each year include the payment of 125 percent of annual debt service for the Bonds in that year, the amount of such payments that is not required to pay debt service on the Bonds in that year is credited back to the Contractors, the historical payments do not reflect such credits or any other subsequent adjustments.

<sup>(2)</sup> As of July 1, 1989, Santa Barbara County FCWCD transferred certain of its rights under its Water Supply Contract to certain local water purveyors and users within Santa Barbara County. Thereafter, on September 26, 1991, the local water purveyors and users transferred those rights to the Central Coast Water Authority in consideration for its agreement to provide for the delivery of State Water Project water to the local water purveyors and users. Although the Department did not object to these transfers, the Department considers Santa Barbara County FCWCD to be the party to which the Department is obligated under the Water Supply Contract, and the Department did not release Santa Barbara County FCWCD from its Water Supply Contract obligations.

<sup>(3)</sup> Have not signed the Monterey Amendment.

<sup>(4)</sup> Totals may not sum due to rounding.

Source: Department of Water Resources, State Water Project Analysis Office

## Payment History

The Department has not experienced payment delinquencies or defaults by Contractors that have had a materially adverse effect on the maintenance or operation of the State Water Project, or the ability of the Department to pay its obligations when due. Under the Water Supply Contracts, if a Contractor defaults in payment, the Department may, and under certain conditions is required to, upon six months' notice, suspend water deliveries during the period of default. In accordance with a statutory requirement, each Water Supply Contract requires that whenever the Contractor fails or is unable to raise sufficient funds by other means the Contractor must levy upon all taxable property in the Contractor's service area a tax or assessment sufficient (with other available moneys) to provide for all payments under the Water Supply Contract. (See "CERTAIN LIMITATIONS ON CONTRACTOR REVENUE SOURCES.")

## Selected Contractor Financial Information

*Relative Contributions of Contractors.* The following table lists the three largest Contractors based on projected payments to the Department through the final maturity of the Bonds, these percentages may change over time.

<b>Contractor</b>	<b>Projected Percentage Contribution</b>
The Metropolitan Water District of Southern California.....	46%
Santa Barbara County Flood Control and Water Conservation District/Central Coast Water Authority .....	12
Kern County Water Agency.....	8
Twenty-six other Contractors.....	34
<b>Total .....</b>	<b>100%</b>

*Metropolitan.* The audited financial statements of Metropolitan for the year ended June 30, 2012, can be obtained at <http://www.munios.com>, then searching for keyword "Series AM" and choosing the appropriate link.

*Santa Barbara County FCWCD/Central Coast Water Authority.* As of July 1, 1989, Santa Barbara County FCWCD transferred certain of its rights under its Water Supply Contract to certain local water purveyors and users within Santa Barbara County. On September 26, 1991, the local water purveyors and users transferred those rights to the Central Coast Water Authority in consideration for its agreement to provide for the delivery of State Water Project water to the local water purveyors and users. Although the Department did not object to these transfers, the Department considers Santa Barbara County FCWCD to be the party to which the Department is obligated under the Water Supply Contract, and the Department did not release Santa Barbara County FCWCD from its Water Supply Contract obligations. The audited financial statements of Santa Barbara County FCWCD for the year ended June 30, 2012, and the audited financial statements of Central Coast Water Authority for the year ended June 30, 2012, can be obtained at <http://www.munios.com>, then searching for keyword "Series AM" and choosing the appropriate link.

*KCWA.* The audited financial statements of KCWA for the year ended June 30, 2011, can be obtained at <http://www.munios.com>, then searching for keyword "Series AM" and choosing the appropriate link.

*Certain Limitations.* **The Department has made no independent verification of the data contained in the audited financial statements of any Contractor and makes no representations as to its correctness, completeness, or comparability.** Macias, Gini & O’Connell LLP, independent auditors for the State Water Resources Development System, are not the independent auditors for any of the three largest Contractors listed in the table above.

*Contractor Official Statements and Continuing Disclosure Filings.* Various contractors periodically file Official Statements and disclosure reports with the MSRB in connection with their publicly offered debt. Such Official Statements and disclosure reports are available from the MSRB but are not incorporated by reference herein and neither the Department nor the Underwriters assume any responsibility for the completeness or accuracy thereof.

## **CERTAIN LIMITATIONS ON CONTRACTOR REVENUE SOURCES**

This section describes certain constitutional or statutory provisions that may limit the ability of some or all of the Contractors to levy and collect fees, charges, taxes or assessments.

### **Article XIII A of the Constitution**

An initiative measure approved by the California voters on June 6, 1978 (Proposition 13), added Article XIII A to the California Constitution. Section 1(a) of Article XIII A limits the maximum *ad valorem* taxes on real property to one percent of the “full cash value” of the property, subject to certain exceptions, including *ad valorem* taxes to pay debt service indebtedness approved by voters prior to July 1, 1978. (See “THE WATER SUPPLY CONTRACTS – Obligation to Levy Taxes or Assessments.”) “Full cash value” is defined as the valuation of real property as shown on the 1975-76 tax roll, and thereafter the appraised value of property when purchased, newly constructed or a change in ownership has occurred. The value base of the property may also be increased to reflect the inflation rate, but not to exceed 2 percent per year.

On June 3, 1986, the California voters approved an amendment to Section 1(b) of Article XIII A permitting *ad valorem* taxes or special assessments in excess of the one percent limit in Section 1(a) to pay the interest and redemption charges on any bonded indebtedness for the acquisition or improvement of real property approved on or after July 1, 1978 by two-thirds of the votes cast by the voters voting on the proposition.

### **Article XIII B of the Constitution**

An initiative amendment to the California Constitution (Article XIII B) was approved by the California electorate on November 6, 1979. This amendment establishes limits on certain annual appropriations of state and local government entities. Initially, the limits are based generally on appropriations for the fiscal year 1978-79 with future adjustments permitted for changes in the cost of living, population and certain other factors. The definition of appropriations subject to limitation is stated so as to exclude, among other things, (1) appropriations of proceeds received by a government entity from user fees to the extent such proceeds do not exceed the costs reasonably borne by such entity in providing the product or service, (2) the appropriations of any special district “which did not as of the 1977-78 fiscal year levy an *ad valorem* tax on property in excess of 12 1/2 cents per \$100 of assessed value,” and (3) “appropriations required to pay the cost of interest and redemption charges, including the funding of any reserve or sinking fund required in connection therewith, on indebtedness existing or legally authorized as of January 1, 1979, or a bonded indebtedness thereafter approved . . .” by vote of the electors of the issuing entity. In addition, the amendment provides that nothing in it “shall be construed

to impair the ability of the State or any local government to meet its obligations with respect to existing or future bonded indebtedness.”

### **Article XIII C and Article XIII D of the Constitution**

A substantial portion of the revenues of the Contractors is derived from the collection of charges for water service. In addition, each Contractor has agreed to levy a tax or assessment sufficient to provide for all payments under its Water Supply Contract if it is unable to raise sufficient funds by other means. The Contractors’ ability to collect such charges, and to levy such taxes or assessments, may be limited by the Right to Vote on Taxes Act (“Proposition 218”), an initiative amendment to the California Constitution approved by the California voters in November 1996.

Proposition 218 added Articles XIII C and XIII D to the California Constitution, creating additional requirements for the imposition by most local governments of “general taxes,” “special taxes,” “assessments,” “fees,” and “charges.” Proposition 218 became effective, pursuant to its terms, as of November 6, 1996, although compliance with some of its provisions was deferred until July 1, 1997, and certain of its provisions purport to apply to any tax imposed for general governmental purposes (i.e., “general taxes”) imposed, extended or increased on or after January 1, 1995 and prior to November 6, 1996. Article XIII D imposes substantive and procedural requirements on the imposition, extension or increase of any “fee” or “charge” subject to its provisions. A “fee” or “charge” subject to Article XIII D includes any levy, other than an ad valorem tax, special tax, or assessment, imposed by an agency upon a parcel or upon a person as an incident of property ownership. Article XIII D prohibits, among other things, the imposition of any proposed fee or charge, and, possibly, the increase of any existing fee or charge, in the event written protests against the proposed fee or charge are presented at a required public hearing on the fee or charge by a majority of owners of the parcels upon which the fee or charge is to be imposed. Except for fees and charges for water, sewer and refuse collection services, the approval of a majority of the property owners subject to the fee or charge, or at the option of the agency, by a two-thirds vote of the electorate residing in the affected area, is required within 45 days following the public hearing on any such proposed new or increased fee or charge. The California Supreme Court decisions in Richmond v. Shasta Community Services District, 32 Cal. 4th 409 (2004) (“Richmond”), and Bighorn-Desert View Water Agency vs. Verjil (published July 24, 2006) (“Bighorn”) have clarified some of the uncertainty surrounding the applicability of Section 6 of Article XIII D to service fees and charges. In Richmond, the Shasta Community Services District charged a water connection fee, which included a capacity charge for capital improvements to the water system and a fire suppression charge. The Court held that both the capacity charge and the fire suppression charge were not subject to Article XIII D because a water connection fee is not a property-related fee or charge because it results from the property owner’s voluntary decision to apply for the connection. In both Richmond and Bighorn, however, the Court stated that a fee for ongoing water service through an existing connection is imposed “as an incident of property ownership” within the meaning of Article XIII D, rejecting, in Bighorn, the water agency’s argument that consumption-based water charges are not imposed “as an incident of property ownership” but as a result of the voluntary decisions of customers as to how much water to use.

Article XIII D also provides that “standby charges” are considered “assessments” and must follow the procedures required for “assessments” under Article XIII D and imposes several procedural requirements for the imposition of any assessment, which may include (1) various notice requirements, including the requirement to mail a ballot to owners of the affected property; (2) the substitution of a property owner ballot procedure for the traditional written protest procedure, and providing that “majority protest” exists when ballots (weighted according to proportional financial obligation) submitted in opposition exceed ballots in favor of the assessments; and (3) the requirement that the levying entity “separate the general benefits from the special benefits conferred on a parcel” of land. Article XIII D also precludes standby charges for services that are not immediately available to the parcel being charged.

Article XIID provides that all existing, new or increased assessments are to comply with its provisions beginning July 1, 1997. Existing assessments imposed on or before November 5, 1996, and “imposed exclusively to finance the capital costs or maintenance and operations expenses for [among other things] water” are exempted from some of the provisions of Article XIID applicable to assessments.

Article XIIC extends the people’s initiative power to reduce or repeal existing local taxes, assessments, fees and charges. This extension of the initiative power is not limited by the terms of Article XIIC to fees, taxes, assessment fees and charges imposed after November 6, 1996 and absent other authority could result in retroactive reduction in any existing taxes, assessments, fees or charges. In Bighorn, the Court concluded that under Article XIIC local voters by initiative may reduce a public agency’s water rates and delivery charges. The Court noted, however, that it was not holding that the authorized initiative power is free of all limitations, stating that it was not determining whether the electorate’s initiative power is subject to the public agency’s statutory obligation to set water service charges at a level that will “pay the operating expenses of the agency, ... provide for repairs and depreciation of works, provide a reasonable surplus for improvements, extensions, and enlargements, pay the interest on any bonded debt, and provide a sinking or other fund for the payment of the principal of such debt as it may become due.”

In November 2010, the California voters approved the Supermajority Vote to Pass New Taxes and Fees Act (“Proposition 26”), an initiative amendment to Article XIIC. Proposition 26 amended Article XIIC to add additional restrictions on local agencies’ ability to impose new or increase existing charges. These additional restrictions do not, however, apply to, among other things, “property-related fees imposed in accordance with the provisions of Article XIID,” which includes a fee for ongoing water service.

No assurance may be given that Articles XIIC and XIID will not have a material adverse impact on Contractors’ ability to generate revenues.

### **Other Initiative Measures**

Articles XIIA, XIIB, XIIC and XIID were adopted, and in some cases amended, pursuant to California’s constitutional initiative process. From time to time other initiative measures could be adopted by California voters, placing additional limitations on the ability of the Contractors to increase revenues.

### **Special Limitations Applicable to Metropolitan**

In 1983, the California Legislature placed additional restrictions on the taxing power of Metropolitan. The restrictions reflected the ongoing debates among Metropolitan’s member agencies over whether to continue using property taxes as a major source of revenue or whether to shift to reliance on water rates. The legislation permitted Metropolitan to raise its property tax rate above one percent only under limited circumstances. The rate could be higher in 1983-84, but in 1984-85 and 1985-86, the rate would have to return to its 1982-83 level unless 80 percent of Metropolitan’s board found that a fiscal emergency existed. The bill also required Metropolitan to report to the Legislature regarding its efforts to reduce its reliance on property taxes. Metropolitan reached an agreement among its member agencies for gradually shifting to an increased reliance on water rates and filed its report. In response, the Legislature codified the agreement in SB 1445 in 1984 (Chapter 271, Statutes of 1984), which, among other things, made several amendments to Metropolitan’s organizing Act. One provision provides that commencing with fiscal year 1990-91, any *ad valorem* property tax levied by Metropolitan, other than special annexation tax levies, shall not exceed the composite amount required to pay (1) its general obligation

bond debt service, and (2) that portion of its Water Supply Contract payment that is reasonably allocable, as determined by Metropolitan, to the portion of the debt service payment for the Burns-Porter Act bonds that were approved by the State's voters in 1960 and which were used to finance construction of facilities for the benefit of Metropolitan. This statutory tax levy restriction would not apply, however, if Metropolitan's board, following a hearing to consider the issue, should find that a tax in excess of the limitation would be essential to Metropolitan's fiscal integrity.

## **TAX MATTERS**

In the opinion of Orrick, Herrington & Sutcliffe LLP, Bond Counsel to the Department ("Bond Counsel"), based upon an analysis of existing laws, regulations, rulings and court decisions, and assuming, among other matters, the accuracy of certain representations and compliance with certain covenants, interest on the Series AM Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986 (the "Code") and is exempt from State of California personal income taxes. Bond Counsel is of the further opinion that interest on the Series AM Bonds is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although Bond Counsel observes that such interest is included in adjusted current earnings when calculating corporate alternative minimum taxable income. A complete copy of the proposed form of opinion of Bond Counsel is set forth in APPENDIX F hereto.

Series AM Bonds purchased, whether at original issuance or otherwise, for an amount higher than their principal amount payable at maturity (or, in some cases, at their earlier call date) ("Premium Bonds") will be treated as having amortizable bond premium. No deduction is allowable for the amortizable bond premium in the case of bonds, like the Premium Bonds, the interest on which is excluded from gross income for federal income tax purposes. However, the amount of tax exempt interest received, and a beneficial owner's basis in a Premium Bond, will be reduced by the amount of amortizable bond premium properly allocable to such beneficial owner. Beneficial owners of Premium Bonds should consult their own tax advisors with respect to the proper treatment of amortizable bond premium in their particular circumstances.

The Code imposes various restrictions, conditions and requirements relating to the exclusion from gross income for federal income tax purposes of interest on obligations such as the Series AM Bonds. The Department has made certain representations and covenanted to comply with certain restrictions, conditions and requirements designed to ensure that interest on the Series AM Bonds will not become includable in federal gross income. Inaccuracy of these representations or failure to comply with these covenants may result in interest on the Series AM Bonds being included in gross income for federal income tax purposes, possibly from the date of original issuance of the Series AM Bonds. The opinion of Bond Counsel assumes the accuracy of these representations and compliance with these covenants. Bond Counsel has not undertaken to determine (or to inform any person) whether any actions taken (or not taken) or events occurring (or not occurring), or any other matters coming to Bond Counsel's attention after the date of issuance of the Series AM Bonds may adversely affect the value of, or the tax status of interest on, the Series AM Bonds. Accordingly, the opinion of Bond Counsel is not intended to, and may not, be relied upon in connection with any such actions, events or matters.

Although Bond Counsel is of the opinion that interest on the Series AM Bonds is excluded from gross income for federal income tax purposes and is exempt from State of California personal income taxes, the ownership or disposition of, or the accrual or receipt of interest on, the Series AM Bonds may otherwise affect a beneficial owner's federal, state or local tax liability. The nature and extent of these other tax consequences depends upon the particular tax status of the beneficial owner or the beneficial owner's other items of income or deduction. Bond Counsel expresses no opinion regarding any such other tax consequences.

Current and future legislative proposals, if enacted into law, clarification of the Code or court decisions may cause interest on the Series AM Bonds to be subject, directly or indirectly, to federal income taxation or to be subject to or exempted from state income taxation, or otherwise prevent beneficial owners from realizing the full current benefit of the tax status of such interest. The introduction or enactment of any such legislative proposals, clarification of the Code or court decisions may also affect, perhaps significantly, the market price for, or marketability of, the Series AM Bonds. Prospective purchasers of the Series AM Bonds should consult their own tax advisors regarding any pending or proposed federal or state tax legislation, regulations or litigation, and regarding the impact of future legislation, regulations or litigation, as to which Bond Counsel expresses no opinion.

The opinion of Bond Counsel is based on current legal authority, covers certain matters not directly addressed by such authorities, and represents Bond Counsel's judgment as to the proper treatment of the Series AM Bonds for federal income tax purposes. It is not binding on the Internal Revenue Service ("IRS") or the courts. Furthermore, Bond Counsel cannot give and has not given any opinion or assurance about the future activities of the Department or about the effect of future changes in the Code, the applicable regulations, the interpretation thereof or the enforcement thereof by the IRS. The Department has covenanted, however, to comply with the requirements of the Code.

Unless separately engaged, Bond Counsel is not obligated to defend the Department or the beneficial owners regarding the tax-exempt status of the Series AM Bonds in the event of an audit examination by the IRS. Under current procedures, parties other than the Department and their appointed counsel, including the beneficial owners, would have little, if any, right to participate in the audit examination process. Moreover, because achieving judicial review in connection with an audit examination of tax-exempt bonds is difficult, obtaining an independent review of IRS positions with which the Department legitimately disagrees may not be practicable. Any action of the IRS, including but not limited to selection of the Series AM Bonds for audit, or the course or result of such audit, or an audit of bonds presenting similar tax issues may affect the market price for, or the marketability of, the Series AM Bonds, and may cause the Department or the beneficial owners to incur significant expense.

## **RATINGS**

Moody's Investors Service, Inc. ("Moody's"), and Standard & Poor's Rating Services, a Standard & Poor's Financial Services LLC business ("Standard & Poor's"), have assigned ratings of "Aa1" and "AAA," respectively, to the Series AM Bonds. Such ratings are based in part upon information provided by the Department. Each rating reflects only the views of the applicable rating agency, and an explanation of the significance of such rating may be obtained only from such rating agency. Such ratings are not a recommendation to buy, sell or hold the Series AM Bonds. There can be no assurance that either such rating will continue for any given period of time or that it will not be revised downward or withdrawn entirely if, in the judgment of the applicable rating agency, circumstances so warrant. Any such downward revision or withdrawal of any rating may have an adverse effect on the marketability or market price of the Series AM Bonds. The Department undertakes no responsibility to maintain its current credit ratings on the Bonds or to oppose any downward revision, suspension or withdrawal.

## **FINANCIAL ADVISOR**

Montague DeRose and Associates, LLC served as financial advisor to the Department in connection with the issuance of the Series AM Bonds.

## **APPROVAL OF LEGAL PROCEEDINGS**

The issuance of the Series AM Bonds is subject to the delivery on the issuance date of the approving opinions of The Honorable Kamala D. Harris, the Attorney General of the State, and Orrick, Herrington & Sutcliffe LLP, Bond Counsel. The proposed forms of such opinions are set forth in APPENDIX E and APPENDIX F, respectively to this Official Statement. Certain matters are also subject to the approval of Stradling Yocca Carlson & Rauth, a Professional Corporation counsel to the Underwriters.

## **FINANCIAL STATEMENTS**

The financial statements of the State Water Resources Development System at June 30, 2012, and June 30, 2011, and for the years then ended, appearing in APPENDIX B to this Official Statement have been audited by Macias, Gini & O'Connell LLP, independent auditors (the "Auditor"), as set forth in the report of Macias, Gini & O'Connell LLP appearing in APPENDIX B.

The State Water Resources Development System (a component unit of the State) includes the State Water Project, the Davis-Grunsky Act Program and the San Joaquin Drainage Program.

## **VERIFICATION**

Grant Thornton LLP, a firm of independent public accountants, has delivered to the Department its verification report indicating that it has verified, in accordance with attestation standards established by the American Institute of Certified Public Accountants, the mathematical accuracy of (a) the mathematical computations of the adequacy of the amounts deposited or to be deposited with the State Treasurer in the Escrow Account established for the Series AM Refunded Bonds to pay the redemption price of and interest on the Refunded Bonds, when due and (b) the mathematical computations of yield used by Bond Counsel to support its opinion that interest on the Series AM Bonds will be excluded from gross income for federal income tax purposes. On the date of issuance of the Series AM Bonds, Grant Thornton LLP will deliver a supplement to the verification report referenced above confirming the accuracy of the information in such verification report described in clause (a) of this paragraph as of the issuance date of the Series AM Bonds.

The verification performed by Grant Thornton LLP has been, and the confirmation of such verification as described in the preceding paragraph will be, solely based upon data, information and documents provided to Grant Thornton LLP by the Department and its representatives. Grant Thornton LLP has restricted and will restrict, as applicable, its procedures for recalculating the computations provided by the Department and its representatives and has not evaluated or examined the assumptions or information used in the computations. (See "PLAN OF REFUNDING.")

## **UNDERWRITING**

The Series AM Bonds are being purchased by an underwriting group, represented by RBC Capital Markets, LLC (referred to herein as the "Underwriters"), from the State Treasurer, who is authorized pursuant to the Act to sell the Series AM Bonds on behalf of the Department. The Underwriters have agreed to purchase the Series AM Bonds at a price of \$212,985,716.64, representing the principal amount of the Series AM Bonds, plus original issue premium of \$29,917,131.00, less an Underwriters' discount of \$891,414.36. The purchase contract pursuant to which the Series AM Bonds are being sold provides that the Underwriters will purchase all of the Series AM Bonds, if any Series AM Bonds are purchased, the obligation to make such purchase is subject to certain terms and conditions set forth in the purchase contract, the approval of certain legal matters by counsel and certain other conditions.



The Underwriters have certified the reoffering prices or yields set forth on the inside cover hereof. The Department takes no responsibility for the accuracy of these prices or yields. The Underwriters may offer and sell the Series AM Bonds to certain dealers and others at prices lower than the offering prices stated on the inside cover page. The offering prices may be changed from time to time by the Underwriters.

The Underwriters may over-allot or effect transactions which stabilize or maintain the market price of the Series AM Bonds at levels above that which might otherwise prevail in the open market. Such stabilizing, if commenced, may be discontinued at any time.

BMO Capital Markets is the trade name for certain capital markets and investment banking services of Bank of Montreal and its subsidiaries, including BMO Capital Markets GKST Inc. which is a direct, wholly-owned subsidiary of BMO Financial Corp., which is itself a wholly-owned subsidiary of Bank of Montreal.

Several of the Underwriters have provided letters to the State Treasurer relating to their retail distribution practices for inclusion in this Official Statement, which letters are set forth herein as APPENDIX H. The Department does not guarantee the accuracy or completeness of the information contained in such letters and the information therein is not to be construed as a representation of the Department or any Underwriter other than the Underwriter providing such representation.

#### **CERTAIN RELATIONSHIPS**

The financing of the Water System Project and related activities, including the sale of Bonds, has been made possible, in part, by hiring underwriters, financial advisors, consultants and lawyers to assist and advise the Department. Many of the firms and individuals involved in this effort have prior or ongoing relationships with other governmental entities (including Contractors), utilities and other businesses that contract or compete with the Department or contract with the State and other State agencies or that may do so in the future. The Department has required disclosure of, and has taken into account, these relationships and has determined it to be in the best interests of the Department to continue to work with these firms and individuals.

In addition, in the ordinary course of sales, trading, brokerage and financing activities, certain of the Underwriters may at any time hold long or short positions, and may trade or otherwise effect transactions, for their own accounts or the accounts of customers, in debt or equity securities or senior loans, as applicable, of the Department, the State, other governmental entities and utilities. In connection with these activities and the provision of other services, certain of the Underwriters may be or become creditors of such entities. In addition, many of the Underwriters, or their affiliates, currently serve as remarketing agents or providers of credit enhancement or liquidity facilities for variable rate obligations issued by, or as interest rate swap providers to, the Department, the State, other State agencies, other governmental entities and utilities.

#### **LITIGATION**

No litigation is pending or threatened concerning the validity or enforceability of the Series AM Bonds. Except as described above under “WATER SUPPLY CONTRACT RELATED LITIGATION – Monterey Amendment Litigation,” no litigation is pending or threatened concerning the validity or enforceability of the Water Supply Contracts.

At any given time, including the present, there are a number of civil actions pending against the Department, which could, if determined adversely to the Department, affect the Department’s

expenditures and in some cases, its revenues. However, based in part upon discussions with the Attorney General, the Department does not believe there are any pending actions that are likely to have a material adverse effect on the Department's ability to pay principal of, and premium, if any, and interest on the Bonds when due.

### **CONTINUING DISCLOSURE**

The Department will covenant for the benefit of the holders and beneficial owners of the Series AM Bonds to provide certain financial information and operating data relating to the Department by not later than 270 days following the end of the Department's fiscal year (which fiscal year as of the date hereof ends June 30) (the "Annual Report"), commencing with the report containing 2012-2013 Fiscal Year financial information, and to provide notices of the occurrence of certain enumerated events ("Event Notices"). These covenants have been made in order to assist the Underwriters in complying with Rule 15c2-12 of the Securities and Exchange Commission. Unless otherwise directed by the Municipal Securities Rulemaking Board ("MSRB") or the Securities and Exchange Commission, the Annual Report and Event Notices will be filed by the Department with the MSRB through its Electronic Municipal Market Access website. The specific nature of the information to be contained in the Annual Report or the Event Notices and certain other terms of this continuing disclosure obligation summarized in APPENDIX D – "Summary of Continuing Disclosure Certificate." Pursuant to the Resolution, failure of the Department to comply with its obligations under the Continuing Disclosure Certificate (as supplemented in connection with the issuance of the Series AM Bonds, the "Continuing Disclosure Certificate") will not be considered an event of default under the Resolution. However, the State Treasurer, any holder or beneficial owner may take such actions as may be necessary and appropriate, including seeking mandate or specific performance by court order, to cause the Department to comply with its obligations under the Continuing Disclosure Certificate.

Within the past five years the Department has not failed to comply, in all material respects, with all previous similar undertakings under continuing disclosure certificates.

### **MISCELLANEOUS**

The Appendices to this Official Statement are integral parts of this Official Statement and must be read together with all other parts of this Official Statement.

All references to the Bonds, the Resolution, any supplemental resolution, the Water Supply Contracts, the Continuing Disclosure Certificate and any provision of law are subject to the terms and provisions of each such document or law and do not purport to be complete statements of the terms and provisions thereof, and reference to the complete texts is made for further information in connection therewith. Copies of the Resolution, the Water Supply Contracts and the Continuing Disclosure Certificate are on file at the offices of the Department and the State Treasurer. Statements herein involving matters of opinion, whether or not specifically so designated, are intended merely as such and not as representations of fact.

The Department maintains a website at <http://www.water.ca.gov>. The information contained in such website is not incorporated herein by reference and is not intended to be relied upon in making an investment decision with respect to the Series AM Bonds.

The agreement of the Department is fully set forth in the Resolution, and this Official Statement is not to be construed as, and is not, a contract with the purchasers of the Series AM Bonds.



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**ESTIMATED DIRECT AND OVERLAPPING DEBT OF CERTAIN CONTRACTORS**

The data presented in this Appendix summarize certain information regarding taxes and tax-supported debt outstanding within the service territory of each of the three Contractors that are expected to provide the largest amounts of Revenues for payment of the Bonds. These three Contractors and the expected percentage contribution of each to such Revenues over the term of the Bonds are as follows (these percentages may change over time).

<b>Contractor</b>	<b>Percentage Contribution</b>
The Metropolitan Water District of Southern California .....	46%
Santa Barbara County Flood Control and Water Conservation District/Central Coast Water Authority* .....	12
Kern County Water Agency .....	8
Twenty-six other Contractors.....	34
Total .....	<u>100%</u>

\* As of July 1, 1989, Santa Barbara County FCWCD transferred certain of its rights under its Water Supply Contract to certain local water purveyors and users within Santa Barbara County. Thereafter, on September 26, 1991, the local water purveyors and users transferred those rights to the Central Coast Water Authority in consideration for its agreement to provide for the delivery of State Water Project water to the local water purveyors and users. Although the Department did not object to these transfers, the Department considers Santa Barbara County FCWCD to be the party to which the Department is obligated under the Water Supply Contract, and the Department did not release Santa Barbara County FCWCD from its Water Supply Contract obligations.

The Department has made no independent verification of the data contained in this Appendix and makes no representations as to its correctness, completeness, or comparability.

Macias, Gini & O’Connell LLP, independent auditors for the State Water Resources Development System, are not the independent auditors for any of the Contractors described in this Appendix.

**METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA**  
**ESTIMATED DIRECT AND OVERLAPPING BONDED DEBT**  
(unaudited)

2012-13 Assessed Valuation: \$2,097,369,921,305 <sup>(1)</sup>

<u>OVERLAPPING TAX AND ASSESSMENT DEBT:</u>	<u>% Applicable</u>	<u>Debt 2/1/13</u>
Los Angeles County Flood Control District	94.850%	\$ 35,279,458
Community College Districts	Various	8,339,882,329
Los Angeles Unified School District	99.639	10,906,181,041
San Diego Unified School District	99.950	1,835,090,691
Other Unified School Districts	Various	8,786,466,061
High School and School Districts	Various	3,776,321,235
City of Los Angeles	99.996	1,103,240,869
Other Cities	Various	371,423,673
Irvine Ranch Water District Improvement Districts	99.999-100.	539,398,744
Santa Margarita Water District Improvement Districts	100.	156,015,000
Other Water Districts	Various	74,072,826
Other Special Districts	Various	683,574,742
Community Facilities Districts	Various	6,822,866,051
1915 Act Bonds and Other Special Assessment District Bonds	Various	<u>1,398,523,352</u>
<b>TOTAL OVERLAPPING TAX AND ASSESSMENT DEBT</b>		<b>\$44,828,336,072</b>
<b>METROPOLITAN WATER DISTRICT TOTAL DIRECT DEBT</b>		<b>\$196,545,000</b>
<b>TOTAL DIRECT AND OVERLAPPING TAX AND ASSESSMENT DEBT</b>		<b>\$45,024,881,072</b>
<u>OVERLAPPING GENERAL FUND DEBT:</u>		
Los Angeles County Obligations	92.969%	\$ 1,630,821,598
Orange County Obligations	99.884	581,617,784
Riverside County Obligations	64.219	649,735,728
San Diego County Obligations	96.552	1,130,759,333
Other Counties Obligations	Various	619,445,787
City of Anaheim General Fund Obligations	99.820	538,107,126
City of Long Beach General Fund Obligations and Pension Obligations	100.	238,540,000
City of Los Angeles General Fund and Judgment Obligations	99.996	1,880,459,778
City of Pasadena General Fund and Pension Obligations	100.	615,555,406
City of San Diego General Fund Obligations	99.936	528,454,511
Other City General Fund Obligations	Various	3,164,512,953
Water District General Fund Obligations	Various	149,875,407
Los Angeles Unified School District Certificates of Participation	99.639	394,033,416
Other School District General Fund Obligations	Various	1,913,492,869
Other Special District General Fund Obligations	Various	<u>307,445,144</u>
<b>TOTAL GROSS OVERLAPPING GENERAL FUND DEBT</b>		<b>\$14,342,856,840</b>
Less: Obligations supported from other revenue sources		<u>887,917,519</u>
<b>TOTAL NET OVERLAPPING GENERAL FUND DEBT</b>		<b>\$13,454,939,321</b>
<b>OVERLAPPING TAX INCREMENT DEBT</b>		<b>\$9,073,249,918</b>
<b>GROSS COMBINED TOTAL DEBT</b>		<b>\$68,440,987,830<sup>(2)</sup></b>
<b>NET COMBINED TOTAL DEBT</b>		<b>\$67,553,070,311</b>

(1) Excludes Orange County November 2012 unsecured adjustment.

(2) Debt instruments included are general obligation bonds, lease revenue bonds and certificates of participation (when supported by the general fund), pension obligation bonds, 1915 Act special assessment bonds and Mello-Roos Act special assessment bonds. Excluded are enterprise revenue bonds, tax allocation bonds, mortgage revenue bonds, tax and revenue anticipation notes and non-bonded capital lease obligations. Qualified Zone Academy Bonds are included based on principal due at maturity.

Ratios to 2012-13 Assessed Valuation:

<b>Direct Debt (\$196,545,000)</b> .....	<b>0.01%</b>
Total Direct and Overlapping Tax and Assessment Debt.....	2.15%
Gross Combined Total Debt.....	3.26%
Net Combined Total Debt .....	3.22%

Ratios to Redevelopment Incremental Valuation (\$261,507,381,222):

Total Overlapping Tax Increment Debt.....	3.47%
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Source: California Municipal Statistics, Inc.

**METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA**  
**ESTIMATED DIRECT AND OVERLAPPING BONDED DEBT**  
**(unaudited)**

Fiscal Year Ended 6/30	Assessed Valuation <sup>(1)</sup>	Tax on Secured Property <sup>(2)</sup>	Delinquencies at June 30		Tax Rate Per \$100 Assessed Valuation		
			Amount	Percent	Agency Total Rate <sup>(3)</sup>	Typical Total Rate <sup>(6)</sup>	
1994	\$ 802,129,610,162	\$59,612,366	\$3,412,019	5.72%	<sup>(5)</sup>	0.0089	1.037135
1995	807,661,342,152	55,677,215	2,333,451	4.30	<sup>(5)</sup>	0.0089	1.046181
1996	802,593,757,003	56,452,511	3,837,697	6.80	<sup>(5)</sup>	0.0089	1.053047
1997	804,045,644,470	(4)	(4)	(4)	(4)	0.0089	1.051802
1998	817,424,957,700	(4)	(4)	(4)	(4)	0.0089	1.055796
1999	851,898,186,329	(4)	(4)	(4)	(4)	0.0089	1.067214
2000	910,809,885,402	(4)	(4)	(4)	(4)	0.0089	1.074728
2001	980,279,077,736	(4)	(4)	(4)	(4)	0.0088	1.078822
2002	1,169,293,222,451	(4)	(4)	(4)	(4)	0.0077	1.114077
2003	1,258,093,521,782	(4)	(4)	(4)	(4)	0.0067	1.102497
2004	1,359,534,425,177	(4)	(4)	(4)	(4)	0.0061	1.155130
2005	1,478,635,379,913	(4)	(4)	(4)	(4)	0.0058	1.169638
2006	1,643,013,823,543	(4)	(4)	(4)	(4)	0.0052	1.155967
2007	1,839,880,963,698	(4)	(4)	(4)	(4)	0.0047	1.179045
2008	2,015,721,475,188	(4)	(4)	(4)	(4)	0.0045	1.174687
2009	2,120,944,531,740	(4)	(4)	(4)	(4)	0.0043	1.189738
2010	2,081,864,775,527	(4)	(4)	(4)	(4)	0.0043	1.220441
2011	2,049,887,037,949	(4)	(4)	(4)	(4)	0.0037	1.269859
2012	2,068,668,852,729	(4)	(4)	(4)	(4)	0.0037	1.245849
2013	2,097,369,921,305 <sup>(7)</sup>	(4)	(4)	(4)	(4)	0.0035	1.265550

Direct and Overlapping Bonded Debt at February 1, 2013:

Total Gross Direct Debt	\$196,545,000
Less: Self-supporting Debt	<u>0</u>
Total Net Direct Debt	\$196,545,000
Total Overlapping Tax and Assessment Debt	\$44,828,336,072
Direct and Overlapping Tax and Assessment Debt	\$45,024,881,072
Total Gross Overlapping General Fund Obligation Debt	\$14,342,856,840
Less: Self-supporting Debt	<u>887,917,519</u>
Total Net Overlapping General Fund Obligation Debt	\$13,454,939,321
Overlapping Tax Increment Debt	\$9,073,249,918
Gross Direct and Overlapping Bonded Debt	\$68,440,987,830
Net Direct and Overlapping Bonded Debt	\$67,553,070,311

Ratios to Assessed Valuation at February 1, 2013:

Gross Direct Debt.....	0.01%
Net Direct Debt.....	0.01%
Direct and Overlapping Tax and Assessment Debt.....	2.15%
Total Gross Direct and Overlapping Bonded Debt.....	3.26%
Total Net Direct and Overlapping Bonded Debt.....	3.22%

- (1) Assessed Valuations are based on 100% of cash value beginning in 1981-82, rather than 25% as in previous years. The assessed valuations include state-reimbursable exemptions. Beginning in 1988-89, assessed valuations exclude unitary utility valuations.
- (2) Excludes tax levy on inventories and other unsecured property.
- (3) Base rate for all member areas. Some areas added after formation of the District pay higher rates.
- (4) Information unavailable.
- (5) Los Angeles County portion only.
- (6) Los Angeles County TRA 67.
- (7) Excludes Orange County November 2012 unsecured adjustments.

Source: California Municipal Statistics, Inc.



**SANTA BARBARA COUNTY FLOOD  
CONTROL AND WATER CONSERVATION DISTRICT  
OVERLAPPING INDEBTEDNESS  
(unaudited)**

Fiscal Year Ended 6/30	Assessed Valuation <sup>(1)</sup>	Tax on Secured Property <sup>(2)</sup>	Delinquencies at June 30		Tax Rate Per \$100 Assessed Valuation	
			Amount	Percent	Agency Total Rate	Typical Total Rate
1994	\$23,565,169,448	\$244,026,174	\$10,006,296	4.10%	0.00000	1.00156
1995	23,261,622,373	247,611,391	6,653,174	2.69	0.00000	1.00102
1996	23,727,401,813	254,306,422	5,249,677	2.06	0.00000	1.00761
1997	24,437,672,493	263,655,875	4,229,750	1.60	0.00000	1.01223
1998	25,413,740,531	272,955,441	3,252,689	1.19	0.00000	1.01106
1999	26,929,428,510	292,586,142	2,482,863	0.85	0.00000	1.02221
2000	28,506,012,483	312,186,449	4,545,263	1.46	0.00000	1.01919
2001	30,811,725,758	336,579,195	6,194,044	1.84	0.00000	1.02724
2002	33,470,431,216	325,958,442	4,097,562	1.26	0.00000	1.02799
2003	35,986,575,550	348,404,287	4,327,765	1.24	0.00000	1.02707
2004	38,619,690,313	378,733,525	3,827,763	1.01	0.00000	1.02530
2005	42,010,491,267	412,156,061	4,490,277	1.09	0.00000	1.02086
2006	46,430,715,568	459,630,599	5,978,796	1.30	0.00000	1.02586
2007	51,053,483,690	508,780,407	10,760,629	2.11	0.00000	1.02631
2008	54,591,882,970	547,037,318	13,322,133	2.44	0.00000	1.02633
2009	56,957,844,751	570,319,442	15,942,615	2.80	0.00000	1.03483
2010	57,102,686,939	573,825,003	13,723,941	2.39	0.00000	1.03496
2011	57,601,688,658	575,911,027	9,363,054	1.63	0.00000	1.03496
2012	58,359,033,685	582,738,827	7,131,251	1.22	0.00000	1.03619
2013	58,837,930,366	<sup>(3)</sup>	<sup>(3)</sup>	<sup>(3)</sup>	0.00000	1.03969

Direct and Overlapping Bonded Debt at February 1, 2013:

Total Gross Direct Debt	\$0
Less: Supported Debt	<u>0</u>
Total Net Direct Debt	\$0
Total Gross Overlapping Tax and Assessment Debt	\$561,514,583
Less: Supported Debt	<u>0</u>
Total Net Overlapping Tax and Assessment Debt	\$561,514,583
Total Gross Overlapping General Fund Debt	\$168,039,862
Less: Supported Debt	<u>57,996,102</u>
Total Net Overlapping General Fund Debt	\$110,043,760
Total Gross Overlapping Tax Increment Debt	\$82,725,000
Less: Supported Debt	<u>0</u>
Total Net Overlapping Tax Increment Debt	\$82,725,000
Total Gross Direct and Overlapping Bonded Debt	\$812,279,445
Less: Self-supporting Debt	<u>57,996,102</u>
Total Net Direct and Overlapping Bonded Debt	\$754,283,343

Ratio to Assessed Valuation at February 1, 2013:

Gross Direct Debt.....	0.00%
Net Direct Debt.....	0.00%
Total Gross Overlapping Tax and Assessment Debt.....	0.95%
Total Net Overlapping Tax and Assessment Debt.....	0.95%
Gross Direct and Overlapping Bonded Debt.....	1.38%
Net Direct and Overlapping Bonded Debt.....	1.28%

(1) The assessed valuations include state-reimbursable exemptions and exclude redevelopment incremental valuations. Beginning in 1988-89, assessed valuations exclude unitary utility valuations.

(2) Excludes tax levy on inventories and other unsecured property.

(3) Not available until after fiscal year ends.

Source: California Municipal Statistics, Inc.

**KERN COUNTY WATER AGENCY  
OVERLAPPING INDEBTEDNESS  
(unaudited)**

Fiscal Year Ended 6/30	Assessed Valuation <sup>(1)</sup>	Tax on Secured Property <sup>(2)</sup>	Delinquencies at June 30		Tax Rate Per \$100 Assessed Valuation		
			Amount	Percent	Agency Rate	City of Bakersfield Total Rate	Elk Hills School District
1994	\$32,986,554,039	\$12,246,716	\$364,041	2.97%	0.066719	1.171248	1.020210
1995	30,100,052,112	9,370,510	287,927	3.07	0.070116	1.135179	1.019195
1996	30,538,512,132	12,656,809	338,224	2.67	0.095807	1.173827	1.020669
1997	31,943,215,222	13,283,378	395,321	2.98	0.091633	1.179749	1.022585
1998	34,411,749,796	12,984,313	480,525	3.70	0.091601	1.172489	1.019745
1999	32,692,348,290	13,035,390	282,929	2.17	0.089041	1.139540	1.016470
2000	36,368,798,648	<sup>(3)</sup>	<sup>(3)</sup>	<sup>(3)</sup>	0.088270	1.162026	1.035082
2001	38,813,931,812	15,981,366	295,032	1.85	0.077322	1.157759	1.017135
2002	41,429,323,346	15,210,702	339,798	2.23	0.061936	1.117621	1.015612
2003	39,976,729,738	15,776,379	476,821	3.02	0.060665	1.160526	1.019332
2004	42,165,212,745	18,525,332	<sup>(3)</sup>	<sup>(3)</sup>	0.063662	1.146391	1.021406
2005	45,443,236,748	16,054,006	237,483	1.48	0.063200	1.156496	1.056077
2006	52,596,138,408	13,726,652	258,314	1.88	0.047579	1.133705	1.055929
2007	64,149,863,242	12,223,309	384,215	3.14	0.038184	1.122182	1.047846
2008	71,491,760,384	18,521,313	802,472	4.33	0.053401	1.157296	1.050210
2009	75,766,431,779	17,059,057	572,984	3.36	0.052517	1.151185	1.054710
2010	70,423,049,669	19,500,828	565,663	2.90	0.064063	1.180167	1.064484
2011	74,597,201,953	17,863,779	345,942	1.94	0.058402	1.176436	1.053897
2012	76,240,534,603	25,718,178	379,982	1.48	0.074783	1.191102	1.054265
2013	81,254,773,400	<sup>(4)</sup>	<sup>(4)</sup>	<sup>(4)</sup>	0.057330	1.174290	1.043923

Direct and Overlapping Bonded Debt at February 1, 2013:

Total Gross Direct Debt	\$0
Less: Supported Debt	<u>0</u>
Total Net Direct Debt	\$0
Total Gross Overlapping Tax and Assessment Debt	\$1,021,380,111
Less: Supported Debt	<u>2,770,000</u>
Total Net Overlapping Tax and Assessment Debt	\$1,018,610,111
Total Gross Overlapping General Fund Debt	\$951,800,068
Less: Self-supporting Debt	<u>0</u>
Total Net Overlapping General Fund Debt	\$951,800,068
Total Gross Overlapping Tax Increment Debt	\$92,170,089
Less: Supported Debt	<u>0</u>
Total Net Overlapping Tax Increment Debt	\$92,170,089
Gross Direct and Overlapping Bonded Debt	\$2,065,350,268
Net Direct and Overlapping Bonded Debt	\$2,062,580,268

Ratios to Assessed Valuation at February 1, 2013:

Gross Direct Debt.....	0.00%
Net Direct Debt.....	0.00%
Gross Direct and Overlapping Tax and Assessment Debt.....	1.26%
Net Direct and Overlapping Tax And Assessment Debt.....	1.25%
Gross Direct and Overlapping Bonded Debt.....	2.54%
Net Direct and Overlapping Bonded Debt.....	2.54%

(1) Assessed Valuations are based on 100% of cash value beginning in 1981-82, rather than 25% as in previous years. The assessed valuations include state-reimbursable exemptions and exclude redevelopment incremental valuations. Beginning in 1988-89, assessed valuations exclude unitary utility valuations.

(2) Excludes tax levy on inventories and other unsecured property.

(3) Information unavailable.

(4) Not available until after fiscal year ends

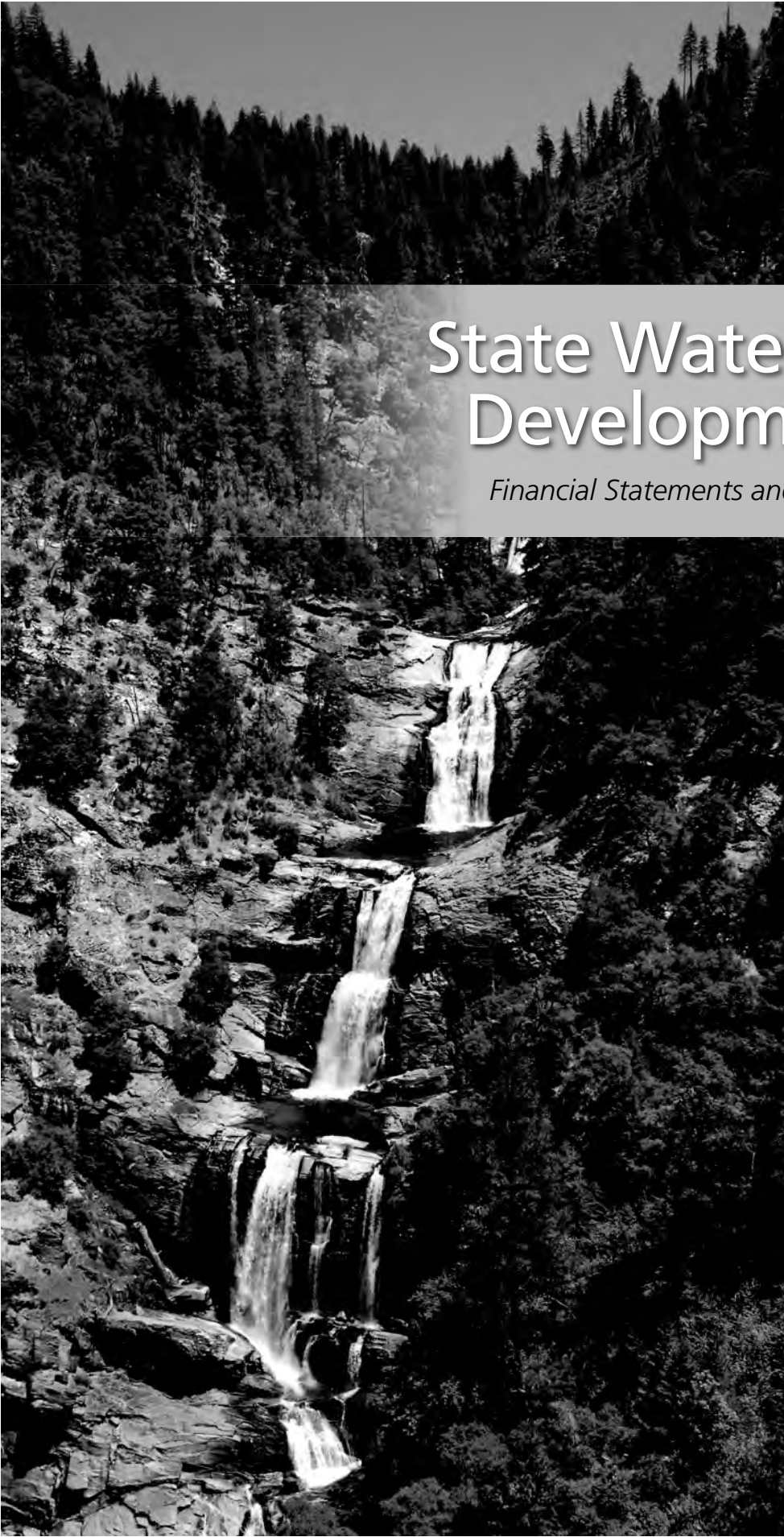
Source: California Municipal Statistics, Inc.

**STATE WATER RESOURCES  
DEVELOPMENT SYSTEM**

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**AUDITED FINANCIAL STATEMENTS**  
**for the years ended June 30, 2012 and 2011**

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State of California  
Natural Resources Agency  
Department of Water Resources

# State Water Resources Development System

*Financial Statements and Supplementary Information*

**ANNUAL REPORT**  
Years Ended June 30  
**2012-2011**



Cover photo shows an aerial view of Seven Falls.

*Photo by Paul Hames/DWR Photography*

*Cover design by DWR Graphic Services*

**STATE OF CALIFORNIA**  
*Edmund G. Brown Jr., Governor*

**NATURAL RESOURCES AGENCY**  
*John Laird, Secretary for Natural Resources*

**DEPARTMENT OF WATER RESOURCES**  
*Mark W. Cowin, Director*

Carl Torgersen  
Deputy Director

Dale Hoffman-Floerke  
Chief Deputy Director

Kathie Kishaba  
Deputy Director

Paul Helliker  
Deputy Director

John Pacheco  
Acting Deputy Director

Gary Bardini  
Deputy Director

Cathy Crothers  
Chief Counsel

Kasey D. Schimke  
Assistant Director

**Division of Fiscal Services**  
Perla M. Netto-Brown, Chief

**This document was prepared under the direction of:**

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# **State Water Resources Development System**

**Financial Statements and  
Supplementary Information**

**For the years ended June 30, 2012 and 2011**

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# State Water Resources Development System

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Walnut Creek

Oakland

LA/Century City

Newport Beach

San Diego

Seattle

To the Director of the State of California  
Department of Water Resources

### Independent Auditor's Report

We have audited the accompanying basic financial statements of the State Water Resources Development System (System), a component unit of the State of California, as of and for the fiscal years ended June 30, 2012 and 2011, as listed in the table of contents. These financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the System as of June 30, 2012 and 2011, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis as listed in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming an opinion on the System's basic financial statements. The supplementary information as listed in the table of contents is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

*Maclean Gini & O'Connell LLP*

Sacramento, California  
November 29, 2012

# **State Water Resources Development System Management's Discussion and Analysis (Unaudited) For the years ended June 30, 2012 and 2011**

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## **Management's Discussion and Analysis (Required Supplementary Information)**

This discussion and analysis is designed to assist the reader in focusing on significant financial issues and activities and to identify any significant changes in the financial position of the State Water Resources Development System (the System), which is administered by the California Department of Water Resources (DWR). Readers are encouraged to consider the information presented in conjunction with the financial statements as a whole, which follow Management's Discussion and Analysis. This discussion and analysis and the financial statements do not relate to DWR's other governmental and proprietary funds. The System includes the State Water Project (SWP), the Davis-Grunsky Act Program and the San Joaquin Drainage Implementation Program.

The SWP encompasses a complex of dams, reservoirs, pumping plants, power plants, aqueducts and pipelines owned and operated by the State of California. The SWP was developed in order to deliver water to areas of need throughout the State for domestic, industrial and agricultural purposes, as well as to provide flood control, recreation, fish and wildlife enhancement, hydroelectric power and other benefits. DWR is responsible for the planning, construction and operation of the SWP. The construction program commenced in 1957 and approximately 700 miles of the System has been completed. The System has entered into long-term water supply contracts with 29 customers; known as the "Water Contractors," in order to recover substantially all System costs. The Water Contractors may request up to maximum annual amounts totaling 4,172,786 acre-feet of water from the System. This maximum does not assure delivery of that amount of water, but rather provides the basis for proportional allocation of available supplies among the Water Contractors.

Portions of the SWP system consist of facilities developed and used jointly with the Federal Central Valley Water Project (CVP) operated by the U.S. Bureau of Reclamation (USBR). In addition, both projects have primary sources of water north of the Sacramento-San Joaquin Delta (Delta), transport water across the Delta and draw water from the southern edge of the Delta. The CVP, like the SWP, provides water for irrigation in the Central Valley, urban water supply, water quality, flood control, power, recreation, and fish and wildlife enhancement. Costs for the jointly developed facilities are shared approximately 55 percent State and 45 percent Federal. In 1986, the System and USBR entered into a Coordinated Operation Agreement (COA) under which the SWP and the CVP coordinate operations, including releases from upstream reservoirs and pumping from the Delta. The COA permits increased operational efficiency of both projects, ensures that each project receives an equitable share of available surplus water, and provides for sharing of responsibilities in meeting certain Delta water quality standards.

### **Financial Highlights**

- The System recorded an increase in total assets of \$21.3 million on total operating revenues of \$1.0 billion. This did not cause an increase in net assets as a result of appropriately reflecting the timing differences in the deferral of expenses incurred and the deferral of capital recovery.

# **State Water Resources Development System Management's Discussion and Analysis (Unaudited) For the years ended June 30, 2012 and 2011**

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- On September 7, 2011, the System issued \$92.3 million of CVP Water System Revenue Bonds Series AI with an average yield on the bonds of 3.06% to refund \$103.2 million of CVP Water System Revenue Bonds Series W.
- On October 13, 2011, the System issued \$216.9 million of CVP Water System Revenue Bonds Series AJ with an average yield on the bonds of 3.13% to retire \$155.2 million of CVP Water System Revenue Bonds Series X, Y, Z, AA, AC, and AD.
- On March 13, 2012, the System issued \$36.4 million of CVP Water System Revenue Bonds Series AK with an average yield on the bonds of 3.05% to refund \$8.4 million of CVP Water System Revenue Bonds Series X and AC.

## **Overview of Financial Statements**

### ***Reports Included in Financial Statements***

The System is accounted for as an enterprise fund. Enterprise funds account for the acquisition, operation, and maintenance of governmental facilities and services that are entirely or predominantly self-supported by user charges. This financial report consists of three financial statements, prepared on the accrual basis of accounting, with accompanying note disclosures. These financial statements report information using accounting methods similar (although not identical) to those used by private sector companies. The statements of net assets include all the assets, liabilities and the net assets of the System. The statements of revenues, expenses, and changes in net assets report all of the revenues and expenses incurred during the fiscal years presented. The statements of cash flows report the cash inflows and outflows classified by operating, investing, noncapital financing and capital and related financing activities during the reporting periods presented. The notes to the financial statements communicate certain information required by generally accepted accounting principles.



# State Water Resources Development System Management's Discussion and Analysis (Unaudited) For the years ended June 30, 2012 and 2011

## Condensed Statements of Net Assets

	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>%Change</u>	<u>%Change</u>
	(amounts in thousands)			<u>2012-2011</u>	<u>2011-2010</u>
Total utility plant	\$ 3,212,952	\$ 3,201,464	\$ 3,215,188	0.4%	-0.4%
Other assets	1,755,503	1,745,724	1,797,764	0.6%	-2.9%
Total assets	<u>\$ 4,968,455</u>	<u>\$ 4,947,188</u>	<u>\$ 5,012,952</u>	0.4%	-1.3%
Capitalization:					
Net assets:					
Capital, net of related debt	\$ 684,025	\$ 554,854	\$ 486,347	23.3%	14.1%
Restricted	521,406	650,577	719,084	-19.9%	-9.5%
Total net assets	1,205,431	1,205,431	1,205,431	0.0%	0.0%
Total long-term liabilities	2,809,583	2,913,479	2,975,096	-3.6%	-2.1%
Total capitalization	4,015,014	4,118,910	4,180,527	-2.5%	-1.5%
Other liabilities	953,441	828,278	832,425	15.1%	-0.5%
Total net assets and liabilities	<u>\$ 4,968,455</u>	<u>\$ 4,947,188</u>	<u>\$ 5,012,952</u>	0.4%	-1.3%

## Condensed Statements of Revenues, Expenses, and Changes in Net Assets

	<u>2012</u>	<u>2011*</u>	<u>2010</u>	<u>%Change</u>	<u>%Change</u>
	(amounts in thousands)			<u>2012-2011</u>	<u>2011-2010</u>
Water supply	\$ 860,891	\$ 874,748	\$ 853,158	-1.6%	2.5%
Power sales	148,360	193,154	165,664	-23.2%	16.6%
Federal reimbursements	36,561	28,294	24,021	29.2%	17.8%
Total operating revenues	<u>1,045,812</u>	<u>1,096,196</u>	<u>1,042,843</u>	-4.6%	5.1%
Operations and maintenance expense	523,951	428,559	435,801	22.3%	-1.7%
Purchased power expense	271,377	342,446	212,658	-20.8%	61.0%
Depreciation expense	87,400	100,257	80,813	-12.8%	24.1%
Operating expenses recovered, net	57,076	109,535	189,000	-47.9%	-42.0%
Total operating expenses	<u>939,804</u>	<u>980,797</u>	<u>918,272</u>	-4.2%	6.8%
Income from operations	<u>106,008</u>	<u>115,399</u>	<u>124,571</u>	-8.1%	-7.4%
Capital revenues recovered	31,396	14,022	19,823	123.9%	-29.3%
Interest expense	(107,770)	(134,996)	(151,390)	-20.2%	-10.8%
Other revenue (expenses), net	(29,634)	5,575	6,996	-631.6%	-20.3%
Change in net assets	-	-	-	0.0%	0.0%
Net assets, beginning of year	1,205,431	1,205,431	1,205,431	0.0%	0.0%
Net assets, end of year	<u>\$ 1,205,431</u>	<u>\$ 1,205,431</u>	<u>\$ 1,205,431</u>	0.0%	0.0%

\* Certain amounts have been reclassified from amounts previously reported to conform with the current year presentation.

# State Water Resources Development System Management's Discussion and Analysis (Unaudited) For the years ended June 30, 2012 and 2011

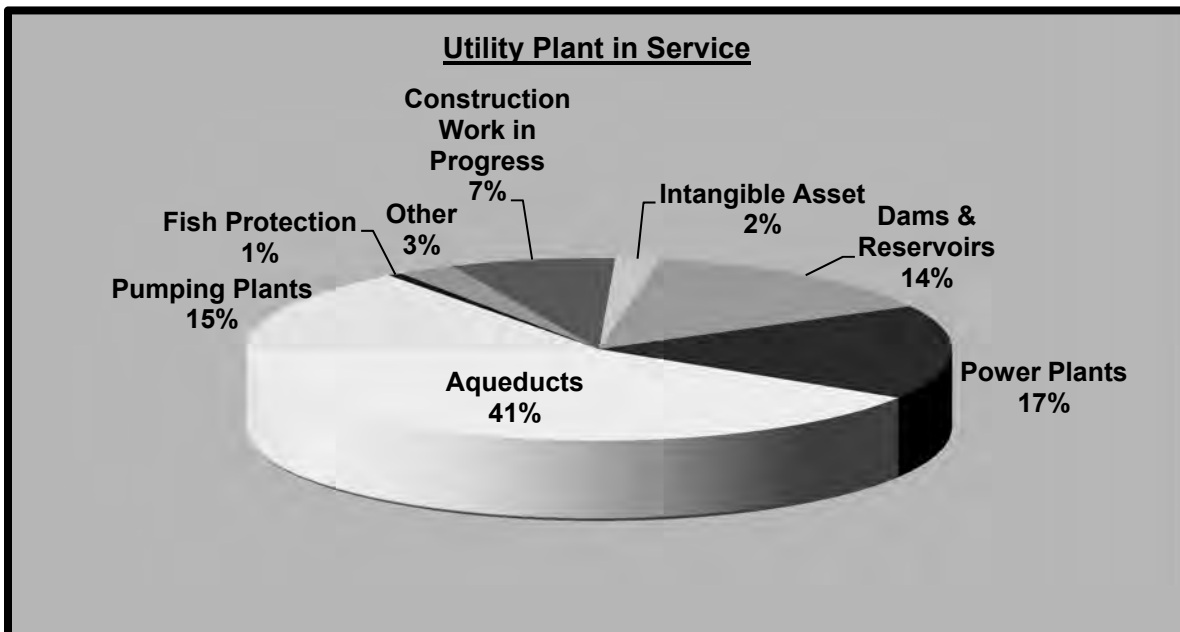
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## Assets

### Utility Plant

Utility Plant represents the accumulated original costs of labor, materials and indirect costs incurred during the construction of the SWP that are in service to provide water deliveries. The SWP utility includes thirty-three storage facilities, twenty-three pumping plants, four generating plants, eight power plants, as well as fish protection facilities, aqueducts, and internally generated intangible assets.

Utility plant in service, net of accumulated depreciation (UPIS) decreased by \$29.6 million during fiscal 2012 to a balance of \$2,805 million. Transfers were made from Construction Work in Progress to UPIS of \$47.2 million including Edmonston Pump Replacement of \$39.3 million, Facilities Repair and Improvement of \$7.3 million, South Bay Aqueduct Del Valle Pipeline of \$2.9 million, and a reduction of \$2.3 million for Hyatt Refurbishment in fiscal 2012 in comparison to \$117.1 million in fiscal 2011. The amount of additions and transfers to UPIS in the current year was \$57.8 million compared to \$119.8 million in 2011. While depreciation expense usually remains fairly constant each year, fiscal 2012 experienced a decrease of \$12.9 million in depreciation expense due to several pumping plants being fully depreciated at the end of fiscal 2011 and post capitalization of certain capital projects. These fiscal 2011 post capitalized projects included Tehachapi East Afterbay, Hyatt Refurbishment, and Reid Gardner. This caused an increase in the depreciation expense for fiscal 2011 that did not occur in fiscal 2012. Depreciation expense for fiscal 2012 was \$87.4 million compared to 2011 of \$100.3 million. Ensuing annual depreciation expense should remain relatively constant, as the majority of the System's is complete and depreciation is recorded on a straight-line basis over the estimated useful life of the assets, which generally range from 20 to 100 years.



## **State Water Resources Development System Management's Discussion and Analysis (Unaudited) For the years ended June 30, 2012 and 2011**

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### ***Construction Work in Progress***

Construction work in progress increased by \$41.1 million during the year, which represents an 11.2% increase from fiscal 2011. In fiscal 2011, construction work in progress decreased by \$33.3 million, or 8.3% from fiscal 2010. The current year increase is attributable to new and on-going projects including South Bay Aqueduct Enlargement projects of \$25.8 million, Facilities Repair and Improvement of \$20.9 million, East Branch Extension Phase II projects of \$13.4 million, South Bay Aqueduct Improvement projects of \$12.4 million, South Bay Aqueduct Del Valle Pipeline of \$2.9 million, Edmonston Pump Replacement of \$2.7 million, Oroville Complex facilities of \$2.4 million, Perris Dam Remediation of \$2.3 million, Delta Fish Survival Improvement of \$1.3 million, and \$4.2 million of Intangible Assets including the Federal Energy Regulatory Commission (FERC) re-licensing costs and internally generated computer software. These increases were offset by the transfer of \$47.2 million from Construction Work in Progress to UPIS for projects including Edmonston Pump Replacement of \$39.3 million, Facilities Repair and Improvement of \$7.3 million, South Bay Aqueduct Del Valle Pipeline of \$2.9 million, and a reduction of \$2.3 million for Hyatt Refurbishment.

The decrease in fiscal 2011 from 2010 was primarily due to transfers of \$117.1 million from Construction Work in Progress to UPIS offset by an increase of \$83.8 million for new and on-going projects. The transfers to UPIS included Facilities Repair and Improvement of \$60.1 million, Arroyo Pasajero of \$19.5 million, South Bay Aqueduct Del Valle Pipeline of \$15.4 million, North Bay Aqueduct New Terminal of \$13.6 million, and Delta Facilities of \$8 million. These decreases were mitigated in part by increases of new and on-going projects including the South Bay Aqueduct Enlargement projects of \$27.5 million, South Bay Aqueduct Improvement projects of \$14.1 million, East Branch Extension Phase II projects of \$10.3 million, Edmonston Pump Replacement of \$8.8 million, Fish Restoration Program Agreement - Battle Creek project of \$5.3 million, Pearblossom Administration Building project of \$2.3 million, Perris Dam Remediation project of \$1.8 million, other Water Systems projects totaling \$14.7 million, \$1.9 million of Intangible Assets, and a decrease of \$2.9 million for the Reid Gardner project.

At June 30, 2012, total construction work in progress comprised of \$188 million for the South Bay Aqueduct Enlargement projects, \$154.3 million of other Water Systems projects, \$59.2 million of East Branch Extension Phase II projects, \$6.1 million of Intangible Assets, and \$0.4 million of East Branch Improvement projects.

### ***Restricted Cash and Investments***

Restricted cash and cash equivalents decreased by \$5.1 million during fiscal 2012 to a total of \$156.9 million. This compares to a balance of \$162 million in fiscal 2011. The current year decrease is attributed to a decline in the cash for plant replacement of \$6.2 million, offset by an increase of \$1.1 million in the debt service reserve requirement associated with the issuance of bond Series AI, AJ, and AK. The \$6.2 million decline in cash for plant replacement represents the excess total disbursements of \$20.4 million over total collections of \$14.2 million. Major disbursements include a \$10 million refund paid to water contractors to reduce excess reserves as well as other payments, such as charges relating to the Gianelli Power Generating Plant. The prior year increase of \$2.5 million was in the cash restricted for debt service due to the issuance of Series AH bonds.

### ***Other Long-term Assets***

Long term loans receivable from local water agencies decreased by \$1.9 million to a total of \$19.1 million. As required by the Davis-Grunsky Act, the System has made loans to local water

## **State Water Resources Development System Management's Discussion and Analysis (Unaudited) For the years ended June 30, 2012 and 2011**

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agencies of which a long-term portion of \$17 million remains outstanding at the end of fiscal 2012 compared to an outstanding balance of \$18.8 million at the end of fiscal 2011. Additionally, \$2.1 million remained outstanding in the Groundwater loan receivable compared to an outstanding balance of \$2.2 million in 2011. Advances to other State Funds represent the System's advance of \$92 million to DWR's internal service fund, which functions as a revolving working capital facility for DWR.

### ***Cash and Cash Equivalents***

In fiscal year 2012, cash and cash equivalents decreased by \$42.6 million to a balance of \$422.4 million. This decrease is due in part to a \$30 million release of debt service reserves in accordance with the Springing Amendment and decreases in receipts from power sales and from the Water Contractors, offset by an increase in Federal reimbursements and a decrease in power purchases.

### ***Receivables***

In fiscal 2012, water supply and power billings receivable increased by \$30.3 million as compared to fiscal 2011. The increase is primarily due to a reduction in refunds and credits issued to water contractors. Other increases included an increase in receivables of \$3.4 million in variable invoices and an increase in power sales accruals of \$3.8 million. In fiscal 2011, water supply and power billings receivable decreased by \$4.8 million. The decrease was primarily due to a decrease of \$6.4 million in power sales accruals, a decrease of \$2.1 million for reduction of aged receivables for Angeles Tunnel billings, offset by an increase of \$2.4 million in SWP Contractors receivables, and an increase of \$1.3 million for Highway 12 and 46 encasements receivables.

### ***Deferred Charges***

Deferred charges represent timing differences between expenses incurred by the System and their ultimate recovery from the Water Contractors. Expense recognition is expected to match recovery from the Water Contractors in the future. In 2012, the deferred charges increased by \$37 million to an ending balance of \$908 million compared to \$871 million for 2011, as the System defers expenses to be recovered from future revenues from the Water Contractors. In fiscal 2011, recoveries resulted in a decrease of deferred charges of \$60 million.

## **Liabilities**

### ***General Obligation Bonds***

In addition to the revenue bond obligation described below, a large portion of the SWP was financed by the sale of general obligation bonds of the State pursuant to the provisions of the Burns-Porter Act, which authorized the issuance of \$1,750 million of such bonds for the construction of the SWP. The Burns-Porter Act was adopted by the voters at the State's general election of November 1960. Of that authorization, \$1,582 million (including the entire amount available for construction of the initial components of the SWP) has been issued, of which \$362 million remains outstanding at the end of fiscal 2012 compared to \$421 million at fiscal 2011 and \$477 million at fiscal 2010. The un-issued \$168 million of the authorization is available only to provide funds for the construction of certain additional water conservation facilities.

**State Water Resources Development System  
Management's Discussion and Analysis (Unaudited)  
For the years ended June 30, 2012 and 2011**

**Revenue Bonds**

The System has issued 37 series of Water System Revenue Bonds totaling \$7,003 million in the aggregate principal, of which \$2,343 million remains outstanding at the end of fiscal 2012. This compares to outstanding balances of \$2,380 million and \$2,421 million at the end of fiscal year 2011 and 2010, respectively. During the year, the System completed the issuance of CVP Water Systems Revenue Bond Series AI, AJ, and AK totaling \$346 million. The majority of the proceeds from the issuance were used to retire portions of the Series W, X, Y, Z, AA, AC, and AD bonds, pay off all outstanding commercial paper as of the date of issuances, make deposits to the Debt Service Reserve Account, fund interest on a portion of the Series AI, AJ and AK Bonds, and pay costs of issuance.

The System has also issued \$139 million of revenue bonds to finance the Devil Canyon-Castaic power facility. Under the Devil Canyon-Castaic bond resolution, \$73 million is outstanding at the end of fiscal 2012, compared to \$78 million at fiscal 2011 and \$82 million at fiscal 2010.

	<u>2012</u>	<u>2011</u>	<u>2010</u>
	(amounts in thousands)		
CVP revenue bonds par amount	\$ 2,269,900	\$ 2,302,665	\$ 2,339,310
Unamortized bond issuance premiums/(discounts)	144,892	111,649	104,948
Deferred amount on refunding	<u>(60,381)</u>	<u>(29,260)</u>	<u>(26,084)</u>
Total CVP revenue bonds outstanding	2,354,411	2,385,054	2,418,174
Devil Canyon - Castaic revenue bond par amount	<u>72,945</u>	<u>77,540</u>	<u>81,875</u>
Total revenue bonds outstanding	2,427,356	2,462,594	2,500,049
Less current maturities	<u>(124,155)</u>	<u>(116,150)</u>	<u>(108,870)</u>
Total long-term portion	<u>\$ 2,303,201</u>	<u>\$ 2,346,444</u>	<u>\$ 2,391,179</u>

**Pooled Money Investment Loan**

The System applied for and received a loan from the Pooled Money Investment Account (PMIA) pursuant to Government Code section 16313 for \$29.6 million. The proceeds of the loan were used to establish escrow accounts that defeased certain Water System Revenue Bonds that financed recreation, fish, and wildlife enhancement related costs of the acquisition and construction of the System. The loan is to be repaid with surplus revenues of the System made available under Water Code section 12937(b) (4). DWR executed the Pooled Money Investment Board Loan on March 26, 2008. The loan agreement requires minimum quarterly payments of \$1 million on the first day of every March, June, September and December; the first payment was made on September 1, 2008. Interest is computed on the unpaid principal balance of the loan at the Variable Rate on the basis of a 360-day year or twelve 30-day months and the number of days elapsed. The Variable Rate means (a) for the period from the date of the Loan Agreement, March 26, 2008, through and including the day before the first Reset Date (March 25, 2009), five percent per annum, and (b) for each Renewal Period thereafter, the greater of (i) five percent per annum, or (ii) the last available daily rate of return by the PMIA on the day before the Reset Date on which such Renewal Period commences. In fiscal year 2012, the outstanding balance decreased from \$21.1 million to \$18.1 million due to \$3.0 million of principal payments made during fiscal year 2012. In fiscal year 2011, the outstanding balance

## **State Water Resources Development System Management's Discussion and Analysis (Unaudited) For the years ended June 30, 2012 and 2011**

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decreased from \$23.9 million to \$21.1 million due to \$2.8 million of principal payments made during fiscal year 2011.

### ***Postemployment Benefits Other than Pensions***

The Postemployment Benefits Other than Pensions (OPEB) increased by \$20 million to a net OPEB obligation ending balance of \$117.9 million in fiscal 2012 due to the difference between the Annual Required Contribution (ARC) to fully fund the obligation as calculated pursuant to the requirements of GASB Statement No. 45 in the amount of \$31.1 million and the actual contribution charged by the California Department of Finance through pro rata charges of \$11.1 million. The \$20 million increase for fiscal 2012 and \$26.4 million increase in fiscal 2011 reflect the System's under funding of the ARC.

### ***Accounts Payable and Other Current Liabilities***

Accounts payable and other current liabilities totaled \$335.5 million at June 30, 2012, compared to \$299.2 million in fiscal 2011, and \$303 million in fiscal 2010. The increase of \$36.3 million in the current year is due to an increase in accounts payable vendor liabilities of \$28.1 million which resulted from increased invoices billed to the System for Reid Gardner power activities and significant contract and consulting services performed during the current fiscal year and billed in the next fiscal year. Other changes included an increase of \$9.3 million for the current portion of long term bond principal; an increase of \$1 million for the current portion of the System's pollution remediation obligations for the Delta Methylmercury Control Program; an increase of \$686 thousand to the current liability portion of accrued vacation; a decrease of \$2.8 million due to a timing differences in the transfer of cash settlements with DWR's Internal Service Fund and slight decreases in accrued bond interest and current portions of loans payables.

In fiscal 2011, the decrease of \$3.8 million is due to increased production in payables invoice processing resulting in a decrease of \$18.1 million in accounts payable vendor liabilities; a decrease of \$4.2 million to the current liability portion of accrued vacation; an increase of \$9.2 million for the current portion of long term bond principal; an increase of \$600 thousand for the current portion of the System's pollution remediation obligations for the Delta Methylmercury Control Program; an increase of \$8.3 million due to a timing difference in the transfer of cash settlements with DWR's Internal Service Fund; and an increase of \$444 thousand attributable to slight increases in accrued bond interest current portions of loans payables.

### ***Proceeds Due to Water Contractors***

Proceeds Due to Water Contractors are comprised primarily of the additional 25% billing for revenue bond debt service in excess of debt service requirements (known as "cover"), plus certain investment income and off-aqueduct power sales, all defined as refundable to the Water Contractors under terms of the water supply contracts.

Proceeds Due to Water Contractors increased by \$31 million during fiscal 2012 to an ending balance of \$142 million. The increase in fiscal 2012 can be primarily attributed to a \$36.4 million increase in refunds due to the Water Contractors resulting from a release in debt service reserves. The debt service reserve requirement was lowered with the implementation of the Springing Amendment and excess funds are returned to the water contractors. Other increases include \$3.3 million refund due to the water contractors for adjustments in the Off Aqueduct Power facility charges for fiscal years 2000 to 2008, \$6.3 million increase in deferred operating revenue prepayments for Off Aqueduct Power, and a \$2.3 million increase in cover. These

## **State Water Resources Development System Management's Discussion and Analysis (Unaudited) For the years ended June 30, 2012 and 2011**

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increases were offset by \$9.9 million refund to the Water Contractors for the discontinued gas hedging activities, \$5.2 million net decrease in interest earnings to be refunded to the water contractors, and \$2.2 million decrease as delivery structure revenue was recognized for the North Bay Aqueduct Alternate Project.

In fiscal year 2011, Proceeds Due to Water Contractors decreased from \$121 million to \$111 million, a decrease of \$10 million. The decrease was due to the discontinuation of gas hedging activities and a decrease in deferred operating revenue prepayments in Off Aqueduct power facilities

### ***Deferred Revenue – State and Federal Capital Recovery***

The System received funds from the State and Federal governments to build certain projects that relate to recreational use and flood control. Those funds are deferred and then recognized as revenue as the projects are depreciated. Deferred revenue decreased \$3.6 million in fiscal 2012 to \$149.3 million. This compares to a \$1 million decrease in fiscal 2011. These decreases represent the recognition of revenue equal to the amount of depreciation recorded.

### ***Deferred Capital Costs***

The system had \$123 million in deferred revenues for capital costs for 2012 compared to \$25 million in deferred revenues in fiscal 2011, an increase of \$98 million. This is a result of principal recoveries of \$176 million netted with capital costs of \$78 million. Principal recovery of capital costs was \$176 million in 2012 in comparison to \$159 million in 2011, generally as a result of an increase in Water Systems capital recovery and an additional \$2 million added to the component of capital recovery after the Tehachapi Afterbay project was placed in service and began depreciating in fiscal 2012. Deferred capital costs for Transportation and Conservation facilities were \$78 million in 2012 compared to \$93 million in 2011. The decrease was primarily due to the post capitalization of Tehachapi Afterbay and Reid Gardner projects in 2011 resulting in additional depreciation in 2011 which did not occur in 2012.

### ***Deferred Power Sales Credit Due to Water Contractors***

The deferred power sales credit results from a timing difference of revenue collected from certain Water Contractors for power generated by the Hyatt-Thermalito power plant and the corresponding credit that is issued to all Water Contractors through a reduced capital charge. In fiscal year 2012, the credits issued through the Delta Water Charge of \$24.6 million were offset in part by the \$14.7 million of revenue collected through the Variable charge for power generated at Hyatt-Thermalito for a \$9.9 million decrease in the deferral for the 2012 fiscal year. This compares to fiscal year 2011 where the credits issued through the Delta Water Charge were \$23.5 million, offset in part by \$14.7 million of revenue collected through the Variable charge for power generated at Hyatt-Thermalito for an \$8.8 million decrease in the deferral.

### ***Advances for Plant Replacements***

Advances for plant replacements represents amounts collected in advance from the Water Contractors for future plant equipment replacements. Advances for plant replacements decreased from \$36.5 million in fiscal 2011 to a total of \$35.2 million in fiscal 2012. The \$1.3 million decrease in fiscal 2012 is primarily due to revenue collection of \$14.4 million that was offset by \$10 million in refunds to the Metropolitan Water District and \$5.7 million paid for replacements at Gianelli, Banks, Buena Vista, and Hyatt pumping plants.

## **State Water Resources Development System Management's Discussion and Analysis (Unaudited) For the years ended June 30, 2012 and 2011**

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Advances for plant replacements decreased from \$39.5 million in fiscal 2010 to a total of \$36.5 million in fiscal 2011. The \$3 million decrease in 2011 is due to revenue collection of \$6.5 million offset by \$9.8 million paid for replacements at Gianelli, Banks, Buena Vista, and Hyatt pumping plants.

### ***Operating Revenues***

Operating revenues for fiscal 2012 were \$1.04 billion compared to \$1.09 billion in fiscal 2011 and \$1.04 billion in fiscal 2010. The decrease of \$50.4 million in fiscal 2012 was primarily due to a decrease in water supply revenue of \$13.9 million, a decrease in power sales revenue of \$44.8 million offset by an increase of \$8.3 million in federal reimbursements. The increase of \$53.4 million in fiscal 2011 was primarily due to an increase in water supply revenue of \$32 million, an increase in power sales revenue of \$27.5 million, and a decrease of \$6.1 million in federal reimbursements.

### ***Water Supply Revenue***

Under the terms of the water supply contracts, the System is required to collect from the Water Contractors all costs of the SWP allocated to water supply in proportion to each Water Contractor's contractual allocation of water. Generally, the System's costs, including the costs of gathering, storing, conveying and delivering water, and interest, are billable to Water Contractors whether or not water is delivered.

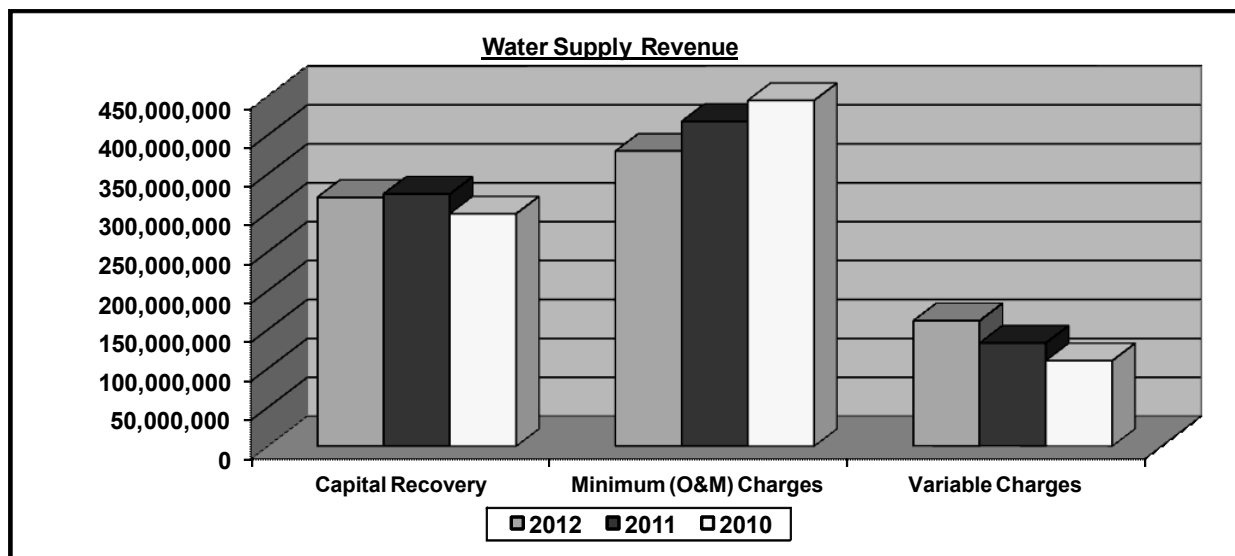
Water supply revenues consist of three main categories, as defined in the water supply contracts: Capital, Minimum and Variable. The Capital component of revenue enables the System to recover all the costs plus interest related to the construction of the System facilities, including its dams, aqueducts, pumping stations and power plants. Once a project is completed, its cost plus interest are amortized and recovered over the remaining term of the water supply contracts (through 2035). The Minimum component of revenue enables the System to recover the operating and maintenance costs associated with operating the System. These costs are generally recovered as they are incurred. Finally, the Variable component of revenue enables the System to recover the net cost of energy used to deliver water to the Water Contractors. Similar to Minimum, these costs, net of power sales, are generally recovered as they are incurred.

On or before July 1 of each year, the System furnishes each Water Contractor with a statement of estimated charges for the Capital, Minimum, and Variable components for the following calendar year. The Capital components are due on January 1 and July 1 of the year following receipt of the statement of charges. The Minimum and Variable component payments are due in twelve monthly installments commencing on January 1 of the year following receipt of the statement of charges. On or about July 1 of each year, the System determines the rate (per acre-foot) to be charged to each Water Contractor in the following calendar year for the Variable components. The Variable components in such calendar year are calculated and billed monthly based on metered water deliveries for the preceding month and the rate determined on July 1st of each year. However, this rate can be modified over the course of the next year. On July 1 of each year, the System furnishes each Water Contractor with a statement showing the difference between the estimated water charges paid and the actual costs incurred in the prior calendar year. The difference is paid by or credited to each Water Contractor, as applicable, in equal monthly installments commencing on January 1 of the year following the "true-up" calculation. This process results in an approximately two-year delay in the reconciliation of estimated charges paid and actual costs reimbursed to the System.



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In 2012, the System generated \$860.9 million in water supply revenue, compared to \$874.8 million in fiscal 2011, and \$853.2 million in fiscal 2010. The following table shows a comparative breakdown of the components of water supply revenue for fiscal years 2012, 2011 and 2010.



Water Supply Billings decreased by \$13.9 million in 2012 to a total of \$860.9 million. This decrease is due to a decrease of \$38.4 million in minimum operating & maintenance (O&M) recovery, a \$4.1 million decrease in Capital recovery, offset by an increase of \$28.6 million in Variable recovery.

The Capital recovery revenues decrease of \$4.1 million is primarily due to increases in rate management credits given to the Water Contractors for Capital Delta Water Charge and Capital Transportation.

The \$28.6 million increase in Variable recovery revenues is primarily due to a 6.78 mills/kWh increase in the average mil rate. The average mil rate in 2012 was 36.62 mills/kWh compared to 29.84 mills/kWh in 2011. Actual water deliveries in fiscal 2012 were 3.39 million acre-feet compared to 3.53 million acre-feet in fiscal 2011. Although the water deliveries decreased by 0.14 million acre-feet, the increase in the average mil rate results in \$18.9 million additional recovery revenues. An additional \$9 million increase in revenues resulted from prior year under collections which amounted to \$44.8 million in fiscal 2012 compared to \$53.8 million in fiscal 2011.

Minimum O&M recovery revenues for FY 2012 decreased by \$38.4 million. The largest decrease of \$57.6 million was in recovery revenues for the Delta Habitat Conservation and Conveyance Program (DHCCP) due to lack of a funding source. A decrease of \$19.3 million was for adjustments in the Off-Aqueduct Power recovery revenues due to lower fuel and transmission costs and higher Off-Aqueduct power sales. Although replacement recoveries increased by \$4.1 million, \$10 million was refunded to the water contractors to lower the balance in the reserve account which resulted in a net decrease in replacements of \$5.9 million. These decreases were offset in part by a \$10.4 million increase in the Minimum Delta Water

## **State Water Resources Development System Management's Discussion and Analysis (Unaudited) For the years ended June 30, 2012 and 2011**

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Charge billings and \$29.1 million in the Transportation Minimum billings to recover operational costs to meet environmental compliances. Additional increases include \$3.8 million in recovery for the Reid Gardner Unit 4 separation costs and \$2.7 million increase of Delivery Structure revenues collected in advance for the North Bay Aqueduct Alternate Intake Project, and by \$1 million in East Branch Enlargement revenues, offset by \$2.7 million in decreases in other revenues.

In fiscal 2011, Water Supply Billings increased by \$21.6 million to a total of \$874.7 million. There were several contributing factors. A \$25.4 million increase occurred as a result of Capital recovery, a \$23 million increase was in Variable recovery, with an offsetting decrease of \$16.4 million in O&M recovery and a \$10.4 million in reclassification of DHCCP revenues. The increase in Capital recovery revenues was primarily due to an increase of \$12 million in Capital Transportation costs for completion of the Del Valle Surge Tank Pipeline repair and design and an increase of \$8.8 million due to increased Capital costs in the Delta. The increase in Variable recovery was primarily due to increased water deliveries in the southern part of the state where the cost to deliver water is higher, offset by a decrease in revenues for prior year over collections. The decrease in O&M recovery was primarily due to a decrease of \$25.9 million recovery and a \$10.4 million in reclassification for DHCCP revenues, a \$7.5 million decrease for prior year over collections, and \$3.8 million for replacements. These decreases were offset by increases of \$20.5 million in the Delta Water Charge recovery and \$4.6 million increase in recovery for Reid Gardner Unit 4 separations.

### ***Overview of the System's Power Activities***

The SWP is one of the largest consumers and suppliers of electric power in the western United States. Since the commencement of the major facilities of the SWP in the 1960s, the System has been an active participant in the power markets of California and the western United States. The System has provided for the financing, construction and operation of a variety of power projects including hydroelectric, geothermal and coal-fired electric generating facilities and facilities to transmit electric energy. The System currently owns eight power plants with a total nameplate capacity of approximately 1,800 Mw and with total annual energy generation in recent years ranging between approximately 3,100 and 7,500 Gwh. The System also owns and operates 23 pumping plants with a total load, when operational, of approximately 2,000 Mw and total annual energy consumption in recent years ranging between 5,300 and 10,000 Gwh. Typically, the majority of generation is during the on-peak hours; however, ancillary services are provided in all hours of the day.

Every hour the SWP must enter the power market to facilitate the operation of the California aqueduct. Operations continue 24 hours a day, seven days a week, with constant coordination with other utilities, water contractors, the California Independent System Operator (CAISO), and State Water Project pumping and generating plants. The power market controlled by CAISO can affect the bottom line cost or revenue from the System's hydro-electric facilities.

Every year the DWR is confronted with factors that affect how the operation of the SWP is conducted. Some factors include plant or unit outages, environmental concerns, weather, fluctuation in natural gas prices, transmission line outages and wild fires. Average rainfall during fiscal 2012 allowed for System reservoirs to maintain levels and schedule reasonable allocation of entitlement water to the water contractors. The SWP experienced both a decrease in energy sales and purchases in fiscal 2012. The CAISO cost increased during fiscal year 2012 due to continued increased pumping demand and limited resources at Oroville Reservoir.

## **State Water Resources Development System Management's Discussion and Analysis (Unaudited) For the years ended June 30, 2012 and 2011**

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Unavailability of units at DWR's Oroville complex continued to effect power activities in fiscal 2012.

Fiscal 2012 is the third year under the implemented Market Redesign and Technology Upgrades (MRTU). The new CAISO market requires all SWP load and generation be submitted into the market and priced using Locational Marginal Pricing (LMP). The implementation of the new energy market by the CAISO has completely changed the way the SWP handles bi-lateral transactions. In prior years, the financial aspect of the bi-lateral market was handled between the counterparties. In today's market, the bi-lateral trades have financial impact with both the CAISO and the trading counterparty. In addition, the new market requires every megawatt of generation or load to have a price and therefore a financial impact to the scheduling party.

### ***Power Sales***

Energy sales from SWP hydro-electric generating plants allow some recovery of cost of the System's hydro-electric pumping plants. Running the pumping plants as much as possible when energy prices are generally lower and generating energy during on-peak hours, when prices are generally higher is a proven strategy of the SWP. Reservoir storage levels greatly impact the SWP's ability to recover costs as generating energy requires more than adequate reservoir storages. The Oroville complex is the largest SWP resource and required by FERC to help mitigate negative environmental impacts. Mitigation could include controlling river temperatures, to assisting with after-bay and fore-bay elevation control, to help with nesting Grebe or Garter snake habitat. Required mitigation can occur despite having minimal storage available at Oroville Lake.

In Fiscal 2012, power sales decreased by \$44.8 million to a total of \$148.3 million. Transmission sold decreased by \$2.4 million. CAISO market reruns for prior years invoicing amounts applied by CAISO in Fiscal Year 2012 accounted for a \$12.2 million reduction in power sales revenues. An audit settlement agreement concerning payments made by PG&E during calendar years 2009 and 2010 required the reclassification of revenues to power purchases. This reclassification resulted in a decrease of current year power sales by \$4.0 million. The remaining \$28.5 million decrease is attributable to the fact that the system experienced a decrease in the quantity of energy sold and a slight decrease in the MWh rate. In Fiscal 2011, 1,338,296 MWh were sold compared to 988,839 MWh in fiscal 2012, a 26.11% decline from the prior year. The MWh rate decreased by less than 1%, from \$119.40 in fiscal 2011 to \$118.74 in fiscal 2012. The drop in sales was partially impacted by the new MRTU market's requirement of LMP and water deliveries.

The non-physical bi-lateral power sales transactions (financial only) when netted with the non-physical bi-lateral power purchase transactions between counterparties, resulted in less of a need to hedge the physical energy or generation to the CAISO. Average amounts of rainfall in fiscal 2012 resulted in only minor decreases to scheduled water deliveries. Water deliveries decreased from 3,531,739 acre feet in fiscal 2011 to 3,388,305 acre feet in 2012, a decrease of 143,434 acre feet or 4.06%.

In Fiscal 2011, power sales increased by \$27.5 million to a total of \$193 million. Although, the system experienced a decrease in the quantity of energy sold there was a substantial increase in the MWh rate as well as a slight increase in Transmission sold. In Fiscal 2010, 1,850,294 MWh were sold compared to 1,338,296 MWh in fiscal 2011, a 27.67% decline from the prior

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year. The overall rate increased by 65.4%, from \$72.19 in fiscal 2010 to \$119.4 in fiscal 2011. The drop in sales was also partially impacted by the new MRTU market's requirement of LMP.

The following tables shows the relationship between volume and rate for fiscal 2012 compared to fiscal 2011, and fiscal 2011 compared to fiscal 2010:

	<u>Total Sold</u>	<u>Transmission Sold</u>	<u>Power Sold</u>	<u>MWh Sold</u>	<u>Rate/MWh</u>
2011	\$ 193,153,799	\$ (33,357,996)	\$ 159,795,803	1,338,296	\$ 119.40
2012	148,360,007	(30,945,193)	117,414,814	988,839	118.74
Change in total MWh sold					(349,457)
Multiplied by 2011 rate/MWh					\$ 119.40
Difference attributed to decrease in sales					<u>\$ (41,725,000)</u>
Change in MWh rate					\$ (0.66)
Multiplied by 2012 MWh sold					988,839
Difference attributed to rate change					<u>\$ (653,000)</u>
Total decrease in power sales					<u>\$ (42,378,000)</u>

	<u>Total Sold</u>	<u>Transmission Sold</u>	<u>Power Sold</u>	<u>MWh Sold</u>	<u>Rate/MWh</u>
2010	\$ 165,663,966	\$ (32,091,514)	\$ 133,572,452	1,850,294	\$ 72.19
2011	193,153,799	(33,357,996)	159,795,803	1,338,296	119.40
Change in total MWh sold					(511,998)
Multiplied by 2010 rate/MWh					\$ 72.19
Difference attributed to decrease in sales					<u>\$ (36,961,000)</u>
Change in MWh rate					\$ 47.21
Multiplied by 2011 MWh sold					1,338,296
Difference attributed to rate change					<u>\$ 63,181,000</u>
Total increase in power sales					<u>\$ 26,220,000</u>

**Federal Reimbursements Revenue**

Federal reimbursements revenue for fiscal 2012 was \$36.6 million, compared to \$28.3 million for fiscal year 2011. The current year increase of \$8.3 million is due to an increase of \$5 million in DHCCP revenue; a \$4 million increase in expenses incurred at the Gianelli Pumping Plant, Dos Amigos Pumping Plant, and the San Luis Canal; and a \$3.3 million increase in Suisun Marsh facilities due to the change in recreation allocation from 14% to 3.4% in 2011. These increases were offset by a \$4.1 million decrease in USBR for disputed charges. These facilities are located within the Delta, San Luis, and Suisun Marsh facilities for which the System is reimbursed by the Federal government.

## **State Water Resources Development System Management's Discussion and Analysis (Unaudited) For the years ended June 30, 2012 and 2011**

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### ***Operating Expenses***

Total operating expenses decreased by \$41 million for 2012 to a total of \$940 million. The decrease is due to a decrease in power purchases of \$71 million, a decrease in depreciation expense of \$13 million and a decrease in deferred expenses of \$52 million, offset by an increase of \$95 million in operations and maintenance expense. The decrease in deferred expenses is represented by \$57 million of recognized expense in 2012 compared to \$110 million of recognized expense in 2011.

Total operating expenses for 2011 increased by \$62.5 million to a total of \$981 million. The increase is due to an increase in power purchases of \$129.8 million, and an increase in depreciation expense of \$19.4 million offset by a decrease in deferred expenses of \$79.5 million, and a decrease of \$7.2 million in operations and maintenance expense.

### ***Operations and Maintenance Expense***

Total operations and maintenance expenses were \$524 million for fiscal 2012, compared to \$428.6 million for fiscal 2011 and \$435.8 million for fiscal 2010. The increase of \$95.4 million in fiscal 2012 can be attributed to the following factors; increases of \$29.8 million related to the valuation of Easements and internally generated software that were classified as intangible assets in fiscal 2011; increases in salaries and wages of \$26.2 million mainly due to increased personnel to address heightened environmental responsibilities and continued maintenance of the aging infrastructure of the SWP; an increase of \$11.5 million in the procurement of external consultants and professional and legal service providers due to heightened environmental compliance efforts; \$10 million in increases for operation and maintenance of the Reid Gardner Power Plant; increases of \$3.8 million for maintenance and repairs; an increase of \$3.6 million in Pollution Remediation expense accrual; an increase of \$3.1 million in pro rata charges for services provided by the State Controller's Office; \$1.5 million in increased bond issuance cost; \$1.5 million increases in taxes and assessments; \$10.8 million in increases in overhead, supplies and miscellaneous expenses offset by a decrease in Post Retirement Employment Benefit Costs of \$6.4 million.

The decrease of \$7.2 million in fiscal 2011 was mainly attributable to the post capitalization of intangible assets. Operations and maintenance expenses were reduced in fiscal 2011 by \$29.8 million related to the valuation of easements and internally generated computer software which were reclassified as intangible assets pursuant to GASB Statement No. 51. Other decreases totaling \$17.3 million included Pollution Remediation accruals, reductions in Federal Cooperative contracts; reductions in the repairs and maintenance costs for South Bay and Edmonston Pumping Plants, and decreases in expense accruals. The fiscal 2011 decreases were offset by \$39.9 million in increases in environmental compliance cost, labor cost, bond issuance cost, and other operations and maintenance expenses.

### ***Power Purchases***

The System uses a significant amount of power to operate its pumping stations in order to deliver water to the Water Contractors. The System's sources of power include self-generated power by the eight power plants owned by the System, along with purchases of power from third party suppliers. As with power sales, in any given year, a combination of factors, including hydrological production, energy market rates, and energy market supply and demand, impact the System's energy requirements.

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For the years ended June 30, 2012 and 2011**

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Power purchases decreased \$71 million in fiscal 2012 to a total of \$271 million. In fiscal 2012 the results of an audit agreement regarding power sales reached with PG&E accounted for a \$4.0 million of this decrease. Transmission purchases decreased by \$8.2 million. Another decrease of \$4.9 million in power purchases resulted when all remaining settlement expenses terminating the Gas Hedging program ceased after fiscal 2011. The remaining \$53.9 million decrease is attributable to the fact that the system experienced a decrease in the quantity of energy purchased offset by an increase in MWh rate. In Fiscal 2011 4,703,953 MWh were purchased compared to 3,396,958 MWh in fiscal 2012, a 27.79% decline from the prior year. The MWh rate increased by less than 1% from \$60.69 in fiscal 2011 to \$65.54 in fiscal 2012. The decrease in purchases was impacted by the new MRTU market's requirement of LMP.

Power purchases are generally for off-peak pumping and are a reflection of water demand. Average rainfall in 2012 allowed for maintained reservoir levels and similar water deliveries from 2011. The result of this rainfall stability indicates the decrease in purchases was not significantly impacted by hydrological production in 2012. DWR tends to be more of a net energy purchaser in the energy market due to required water deliveries, which remained reasonable and similar from fiscal 2011 to 2012.

In fiscal 2011, purchased power increased \$130 million from fiscal 2010 to a total of \$342 million. Of that amount, \$67 million was attributed to increased units purchased and \$51.7 million was attributed to increase in the average rate per MWh purchased, while changes in transmission increased by \$11 million.

The following tables show the relationship between volume and rate for fiscal 2012 compared to fiscal 2011, and fiscal 2011 compared to fiscal 2010.

	<u>Total Purchased</u>	<u>Transmission Purchased</u>	<u>Power Purchased</u>	<u>MWh Purchased</u>	<u>Rate/MWh</u>
2011	\$ 342,445,800	\$ (56,971,668)	\$ 285,474,132	4,703,953	\$ 60.69
2012	271,377,161	(48,734,005)	222,643,156	3,396,958	65.54
Change in MWh purchased					(1,306,995)
Multiplied by 2012 rate					<u>\$ 65.54</u>
Difference attributed to increased purchases					<u>\$ (85,660,000)</u>
Change in MWh rate					\$ 4.85
Multiplied by 2011 purchased					<u>4,703,953</u>
Difference attributed to rate change					<u>\$ 22,814,000</u>
Total increase in power purchases					<u>\$ 62,846,000</u>

**State Water Resources Development System  
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For the years ended June 30, 2012 and 2011**

	<u>Total Purchased</u>	<u>Transmission Purchased</u>	<u>Power Purchased</u>	<u>MWh Purchased</u>	<u>Rate/MWh</u>
2010	\$ 212,658,256	\$ (45,960,886)	\$ 166,697,370	3,599,322	\$ 46.31
2011	342,445,800	(56,971,668)	285,474,132	4,703,953	60.69
Change in MWh purchased					1,104,631
Multiplied by 2011 rate					<u>\$ 60.69</u>
Difference attributed to increased purchases					<u>\$ 67,040,000</u>
Change in MWh rate					\$ 14.37
Multiplied by 2010 purchased					<u>3,599,322</u>
Difference attributed to rate change					<u>\$ 51,758,000</u>
Total increase in power purchases					<u>\$ 118,798,000</u>

***Operating Expenses Recovered***

In fiscal 2012, \$57.1 million in operating expenses were recognized, compared to fiscal 2011 in which the System recognized \$109.5 million in operating expenses. The 2012 net change of \$52.4 million is the result of a \$72.5 million decrease in deferred operation and maintenance expense; a \$9.6 million decrease in unbilled interest; a \$1.2 million decrease in power sales credit; and a \$548 thousand decrease in unamortized projects. These decreases were offset by an increase of \$31.4 million in deferred depreciation.

In fiscal 2011, \$109.5 million in operating expenses were recognized, compared to fiscal 2010 in which the System recognized \$189 million in operating expenses. The 2011 net change of \$79.5 million is the result of a \$14.6 million decrease in deferred depreciation due to Tehachapi East Afterbay, Hyatt Refurbishment, and Reid Gardner being placed into service; a \$2.2 million decrease in power sales credit; and a \$92.8 million decrease in deferred operation and maintenance expense. These decreases are offset by an increase of \$27.5 million in unbilled interest and \$2.7 million in unamortized projects.

***Capital Revenues Recovered***

Capital revenues recovered represents the timing difference between net capital revenue recovered, and certain operating costs incurred. Capital revenues recovered increased by \$17.4 million in 2012 to a total of \$31.4 million recovered compared to \$14 million in capital revenues recovered from the Water Contractors in fiscal 2011.

Capital revenues recovered decreased by \$5.8 million in 2011 to a total of \$14 million recovered compared to \$19.8 million in capital revenues recovered from the Water Contractors in fiscal 2010.

***Interest Expense***

Interest expense for fiscal 2012 was \$108 million, which represents a decrease of \$27.2 million from the prior year. This \$27.2 million decrease is attributable to three major factors; a \$9.8 million decrease in amortization of bond premium and discount, a \$7.2 million decrease in amortization of deferred losses on defeased bonds, and a \$10.2 million decrease in Interest Expense on debt service. The \$9.8 million variance in the amortization of premium and discount reflects an \$8.3 million increase in premium write-off and a \$1.5 million increase in amortization of premium and discount. The \$7.2 million decrease in the amortization of the

## **State Water Resources Development System Management's Discussion and Analysis (Unaudited) For the years ended June 30, 2012 and 2011**

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deferred amount on refunding is attributed to an \$8.3 million increase in premium write-off and \$1.1 million increase in amortization expense when compared to fiscal year 2011. The \$10.2 million decrease in interest expense reflects the decrease in bonds outstanding and the savings resulting from the current year debt refunding.

Interest expense for fiscal 2011 was \$135 million, which represents a decrease of \$16.4 million from the prior year. This \$16.4 million decrease is attributable to three major factors; a \$7.4 million decrease in amortization of bond premium and discount, a \$6 million decrease in amortization of deferred losses on defeased bonds, and a \$3 million decrease in Interest Expense on debt service. The \$7.4 million in the amortization of premium and discount variance occurred as a result of a larger amount of discount written off during fiscal 2010 than in fiscal 2011 and an adjustment relating to a change in the method of amortization to the straight line effective in fiscal 2010. The \$6 million variance in amortization gain and loss is attributed to a larger amount of discount written off during fiscal 2010 than in fiscal 2011 and an adjustment relating to a change in the method for recording amortization of gain and loss from the effective interest to the straight line in FY 2010. The \$3 million decrease in interest expense reflects the decrease in bonds outstanding and the savings resulting from the current year debt refunding.

### ***Other Revenues (Expenses)***

Other revenues, net of expenses decreased by \$35.2 million from \$5.6 million in revenues for fiscal year 2011 to \$29.6 million in expenses for fiscal year 2012. This decrease is attributable to a \$36.3 million accrual for a debt service release representing excess reserves, partially offset by a \$1.4 million increase in bond proceeds related to the issuance of bond Series AI, AJ, and AK. In addition, interest income decreased by \$1.1 million due to declines in interest rates. The decrease in revenues was partially offset by an \$800 thousand decrease in the amount of refunds paid to the water contractors.

Other revenues were \$5.5 million in fiscal year 2011, versus \$7 million in fiscal 2010. The \$1.5 million decrease in 2011 is primarily the result of a \$10 million decrease in unrealized gains and losses due to the discontinuance of gas hedging activities, offset by a \$500 thousand increase in investment income and \$8.9 million increase in bond proceeds. The \$8.9 million increase is primarily the result of a \$5.8 million Springing Amendment debt service reserves released in fiscal 2010, and a \$3.8 million increase in bond proceeds for Series AH.



## **Basic Financial Statements**

**State Water Resources Development System**  
**Statements of Net Assets**  
**June 30, 2012 and 2011**

(in thousands)

	<u>2012</u>	<u>2011</u>
<b>Assets</b>		
Utility plant:		
Utility plant in service	\$ 5,086,686	\$ 5,028,895
Less accumulated depreciation	<u>(2,281,806)</u>	<u>(2,194,406)</u>
Net utility plant in service	2,804,880	2,834,489
Construction work in progress	<u>408,072</u>	<u>366,975</u>
Total utility plant	<u>3,212,952</u>	<u>3,201,464</u>
Long-term assets:		
Restricted assets:		
Cash and cash equivalents restricted for plant replacements	32,227	38,502
Cash and investments restricted for debt service	115,481	114,346
Cash and cash equivalents on deposit with revenue bond trustee	9,205	9,208
Loans receivable from local water agencies	19,142	21,040
Advance to other state funds	<u>91,517</u>	<u>91,517</u>
Total long-term assets	<u>267,572</u>	<u>274,613</u>
Current assets:		
Cash and cash equivalents	422,404	464,978
Receivables:		
Interest on investments	1,288	1,726
Water supply and power billings (net)	110,649	80,301
Due from federal government	15,787	19,625
Due from others	-	480
Inventories	<u>29,653</u>	<u>32,984</u>
Total current assets	<u>579,781</u>	<u>600,094</u>
Deferred charges:		
Amounts recoverable through future billings under long-term water supply contracts:		
Operations and maintenance expense	27,733	-
Capital credit due from water contractors	80,483	49,087
Unamortized project costs	332,302	341,585
Unbilled interest incurred on unrecovered capital costs	<u>467,632</u>	<u>480,345</u>
Total deferred charges	<u>908,150</u>	<u>871,017</u>
Total assets	<u>\$ 4,968,455</u>	<u>\$ 4,947,188</u>

The accompanying notes are an integral part of these financial statements.

**State Water Resources Development System**  
**Statements of Net Assets (continued)**  
**June 30, 2012 and 2011**

(in thousands)

	<u>2012</u>	<u>2011</u>
<b>Capitalization and Liabilities</b>		
Capitalization:		
Net assets:		
Capital, net of related debt	\$ 684,025	\$ 554,854
Restricted	521,406	650,577
Total net assets	<u>1,205,431</u>	<u>1,205,431</u>
Long-term liabilities		
General obligation bonds	302,920	362,375
Revenue bonds	2,303,201	2,346,444
Commercial paper	28,783	54,578
Other postemployment benefits	117,924	97,898
Pooled Money Investment Account (PMIA) Loan	14,896	18,052
Accrued vacation	32,939	29,052
Pollution remediation	8,920	5,080
Total long-term liabilities	<u>2,809,583</u>	<u>2,913,479</u>
Total capitalization	<u>4,015,014</u>	<u>4,118,910</u>
Current liabilities:		
Current maturities of bonds	183,610	174,315
Accounts payable	88,025	59,852
Accrued vacation	7,318	6,632
Pollution remediation	2,000	1,000
Accrued interest on long-term debt	17,370	17,845
Pooled Money Investment Account (PMIA) Loan	3,156	3,003
Due to other state funds	34,024	36,547
Proceeds due to water contractors	142,048	111,004
Total current liabilities	<u>477,551</u>	<u>410,198</u>
Deferred credits:		
Deferred revenue - State and Federal capital recovery	149,348	152,982
Operations and maintenance expense	-	25,281
Capital costs	123,153	25,123
Power sales credit due to water contractors	168,236	178,222
Advances for plant replacements	35,153	36,472
Total deferred credits	<u>475,890</u>	<u>418,080</u>
Total net assets and liabilities	<u>\$ 4,968,455</u>	<u>\$ 4,947,188</u>

The accompanying notes are an integral part of these financial statements.

**State Water Resources Development System**  
**Statements of Revenues, Expenses, and Changes in Net Assets**  
**For the years ended June 30, 2012 and 2011**

**(in thousands)**

	<u>2012</u>	<u>2011</u>
Operating revenues:		
Water supply	\$ 860,891	\$ 874,748
Power sales	148,360	193,154
Federal reimbursements	36,561	28,294
Total operating revenues	<u>1,045,812</u>	<u>1,096,196</u>
Operating expenses:		
Operations and maintenance	523,951	428,559
Purchased power	271,377	342,446
Depreciation expense	87,400	100,257
Operating expenses recovered, principally under long-term water supply contracts, net	<u>57,076</u>	<u>109,535</u>
Total operating expenses	<u>939,804</u>	<u>980,797</u>
Income from operations	106,008	115,399
Nonoperating revenue (expenses):		
Capital revenues recovered	31,396	14,022
Interest expense	(107,770)	(134,996)
Other revenues (expenses), net	<u>(29,634)</u>	<u>5,575</u>
Change in net assets	-	-
Net assets, beginning of year	<u>1,205,431</u>	<u>1,205,431</u>
Net assets, end of year	<u>\$ 1,205,431</u>	<u>\$ 1,205,431</u>

The accompanying notes are an integral part of these financial statements.

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**State Water Resources Development System**  
**Statements of Cash Flows**  
**For the years ended June 30, 2012 and 2011**

**(in thousands)**

	<u>2012</u>	<u>2011</u>
<b>Cash flows from operating activities:</b>		
Receipts from customers	\$ 1,045,826	\$ 1,068,964
Payments to employees for services	(258,226)	(232,016)
Payments to suppliers	(478,686)	(526,170)
Other expenses	(36,488)	(3,040)
Net cash provided by operating activities	<u>272,426</u>	<u>307,738</u>
<b>Cash flows from capital and related financing activities:</b>		
Proceeds from issuance of revenue obligation bonds including premium	112,033	74,591
Principal payments on long-term debt	(174,315)	(165,245)
Commercial paper notes issued	75,444	79,643
Principal payments on commercial paper notes	(101,239)	(71,538)
Principal payments on PMIA note	(3,003)	(2,857)
Interest payments on long-term debt	(139,367)	(137,729)
Additions to utility plant and CWIP	(98,887)	(86,537)
Net cash used by capital and related financing activities	<u>(329,334)</u>	<u>(309,672)</u>
<b>Cash flows from investing activities:</b>		
Cash received from investment earnings	6,991	8,944
Proceeds of investments matured	302,608	252,174
Purchases of investments	(302,608)	(252,174)
Loan payments from local water agencies	1,898	1,570
Net cash provided by investing activities	<u>8,889</u>	<u>10,514</u>
<b>Net increase (decrease) in cash and cash equivalents</b>	(48,019)	8,580
<b>Cash and cash equivalents, beginning of year</b>	551,721	543,141
<b>Cash and cash equivalents, end of year</b>	<u>\$ 503,702</u>	<u>\$ 551,721</u>
<b>Noncash capital and related financing activities:</b>		
Amortization of Bond Premium/Discount	\$ 16,431	\$ 6,677
Principal retirements of long-term debt on proceeds received from issuance of Series AH, AI, AJ and AK Water System Revenue Bonds	266,785	29,785
<b>Noncash capital and related financing activities:</b>	<u>\$ 283,216</u>	<u>\$ 36,462</u>

The accompanying notes are an integral part of these financial statements.

**State Water Resources Development System**  
**Statements of Cash Flows (continued)**  
**For the years ended June 30, 2012 and 2011**

**(in thousands)**

	<u>2012</u>	<u>2011</u>
<b>Reconciliation to the statement of net assets:</b>		
Cash and cash equivalents	\$ 422,404	\$ 464,978
Restricted assets:		
Cash and cash equivalents restricted for plant replacements	32,227	38,502
Cash and cash equivalents restricted for debt service (net of \$75,615 and \$75,313 of U.S. Agency securities for 2012 and 2011, respectively)	39,866	39,033
Cash and cash equivalents on deposit with revenue bond trustee	9,205	9,208
<b>Cash and cash equivalents</b>	<u>\$ 503,702</u>	<u>\$ 551,721</u>
	<u>2012</u>	<u>2011</u>
<b>Reconciliation of income from operations to net cash provided by operating activities:</b>		
Income from operations	\$ 106,008	\$ 115,399
Adjustment to reconcile income from operations to net cash provided by operating activities		
Depreciation expense	87,400	100,257
Other expenses	(36,488)	(3,040)
Decrease in deferred charges and credits, net	52,072	83,383
Changes in assets and liabilities:		
(Increase) decrease in receivables	(29,868)	4,266
(Increase) decrease in inventories	3,331	(9,902)
Decrease in due from federal government	3,838	4,689
Increase in accounts payable, accrued vacation, pollution remediation and other postemployment benefits	57,612	14,456
Increase (decrease) in due to other state funds	(2,523)	8,264
Increase (decrease) in proceeds due to Water Contractors	31,044	(10,034)
Total adjustments	<u>166,418</u>	<u>192,339</u>
<b>Net cash provided by operating activities</b>	<u>\$ 272,426</u>	<u>\$ 307,738</u>

The accompanying notes are an integral part of these financial statements.

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# State Water Resources Development System

## Notes to Financial Statements

For the years ended June 30, 2012 and 2011

(in thousands)

### 1. Reporting Entity

The State Water Resources Development System (System), a component unit of the State of California (State), includes the State Water Project (SWP), the Davis-Grunsky Act Program and the San Joaquin Drainage Implementation Program, was constructed as the result of initial legislation in 1951 and subsequent legislation in the 1960s providing various financing mechanisms. The SWP is a complex of dams, water storage facilities, aqueducts, pumping stations and electric generation facilities which have been constructed for purposes of developing firm water supply and conveying water to areas of need within the State and providing flood control, recreation, fish and wildlife enhancement and hydroelectric power. The System has entered into long-term water supply contracts with 29 customers (Water Contractors) in order to recover substantially all System costs. The 29 Water Contractors are principally located in the San Francisco Bay Area, the Central Valley and Southern California and their service areas encompass approximately 25% of the State's land area and 70% of its population.

The System is accounted for as an enterprise fund and is financed and operated in a manner similar to that of a private business enterprise. The System uses the economic resources measurement focus and the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. Under the provisions of GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, the System applies all GASB pronouncements, as well as any applicable pronouncements of the Financial Accounting Standards Board (FASB), the Accounting Principles Board (APB), or any Accounting Research Bulletins (ARB) issued on or before November 30, 1989, except for those that conflict or contradict GASB pronouncements. The System has elected not to follow subsequent FASB pronouncements issued after November 30, 1989. The System is administered by the State of California Department of Water Resources (DWR).

### 2. Summary of Significant Accounting Policies

#### Utility Plant

Utility plant is recorded at original cost. Cost includes labor, materials and indirect items such as engineering, supervision, transportation and interest on borrowed funds incurred during construction. Repairs, maintenance and minor purchases of equipment are charged to expense as incurred.

# State Water Resources Development System

## Notes to Financial Statements

For the years ended June 30, 2012 and 2011

(in thousands)

### Depreciation

Depreciation is provided on a straight-line basis over the estimated useful lives of the various classes of utility plant, as follows:

Aqueducts	80 - 100 years
Dams and reservoirs	85 years
Environmental preservation and mitigation	50 years
Power plants	30 - 50 years
Pumping plants	30 - 40 years
Fish protection	35 - 36 years
Facilities	20 - 30 years
Machinery, equipment and vehicles	3 - 5 years
General	5 years

The System's intangible assets, consisting of software, land use and legal rights, and costs associated with the FERC licenses, are included in utility plant in service. Software costs are being amortized on a straight-line basis over a 10 year useful life. Easements are land use rights and are considered as either permanent or temporary. Permanent easements have an indefinite useful life and are non-depreciable while temporary easements are being depreciated over a 5 year useful life, unless otherwise specified in the purchase agreement.

### Cash and Cash Equivalents

Cash and cash equivalents, for purposes of the statement of cash flows, includes cash on hand, restricted cash for plant replacements, restricted cash for debt service and restricted cash on deposit with revenue bond trustee. Such amounts include deposits in the State of California Pooled Money Investment Account-Surplus Money Investment Fund (SMIF) and instruments with original maturities of three months or less. Cash and cash equivalents do not include U.S. Government and Agency securities with maturities of more than three months.

### Restricted Cash and Investments

Cash on deposit with revenue bond trustee consists of debt service reserve funds held with a major national bank for the Series 1973 Devil Canyon – Castaic Facilities bonds.

Cash and investments with the State Treasurer for plant replacements and debt service are restricted as required by the provisions of the water supply contracts and bond resolutions. Restricted funds consist of investments of the same type as those described below.

### Investments

Cash not required for current use, including restricted cash, is invested in the Surplus Money Investment Fund (SMIF), which is stated at fair value. SMIF is part of the State of California Pooled Money Investment Account (PMIA), which as of June 30, 2012 and 2011 had a balance of \$62.7 billion and \$68.2 billion, respectively. The weighted average to maturity of PMIA investments was 270 days and 237 days as of June 30, 2012 and 2011, respectively. The total amount of deposits in SMIF as of June 30, 2012 and 2011 was \$30 billion and \$35 billion, respectively. The Pooled Money Investment Board (PMIB) has oversight responsibility for SMIF. The Board consists of three members as designated by state statute. The value of the pool shares in SMIF which may be withdrawn is determined on an amortized cost basis, which is different than the fair value of the System's portion of the pool. PMIA funds are on deposit with the State's Centralized Treasury System and are

# State Water Resources Development System

## Notes to Financial Statements

For the years ended June 30, 2012 and 2011

(in thousands)

not SEC registered, but are managed in compliance with the California Government Code, according to a statement of investment policy which sets forth permitted investment vehicles, liquidity parameters and maximum maturity of investments. These investments consist of U.S. government securities, securities of federally-sponsored agencies, U.S. corporate bonds, interest bearing time deposits in California banks, prime-rated commercial paper, bankers' acceptances, negotiable certificates of deposit, repurchase and reverse repurchase agreements. The PMIA policy limits the use of reverse repurchase agreements subject to limits of no more than 10% of PMIA. The PMIA does not invest in leveraged products or inverse floating rate securities. Included in PMIA's investment portfolio are structured notes and asset-backed securities totaling \$800 million and \$1.3 billion as of June 30, 2012 and \$1.1 billion and \$2.2 billion as of June 30, 2011.

The System is authorized by statute to invest in the same types of investment vehicles permitted by the State's Centralized Treasury System. U.S. Treasury and agency debt securities are carried at fair value. Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, and is determined from published data provided by the exchanges, computerized pricing sources, the National Association of Securities Dealers' National Market System, securities custodians, and other authoritative sources. Investments made by the System during the year ended June 30, 2012, are of a similar nature as those held at June 30, 2011.

### **Advance to Other State Funds**

Advance to Other State Funds represents the System's advance of \$92 million to DWR's internal service fund, and functions as a revolving working capital facility for the System.

### **Receivables**

Receivables include amounts due from the Water Contractors and organizations that purchase power from the System, totaling \$110,649 and \$80,301, net of the allowance for uncollectible amounts, at June 30, 2012 and 2011, respectively. Additionally, the Federal government owed the System \$15,787 and \$19,625 at June 30, 2012 and 2011, respectively, as reimbursement for certain costs related to flood control and jointly owned facilities. The allowance for uncollectible amounts totaled \$197 and \$24,275 at June 30, 2012 and 2011, respectively. Uncollectible amounts are generally recoverable from the Water Contractors.

### **Deferred Charges and Credits**

The System has the authority to establish the level of rates to recover all System costs, including debt service. As a regulated entity, the System's financial statements are prepared in accordance with FASB ASC 980, *Regulated Operations*, formerly known as SFAS 71, *Accounting for the Effects of Certain Types of Regulation*, which requires that the effects of the rate-making process be recorded in the financial statements. Accordingly, certain expenses and credits, normally reflected in the change in net assets, as incurred, are recognized when included in rates and recovered from, or refunded to customers and the state and federal governments. The System records various regulatory assets and credits to reflect rate-making actions of management. The System records costs that are recoverable through future billings as deferred charges and revenues that are in excess of total project costs from inception of the SWP as deferred credits. These costs include capital costs and operations and maintenance costs.

# State Water Resources Development System

## Notes to Financial Statements

For the years ended June 30, 2012 and 2011

(in thousands)

Unamortized project costs represent abandoned utility plant and research and development expenses that are recoverable through future billings to the Water Contractors under the terms of the water supply contracts.

Unbilled interest earned on unrecovered capital costs are classified as deferred charges until billed under the terms of the water supply contracts. Unbilled interest earned represents the System's unrecovered interest since inception, recalculated annually at the System's cumulative weighted average cost of borrowing (Project Interest Rate). The System's Project Interest Rate was 4.610% and 4.608% for the years ended June 30, 2012 and 2011 respectively.

Deferred revenue represents payments by the State and Federal governments for their share of the System's recreation and flood control capital costs in excess of the related depreciation expense recognized in the statements of revenues, expenses, and changes in net assets.

The deferred power sales credit arises from revenue collected for the power generated by the Hyatt-Thermalito Power Plant. The deferred power sales credit is amortized over time by a credit issued to the Water Contractors through the Delta Water Capital Charge.

Advances for plant replacements represent billings under the terms of water supply contracts for future replacement of certain System assets. Assets from such billings are restricted. Costs of plant replacements are charged to the reserve as incurred.

### **Bond Issuance Discounts and Premiums**

Bond issuance discounts and premiums are reflected as a reduction/increase to the carrying value of the bonds outstanding and are amortized over the lives of the related debt instruments.

### **Deferred Amount on Refunding**

Gains or losses associated with the advance refunding of debt are deferred and amortized over the shorter of the weighted average lives of the new debt or the refunded debt.

### **Net Assets**

The System classifies its net assets into two components, invested in capital assets, net of related debt and restricted net assets. Net assets invested in capital assets includes total utility plant, net of accumulated depreciation, related long-term debt and other assets and liabilities relating to the recovery of utility plant. The remaining net assets of the System are classified as restricted due to the requirements of legislation that created the System and authorized the construction of the SWP, to use the System's net assets solely in support of the SWP, the Davis-Grunsky Act Program and the San Joaquin Drainage Implementation Program.

### **Revenues**

The cost of providing services from the System is required to be recovered through user charges and other reimbursements. Under the terms of the long-term water supply contracts, the System granted the Water Contractors rate management reductions of approximately \$32,926 and \$16,788 during the years ended June 30, 2012 and 2011, respectively. Rate management reductions are permanent reductions in capital related billings to the Water Contractors.

# State Water Resources Development System

## Notes to Financial Statements

For the years ended June 30, 2012 and 2011

(in thousands)

Revenues under long-term water supply contracts are recognized when billings are due and payable. The billings cover debt service requirements, an additional 25% of revenue bond debt service to satisfy certain bond covenants and current and past unrecovered operations and maintenance costs. The water supply contracts provide that the 25% portion of the billings collected for the purpose of satisfying certain bond covenants be refunded in the subsequent year. These billings, which totaled \$56,385 and \$55,542 for the years ended June 30, 2012 and 2011, respectively, are recorded as Proceeds due to water contractors in the financial statements. The System refunded \$55,849 and \$52,967 for the years ended June 30, 2012 and 2011, respectively, to the Water Contractors for the 25% bond cover requirement.

Revenues from the sale of surplus power are recognized as the power is delivered.

The Federal government reimburses the System for certain operating and capital costs incurred by the System for flood control purposes. In addition, the Federal government reimburses the System for the Federal government's 45% share of the operating costs of the San Luis joint use facilities and other water facilities. Revenue from the State and Federal government in excess of their share of the related depreciation expense is deferred until the related depreciation expense is recognized.

### Segments

The System has two segments, which are defined under governmental accounting standards as an identifiable activity for which one or more revenue bonds or other revenue-backed debt instruments are outstanding:

1) Activities Allowed Under the Burns-Porter Act – This segment accounts for the costs to build, operate and maintain the facilities financed by general obligation bonds as authorized by the Burns-Porter Act. Transportation and conservation revenues from the Water Contractors are recorded in this segment as well as power sales and reimbursements from Federal and State governments, and interest on investments. Expenses are limited to operations and maintenance of the SWP constructed with general obligation bond proceeds, power purchases, replacements and debt service on the general obligation bonds.

2) Activities Allowed Under the Central Valley Project Act – This segment accounts for the costs to build, operate and maintain the facilities financed by the Central Valley Project Water System revenue bonds. Capital and operating revenues from the Water Contractors for projects financed by revenue bond proceeds are recorded in this segment as well as commercial paper sales, reimbursements from Federal and State governments for the San Luis Dam and Reservoir, Suisun Marsh and recreation costs, and interest on investments. Expenses are limited to the construction and operation of SWP facilities constructed with revenue bond proceeds and power facilities, and debt service payments on the revenue bonds.

### Reclassifications

Certain amounts presented in the prior year have been reclassified in order to be consistent with the current year's presentation.

# State Water Resources Development System

## Notes to Financial Statements

For the years ended June 30, 2012 and 2011

(in thousands)

### 3. Interests in Jointly Owned Facilities

At June 30, 2012 and 2011, the System owned the following undivided interests in jointly owned facilities:

	System's Share					
	% Owned by System		Utility Plant in Service		Accumulated Depreciation	
	2012	2011	2012	2011	2012	2011
Reid Gardner Power Plant Unit No. 4	67.8%	67.8%	\$ 359,959	\$ 360,539	\$ 344,857	\$ 323,859
San Luis joint use facilities	55.0%	55.0%	281,455	281,140	125,068	120,960

The amounts above include the System's share of direct costs related to building the facilities. Each participant provides its own financing for the jointly owned facility.

DWR is the operator of the San Luis joint use facilities. All of the operating expenses related to these facilities are included as operating expenses in the statement of revenues, expenses, and changes in net assets. The Federal government is billed for its share of the operating expenses, and these billings are included as operating revenues in the statement of revenues, expenses, and changes in net assets.

DWR does not operate the Reid Gardner Power Plant Unit No. 4. The portion of Reid Gardner Power Plant Unit No. 4 operations attributable to the System's share is included in operations and maintenance expense in the statement of revenues, expenses, and changes in net assets.

**State Water Resources Development System**  
**Notes to Financial Statements**  
**For the years ended June 30, 2012 and 2011**

**(in thousands)**

**4. Utility Plant**

The summarized activity of the System's utility plant during 2012 is presented below:

	Beginning Balance June 30, 2011	Transfers and Additions	Transfers and Deletions	Ending Balance June 30, 2012
Nondepreciable Utility Plant:				
Land	\$ 136,129	\$ -	\$ -	\$ 136,129
Construction work in progress (CWIP)	366,975	88,287	(47,190)	408,072
Land use rights	11,005	245	-	11,250
Other intangible assets	81,976	6,954	-	88,930
Total nondepreciable utility plant	<u>596,085</u>	<u>95,486</u>	<u>(47,190)</u>	<u>644,381</u>
Depreciable Utility Plant:				
Aqueducts	2,057,437	6,771	-	2,064,208
Dams & reservoirs	781,110	92	-	781,202
Power plants	910,100	2,270	(5,816)	906,554
Pumping plants	787,008	42,336	-	829,344
Environmental preservation and mitigation	67,797	-	-	67,797
Fish protection	33,934	-	-	33,934
Facilities	64,810	1,010	-	65,820
Equipment and other depreciable assets	67,996	2,597	-	70,593
Computer software	23,629	533	-	24,162
Land use rights	-	272	-	272
General	5,964	527	-	6,491
	<u>4,799,785</u>	<u>56,408</u>	<u>(5,816)</u>	<u>4,850,377</u>
Less: accumulated depreciation	(2,182,591)	(85,037)	-	(2,267,628)
Less: accumulated amortization	(11,815)	(2,363)	-	(14,178)
	<u>(2,194,406)</u>	<u>(87,400)</u>	<u>-</u>	<u>(2,281,806)</u>
Total depreciable plant	<u>2,605,379</u>	<u>(30,992)</u>	<u>(5,816)</u>	<u>2,568,571</u>
Total Utility Plant - net	<u>\$ 3,201,464</u>	<u>\$ 64,494</u>	<u>\$ (53,006)</u>	<u>\$ 3,212,952</u>

**State Water Resources Development System**  
**Notes to Financial Statements**  
**For the years ended June 30, 2012 and 2011**

**(in thousands)**

The summarized activity of the System's utility plant during 2011 is presented below:

	Beginning Balance June 30, 2010	Transfers and Additions	Transfers and Deletions	Ending Balance June 30, 2011
<b>Nondepreciable Utility Plant:</b>				
Land	\$ 136,129	\$ -	\$ -	\$ 136,129
CWIP	400,229	83,880	(117,134)	366,975
Land use rights	10,925	80	-	11,005
Other intangible assets	81,976	-	-	81,976
<b>Total nondepreciable utility plant</b>	<b>629,259</b>	<b>83,960</b>	<b>(117,134)</b>	<b>596,085</b>
<b>Depreciable Utility Plant:</b>				
Aqueducts	2,029,898	27,539	-	2,057,437
Dams & reservoirs	765,246	15,864	-	781,110
Power plants	909,904	196	-	910,100
Pumping plants	784,247	2,761	-	787,008
Environmental preservation and mitigation	67,797	-	-	67,797
Fish protection	33,934	-	-	33,934
Facilities	-	64,810	-	64,810
Equipment and other depreciable assets	65,580	2,616	(200)	67,996
Computer software	23,629	-	-	23,629
General	-	5,964	-	5,964
	4,680,235	119,750	(200)	4,799,785
Less: accumulated depreciation	(2,084,854)	(97,894)	157	(2,182,591)
Less: accumulated amortization	(9,452)	(2,363)	-	(11,815)
	(2,094,306)	(100,257)	157	(2,194,406)
<b>Total depreciable plant</b>	<b>2,585,929</b>	<b>19,493</b>	<b>(43)</b>	<b>2,605,379</b>
<b>Total Utility Plant - net</b>	<b>\$ 3,215,188</b>	<b>\$ 103,453</b>	<b>\$ (117,177)</b>	<b>\$ 3,201,464</b>

**5. Investments**

As of June 30, 2012, the System's investments and credit ratings are as follows:

	Credit Rating (S&P)	-----Maturities-----					Fair Value
		Under 30 Days	31-180 Days	181-365 Days	1-5 Years	Over 5 Years	
<b>Investments:</b>							
Money Market Mutual Funds	Not Rated	\$ 3	\$ -	\$ -	\$ -	\$ -	\$ 3
PMIA	Not Rated	-	-	494,494	-	-	494,494
US Federal Agency Notes							
Federal National Mortgage Association	AA+	-	51,160	-	12,202	12,253	75,615
							<u>570,112</u>
Investment with Fiscal Agent							
Money Market Mutual Funds	AAA	9,205	-	-	-	-	9,205
<b>Total Investments</b>							<u><b>\$ 579,317</b></u>



# State Water Resources Development System

## Notes to Financial Statements

For the years ended June 30, 2012 and 2011

(in thousands)

As of June 30, 2011, the System's investments and credit ratings are as follows:

	Credit Rating (S&P)	Maturities					Fair Value
		Under 30 Days	31-180 Days	181-365 Days	1-5 Years	Over 5 Years	
<b>Investments:</b>							
Money Market Mutual Funds	Not Rated	\$ 3	\$ -	\$ -	\$ -	\$ -	\$ 3
PMIA	Not Rated	-	-	542,510	-	-	542,510
US Federal Agency Notes							
Federal National Mortgage Association	AAA	-	51,000	-	-	24,313	75,313
							617,826
Investment with Fiscal Agent							
Money Market Mutual Funds	AAA	9,208	-	-	-	-	9,208
<b>Total Investments</b>							<b>\$ 627,034</b>

**Interest Rate Risk:** In accordance with its investment policy, the State of California manages its exposure to declines in fair value by spreading investments over the various maximum maturities: U.S. Treasury securities, 5 years; federal agency securities, 5 years; bankers acceptances – domestic and foreign, 180 days; certificates of deposits, 5 years; collateralized time deposits, 5 years; commercial paper, 180 days; corporate bonds and notes, 5 years; repurchase agreements and reverse repurchase agreements, 1 year.

**Custodial Credit Risk:** For deposits, custodial credit risk is that in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The California Government Code does not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits or investments, other than the following provision for deposits: The California Government Code requires that a financial institution secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by depository regulated under state law. The market value of the pledged securities in the collateral pool must equal at least 110% of the total amount deposited by the public agencies. California law also allows financial institutions to secure deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits.

**Credit Risk:** PMIA funds are on deposit with the State's Centralized Treasury System and are managed in compliance with the California Government Code, according to a statement of investment policy discussed in Note 2. The PMIA is not rated.

**Concentration of Credit Risk:** The PMIA's concentration of credit risk is limited by spreading the investment mix over different investment types, credit ratings and issuers to minimize the impact any one industry, investment class, or institution can have on the PMIA portfolio. As of June 30, 2012 and 2011, nearly 13% and 12%, respectively of the System's investments at year-end were in U.S. Agency Securities. There is no limitation on amounts invested in these types of issues. Investments in any one issuer (other than U.S. Treasury Notes, mutual funds and external investment pools) that represented 5% or more of the total investments of the System as of June 30, 2012 and 2011, was as follows:

# State Water Resources Development System

## Notes to Financial Statements

For the years ended June 30, 2012 and 2011

(in thousands)

	<u>2012</u>	<u>2011</u>
Federal National Mortgage Association	\$ 75,615	\$ 75,313

Interest on deposits in PMIA varies with the rate of return of the underlying portfolio and averaged 0.382% and 0.495% for the years ended June 30, 2012 and 2011, respectively. For the years ended June 30, 2012 and 2011, interest earned on the deposits with PMIA approximated \$2,188 and \$2,947, respectively and are included in the other expenses line item on the statement of revenues, expenses and change in net assets.

Total interest and investment income is comprised of interest, dividends, realized gains and losses, and unrealized gains and losses due to changes in the fair value of investments held at year-end. The change in fair value of the System's investments (U.S. Federal Agency Securities) is calculated as follows:

	<u>2012</u>	<u>2011</u>
Fair Value of Investments at the beginning of the fiscal year	\$ 75,313	\$ 75,593
Less: Proceeds of investments matured in fiscal year	(302,608)	(252,174)
Add: Purchase of investments in fiscal year	302,608	252,174
Add: Amortization of Discounts	63	63
Change in fair value of investments during fiscal year	239	(343)
Fair value of investments at the end of the fiscal year	<u>\$ 75,615</u>	<u>\$ 75,313</u>

## 6. Long-term Debt

The following is a summary of changes in long-term debt for the years ended June 30, 2012 and 2011:

	General Obligation Bonds		Revenue Bonds			Commercial Paper	PMIA Loan	Total Long Term Debt
	Par Amount	Par Amount	Unamortized (Discounts) and Premium	Deferred Amount on Refunding	Total Revenue Bonds	Par Amount		
Balance at June 30, 2010	\$ 476,915	\$ 2,421,185	\$ 104,948	\$ (26,084)	\$ 2,500,049	\$ 46,473	\$ 23,912	\$ 3,047,349
Additions	-	97,675	13,378	(4,809)	106,244	79,643	-	185,887
Payments/amortization	(56,375)	(138,655)	(6,677)	1,633	(143,699)	(71,538)	(2,857)	(274,469)
Balance at June 30, 2011	420,540	2,380,205	111,649	(29,260)	2,462,594	54,578	21,055	2,958,767
Additions	-	345,575	49,674	(35,647)	359,602	75,444	-	435,046
Payments/amortization	(58,165)	(382,935)	(16,431)	4,526	(394,840)	(101,239)	(3,003)	(557,247)
Balance at June 30, 2012	362,375	2,342,845	144,892	(60,381)	2,427,356	28,783	18,052	2,836,566
Less current portion	(59,455)	(124,155)	-	-	(124,155)	-	(3,156)	(186,766)
Total Long-term Debt	<u>\$ 302,920</u>	<u>\$ 2,218,690</u>	<u>\$ 144,892</u>	<u>\$ (60,381)</u>	<u>\$ 2,303,201</u>	<u>\$ 28,783</u>	<u>\$ 14,896</u>	<u>\$ 2,649,800</u>

# State Water Resources Development System

## Notes to Financial Statements

For the years ended June 30, 2012 and 2011

(in thousands)

### General Obligation Bonds

The Burns-Porter Act authorized the issuance of State Water Resources Development (WRD) General Obligation Bonds in the amount of \$1,750,000 for construction of the System. This amount included \$130,000 to be set aside for financial assistance to local water agencies as provided in the Davis-Grunsky Act. The Burns-Porter Act also made a continuing appropriation of the California Water Fund, a fund unrelated to the System, to supplement the bond authorization. To the extent Water Fund money was used for construction of the State water facilities in lieu of bond proceeds, an equal amount of bond authorization was set aside to be used only for the construction of additional facilities of the System that meet certain requirements set forth in the Burns-Porter Act.

Under the Burns-Porter Act, revenues of the System, other than revenues attributable to facilities financed with Central Valley Project Water System (CVP) Revenue Bonds, are deposited in the California Water Resources Development Bond Fund and are to be used annually only for the following purposes and in the following order of priority:

- (1) To pay the maintenance, operation and replacement costs of the System,
- (2) To pay, or reimburse the General Fund of the State for, the principal of and interest on the WRD General Obligation Bonds issued for the System as it becomes due,
- (3) To reimburse the California Water Fund for funds utilized from said fund for construction of the System (complete reimbursement has been made), and
- (4) To pay additional costs of the acquisition and construction of the System.

All such revenues are pledged for those uses and purposes for the benefit of the owners of the WRD General Obligation Bonds.

As of June 30, 2012, the amount of the revenues pledged to repay the Burns-Porter Act WRD General Obligation Bonds debt service is \$421,631 with payments through 2025. Principal and interest paid for the current year were \$75,728 and Burns-Porter Act water supply operating revenues were \$499,140. As of June 30, 2011 the amount of the revenues pledged to repay the Burns-Porter Act WRD General Obligation Bonds debt service were \$497,359 with payments through 2025. Principal and interest paid for 2011 were \$76,436 and Burns-Porter Act WRD Water supply operating revenues were \$564,520.

WRD General Obligation Bonds of \$168 million are authorized but un-issued as of June 30, 2012 and 2011, and may only be used for additional facilities, meeting certain requirements of the Burns-Porter Act.

WRD General Obligation Bonds Series A through Series S may be called at any time for early redemption. WRD General Obligation Bonds Series W through Series Y do not have early redemption provisions.

# State Water Resources Development System

## Notes to Financial Statements

For the years ended June 30, 2012 and 2011

(in thousands)

WRD General Obligation Bonds consist of the following at June 30:

Fiscal Year of Issue	Series	Fixed Rates	Fiscal Year of Final Maturity	Amounts Outstanding	
				2012	2011
1964	A	0.1-3.6%	2014	\$ 8,000	\$ 12,000
1964	B&C	0.05-3.7%	2015	16,000	22,000
1965	D&E	3.0-3.8%	2016	30,500	38,600
1966	F&G	3.5-4.1%	2017	42,600	50,400
1967	H,J&K	3.0-4.8%	2018	71,700	83,000
1968	L&M	4.0-4.9%	2019	57,800	65,000
1970	N&P	5.0-5.8%	2020	65,000	72,000
1971	Q&R	4.8-5.2%	2021	54,000	58,950
1972	S	5.3-5.5%	2022	15,720	17,000
1991	W	10.0%	2012	-	450
1993	X	4.80%	2024	600	650
1994	Y	7.0-7.1%	2025	455	490
Total General Obligation bond debt outstanding at par				362,375	420,540
Less current maturities				(59,455)	(58,165)
Total Long term General Obligation bond debt outstanding				<u>\$ 302,920</u>	<u>\$ 362,375</u>

### Revenue Bonds

The Central Valley Project Water System (CVP) Revenue Bonds have been issued for the acquisition or construction of projects to provide water and power for the SWP. Under the statute pursuant to which CVP Revenue Bonds are issued, principal of and interest on the bonds are secured by and payable solely from revenues attributable to the facilities financed by the bonds, primarily certain payments under the water supply contracts between the System and Water Contractors.

As of June 30, 2012, the amount of the revenues pledged to repay the (CVP) Revenue Bonds debt service is \$3,441,169 with payments through 2036. Principal and interest paid for the current year were \$229,011 and Central Valley Project Act water supply operating revenues were \$307,438. As of June 30, 2011, the amount of the revenues pledged to repay the (CVP) Revenue Bonds debt service were \$3,541,604 with payments through 2036. Principal and Interest paid for the year were \$228,511 and Central Valley Project Act Water Supply operating revenues were \$320,631.

The System is subject to certain bond covenants, the most restrictive of which requires that the revenues in each year shall be at least equal to 1.25 times the debt service payable from revenues on all bonds outstanding in such year, plus operating costs, and the required funding of a debt service reserve account. The bonds are limited special obligations of the System; neither the principal nor any interest thereon constitutes a debt of the State. Certain of the bonds are redeemable prior to maturity at a redemption price of 100%.

**State Water Resources Development System**  
**Notes to Financial Statements**  
**For the years ended June 30, 2012 and 2011**

**(in thousands)**

CVP Revenue Bonds consist of the following at June 30:

Fiscal Year of Issue	Series	Fixed Rates	Fiscal Year of Final Maturity	Fiscal Year of First Call Date	Amounts Outstanding	
					2012	2011
Devil Canyon-Castaic Facilities:						
1973	A&B	5.3-5.4%	2023	1983	\$ 72,945	\$ 77,540
CVP Water System:						
1992	J	7.0%	2013	2001	27,720	53,535
1999	V	6.3%	2025	None	20,235	20,235
2001	W	5.5%	2015	2012	48,845	153,365
2002	X	4.2-5.5%	2030	2013	119,290	122,550
2003	Y	5.0-5.3%	2026	2013	160,305	251,975
2003	Z	3.3-5.0%	2020	2013	82,550	110,525
2003	AA	5.0%	2024	2013	69,630	107,215
2005	AC	3.3-5.0%	2030	2015	222,110	262,470
2006	AD	3.3-5.0%	2030	2015	107,515	109,520
2008	AE	3.0-5.0%	2030	2018	577,790	595,565
2009	AF	2.0-5.0%	2033	2019	221,860	248,920
2010	AG	3.0-5.0%	2033	2020	168,800	169,115
2011	AH	3.0-5.3%	2036	2021	97,675	97,675
2012	AI	5.0%	2030	2022	92,275	-
2012	AJ	3.0-5.0%	2036	2022	216,930	-
2012	AK	2.0-5.0%	2036	2022	36,370	-
Total revenue bond debt outstanding at par					2,342,845	2,380,205
Net Unamortized bond issuance premiums/discounts					144,892	111,649
Net Deferred amount on refunding					(60,381)	(29,260)
Current fiscal maturities					(124,155)	(116,150)
Total long term bond debt outstanding					<u>\$2,303,201</u>	<u>\$2,346,444</u>

# State Water Resources Development System

## Notes to Financial Statements

For the years ended June 30, 2012 and 2011

(in thousands)

### Future Debt Service Requirements

Future principal and interest payment requirements on the bonds are as follows at June 30, 2012:

Year	General Obligation Bonds		Revenue Bonds		Total
	Principal	Interest	Principal	Interest	
2013	\$ 59,455	\$ 15,008	\$ 124,155	\$ 112,714	\$ 311,332
2014	61,085	12,503	118,430	106,778	298,796
2015	56,875	10,098	115,710	101,291	283,974
2016	49,915	7,742	120,715	95,611	273,983
2017	46,745	5,661	126,770	89,577	268,753
2018-2022	88,095	8,228	648,025	353,381	1,097,729
2023-2027	205	16	637,250	189,615	827,086
2028-2032	-	-	406,570	44,793	451,363
2033-2036	-	-	45,220	4,564	49,784
	<u>\$ 362,375</u>	<u>\$ 59,256</u>	<u>\$ 2,342,845</u>	<u>\$ 1,098,324</u>	<u>\$ 3,862,800</u>

### Pooled Money Investment Loan (PMIA)

The System applied for and received a loan from the Pooled Money Investment Account pursuant to Government Code section 16313 for \$29.6 million. The proceeds of the loan were used to establish escrow accounts that defeased certain Water System Revenue Bonds that financed recreation, fish, and wildlife enhancement related cost of the acquisition and construction of the System. The loan is to be repaid with surplus revenues of the System made available under Water Code section 12937(b)(4). DWR executed the Pooled Money Investment Board Loan on March 26, 2008. The loan agreement requires minimum quarterly payments of \$1 million on the first day of every March, June, September and December; the first payment was made on September 1, 2008. Interest is computed on the unpaid principal balance of the loan at the Variable Rate on the basis of a 360-day year or twelve 30-day months and the number of days elapsed. The Variable Rate means (a) for the period from the date of the Loan Agreement, March 26, 2008, through and including the day before the first Reset Date (March 25, 2009), five percent per annum, and (b) for each Renewal Period thereafter, the greater of (i) five percent per annum, or (ii) the last available daily rate of return by the PMIA on the day before the Reset Date on which such Renewal Period commences.

# State Water Resources Development System

## Notes to Financial Statements

For the years ended June 30, 2012 and 2011

(in thousands)

The minimum future principal and interest payment requirements on the PMIA loan are as follows at June 30, 2012:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2013	\$ 3,156	\$ 844	\$ 4,000
2014	3,317	683	4,000
2015	3,486	514	4,000
2016	3,663	337	4,000
2017	3,850	150	4,000
2018	580	7	587
	<u>\$ 18,052</u>	<u>\$ 2,535</u>	<u>\$ 20,587</u>

### Commercial Paper Notes

The System has a commercial paper borrowing program of up to \$139,668. Under this program, the System may issue commercial paper at prevailing interest rates for periods of not more than 270 days from the date of issuance. To provide liquidity for the programs, the System entered into a revolving credit agreement with a commercial bank equal to the authorized amount of commercial paper. Under the credit agreement dated October 1, 2011, the bank has agreed to make advances to the System if necessary, to provide moneys for the payment of the commercial paper notes. The bank is obligated to provide \$150,000 with the principal amount of commercial paper notes limited to \$139,668 and \$10,332 of accrued interest, calculated for sizing purposes at 10% per annum for 270 days on a maximum principal commitment of \$139,668. The Line of Credit is scheduled to expire on October 24, 2014 but can be extended for up to three years upon written request and approval of the bank. The credit agreement requires quarterly payments the first day of July and October and on the last day of December and March. As of June 30, 2012, there were no borrowings with the bank under the credit agreement. At June 30, 2012 and 2011, there were commercial paper borrowings of \$28,783 and \$54,578, respectively, outstanding under this program. The weighted average for interest expense approximated 0.18% and 0.31% for the years ended June 30, 2012, and 2011, respectively. The proceeds from the issuance of commercial paper are restricted to construction costs of certain State water projects, reimbursements of construction costs of certain State water projects, and interest and issuance costs of the commercial paper notes. The liability has been classified as long-term as it is the System's policy to redeem the commercial paper outstanding with the issuance of CVP Revenue Bonds. The System's obligation to make debt service payments on the commercial paper notes is subordinate to its payment obligations under the resolutions for the CVP Revenue Bonds and WRD General Obligation Bonds.

The water supply contracts in their original form provide for two charges to the Water Contractors: (a) a Delta Water Charge and (b) a Transportation Charge. These charges are computed so as to return to the State the costs of the facilities necessary to deliver water to the Water Contractors, including capital costs (with interest) and operation and maintenance costs, and expressly including in the case of the facilities to be financed with commercial paper and the related Water System Revenue Bonds, debt service and 1.25 debt service coverage requirements to be satisfied from revenues. DWR expects to redeem its commercial paper liability with proceeds of the additional commercial paper draws until

# State Water Resources Development System

## Notes to Financial Statements

For the years ended June 30, 2012 and 2011

(in thousands)

DWR issues Water System Revenue Bonds to provide permanent financing for those Water System Projects financed with commercial paper.

### 7. Bond Refundings and Defeasances

The System has issued CVP Water System Revenue Refunding Bonds to refund various issues of CVP Water System Revenue Bonds previously issued. The net proceeds from these sales were used to purchase State and Local Government Series Securities (SLGS) and U.S. Treasury securities that were deposited in irrevocable escrow trust accounts with an escrow agent as an independent fiscal agent to provide for all future debt service on the bonds being refunded. As a result, those bonds are considered to be defeased and the related liabilities have been excluded from the System's basic financial statements. At June 30, 2012 and 2011, outstanding CVP Water System Revenue Bonds of \$58,705 and \$83,250, respectively, are considered to be defeased.

Refunding and defeasance transactions during fiscal 2012 were as follows:

- On September 7, 2011, the System issued \$92,275 of CVP Water System Revenue Bonds Series AI with an average yield on the bonds of 3.06% to refund \$103,200 of CVP Water System Revenue Bonds Series W. The bond proceeds of \$92,275 and \$12,549, par and premium respectively along with System funds on hand in the amount of \$1,806 were used to refund \$103,200 of bonds, fund \$2,742 of future interest on the defeased bonds, and cover costs of issuance of \$688.
- On October 13, 2011, the System issued \$216,930 of CVP Water System Revenue Bonds Series AJ with an average yield on the bonds of 3.13% to retire \$2,850 of CVP Water System Revenue Bonds Series X, \$74,495 of CVP Water System Revenue Bonds Series Y, \$6,730 of CVP Water System Revenue Bonds Series Z, \$37,585 of CVP Water System Revenue Bonds Series AA, \$32,010 of CVP Water System Revenue Bonds Series AC, and \$1,560 of CVP Water System Revenue Bonds Series AD. The System caused an Invitation to Tender Bonds, dated September 14, 2011, to be distributed to the holders of the Refunded Bonds (the "Solicitation") and pursuant to the Solicitation, the System purchased the Refunded Bonds to achieve debt service savings. The respective purchase prices for the Refunded Bonds the System elected to purchase were determined pursuant to the terms of the Solicitation and such purchase prices were paid from proceeds of the Series AJ Bonds on October 14, 2011. Upon purchase, the Refunded Bonds were promptly surrendered to the State Treasurer for cancellation in accordance with the CVP Water System Revenue Bonds General Bond Resolution. The bond proceeds of \$216,930 and \$30,448, par and premium respectively along with System funds on hand in the amount of \$3,122 were used to retire \$155,230 of bonds, fund \$18,958 for redemption premium and accrued interest on the retired bonds, redeem commercial paper borrowings of \$69,322, fund capitalized interest of \$3,719, fund deposits to the debt service reserve account of \$1,641, and cover costs of issuance of \$1,630.
- On March 13, 2012, the System issued \$36,370 of CVP Water System Revenue Bonds Series AK with an average yield on the bonds of 3.05% to refund \$410 of



# State Water Resources Development System

## Notes to Financial Statements

For the years ended June 30, 2012 and 2011

(in thousands)

CVP Water System Revenue Bonds Series X, and \$7,945 of CVP Water System Revenue Bonds Series AC. The bond proceeds of \$36,370 and \$6,678, par and premium respectively, along with System funds on hand in the amount of \$125 were used to refund \$8,355 of bonds, fund \$1,131 of future interest on the defeased bonds, redeem commercial paper borrowings of \$32,035, fund capitalized interest of \$903, fund deposits to the debt service reserve account of \$451, and cover costs of issuance of \$298.

Refunding and defeasance transactions during fiscal 2011 were as follows:

- On November 9, 2010, the System issued \$97,675 of CVP Water System Revenue Bonds Series AH with an average yield on the bonds of 3.33% to advance refund \$2,905 of CVP Water System Revenue Bonds Series W, to refund \$22,630 of CVP Water System Revenue Bonds Series X, to refund \$4,250 of CVP Water System Revenue Bonds Series AC. The bond proceeds of \$97,675 and \$13,378, par and premium respectively, along with System funds on hand in the amount of \$684 were used to refund \$29,785 of bonds, fund \$3,641 of future interest on the defeased bonds, redeem commercial paper borrowings of \$71,538, fund capitalized interest of \$3,630, fund deposits to the debt service reserve account of \$2,525, and cover costs of issuance of \$618.

These refundings and defeasances were accomplished to take advantage of lower interest rates. The transactions resulted in cash flow savings of \$34,049 and \$2,276 and economic gains (difference between the present values of the debt service payments on the old debt and new debt) of \$25,480 and \$1,984 for fiscal years 2012 and 2011, respectively. The difference between the book value of the old debt and the amount required to retire the debt is deferred and amortized over the original remaining life of the old debt or the life of the new debt, whichever is less. Bonds payable are reported net of these deferred costs. In fiscal years 2012 and 2011, approximately \$35,647 and \$4,809 of cost were deferred. Amortization of all deferred refunding costs was approximately \$4,526 and \$1,633 in fiscal years 2012 and 2011, respectively.

## 8. Retirement Plan

### Plan Description

The State is a member of the California Public Employees' Retirement System (PERS), an agent multiple-employer pension system which provides a contributory defined-benefit pension for substantially all State employees. The System is included in the State Miscellaneous Category (Tier 1 and Tier 2) within PERS. PERS functions as an investment and administrative agent for participating public agencies within the State of California. Departments and agencies within the State of California, including the System, are in a cost-sharing arrangement in which all risks and costs are shared proportionately by participating State agencies. Copies of PERS' comprehensive annual financial report may be obtained from their executive office at 400 P Street, Sacramento, California 95814.

The pension plan provides retirement benefits, survivor benefits, and death and disability benefits based upon employee's years of credited service, age and final compensation. Vesting occurs after five years of credited service except for second tier benefits, which require ten years of credited service. Employees who retire at or after age 50 with five or

# State Water Resources Development System

## Notes to Financial Statements

For the years ended June 30, 2012 and 2011

(in thousands)

more years of service are entitled to a retirement benefit, payable monthly for the remainder of their lives. Several survivor benefit options that reduce a retiree's unmodified benefit are available. Benefit provisions and all other requirements are established by State statute.

### **Funding Policy**

Active members who participate in Social Security under the State Miscellaneous Tier 1 category are required to contribute 5% of their annual covered salary after excluding the first \$513 of gross monthly pay. Active members who do not participate in Social Security under the State Miscellaneous Tier 1 category are required to contribute 6% of their annual covered salary after excluding the first \$317 of gross monthly pay. Active members who participate in Social Security under the State Miscellaneous Tier 2 category are not required to make contributions to PERS.

The System is required to contribute the actuarially determined remaining amounts necessary to fund the benefits for its members. The actuarial methods and assumptions used are those adopted by the PERS Board of Administration. The required employer contribution rate for the fiscal year ended June 30, 2012, were 18.175% and 17.025% for State Miscellaneous Tiers 1 and 2 respectively. For the fiscal year ended June 30, 2011, the required employer contribution rate for Tiers 1 and 2 were 17.528% and 16.442% respectively. The contribution requirements of the plan members are established by State statute and the employer contribution rate is established and may be amended by PERS.

### **Annual Pension Cost**

For the years ended June 30, 2012 and 2011, the System's annual pension cost and actual contribution amounted to approximately \$25 million and \$23 million, respectively. Annual covered payroll is not available for the System. However the actuarially determined contributions for the years ended June 30, 2012 and 2011, approximated 1.3% and 1.1%, respectively, of the total actuarially determined contribution requirements for the State Miscellaneous Category and approximately 15.84% and 16.12%, respectively, of the total System payroll. The required contribution for the year ended June 30, 2012 was determined as part of the June 30, 2010, actuarial valuation using the entry age normal actuarial cost method with the contributions determined as a percentage of covered payroll. Likewise, the required contribution for the year ended June 30, 2011 was determined as part of the June 30, 2009, actuarial valuation.

Trend information for the last three years regarding the System's required contributions and the percentage contributed, is as follows:

# State Water Resources Development System

## Notes to Financial Statements

For the years ended June 30, 2012 and 2011

(in thousands)

### Three-year Trend Information

Year Ended June 30,	Required Contribution	Percentage of Required Contribution Contributed
2010	\$ 18,384	100%
2011	23,013	100%
2012	24,895	100%

### 9. Postemployment Benefits Other Than Pensions

The State provides health care and dental benefits to annuitants of the retirement systems to which the State contributes as an employer. To be eligible for these benefits, first-tier plan annuitants must retire on or after age 50 with at least five years of service, and second-tier plan annuitants must retire on or after attaining age 55 with at least 10 years of service. In addition, annuitants must retire within 120 days of separation from employment to be eligible to receive these benefits. In accordance with the California Government Code, the State generally pays 100% of the health insurance cost for annuitants, plus 90% of the additional premium required for the enrollment of family members of annuitants. Although the California Government Code does not specify the State's contribution toward dental insurance costs, the State generally pays all or a portion of the dental insurance cost for annuitants, depending upon the completed years of credited state service at retirement and the dental coverage selected by the annuitant. The System participates in the State's plan on a cost sharing basis. The System recognizes the costs of providing health and dental insurance to annuitants based on the required contribution, which is actuarially determined, and is funded on a pay-as-you-go basis.

The System's required contributions and resulting net OPEB obligation is as follows:

	2012	2011
Annual required contribution (ARC)	\$ 30,732	\$ 41,382
Interest on net OPEB obligation	2,922	3,248
Adjustment to the ARC	(2,563)	(2,849)
Annual OPEB cost	31,091	41,781
Contributions made	(11,065)	(15,331)
Increase in net OPEB obligation	20,026	26,450
Net OPEB obligation - beginning of year	97,898	71,448
Net OPEB obligation - end of year	\$ 117,924	\$ 97,898

The System's annual required contribution, percentage of the ARC contributed to the plan, and the net OPEB obligation for the fiscal year ended June 30, 2012, 2011 and 2010, were as follows:

# State Water Resources Development System

## Notes to Financial Statements

For the years ended June 30, 2012 and 2011

(in thousands)

<u>Fiscal Year Ended</u>	<u>Annual Required Contribution</u>	<u>Percentage of ARC Contributed</u>	<u>Net OPEB Obligation</u>
6/30/2010	\$35,525	34%	\$71,448
6/30/2011	41,382	37%	97,898
6/30/2012	31,091	36%	117,924

The annual OPEB cost (AOC) recorded by the System is calculated by the State and represents an allocation of the total ARC of the State, adjusted for interest and other adjustments. The allocation of retiree health benefit costs is based on the number of active employees funded by the System in relation to the total Department retiree health benefits costs.

The actuarial valuation report for OPEB may be obtained by writing to the Office of State Controller John Chiang, P.O. Box 942850, Sacramento, CA 94250 or by visiting the State Controller's Web site at [www.SCO.ca.gov](http://www.SCO.ca.gov). The System's ARC, AOC and Net OPEB obligation will be calculated and adjusted for on an annual basis.

## 10. Commitments and Contingencies

### Commitments

#### *Construction*

The System has entered into long-term construction contract commitments for the State Water Project facilities. The remaining value of contracts in process as of June 30, 2012 and June 30, 2011, approximated \$65,544 and \$62,532, respectively.

#### *Power Transmission and Purchase*

The System has long-term power transmission service contracts requiring future payments of approximately \$235,630 over periods ranging from one to 30 years. Payments made under these contracts approximated \$16,984 and \$14,885 for the years ended June 30, 2012 and 2011, respectively.

The System has also entered into long-term power purchase contracts requiring future payments of approximately \$297,976 over periods ranging from one to 30 years. Payments made under these contracts, excluding payments to the Kings River Conservation District (District) to cover debt service, approximated \$48,051 and \$26,706 for the years ended June 30, 2012 and 2011, respectively.

The remaining amounts of fixed obligations under the long-term power purchase and transmission contracts as of June 30, 2012, are as follows:

# State Water Resources Development System

## Notes to Financial Statements

For the years ended June 30, 2012 and 2011

(in thousands)

<u>For the year ended</u>	<u>Fixed Obligations</u>
2013	\$ 73,739
2014	66,856
2015	59,269
2016	18,959
2017	18,959
2018 - 2042	295,824
	<u>\$ 533,606</u>

The System has a contract with the District that provides that the System receive all power generated by the Pine Flat Power Plant Project (Project). Under the contract, the System is obligated to pay fixed amounts each year to cover the debt service on bonds issued by the District to build the Project, operations and maintenance expenses, and a charge for power supplied. Such payments are to be made until all of the bonds issued by the District to finance the Project have been retired in 2019. Payments to the District totaled approximately \$14,500 and \$14,212 during the years ended June 30, 2012 and 2011, respectively.

The amounts of fixed obligations of the System related to future principal and interest payments of the District's bonds as of June 30, 2012 are as follows:

<u>For the year ended</u>	<u>Fixed Obligations</u>
2013	\$ 4,310
2014	4,302
2015	4,272
2016	4,270
2017	4,253
2018 - 2019	8,496
	<u>\$ 29,903</u>

DWR entered into a Power Sales Agreement with the Northern California Power Agency (NCPA) and other project participants on May 24, 2010 to participate in the Lodi Energy Center Project (LEC Project), which consists of a 296 megawatt natural gas-fired combined cycle power plant constructed by NCPA in Lodi, California. The terms of the agreement provide that DWR will receive 33.5 percent of the output of the LEC Project and purchase power on a long term basis. Participation in the LEC Project will assist DWR in meeting future State Water Project energy requirements, including the replacement of energy currently provided by the Reid Gardner Project. NCPA issued revenue bonds on June 24, 2010 for the DWR's share of construction costs. Construction of the LEC Project commenced in early August 2010 with Commercial Operation currently scheduled for late October 2012. DWR anticipates that the LEC will be one of the most efficient thermal generating units in California and that it will be economically dispatched before other gas-fired units, resulting in power revenues that are sufficient to cover the operational costs and a portion of DWR's debt service on the bonds.

# State Water Resources Development System

## Notes to Financial Statements

For the years ended June 30, 2012 and 2011

(in thousands)

The amounts of fixed obligations of the System related to future principal and interest payments of the LEC's bonds as of June 30, 2012 are as follows:

<u>For the year ended</u>	<u>Fixed Obligations</u>
2013	\$ 6,173
2014	9,131
2015	9,207
2016	9,209
2017	9,206
2018 - 2022	46,041
2022 - 2027	46,043
2027 - 2032	46,037
2032 - 2035	27,625
	<u>\$ 208,672</u>

Market value information for certain power purchase, sale and exchange contracts are disclosed at June 30, 2012, using forward market prices discounted at the prevailing risk-free interest rate. All five sales contracts extending beyond June 30, 2012 expire in Fiscal Year 2013. There are twenty-one purchase contracts that will expire in Fiscal Year 2013, three purchase contracts will expire in Fiscal Year 2014, two purchase contracts will expire in Fiscal Year 2015, and two will expire in Fiscal Year 2016. The long-term energy purchase contracts involve energy delivered from the Reid Gardner and Pine Flat Power Plants which expire in 2013 and 2037, respectively, and a contract with Metropolitan Water District of Southern California (Metropolitan), one of the Water Contractors, which expires in 2019. An agreement with the Northern California Power Agency (NCPA), operator of the Lodi Energy Center (LEC) which commits DWR to purchase power on a long term basis subject to the agreement, has no explicit termination date. The fair value of power purchases and sales commitments extending beyond June 30, 2012 are as follows:

	<u>Number of Contracts</u>	<u>Total Capacity (MWh)</u>	<u>Fair Value at June 30, 2012</u>
Energy sales	5	125	\$ (493)
Energy purchases	28	950	(6,411)
Long-term energy purchases	4	543.8	252
<b>Total</b>			<u>\$ (6,652)</u>

The System suspended the natural gas hedging program. Previously the System entered into transactions to hedge the price of natural gas through bilateral arrangements, but has terminated and settled all contracts effectively as of June 30, 2010. The System did not enter into any transactions during fiscal year 2011-12. During fiscal year 2010-11, the System transferred the balance of \$15.8 million that remained from the deposit back to the State Treasury, leaving a minimal balance with the brokerage firm. During fiscal year 2011-12, the System returned the remaining deposit of \$9.8 million plus accrued interest to the

# State Water Resources Development System

## Notes to Financial Statements

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Water Contractors. The System did not recognize a loss in fiscal year 2012 and recognized a loss of \$4.9 million in fiscal year 2011.

### Contingencies

#### Litigation and Claims

##### *Monterey Amendment*

In 1994, the System and certain Water Contractors adopted a set of principles pursuant to which additional amendments to the water supply contracts have since been negotiated (Monterey Amendment). The Monterey Amendment includes provisions related to the transfer of land and related assets, known as the Kern Water Bank, to the Kern County Water Agency (KCWA) (one of the Water Contractors), the operation of certain System reservoirs, transfers of water allocations between contractors, establishment of certain operating reserves, and the revision of calculating certain Water Contractor billings. The Monterey Amendment has been executed by the System and 27 of the 29 Water Contractors, who receive approximately 99% of water delivered annually and who pay approximately 99% of annual water supply revenue. Certain parties have disputed the Monterey Amendment by challenging the validity of the related environmental impact report (EIR). While the courts have allowed the System to proceed with the implementation of the Monterey Amendment, the System was required to prepare a new EIR. DWR completed the new Final EIR in February 2010 and filed its Notice of Determination in May 2010. In June 2010, two Delta water agencies and several environmental organizations and individuals filed a lawsuit in Sacramento Superior Court challenging DWR's California Environmental Quality Act (CEQA) compliance and the validity of the Monterey Amendment, including DWR's transfer of the Kern Fan Element to the KCWA. In July 2010, the same plaintiffs in the Sacramento Superior Court case filed a lawsuit in Kern County Superior Court challenging the transfer of the Kern Fan Element from KCWA to the Kern Water Bank Authority, a local joint powers agency which now has responsibility for the management of the Kern Fan Element and Kern Water Bank. In addition, in June 2010, two water districts in Kern County filed a separate lawsuit in Kern County Superior Court, primarily challenging DWR's CEQA compliance with respect to the Kern Fan Element transfer from DWR to KCWA. The two lawsuits filed in Kern County Superior Court have been transferred to the Sacramento Superior Court. All three cases are in the pre-trial stage. The System, however, does not believe that there would be any material adverse impact on the System's financial position or results from operations, even if these lawsuits are successful.

##### *2005 Contractor Lawsuit Regarding Oroville Power Credits*

In April, 2005 the Kern County Water Agency and thirteen other Water Contractors filed a lawsuit against the System in Sacramento County Superior Court for declaratory relief and breach of contract. The complaint alleges that pursuant to the water supply contracts, the System is required, but failed, to credit all revenues from power generated by certain project conservation facilities (primarily the Hyatt-Thermalito Power Plants) to the Delta Water charge in the Water Contractor billings, and, as a result, was overcharging the Water Contractor plaintiffs. The complaint seeks a declaration that all "benefits" derived from the sale or other disposal of power from project conservation facilities be credited "in conformity with the terms of the water supply contracts," along with damages and costs in an

# State Water Resources Development System

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unspecified amount. The Metropolitan Water District of Southern California and entities representing 12 other southern Water Contractors received court permission in December, 2005 to intervene in the lawsuit as defendants. Plaintiffs thereafter filed an amended complaint joining two additional contractors. A non-jury trial was held in November and December 2008. In October 2009, the Court issued its decision in favor of DWR and the Water Contractors which intervened in support of DWR, finding that DWR's determinations and administration of the provisions regarding Oroville power credits were consistent with the water supply contracts. In May 2010, the Superior Court entered its judgment in favor of DWR and in July 2010, the Water Contractor plaintiffs appealed the lower court's decision to the Court of Appeal, but no hearing date has been set. If the Water Contractor plaintiffs are ultimately successful in their efforts to reverse the Superior Court's decision, DWR believes certain Water Contractors would pay more to the System under the Water Supply Contracts, while others would pay less and that this cost shifting would not materially adversely impact the System's financial position or results from operations.

### *Other Claims by Water Contractors, Including Claims Concerning Charges for Recreation and Fish and Wildlife Enhancement*

In accordance with the water supply contracts, in December 2005, 27 Water Contractors and entities representing Water Contractors filed "Notices of Contest" with the System challenging the accuracy of various charges in the System's billings. One Water Contractor also filed a claim based on its Notice of Contest with the Victim Compensation and Government Claims Board. The System has been reviewing these Notices of Contest and investigating the items raised.

One item that has been determined to have merit, contested the System's practice of charging the Water Contractors for certain financing costs of the recreation and fish and wildlife enhancement portion of facilities financed with Water System Revenue Bonds. The System rectified the situation by restating past bills to provide appropriate credits back to the Water Contractors for the contested charges and taking other actions to pay for the costs of the recreation and fish and wildlife enhancement portion of System facilities with sources other than direct charges to the Water Contractors. Such actions included obtaining a loan from the State Pooled Money Investment Account (PMIA) in the amount of \$29.6 million, which was used together with certain other available funds to retire or provide for the defeasance of approximately \$28.2 million principal amount of revenue bonds and commercial paper notes, the proceeds of which had been used to pay costs allocated by the System to the development of recreation or fish and wildlife enhancement. The System has agreed to pay a minimum of \$4 million per year to repay the PMIA loan.

With the receipt of the PMIA loan and the waivers in the 2007 and 2008 Tolling and Waiver Agreement obtained from the 27 Water Contractors who signed the Monterey Amendment, the System sold revenue bonds in May 2008. The sale of System revenue bonds had been suspended pending the resolution of the recreation and fish and wildlife enhancement issue.

In addition to waivers included in the 2007 and 2008 Tolling and Waiver Agreements, which helped to facilitate the resumption of the sale of System revenue bonds, the Tolling and Waiver Agreements, as amended, also tolled (i.e. suspended) until December 31, 2012 the running of the time period and statute of limitations for filing by the Water Contractors of (1) protests regarding the System's bills to the Water Contractors for the years 2007 through 2013, (2) claims arising from the System's revisions to prior year invoices that were made to



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adjust for improper charges to the Water Contractors for recreation and fish and wildlife enhancement costs, and (3) certain other specified claims. The Tolling and Waiver Agreement also tolled the running of the time period for bringing an action on the Victim Compensation and Government Claims Board claim regarding the 2006 invoice that was filed by one of the Water Contractors. In the meantime, the System and Water Contractors are continuing their efforts to resolve issues that are covered by the Tolling and Waiver Agreement. However, no assurance can be given that the Water Contractors will not file additional Notices of Contest, claims and/or lawsuits with respect to the issues under discussion once the Tolling and Waiver Agreements expire.

### *Lawsuits Regarding 2004 Delta Levee Failure*

Four lawsuits have been filed to recover damages caused when a Delta levee failed and flooded the Upper Jones Tract and Lower Jones Tract in June 2004. Three of the lawsuits name as defendants a local Delta reclamation district, the State Reclamation Board and the DWR. A cause of action in each of these three lawsuits alleges that the System's operations and activities in the Delta were a cause of the damage. All four lawsuits were consolidated for trial, although the fourth lawsuit does not involve DWR or any other state agency. Upon completion of the trial, the judge issued a decision in August 2012 in favor of DWR. All the plaintiffs, except for two insurance companies, have appealed the decision. The System does not believe that an adverse court decision in any of these consolidated cases would have a material adverse impact on the System's finances or operations because such costs would be recoverable under the long-term water supply contracts.

### *General*

The System, during the ordinary course of its operations, has been named in a number of additional suits and claims, several of which are still pending.

In the opinions of management and the System's legal counsel, such legal actions will not have a material effect on the System's financial position or results from operations. If incurred, such costs would be recoverable from project beneficiaries under the long-term water supply contracts.

### **Federal Energy Regulatory Commission Proceedings**

There are a number of proceedings pending before the Federal Energy Regulatory Commission (FERC) that may impact the cost of System operations. Some of these proceedings address requests from the California Independent System Operator, investor-owned utilities, and others to increase or adjust rates or allocate responsibility for costs for transmission and other services provided to the System and other entities in California. The System is participating in these proceedings, since the outcome of these proceedings has the potential to increase the System's annual power costs. However, the System does not believe that any increased charges arising from these proceedings will materially impact the System's financial position or results from operations. Any increased charges will be passed through to the Water Contractors under the water supply contracts in the form of higher operations charges.

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### Claims for Partial Energy Purchase Refunds

FERC proceedings have also been instituted to address power purchaser requests for partial refunds from sellers of energy and related services in 2000 and 2001, including the System. However, in September 2005, the United States Ninth Circuit Court of Appeals ruled that FERC lacked jurisdiction under the Federal Power Act to order governmental entities, such as the System, to provide refunds in these types of proceedings. As a result of this Ninth Circuit Court of Appeals' ruling, a group of California entities filed similar claims for partial energy purchase refunds with the California Victim Compensation and Government Claims Board (Claims Board) against the governmental entity sellers, including the System. The claims were denied by the Claims Board in April, 2006, which allows the claimants to file lawsuits against the governmental entity sellers, including the System. However, DWR and a group of California entities have agreed to suspend the running of the statute of limitations for the filing of a lawsuit through February 28, 2013. The System believes that amounts, if any, that the System might be required to refund as a result of these claims would not have a material impact on the System's financial position or results from operations because the impact of any refunds would be passed through to the Water Contractors under the water supply contracts in the form of higher operating charges.

### Pollution Remediation

#### Reid Gardner Power Plant

The Reid Gardner (R-G) Power Plant, located near Moapa, Nevada, is operated by Nevada Energy (NVE) and consists of four coal-powered generators—Units 1 through 4. Units 1–3 are 100% owned by NVE, whereas the capital ownership of Unit 4 is shared between the DWR and NVE at 67.8% and 32.2%, respectively. Additionally, DWR has a 29.2% share of the R-G facilities necessary for and common to all four units.

In February 2008, NVE entered into an Administrative Order on Consent (AOC) with the Nevada Division of Environmental Protection (NDEP). Pursuant to the AOC, NVE agreed to undertake investigatory activities into various potential areas of contamination at R-G and also to ultimately remediate groundwater and other contamination attributable to the R-G facility. Groundwater and soils have been affected by certain chemicals of interest associated with flue gas desulfurization effluent settlement and evaporation ponds. Since some of this contamination can be associated with the Unit 4 generation related facilities such as the evaporation ponds, DWR, as co-owner of Unit 4, has voluntarily commenced participation in NVE's investigatory activities which will ultimately lead to the remediation measures prescribed by NDEP to NVE. These activities are projected to continue through at least 2023.

Based on a review of NVE's ongoing and planned investigations and overall AOC planning activities, it is estimated that DWR's equitable share of the current value of outlays could range between \$6 million and \$12.0 million; a quantitative estimate of the ultimate investigatory and remediation cost is difficult at this time as baseline conditions are still being assessed by NDEP. DWR's current estimate is based upon a quantitative assessment of constituents of concern currently known to DWR applied to a range of potential and applicable remediation strategies. DWR calculated the potential financial liability by estimating a reasonable range of potential outlays and applying an estimated probability of occurrence to the potential outlays, yielding a current total expected liability of \$9.42 million.

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The System expended approximately \$175 in FY 2011/2012 and DWR expects to pay \$1.4 million of the total estimated liability during FY 2012/2013. The total remediation outlay estimate is expected to be refined, and adjusted accordingly, as additional site assessment and final remediation disposition information is available to DWR.

### Delta Basin Plan: Mercury Control Program

In June 2011, the State Water Resources Control Board adopted an amendment to the Sacramento-San Joaquin Delta Basin Plan regarding the control in the Delta of methylmercury. The amendment, among other things, assigns certain responsibilities jointly to DWR (with regard to both the System and DWR's flood management programs), the Central Valley Flood Protection Board and the State Lands Commission to reduce methylmercury in the open waters of the Delta. In addition, DWR and others are assigned certain responsibilities regarding the discharge of methylmercury from wetland and other aquatic restoration and enhancement projects. The required actions are divided into two phases. Phase I, which lasts for up to nine years until June 2020, emphasizes studies and pilot projects to control methylmercury, along with some implementation, and Phase II requires implementation of measures to achieve required methylmercury levels by 2030. In July 2011, an organization representing twenty-seven System Water Contractors filed a lawsuit against the State Water Resources Control Board and the Central Valley Regional Water Quality Control Board challenging the portion of the Basin Plan amendment that requires DWR in its capacity as operator of the System to reduce methylmercury in the open waters of the Delta. DWR was named as a real party in interest in the lawsuit. The Contractors contend that since the System's water management activities do not add or introduce methylmercury into the Delta, there is no basis in law for assigning responsibility to the System to reduce the methylmercury that is present in the open waters of the Delta.

The System expended approximately \$213 in fiscal year 2011-2012 and DWR estimates that the System may incur up to about \$600 in fiscal year 2012-2013 and \$900 in fiscal year 2013-2014 on Phase I activities. The ultimate amount to be expended by the System will depend, among other things, upon the results of the Phase I studies and pilot projects, the outcome of the Water Contractors lawsuit challenging the inclusion of the System in the assignment of responsibility for reducing methylmercury in the open waters of the Delta and the distribution of costs among the parties ultimately determined to be responsible.

## 11. Self-Insurance

The System is self-insured for all completed facilities of the SWP other than a portion of the Reid Gardner Project. The System is also self-insured for workers' compensation, general liability and other risks. All workers' compensation claims and other losses are on a "pay-as-you-go" basis. The long-term water supply contracts provide for recovery of such losses from the Water Contractors. Additionally, the CVP Act and the related bond resolutions authorize the issuance of additional bonds, payable from available revenues or federal reimbursements under the National Disaster Act, for the purpose of providing funds for emergency repairs to power projects or water system projects necessitated by natural disasters, provided that certain conditions are met.

# State Water Resources Development System

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### 12. Economic Dependency

The System's water supply revenue is derived from 29 Water Contractors, including the Metropolitan Water District of Southern California whose System billings constituted 56% and 55% of total System water supply revenue for the years ended June 30, 2012 and 2011, respectively, and Kern County Water Agency whose System billings constituted 10% of total System water supply revenue for the years ended June 30, 2012 and 2011.

The System sold power to 13 power companies during the fiscal years ended June 30, 2012 and 2011. The highest percentage of power revenues came from the California Independent System Operator. The following table shows power sales to companies which exceeded 5% of the total power sold by the System excluding power sold to the water contractors in the amount of \$21.6 million and \$25.8 million, for the years ended June 30, 2012 and 2011, respectively.

	2012	%	2011	%
		Total		Total
California Independent System Operator	\$ 73,722	58.16%	\$ 104,079	62.19%
Morgan Stanley Capital Group Inc.	10,216	8.06%	11,914	7.12%
Constellation Energy Commodities Gr	15,557	12.27%	-	-
Sempra Energy Trading Corp.	6,787	5.35%	-	-
BP Energy Company	-	-	19,012	11.36%
Citigroup Energy Inc.	-	-	15,333	9.16%

Similarly, the System purchased power from 22 and 17 power suppliers during the fiscal years ended June 30, 2012 and 2011, respectively. The highest percentage of power provided to the System came from the California Independent System Operator. The following table shows power purchases from suppliers which exceeded 5% of the total power purchased by the System.

	2012	%	2011	%
		Total		Total
California Independent System Operator	\$ 138,257	50.95%	\$ 168,338	49.16%
Morgan Stanley Capital Group Inc.	40,311	14.85%	55,199	16.12%
Citigroup Energy Inc.	13,768	5.07%	20,241	5.91%
Sempra Energy Trading Corp.	-	-	17,811	5.20%
B P Energy Company	-	-	22,667	6.62%
Kings River Conservation District	-	-	17,950	5.24%

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**13. Segment Information**

The table below presents the condensed statements of net assets, the statements of activities and the statements of cash flows for the System's two segments, as of and for the years ended June 30, 2012 and 2011.

	2012			2011		
	Activities Allowed Under			Activities Allowed Under		
	Burns- Porter Act	Central Valley Project Act	Total	Burns- Porter Act	Central Valley Project Act	Total
Condensed Statements of Net Assets:						
Assets						
Capital assets	\$ 874,474	\$ 2,338,478	\$ 3,212,952	\$ 882,579	\$ 2,318,885	\$ 3,201,464
Other assets	627,050	548,672	1,175,722	793,817	351,813	1,145,630
Current assets	248,567	331,214	579,781	261,298	338,796	600,094
Total assets	<u>\$ 1,750,091</u>	<u>\$ 3,218,364</u>	<u>\$ 4,968,455</u>	<u>\$ 1,937,694</u>	<u>\$ 3,009,494</u>	<u>\$ 4,947,188</u>
Capitalization and Liabilities						
Capitalization:						
Net assets:						
Capital (deficit), net of related debt	\$ 781,205	\$ (97,180)	\$ 684,025	\$ 728,142	\$ (173,288)	\$ 554,854
Restricted	397,270	124,136	521,406	450,333	200,244	650,577
Total net assets	<u>1,178,475</u>	<u>26,956</u>	<u>1,205,431</u>	<u>1,178,475</u>	<u>26,956</u>	<u>1,205,431</u>
Long-term liabilities						
	<u>469,579</u>	<u>2,340,004</u>	<u>2,809,583</u>	<u>507,979</u>	<u>2,405,500</u>	<u>2,913,479</u>
Total capitalization	<u>1,648,054</u>	<u>2,366,960</u>	<u>4,015,014</u>	<u>1,717,237</u>	<u>2,401,673</u>	<u>4,118,910</u>
Current liabilities						
	149,456	328,095	477,551	145,319	264,879	410,198
Other liabilities	<u>(78,202)</u>	<u>554,092</u>	<u>475,890</u>	<u>75,139</u>	<u>342,941</u>	<u>418,080</u>
Total capitalization and liabilities	<u>\$ 1,719,308</u>	<u>\$ 3,249,147</u>	<u>\$ 4,968,455</u>	<u>\$ 1,937,695</u>	<u>\$ 3,009,493</u>	<u>\$ 4,947,188</u>
Condensed Statements of Revenues, Expenses and Changes in Net Assets:						
Operating revenues:						
Water supply	\$ 553,453	\$ 307,438	\$ 860,891	\$ 554,117	\$ 320,631	\$ 874,748
Power sales	146,219	2,141	148,360	190,993	2,161	193,154
Federal reimbursements	35,490	1,071	36,561	28,828	(534)	28,294
	<u>735,162</u>	<u>310,650</u>	<u>1,045,812</u>	<u>773,938</u>	<u>322,258</u>	<u>1,096,196</u>
Depreciation expense	(22,302)	(65,098)	(87,400)	(29,264)	(70,993)	(100,257)
Other operating expense	<u>(666,122)</u>	<u>(186,282)</u>	<u>(852,404)</u>	<u>(707,463)</u>	<u>(173,077)</u>	<u>(880,540)</u>
Income from operations	46,738	59,270	106,008	37,211	78,188	115,399
Capital expenses (deferred) recovered	702	30,694	31,396	(18,570)	32,592	14,022
Interest expense	(17,783)	(89,987)	(107,770)	(20,255)	(114,741)	(134,996)
Transfers In	7,543	65,945	73,488	(8,385)	(24,309)	(32,694)
Transfers Out	(38,325)	(35,163)	(73,488)	12,648	20,046	32,694
Other (expense) income	<u>1,125</u>	<u>(30,759)</u>	<u>(29,634)</u>	<u>(2,649)</u>	<u>8,224</u>	<u>5,575</u>
Increase (decrease) in net assets	-	-	-	-	-	-
Net assets, beginning of year	<u>1,178,475</u>	<u>26,956</u>	<u>1,205,431</u>	<u>1,178,475</u>	<u>26,956</u>	<u>1,205,431</u>
Net assets, end of year	<u>\$ 1,178,475</u>	<u>\$ 26,956</u>	<u>\$ 1,205,431</u>	<u>\$ 1,178,475</u>	<u>\$ 26,956</u>	<u>\$ 1,205,431</u>
Condensed Statements of Cash Flows:						
Net cash provided by (used in):						
Operating activities	\$ 77,071	\$ 195,355	\$ 272,426	\$ 73,429	\$ 234,309	\$ 307,738
Capital and related financing activities	(124,566)	(204,768)	(329,334)	(88,894)	(220,778)	(309,672)
Investing activities	<u>2,944</u>	<u>5,945</u>	<u>8,889</u>	<u>3,713</u>	<u>6,801</u>	<u>10,514</u>
Net (decrease) increase in cash and cash equivalents	(44,551)	(3,468)	(48,019)	(11,752)	20,332	8,580
Cash and equivalents, beginning of year	<u>244,128</u>	<u>307,593</u>	<u>551,721</u>	<u>255,880</u>	<u>287,261</u>	<u>543,141</u>
Cash and equivalents, end of year	<u>\$ 199,577</u>	<u>\$ 304,125</u>	<u>\$ 503,702</u>	<u>\$ 244,128</u>	<u>\$ 307,593</u>	<u>\$ 551,721</u>

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### 14. New Governmental Accounting Standards

#### GASB Statement No. 60

In November 2010, the GASB issued Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*. This statement addresses how to account for and report service concession arrangements (SCAs), a type of public-private or public-public partnership that state and local governments are increasingly entering into. The requirements of GASB No. 60 are effective for fiscal year 2013 and thereafter. The System is currently evaluating the impact this statement will have, if any, on its financial statements.

#### GASB Statement No. 61

In November 2010, the GASB issued Statement No. 61, *The Financial Reporting Entity: Omnibus*. This statement amends GASB Statement No. 14 and GASB Statement No. 34, to modify certain requirements for inclusion of component units in the financial reporting entity, to amend the criteria for reporting component units as if they were part of the primary government in certain circumstances, and clarifies the reporting of equity interests in legally separate organizations. The requirements of GASB No. 61 are effective for fiscal year 2013 and thereafter. The System is currently evaluating the impact this statement will have, if any, on its financial statements.

#### GASB Statement No. 62

In December 2010, the GASB issued Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. The requirements in this Statement will improve financial reporting by contributing to the GASB's efforts to codify all sources of generally accepted accounting principles for state and local governments so that they derive from a single source. The requirements of Statement No. 62 are effective for the System beginning in fiscal 2013. The System is currently evaluating the impact this statement will have, if any, on its financial statements.

#### GASB Statement No. 63

In June 2011, the GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. This Statement provides financial reporting guidance which standardizes the presentation of deferred outflows of resources and deferred inflows of resources and their effects on a government's net position. The requirements of Statement No. 63 are effective for the System beginning in fiscal 2013. The System is currently evaluating the impact this statement will have, if any, on its financial statements.

#### GASB Statement No. 64

In June 2011, the GASB issued Statement No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provisions an amendment of GASB Statement No. 53*. The objective of this Statement is to clarify whether an effective hedging relationship continues after the replacement of a swap counterparty or a swap counterparty's credit support provider. The requirements of Statement No. 64 are effective for the System beginning in fiscal 2013. The System does not expect this statement to have any impact on its financial statements.

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### GASB Statement No. 65

In March 2012, the GASB issued Statement No. 65, *Items Previously Reported as Assets and Liabilities*. The objective of this Statement is to (a) properly classify certain items that were previously reported as assets and liabilities as deferred outflows of resources or deferred inflows of resources or (b) recognize certain items that were previously reported as assets and liabilities as outflows of resources (expenses or expenditures) or inflows of resources (revenues). These determinations are based on the definitions of those elements in Concepts Statement No. 4, *Elements of Financial Statements*. The provisions of this Statement are effective for the System beginning in fiscal 2014. The System is currently evaluating the impact this statement will have, if any, on its financial statements.

### GASB Statement No. 66

In March 2012, the GASB issued Statement No. 66, *Technical Corrections—2012—an amendment of GASB Statements No. 10 and No. 62*. The objective of this Statement is to improve accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, Statements No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, and No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. The requirements of GASB No. 66 are effective for fiscal year 2014 and thereafter. The System is currently evaluating the impact this statement will have, if any, on its financial statements.

### GASB Statement No. 68

In June 2012, the GASB issued Statement No. 68, *Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27*. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers about financial support for pensions that is provided by other entities. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency. The requirements of GASB No. 68 are effective for fiscal year 2015 and thereafter. The System is currently evaluating the impact this statement will have, if any, on its financial statements.

## 15. Subsequent Events

On September 5, 2012, The System delivered the CVP Water System Revenue Bonds Series AL (Tax-Exempt) pursuant to a purchase agreement among the Department, the State Treasurer and the Underwriters executed on February 28, 2012. The delayed delivery of the Series AL Bonds was necessary in order to achieve a current refunding of the Series X and Series Z Refunded Bonds for purposes of the Internal Revenue Code 1986, as amended. The CVP Water System Revenue Bonds Series AL was issued with a par amount of \$105,875 and a premium of \$18,176 with an average yield on bonds of 2.33%. The bond proceeds, along with System funds on hand in the amount of \$1,466 were used to retire \$121,945 of outstanding bonds by depositing \$124,927 in an irrevocable escrow account, and to cover costs of issuance of \$590.

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(in thousands)

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On September 27, 2012, the System issued the CVP Water System Revenue Bonds Series AN (Tax-Exempt) with a par amount of \$49,525 and a premium of \$10,113 with an average yield on bonds of 2.98%. The bond proceeds, along with System funds on hand in the amount of \$211 were used to retire \$12,550 of outstanding bonds by depositing \$14,322 in an irrevocable trust with an escrow agent, redeem commercial paper borrowings of \$44,807, fund capitalized interest of \$318, fund deposits to the debt service reserve account of \$159 and cover costs of issuance of \$243.

On September 27, 2012, the System issued CVP Water System Revenue Bonds Series AO (Federally Taxable) with a par amount of \$317,505 with an average yield on bonds of 2.54%. The bond proceeds, along with System funds on hand in the amount of \$5,331 were used to retire \$285,790 of outstanding bonds by depositing \$321,409 in an irrevocable escrow account, and to cover costs of issuance of \$1,427.



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## **Supplementary Information**

**State Water Resources Development System**  
**Calculation of Adequacy of Debt Service Coverage for the**  
**Central Valley Project Revenue Bonds**  
**For the years ended June 30, 2012 and 2011**

**(in thousands)**

	<u>2012</u>	<u>2011</u>
Water supply revenues, Central Valley Project Act	\$307,438	\$320,631
Add: Cover Collected as Proceeds Due To Water Contractors	56,385	55,542
Less: Devil Canyon Castaic Revenues	(16,979)	(16,385)
Revenues not available for Debt Service	<u>(68,469)</u>	<u>(79,631)</u>
Net CVP revenues available for debt service	<u>278,375</u>	<u>280,157</u>
Principal and interest for revenue bonds	<u>\$220,455</u>	<u>\$219,974</u>
Debt service coverage	<u>126.3%</u>	<u>127.4%</u>

Note: Section 805 of the general bond resolution for the Central Valley Project (CVP) Water system Revenue Bonds states, "The total amount of Revenues receivable under all Water Supply Contracts in any Year shall be the sum of (A) 1.25 times the Annual Debt Service for such Year to be paid from the Revenue Fund, plus (B) the amount estimated by the Department, pursuant to Section 605, to be required from the Revenue Fund in such Year to provide for Water System Operating Expenses..."

The Supplementary Information, Calculation of Adequacy of Debt Service Coverage for the Central Valley Project (CVP) Revenue Bonds is based on \$307.4 million in fiscal 2012 and \$320.6 million in 2011, respectively in Water Supply Revenues of the System's (CVP) segment. In fiscal 2012 the revenues include: an increase of \$56.4 million in refundable proceeds, a decrease of \$16.9 million for principal and interest payments for the Devil Canyon Castaic Facilities Bonds (DCC) since the DCC General Bond resolution does not require cover to be collected for these bonds, and a decrease of \$68.5 million of which \$59.3 million is primarily related to operations and maintenance and \$9.2 million is related to miscellaneous revenues not intended for debt service.

In fiscal 2011 the revenues include: an increase of \$55.6 million in refundable proceeds, a decrease of \$16.4 million for principal and interest payments for the DCC Facilities Bonds, and a decrease of \$79.6 million of which \$77.4 million is primarily related to operations and maintenance and \$2.2 million is related to miscellaneous revenues not intended for debt service.

**Edmund G. Brown Jr.**  
Governor, State of California

**John Laird**  
Secretary of Resources,  
Natural Resources Agency

**Mark Cowin**  
Director, Department of Water Resources



**SUMMARY OF CERTAIN PROVISIONS OF THE RESOLUTION**

**General Authority**

The Bonds are authorized by the provisions of the CVP Act. The Department’s authority to issue bonds under the CVP Act was confirmed by a decision of the Supreme Court of California in *Warne v. Harkness*, 70 Cal.2d 570 (1963). The CVP Act and such decision authorize the Department to pledge revenues for the security of CVP Act bonds, free and clear of the pledge of revenues of the State Water Project to the general obligation bonds of the State issued pursuant to the Burns-Porter Act. Under the CVP Act the payment of bond debt service has priority over the payment of operating expenses.

**Issuance of Bonds**

Additional Bonds may be issued on a parity with outstanding Bonds and secured by an equal lien on the Revenues, to finance or refinance the costs of construction or acquisition of facilities for water conservation or transportation, including facilities to generate or transmit electric power, for the State Water Project (“Water System Projects”), the costs of study or planning of any potential Water System Project (“Project Planning Costs”), and to make deposits to the Debt Service Reserve Account. The issuance of additional Bonds is authorized by the adoption of a supplemental resolution and is subject to certain requirements, including the following:

*General Requirements for Additional Bonds.* In order to issue a series of additional Bonds, the Department must certify that (a) after the issuance of such Series, estimated Revenues in each year will not be less than the sum of 1.25 times debt service to be paid from the Revenue Fund plus estimated Water System Operating Expenses and (b) the Debt Service Reserve Account is projected to contain on the first interest payment date on which interest for such Series is payable from Revenues, an amount equal to, for any date of calculation, for all Series of Bonds outstanding for which interest is then payable in whole or in part from Revenues, one-half of the maximum Annual Debt Service for the then current Year or any Year after such date of calculation. In addition, the Treasurer must have received evidence that the issuance of the additional Bonds will not result in the lowering of any rating then assigned to any then outstanding Bonds by any nationally recognized rating agency.

*Additional Requirements for New Money Bonds.* In order to issue a series of Bonds for new money purposes, the Department must (in addition to the foregoing general requirements) also certify that the Water System Project for which such series is being issued can be beneficially used by the Department to assist in the conservation or transportation of water under Water Supply Contracts, that the Water System Project is technically and economically feasible and that moneys, if any, for Project Planning Costs are then required (including an estimate of the amount of moneys required for Project Planning Costs).

**Disposition of Revenues**

Revenues as defined under the Resolution include:

- (a) moneys to be received under the Water Supply Contracts resulting from the construction, acquisition or operation of Water System Projects (but only in the amounts required to meet the rate covenant of the Resolution);

(b) moneys received from any other legally available source that the Department in its discretion determines to be Revenues and so designates in a certificate filed with the Treasurer; and

(c) income from the investment of moneys held in the Revenue Fund pursuant to the Resolution.

Revenues do not include any other income or receipts resulting from the construction, acquisition or operation of a Water System Project other than the income and receipts specified in the immediately preceding clauses (a), (b) and (c).

The Resolution requires the State Controller to establish and maintain the following accounts in the Revenue Fund: the Interest Account, the Principal Retirement Account, the Operating Account, the Debt Service Reserve Account, and the Surplus Account. The State Controller is to allocate to the Operating Account during each Year an amount equal to the amount previously estimated by the Department to be required in such Year for Water System Operating Expenses.

The Resolution requires the State Controller to allocate all Revenues, when received, to these accounts. The allocation is required to be in the following priority: Interest Account, Principal Retirement Account, Operating Account, Debt Service Reserve Account and Surplus Account. The State Controller is to allocate to the Interest Account on or before each interest payment date an amount equal to the interest due on such interest payment date (less amounts then in the Interest Account or the Construction Fund available to pay such interest). The State Controller is to allocate to the Principal Retirement Account on or before each maturity date and sinking fund installment date the sum of (a) the principal amount of any serial Bonds becoming due on such date, plus (b) any sinking fund installments that become due on such date. The State Controller is to maintain separate subaccounts in the Principal Retirement Account for the serial Bonds of each series and for the sinking fund installments of each series of Bonds.

Moneys in the Surplus Account may be applied to any lawful purpose, including transfer to funds not subject to the lien of the Resolution.

### **Debt Service Reserve Account**

A Debt Service Reserve Account is required to be maintained in the State Treasury. On the issuance of each series of Bonds, provision must be made for placing moneys in the Debt Service Reserve Account so that on the first interest payment date when interest on the Bonds of that series is to be paid from Revenues, the Debt Service Reserve Account will contain an amount at least equal to, for any date of calculation, for all Series of Bonds outstanding for which interest is then payable in whole or in part from Revenues, one-half of the maximum Annual Debt Service for the then current Year or any Year after such date of calculation (the "Reserve Account Requirement."). Revenues will be allocated to the Debt Service Reserve Account to the extent necessary, under the priority described under "Disposition of Revenues," so that the amount in the Debt Service Reserve Account will be at least equal to such amount.

The Department, at its option and notwithstanding any contrary provision in the Resolution, may withdraw, in whole or in part, amounts required to be held in the Debt Service Reserve Account upon the deposit of a Reserve Fund Instrument with the Treasurer, as trustee, in a stated amount equal to the amounts so withdrawn. Upon request of the Department or as may be provided in a supplemental resolution, Revenues deposited in the Debt Service Reserve Account shall be used to reimburse draws on any Reserve Fund Instruments therein, but only to the extent that such reimbursement results in a commensurate increase in the amount of available coverage provided under the respective Reserve Fund

Instrument. The amount available to be drawn under any Reserve Fund Instrument on deposit in the Debt Service Reserve Account shall be included in calculating the amount credited to such Account. A Reserve Fund Instrument is a letter of credit, surety bond or other credit facility issued by a provider the unsecured obligations of which, at the time of initial deposit of such facility, are rated not lower than “Aa” by Moody’s and “AA” by S&P, and the deposit of which does result in a withdrawal or downgrading of any rating of the Bonds then in effect.

Moneys in the Debt Service Reserve Account are to be applied, upon the claim of the Treasurer, to make good any deficiency in the Interest Account or the Principal Retirement Account, in that priority.

Any amount in the Debt Service Reserve Account in excess of its requirement may be transferred to any legally permissible fund or account designated by the Department.

### **Security for Payment of Bonds**

Payment of the principal and redemption price of, and interest on, the Bonds is secured by a first and direct charge and lien upon the Revenues and all moneys and securities held and accounts established (except amounts, if any, in any Rebate Account) under the Resolution, by the Department, the State Controller, the Treasurer, or the Paying Agent, subject only to the provisions of the Resolution permitting the payment or the use thereof for the purpose, in the manner, and upon the terms and conditions set forth in the Resolution.

The Department must perform and observe all the obligations and conditions required to be performed and observed by it under the Water Supply Contracts at the times, and in the manner therein prescribed. The Department must diligently enforce its rights under the Water Supply Contracts and must not agree to any amendment to the Water Supply Contracts that would materially adversely affect the security of the Bonds.

The Department must at all times use its best efforts to maintain the Revenues in each year at an amount at least equal to 1.25 times the annual debt service for such year to be paid from the Revenue Fund plus the amount required from the Revenue Fund for Water System Operating Expenses in such year, plus certain amounts required to fund initially the Debt Service Reserve Account.

### **Investment of Moneys Held Under the Resolution**

Moneys held in all accounts other than the Debt Service Reserve Account will be invested under the laws governing the investment of moneys in the State Treasury. Moneys held in the Debt Service Reserve Account shall be invested in obligations of the United States (including trust receipts or certificates evidencing ownership of payments on such obligations), in obligations for which the faith and credit of the United States are pledged for the payment of principal and interest, in certain federal agency securities, in certain state or local government obligations secured by obligations of or guaranteed by the United States or in the Surplus Money Investment Fund operated by the Treasurer.

### **Certain Covenants**

The covenants of the Department contained in the Resolution include the following:

*Punctual Payment.* The Department will pay or cause to be paid the principal or redemption price of and interest to become due in respect of all Bonds, in strict conformity with the terms of the Bonds and of the Resolution, and it will faithfully observe and perform all of the conditions, covenants, and requirements of the Resolution and all supplemental resolutions and of the Bonds.

*Covenant Against Encumbrances, Sale, or Disposition.* The Department shall not create, or permit to be created, any mortgage, lien, or pledge on the Revenues equal or prior to the charge or lien of the Resolution, nor sell or otherwise dispose of all or any part of a Water System Project essential to the maintenance of the Revenues, nor enter into any lease or agreement that would materially adversely affect the rights or security of the Bondholders under the Resolution.

*Tax Covenants.* The Department may include in any supplemental resolution authorizing the issuance of a series of Bonds covenants designed to preserve the tax-exempt status of such series of Bonds, including covenants concerning the rebate of excess investment earnings on moneys held under the Resolution.

### **Events of Default; Remedies of Bondholders**

The Bondholders and the Treasurer, as trustee, acting for the Bondholders shall be entitled to all of the rights and remedies provided in the CVP Act and to all of the rights and remedies otherwise provided or permitted by law.

In the event the Department shall default in the payment of principal or redemption price of any Bond, or in the payment of interest on any Bond, or in the event the Department shall not comply with any of the covenants or agreements contained in the Resolution or the Bonds and such defaults shall have continued for a period of 60 days after written notice thereof shall have been given to the Department by the Treasurer, or to the Department and the Treasurer by the holders of at least 25 percent in principal amount of the outstanding Bonds; then the Treasurer or the holders of at least a majority in principal amount of the outstanding Bonds shall be entitled to declare the principal of all of the outstanding Bonds, and the interest accrued thereon, to be due and payable immediately.

Under any default or other occurrence creating a right in the Treasurer to represent the holders of Bonds, the Treasurer may take such action as he or she may deem appropriate, and shall take such action as shall be specified in a written request of the holders of at least 25 percent in principal amount of the outstanding Bonds and upon the furnishing to the Treasurer of indemnity satisfactory to him or her.

### **Amendment of the Resolution**

The Resolution and the rights and obligations of the Department and the Bondholders may be changed at any time by a supplemental resolution when approved by the holders of 60 percent of the principal amount of the Bonds then outstanding and affected by such change at a meeting of the Bondholders or by the written consent of the Bondholders. Any such consent shall be binding upon the Bondholder giving such consent and on any subsequent Bondholder (whether or not such subsequent Bondholder has notice thereof) unless such consent is revoked in writing by the Bondholder giving such consent or a subsequent Bondholder by filing such revocation with the Treasurer prior to the date the Department mails notice that the consents of the holders of the requisite percentage of Bonds have been obtained.

No change shall be made, without the consent of all Bondholders, (a) in the principal amount or the redemption price of any Bond, the rate of interest thereon, the maturity of the principal thereof or of any installment of interest thereon or (b) in the percentage of the principal amount of Bonds the vote or consent of the holders of which is required to effect any change.



A change may also be made at any time by supplemental resolution, without the consent of any Bondholders, for any one or more of the following:

- (a) To add to the covenants of the Department, other covenants, or to surrender any right reserved to the Department;
- (b) To cure any ambiguity, defect or inconsistent provision in the Resolution or to make provisions in regard to questions arising under the Resolution as the Department deems necessary and not inconsistent with the Resolution, and which shall not materially adversely affect the interests of the Bondholders;
- (c) To provide for the issuance of an additional series of Bonds;
- (d) To provide for the issuance of Bonds in coupon form rather than or in addition to registered form. No such change may be materially adverse to the interests of the holders of outstanding Bonds; or
- (e) To add such provisions as may be necessary to accommodate such banking, insurance, remarketing and other financial arrangements as may be necessary or desirable to provide additional security for the payment of principal and interest on any one or more series of Bonds or to provide the holders of any one or more series of Bonds the right to tender such Bonds to the Department or to another party for purchase at the times, on the notice and on such other terms as the Department may determine. These arrangements may provide for the reimbursement by the Department, with interest, of moneys advanced by the provider of additional security, the provider of a tender right, the provider of moneys to fund a tender right or anyone performing a related function from the sources available for the payment of Bonds. No such change may be materially adverse to the interests of the holders of outstanding Bonds.

### **Discharge of Obligations Under the Resolution**

The obligations of the Department and the pledge, lien, covenants and agreements of the Department made or provided for in the Resolution will be fully discharged and satisfied as to any Bond and such Bond shall no longer be deemed to be outstanding thereunder, when payments of the principal of and the applicable redemption price, if any, on such Bond, plus interest thereon to the due date thereof, (i) has been made or caused to be made in accordance with the terms thereof or (ii) has been provided for by depositing with the Treasurer in trust for such payment (a) moneys sufficient to make such payments or (b) specified governmental obligations maturing as to principal and interest in such amounts and at such times as will insure the availability of sufficient moneys to make such payments, and, except for the purposes of such payment, such Bond will no longer be secured by or entitled to the benefits of the Resolution; provided that, with respect to Bonds that are to be redeemed or otherwise prepaid prior to the stated maturities thereof, no such deposit will constitute such discharge and satisfaction unless such Bonds have been called or designated for redemption or prepayment in accordance with the provisions thereof and notice of such redemption or prepayment has been given or irrevocable provision has been made for the giving of such notice.

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**SUMMARY OF CONTINUING DISCLOSURE CERTIFICATE**

The Department has executed a Continuing Disclosure Certificate, dated September 25, 2012, and will execute a Supplemental Continuing Disclosure Certificate with respect to the Series AM Bonds at the time of delivery of the Series AM Bonds whereby the terms of the Continuing Disclosure Certificate will be made applicable to such Bonds (the Continuing Disclosure Certificate, as supplemented being referred to as the “Disclosure Certificate.”) The following is a summary of the provisions of the Disclosure Certificate. Such summary is qualified by reference to the complete Disclosure Certificate, which is available from the Department.

**Definitions**

“Annual Report” shall mean the Annual Report filed by the Department as described below under the heading “Annual Reports.”

“Beneficial Owner” shall mean any person who has or shares the power, directly or indirectly, to make investment decisions concerning ownership of any Bonds to which the Disclosure Certificate is applicable (including persons holding Bonds through nominees, depositories or other intermediaries).

“Dissemination Agent” shall mean any Dissemination Agent designated in writing by the Department.

“Listed Event” shall mean any of the events listed under the heading “Reporting of Significant Events.”

“MSRB” shall mean the Municipal Securities Rulemaking Board or any other entity designated or authorized by the SEC to receive reports or notices pursuant to the Rule. Until otherwise designated by the MSRB or the SEC, filings with the MSRB are to be made through the Electronic Municipal Market Access (EMMA) website of the MSRB, currently located at <http://emma.msrb.org>.

“Obligated Person” shall mean any person, including the Department, who is either generally or through an enterprise, fund, or account of such person committed by contract or other arrangement to support payment of all, or part of the Bonds to which the Disclosure Certificate is applicable (other than providers of municipal bond insurance, letters of credit, or other liquidity facilities).

“Official Statement” shall mean the respective Official Statements related to the Bonds to which the Disclosure Certificate is applicable.

“Rule” shall mean Rule 15c2-12(b)(5) adopted by the SEC under the Securities Exchange Act of 1934, as the same may be amended from time to time.

“SEC” means the Securities Exchange Commission.

“State” shall mean the State of California.

## Annual Reports

The Department shall, or shall cause the Dissemination Agent to, not later than 270 days after the end of the Department's fiscal year (which fiscal year as of the date of the Disclosure Certificate ends June 30), provide an Annual Report consistent with the requirements of the Disclosure Certificate to the MSRB in such form as is required by the MSRB; provided that the audited financial statements of the Department may be submitted separately from the balance of the Annual Report and later than the date required above for the filing of the Annual Report if they are not available by that date. If the Department's fiscal year changes, it shall give notice of such change in the same manner as for a Listed Event under Section 5(c).

If in any year the Department does not provide, or cause the Dissemination Agent to provide, the Annual Report to the MSRB by the date required under the Disclosure Certificate, the Department shall file notice with the MSRB stating that the Annual Report has not been filed, and if known, the date by which the Department expects to file, or cause to be filed, the Annual Report.

The Department's Annual Report shall contain or include by reference the following:

1. The audited financial statements of the Department for the prior fiscal year, prepared in accordance with generally accepted accounting principles as promulgated to apply to governmental entities from time to time by the Governmental Accounting Standards Board. If such audited financial statements are not available by the time the Annual Report is required to be filed pursuant to the Disclosure Certificate, the Annual Report shall contain unaudited financial statements in a format similar to the financial statements contained in the final Official Statement, and the audited financial statements shall be filed in the same manner as the Annual Report when they become available.

2. An update of the following information contained in the Official Statement:

- a. The amount on deposit in the Debt Service Reserve Account.
- b. The information under the heading "THE DEPARTMENT – Investments of Department Moneys."
- c. The information relating to the prior year's water deliveries under the heading "STATE WATER PROJECT WATER SUPPLY– Annual Water Deliveries."
- d. The information relating to the current year's water requests under the heading "STATE WATER PROJECT WATER SUPPLY– Annual Water Deliveries."
- e. The information relating to sources of power for the prior year in the table under the heading "POWER OPERATIONS OF THE STATE WATER PROJECT – Historical Sources of Power for State Water Project Operations."
- f. The information relating to water deliveries for the prior year in the table under the heading "THE CONTRACTORS – Water Deliveries and Contractor Payments – Historical Deliveries of Water From the State Water Project to the Contractors."
- g. The information relating to payments for the prior year in the table under the heading "THE CONTRACTORS – Water Deliveries and Contractor Payments – Historical Deliveries of Water From the State Water Project to the Contractors."
- h. The information relating to the Contractors in APPENDIX A for any Contractor whose payments are expected to be five percent (5%) or more of Revenues attributable to the bonds outstanding under the Resolution.

Any or all of the items listed above may be included by specific reference to other documents, including official statements of debt issues with respect to which the Department is an “obligated person” (as defined by the Rule), which have been filed with the MSRB or the SEC. If the document included by reference is a final Official Statement, it must be available from the MSRB. The Department shall clearly identify each such other document so included by reference.

### **Reporting of Significant Events**

(a) Pursuant to the provisions of the Disclosure Certificate, the Department shall give, or cause to be given, notice of the occurrence of any of the following events with respect to the Outstanding Bonds to which the Disclosure Certificate is applicable:

1. principal and interest payment delinquencies;
2. non-payment related defaults, if material;
3. unscheduled draws on the debt service reserves reflecting financial difficulties;
4. unscheduled draws on the credit enhancements reflecting financial difficulties;
5. substitution of the credit or liquidity providers or their failure to perform;
6. adverse tax opinions, the issuance by the Internal Revenue Service of proposed or final determinations of taxability, Notices of Proposed Issue (IRS Form 5701-TEB) or other material notices or determinations with respect to the tax status of the Bonds, or other material events affecting the tax status of the Bonds to which the Disclosure Certificate is applicable;
7. modifications to rights of Bondholders, if material;
8. bond calls, if material, and tender offers;
9. defeasances;
10. release, substitution or sale of property securing repayment of the Bonds, if material;
11. rating changes;
12. bankruptcy, insolvency, receivership, or similar event of the Department;
13. the consummation of a merger, consolidation, or acquisition involving an Obligated Person or the sale of all or substantially all of the assets of an Obligated Person, other than in the ordinary course of business, the entry into a definitive agreement to undertake such an action or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms, if material; and
14. the appointment of a successor or additional trustee, or the change in the name of a trustee, if material.

(b) Whenever the Department obtains knowledge of the occurrence of a Listed Event, the Department shall as soon as possible, if such Listed Event requires such a determination as set forth in the preceding clause (a), determine if such event would be material under applicable federal securities laws.

(c) The Department shall promptly file a notice electronically to the MSRB in a timely manner, but not in excess of 10 Business Days after the occurrence of a Listed Event, subject to a determination of its materiality, as applicable. Reference is made to the Rule for a discussion of when the Listed Event enumerated in subsection (a)(12) is deemed to have “occurred.”

### **Termination of Reporting Obligation**

The Department’s obligations under the Disclosure Certificate shall terminate upon the legal defeasance (or in the event a portion of the Bonds is legally defeased, with respect to such defeased Bonds), prior redemption or payment in full of all of the Bonds. If the Department’s obligations under the Resolution are assumed in full by some other entity, such person shall be responsible for compliance with the Disclosure Certificate in the same manner as if it were the Department and the Department shall have no further responsibility under the Disclosure Certificate. If such termination or substitution occurs prior to the final maturity of the Bonds, the Department shall give notice of such termination or substitution in the same manner as for a Listed Event.

### **Dissemination Agent**

The Department may, from time to time, appoint or engage a Dissemination Agent to assist it in carrying out its obligations under the Disclosure Certificate, and may discharge any such Dissemination Agent, with or without appointing a successor Dissemination Agent.

### **Amendment; Waiver**

The Department may amend or waive any provision of the Disclosure Certificate, provided that the following conditions are satisfied:

(a) If the amendment or waiver relates to the provisions of the Disclosure Certificate dealing with the timing and content of the Annual Report or the giving of notice of Listed Events, it may only be made in connection with a change in circumstances that arises from a change in legal requirements, change in law or change in the identity, nature or status of an Obligated Person with respect to the Bonds to which the Disclosure Certificate is applicable, or the type of business conducted;

(b) The undertaking, as amended or taking into account such waiver, would, in the opinion of nationally recognized bond counsel, have complied with the requirements of the Rule at the time of the original issuance of the Bonds to which the Disclosure Certificate is applicable, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances; and

(c) The amendment or waiver either (i) is approved by the Bondholders of the Bonds to which the Disclosure Certificate is applicable in the same manner as provided in the Resolution for amendments to the Resolution with the consent of Bondholders, or (ii) does not, in the opinion of nationally recognized bond counsel, materially impair the interests of the Bondholders or Beneficial Owners of the Bonds to which the Disclosure Certificate is applicable.

In the event of any amendment or waiver of a provision of the Disclosure Certificate, the Department shall describe such amendment in the next Annual Report, and shall include, as applicable, a narrative explanation of the reason for the amendment or waiver and its impact on the type (or, in the case of a change of accounting principles, on the presentation) of financial information or operating data being presented by the Department. In addition, if the amendment relates to the accounting principles to be followed in preparing financial statements, (i) notice of such change shall be given in the same manner as for a Listed Event, and (ii) the Annual Report for the year in which the change is made should present a

comparison (in narrative form and also, if feasible, in quantitative form) between the financial statements as prepared on the basis of the new accounting principles and those prepared on the basis of the former accounting principles.

### **Additional Information**

Nothing in the Disclosure Certificate prevents the Department from disseminating any other information, using the means of dissemination set forth in the Disclosure Certificate or any other means of communication, or including any other information in any Annual Report or notice of occurrence of a Listed Event, in addition to that which is required by the Disclosure Certificate. If the Department chooses to include any information in any Annual Report or notice of occurrence of a Listed Event, in addition to that which is specifically required by the Disclosure Certificate, the Department shall have no obligation under the Disclosure Certificate to update such information or include it in any future Annual Report or notice of occurrence of a Listed Event.

### **Beneficiaries**

The Disclosure Certificate shall inure solely to the benefit of the Bondholders and Beneficial Owners from time to time of the Bonds to which the Disclosure Certificate is applicable, and shall create no rights in any other person or entity (except the right of the Treasurer of the State of California, as trustee for the Bonds, or any Bondholder or Beneficial Owner to enforce the provisions of the Disclosure Certificate on behalf of the Bondholders). The Disclosure Certificate is not intended to create any monetary rights on behalf of any person based upon the Rule.

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**PROPOSED FORM OF OPINION OF ATTORNEY GENERAL**

*The following form of opinion is expected to be delivered with respect to the Series AM Bonds on the date of issue thereof.*

**[Issue Date]**

**\$183,960,000**

**State of California Department of Water Resources  
Central Valley Project Water System Revenue Bonds  
Series AM**

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**(Final Opinion)**

We have acted as the Attorney General of the State of California in connection with the issuance by the State of California Department of Water Resources (the “Department”) of its Central Valley Project Water System Revenue Bonds, Series AM (the “Series AM Bonds”), in the aggregate principal amount of \$183,960,000. The Series AM Bonds are issued pursuant to Part 3 of Division 6 of the Water Code of the State of California, and under a general bond resolution of the Department, adopted as of July 1, 1986 and a supplemental resolution of the Department, adopted on February 28, 2012 (the general bond resolution and all resolutions supplemental thereto are herein collectively called the “Resolution.”) The Series AM Bonds constitute the forty-first series of bonds issued under the Resolution (all bonds at any time outstanding under the Resolution being herein collectively called the “Bonds”) and are issued for one or more of the purposes set forth in the Resolution. Capitalized terms used but not otherwise defined herein shall have the meanings ascribed thereto in the Resolution.

In such connection, we have reviewed the Resolution, certifications of the Department, the Treasurer of the State of California and others as to certain factual matters, the opinion of counsel to the Department, and such other documents and matters to the extent we deemed necessary to render the opinions set forth herein. We have assumed, without undertaking to verify, the genuineness of all documents, certifications, opinions and signatures presented to us (whether as originals or as copies); the due and legal execution and delivery thereof by, and validity against, any parties other than the Department; the accuracy of the factual matters represented, warranted or certified in such documents, certificates and opinions; and compliance with all covenants and agreements contained in the Resolution.

Certain agreements, requirements and procedures contained or referred to in the Resolution, the Tax Certificate and other relevant documents may be changed and certain actions (including without limitation, defeasance of Bonds) may be taken or omitted under the circumstances and subject to the terms and conditions set forth in such documents. No opinion is expressed herein as to any Bond or the interest thereon if any such change occurs or action is taken or omitted upon the advice or approval of counsel other than ourselves.

This opinion is issued as of the date hereof. The opinions expressed herein are based on an analysis of existing laws, regulations, rulings and court decisions and cover certain matters not directly addressed by such authorities. Such opinions may be affected by actions taken or omitted or events occurring after the date hereof. We have not undertaken to determine, or to inform any person, whether any such actions are taken or omitted or events do occur or any other matters come to our attention after the date hereof and we disclaim any obligation to update this letter. We assume no obligation to update, revise or supplement this opinion to reflect any such action hereafter taken or not taken, or any facts or

circumstances, or any changes in law or in interpretations thereof, that may arise or occur, or for any other reason. We call attention to the fact that the rights and obligations under the Series AM Bonds and the Resolution and their enforceability may be subject to bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium and other laws relating to or affecting creditors' rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases and to limitations on legal remedies against the State of California. We express no opinion with respect to any indemnification, contribution, choice of law, choice of forum, choice of venue or waiver or severability provisions contained in the foregoing documents. Finally, we express no opinion as to the accuracy, adequacy or sufficiency of any financial or other information that has been or will be supplied to the purchasers of the Series AM Bonds and we undertake no responsibility for the accuracy, completeness or fairness of the Official Statement dated February 28, 2012, the updated Official Statement dated February \_\_, 2013, or other offering material relating to the Series AM Bonds and express herein no opinion with respect thereto.

Based on and subject to the foregoing, and in reliance thereon, as of the date hereof, we are of the following opinions:

1. The Series AM Bonds constitute valid and binding limited obligations of the Department, payable only out of the Revenues and moneys and securities held, and accounts established, under the Resolution.

2. The Resolution has been duly and lawfully adopted and is a valid resolution of the Department, enforceable against the Department in accordance with the terms of the Resolution.

3. The Series AM Bonds are secured by a first and direct charge and lien upon the Revenues and all moneys and securities held, and accounts established, under the Resolution (except amounts held in any Rebate Account established under the Resolution), subject only to the provisions of the Resolution permitting the payment or use of such Revenues, moneys, securities and accounts for the purposes, in the manner and upon the terms and conditions set forth in the Resolution. The Series AM Bonds are not secured by any other property or moneys of the Department.

4. The Series AM Bonds do not constitute a debt, liability or obligation of the State of California or of any political subdivision thereof, or a general obligation of the Department. Neither the faith and credit nor the taxing power of the State or any political subdivision thereof is pledged to the payment of the principal of, premium, if any, or interest on the Series AM Bonds. The Department has no taxing power.

Sincerely,

Deputy Attorney General

For \_\_\_\_\_  
Attorney General of the State of California

**PROPOSED FORM OF OPINION OF BOND COUNSEL**

*The following form of opinion is expected to be delivered with respect to the Series AM Bonds on the date of issue thereof.*

[Issue Date]

**State of California Department of Water Resources  
Central Valley Project Water System Revenue Bonds  
Series AM**

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**(Final Opinion)**

We have acted as bond counsel to the Department in connection with the issuance by the State of California Department of Water Resources (the “Department”) of its Central Valley Project Water System Revenue Bonds, Series AM (the “Series AM Bonds”), in the aggregate principal amount of \$183,960,000. The Series AM Bonds are issued pursuant to Part 3 of Division 6 of the Water Code of the State of California, and under a general bond resolution of the Department, adopted as of July 1, 1986 and a supplemental resolution of the Department, adopted as of February 28, 2012 (the general bond resolution and all resolutions supplemental thereto are herein collectively called the “Resolution.”) The Series AM Bonds constitute the forty-first series of bonds issued under the Resolution (all bonds at any time outstanding under the Resolution being herein collectively called the “Bonds”) and are issued for one or more of the purposes set forth in the Resolution. Capitalized terms used but not otherwise defined herein shall have the meanings ascribed thereto in the Resolution.

In such connection, we have reviewed the Resolution, the Tax Certificate of the Department dated March 13, 2012, as supplemented on the date hereof, executed in connection with the Series AM Bonds (the “Tax Certificate”), certifications of the Department, the Treasurer of the State of California and others as to certain factual matters and such other documents and matters to the extent we deemed necessary to render the opinions set forth herein. We have assumed the genuineness of all documents and signatures presented to us (whether as originals or as copies) and the due and legal execution and delivery thereof by, and validity against, any parties other than the Department. We have assumed, without undertaking to verify, the accuracy of the factual matters represented, warranted or certified in the documents referred to in this paragraph.

The opinions expressed herein are based on an analysis of existing laws, regulations, rulings and court decisions and cover certain matters not directly addressed by such authorities. Such opinions may be affected by actions taken or omitted or events occurring after the date hereof. We have not undertaken to determine, or to inform any person, whether any such actions are taken or omitted or events do occur or any other matters come to our attention after the date hereof. Accordingly, this letter speaks only as of its date and is not intended to, and may not, be relied upon or otherwise used in connection with any such actions, events or matters and we disclaim any obligation to update this letter. Furthermore, we have assumed compliance with all covenants and agreements contained in the Resolution and the Tax Certificate, including, without limitation, covenants and agreements compliance with which is necessary to assure that future actions, omissions or events will not cause interest on the Series AM Bonds to be included in gross income for federal income tax purposes. We call attention to the fact that the rights and obligations under the Series AM Bonds, the Resolution and the Tax Certificate and their enforceability

may be subject to bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium and other laws relating to or affecting creditors' rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases and to limitations on legal remedies against the State of California. We express no opinion with respect to any indemnification, contribution, choice of law, choice of forum, choice of venue or waiver or severability provisions contained in the foregoing documents. Our services did not include financial or other non-legal advice. Finally, we undertake no responsibility for the accuracy, completeness or fairness of the Official Statement dated February 28, 2012, the updated Official Statement dated February \_\_\_, 2013, or other offering material relating to the Series AM Bonds, and express herein no opinion with respect thereto.

Based on and subject to the foregoing, and in reliance thereon, as of the date hereof, we are of the following opinions:

1. The Series AM Bonds constitute valid and binding limited obligations of the Department, payable only out of the Revenues and moneys and securities held, and accounts established, under the Resolution.

2. The Resolution has been duly and lawfully adopted, is a valid resolution of the Department and is binding upon the Department in accordance with the terms of the Resolution.

3. The Series AM Bonds are secured by a first and direct charge and lien upon the Revenues and all moneys and securities held, and accounts established, under the Resolution (except amounts held in any Rebate Account established under the Resolution), subject only to the provisions of the Resolution permitting the payment or use of such Revenues, moneys, securities and accounts for the purposes, in the manner and upon the terms and conditions set forth in the Resolution. The Series AM Bonds are not secured by any other property or moneys of the Department.

4. Neither the principal of nor the interest on the Series AM Bonds constitutes a debt, liability or obligation of the State of California or, except as expressly provided in the Resolution, of the Department.

5. Interest on the Series AM Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986 and is exempt from State of California personal income taxes. Interest on the Series AM Bonds is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although Bond Counsel observes that such interest is included in adjusted current earnings when calculating corporate alternative minimum taxable income. We express no opinion regarding other tax consequences related to the ownership or disposition of, or the accrual or receipt of interest on, the Series AM Bonds.

Very truly yours,

ORRICK, HERRINGTON & SUTCLIFFE LLP

per

**DTC AND BOOK-ENTRY**

The information in this appendix concerning The Depository Trust Company, New York, New York (“DTC”) and DTC’s book-entry system has been obtained from sources that the Department and the State Treasurer believe to be reliable, but the Department and the State Treasurer take no responsibility for the accuracy thereof.

DTC will act as securities depository for the Series AM Bonds. The Series AM Bonds will be issued as fully-registered securities registered in the name of Cede & Co. (DTC’s partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered Series AM Bond certificate will be issued for each maturity of Series AM Bonds in the aggregate principal amount of such maturity, and will be deposited with DTC. If, however, the aggregate principal amount of any maturity exceeds \$500 million, one certificate will be issued with respect to each \$500 million of principal amount, and an additional certificate will be issued with respect to any remaining principal amount of such maturity.

DTC is a limited-purpose trust company organized under the New York Banking Law, a “banking organization” within the meaning of the New York Banking Law, a member of the Federal Reserve System, a “clearing corporation” within the meaning of the New York Uniform Commercial Code, and a “clearing agency” registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 3.5 million issues of U.S. and non-U.S. equity, corporate and municipal debt issues, and money market instruments (from over 100 countries) that DTC’s participants (“Direct Participants”) deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants’ accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation (“DTCC.”) DTCC is the holding company for DTC, National Securities Clearing Corporation and Fixed Income Clearing Corporation, all of which are registered clearing agencies. DTCC is owned by the users of its regulated subsidiaries. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly (“Indirect Participants.”) The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at [www.dtcc.com](http://www.dtcc.com) and [www.dtc.org](http://www.dtc.org).

Purchases of Series AM Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Series AM Bonds on DTC’s records. The ownership interest of each actual purchaser of Series AM Bonds (“Beneficial Owner”) is in turn to be recorded on the Direct and Indirect Participants’ records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Series AM Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in Series AM Bonds, except in the event that use of the book-entry system for the Series AM Bonds is discontinued.

To facilitate subsequent transfers, all Series AM Bonds deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Series AM Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Series AM Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such Series AM Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. Beneficial Owners of Series AM Bonds may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Series AM Bonds, such as redemptions, tenders, defaults, and proposed amendments to the Series AM Bond documents. For example, Beneficial Owners of Series AM Bonds may wish to ascertain that the nominee holding the Series AM Bonds for their benefit has agreed to obtain and transmit notices to Beneficial Owners, in the alternative Beneficial Owners may wish to provide their names and addresses to the registrar and request that copies of notices be provided directly to them.

Redemption notices shall be sent to DTC. If less than all of the Series AM Bonds within an issue are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed. Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to Series AM Bonds unless authorized by a Direct Participant in accordance with DTC's Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the issuer as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts Series AM Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal and interest payments on the Series AM Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the Department or the State Treasurer, on payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC, its nominee, the Department or the State Treasurer, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal and interest to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the Department or the State Treasurer, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as depository with respect to the Series AM Bonds at any time by giving reasonable notice to the Department or the State Treasurer. Under such circumstances, in the event that a successor depository is not obtained, Series AM Bond certificates are required to be printed and delivered.

The Department and the State Treasurer may decide to discontinue use of the system of book-entry only transfers through DTC (or a successor securities depository). In that event, Series AM Bond certificates will be printed and delivered to DTC.

THE STATE TREASURER, AS LONG AS A BOOK-ENTRY ONLY SYSTEM IS USED FOR THE SERIES AM BONDS, WILL SEND ANY NOTICE OF REDEMPTION OR OTHER NOTICES TO OWNERS ONLY TO DTC. ANY FAILURE OF DTC TO ADVISE ANY PARTICIPANT, OR OF ANY PARTICIPANT TO NOTIFY ANY BENEFICIAL OWNER, OF ANY NOTICE AND ITS CONTENT OR EFFECT WILL NOT AFFECT THE VALIDITY OR SUFFICIENCY OF THE PROCEEDINGS RELATING TO THE REDEMPTION OF THE SERIES AM BONDS CALLED FOR REDEMPTION OR OF ANY OTHER ACTION PREMISED ON SUCH NOTICE.

The Department and the State Treasurer cannot and do not give any assurances that DTC will distribute to Participants, or that Participants or others will distribute to the Beneficial Owners, payments of principal of and interest and premium, if any, on the Bonds paid or any redemption or other notices or that they will do so on a timely basis or will serve and act in the manner described in this Official Statement. Neither the Department nor the State Treasurer is responsible or liable for the failure of DTC or any Direct Participant or Indirect Participant to make any payments or give any notice to a Beneficial Owner with respect to the Series AM Bonds or any error or delay relating thereto.

The foregoing description of the procedures and record keeping with respect to beneficial ownership interests in the Series AM Bonds, payment of principal of and interest and other payments with respect to the Series AM Bonds to Direct Participants, Indirect Participants or Beneficial Owners, confirmation and transfer of beneficial ownership interest in such Bonds and other related transactions by and between DTC, the Direct Participants, the Indirect Participants and the Beneficial Owners is based solely on information provided by DTC. Accordingly, no representations can be made concerning these matters and neither the Direct Participants, the Indirect Participants nor the Beneficial Owners should rely on the foregoing information with respect to such matters but should instead confirm the same with DTC or the Participants, as the case may be.

SO LONG AS CEDE & CO. IS THE REGISTERED OWNER OF THE SERIES AM BONDS, AS NOMINEE OF DTC, REFERENCES HEREIN TO THE HOLDERS OF SUCH SERIES SHALL MEAN CEDE & CO., AS AFORESAID, AND SHALL NOT MEAN THE BENEFICIAL OWNERS OF THE SERIES AM BONDS.

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**LETTERS FROM CERTAIN UNDERWRITERS**

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February 16, 2012

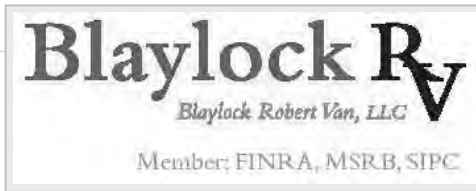
State Treasurer's Office  
Public Finance Division  
915 Capitol Mall, Room 110  
Sacramento, CA 95814

To Whom It May Concern:

Pershing LLC, a subsidiary of The Bank of New York Mellon Corporation, and Barclays Capital Inc. established a strategic alliance in May of 2009, which enables Pershing LLC to participate as a selling group member and a retail distributor for all new issue municipal bond offerings underwritten by Barclays Capital Inc., including the State of California Department of Water Resources, Water System Revenue Bonds offered hereby. Pershing LLC will receive a selling concession from Barclays Capital Inc. in connection with its distribution activities relating to the State of California Department of Water Resources, Water System Revenue Bonds.

Sincerely,

BARCLAYS CAPITAL INC.



February 17, 2012

Ms. Katie Carroll  
Deputy Treasurer  
Office of the Treasurer of the State of California  
915 Capitol Mall, Room 110  
Sacramento, CA 95814

Mr. Blake Fowler  
Director Public Finance  
Office of the Treasurer of the State of California  
915 Capitol Mall, Room 261  
Sacramento, CA 95814

**RE: State of California Department of Water Resources  
Central Valley Project Water System Revenue Bonds  
2012 Series AK, AL and AM**

Dear Ms. Carroll & Mr. Fowler:

Blaylock Robert Van, LLC (“Blaylock Robert Van” or “BRV”) is providing the following language for inclusion in the Official Statement.

Blaylock Robert Van, LLC (“Blaylock Robert Van” or “BRV”) has entered into distribution agreements (the “Agreements”) with TD Ameritrade (“TD”) and Alamo Capital Financial Services (“Alamo”) for the distribution of certain municipal securities offerings underwritten by or allocated to Blaylock Robert Van, including the Series 2012 AK, AL and AM Bonds. Under the Agreements, Blaylock Robert Van will share a portion of the underwriting compensation paid to BRV with TD and Alamo.

Sincerely,

Blaylock Robert Van, LLC



February 15, 2012

Ms. Katie Carroll  
Deputy Treasurer  
Office of the Treasurer of the State of California  
915 Capitol Mall, Room 110  
Sacramento, CA 95814

RE: State of California Department of Water Resources, Series AK, AL and AM

Dear Ms. Carroll:

Citigroup Global Markets Inc. and Morgan Stanley & Co. LLC are providing the following language for inclusion in the Offering Statement.

Citigroup Inc. and Morgan Stanley, the respective parent companies of Citigroup Global Markets Inc. and Morgan Stanley & Co. LLC, each an underwriter of the Bonds, have entered into a retail brokerage joint venture. As part of the joint venture each of Citigroup Global Markets Inc. and Morgan Stanley & Co. LLC will distribute municipal securities to retail investors through the financial advisor network of a new broker-dealer, Morgan Stanley Smith Barney LLC. This distribution arrangement became effective on June 1, 2009. As part of this arrangement, each of Citigroup Global Markets Inc. and Morgan Stanley & Co. LLC will compensate Morgan Stanley Smith Barney LLC. for its selling efforts in connection with their respective allocations of Bonds.

Citigroup Global Markets Inc.  
Morgan Stanley & Co. LLC



February 16, 2012

Ms. Katie Carroll  
Deputy Treasurer  
Office of the Treasurer of the State of California  
915 Capitol Mall, Room 110  
Sacramento, California 95814

Re: State of California Department of Water Resources, Central Valley Project Water System Revenue Bonds (“the Bonds”)

Dear Ms. Carroll:

De La Rosa & Co., one of the Underwriters of the Bonds, has entered into separate agreements with Credit Suisse Securities USA LLC and City National Securities, Inc. for retail distribution of certain municipal securities offerings, at the original issue prices. Pursuant to said agreements, if applicable to the Bonds, De La Rosa & Co. will share a portion of its underwriting compensation with respect to the Bonds, with Credit Suisse Securities USA LLC or City National Securities, Inc.

**De La Rosa & Co.**

**WATER SYSTEM PROJECTS**

Water System Projects consist of the portion of certain State Water Project facilities financed or expected to be financed with Bonds. The Water System Projects are described below. In each case, sources other than Bond Proceeds may have been used to pay certain costs of the facility, particularly those costs allocable to purposes other than water conservation and water transportation.

**Capital Expenditures for Water System Projects**

The following table summarizes the capital costs financed by Bonds for the Water System Projects described below, and sets forth the capital costs expected to be financed for such projects from the issuance of additional Bonds as of February 15, 2013.

**ESTIMATED CAPITAL FINANCING FROM  
WATER SYSTEM REVENUE BONDS FOR EXISTING WATER SYSTEM PROJECTS  
(in Millions)**

Water System Project	Capital Expenditures Series A through AO	Estimated Future Capital Expenditures <sup>(1)</sup>	Total Capital Expenditures <sup>(5)</sup>
Powerplants:			
Small Hydro Project	\$46.6	\$ 0.0	\$46.6
Pyramid Hydroelectric Project	74.4	0.0	74.4
Alamo Project	30.4	0.0	30.4
Bottle Rock Facilities <sup>(2)</sup>	80.2	0.0	80.2
South Geysers Project <sup>(3)</sup>	40.9	0.0	40.9
Reid Gardner Project	176.2	0.0	176.2
East Branch Enlargement – Phase I	453.0	0.0	453.0
Additional East Branch Improvements	124.1	0.0	124.1
East Branch Enlargement – Phase II	0.0	434.5	434.5
Delta Pumping Plant Completion	73.6	0.0	73.6
Suisun Marsh Environmental Facilities	37.2	0.0	37.2
San Bernardino Tunnel Intake Structure	29.3	0.0	29.3
San Luis Rock Quarry	4.5	0.0	4.5
Castle Rock–Lakeville Transmission Line	6.9	0.0	6.9
Midway-Wheeler Ridge Transmission Line	10.1	0.0	10.1
Kern Water Bank	37.0	0.0	37.0
Vista del Lago Visitor Center	9.0	0.0	9.0
North Bay Aqueduct–Phase II	87.1	0.0	87.1
North Bay Aqueduct Improvements – Terminal Tanks	7.4	6.1	13.5
North Bay Aqueduct Alternative Intake	0.0	410.0	410.0
Project Monitor and Control System	71.5	0.0	71.5
Communications System Replacement <sup>(4)</sup>	6.2	29.8	36.0
Arroyo Pasajero Flood Control Project	4.1	10.2	14.3
Hyatt Pump-Turbine Refurbishment	17.8	4.7	22.5
Edmonston Pump Replacement <sup>(4)</sup>	18.2	21.7	39.9
Delta Facilities Program	112.4	86.4	198.8
Tehachapi East Afterbay <sup>(4)</sup>	67.1	15.6	82.7
Perris Dam Remediation <sup>(4)</sup>	26.3	259.7	286.0
Facilities Repair and Improvement Project	167.0	28.1	195.2
Project Planning Costs	112.8	36.2	149.0
Coastal Branch – Phase II	491.3	0.0	491.3
East Branch Extension – Phase I	126.0	0.0	126.0
East Branch Extension – Phase I Improvements <sup>(4)</sup>	49.9	0.0	49.9
East Branch Extension – Phase II	14.1	191.3	205.7
South Bay Aqueduct Enlargement and Improvement <sup>(4)</sup>	222.0	15.0	237.0
<b>Total Water System Projects <sup>(5)</sup></b>	<b>\$2,834.8</b>	<b>\$1,549.4</b>	<b>\$4,384.2</b>

<sup>(1)</sup> The projections contained in this table have been prepared by the Department’s management for management purposes on the basis of certain assumptions, and consistent with certain requirements of the Water Supply Contracts. The projections are the responsibility of the Department. Macias, Gini & O’Connell LLP (“MGO”) has neither examined nor compiled such projections and, accordingly, MGO does not express an opinion or provide any other form of assurance with respect thereto. The MGO report included in APPENDIX B of this Official Statement relates to the State Water Project’s historical financial information. The MGO report does not extend to the projections set forth above and should not be read to do so. These projections were not prepared with a view toward compliance with the guidelines established by the American Institute of Certified Public Accountants for preparation and presentation of prospective financial information.

<sup>(2)</sup> Sold by the Department in 2001. (See “WATER SYSTEM PROJECTS – Project Descriptions – *Bottle Rock Facilities*.”)

<sup>(3)</sup> Sold by the Department in 2004. (See “WATER SYSTEM PROJECTS – Project Descriptions – *South Geysers Project*.”)

<sup>(4)</sup> The original Bond Anticipation Bonds (“BABs”) for East Branch Extension – Phase I Improvements exceeded the projected expenditures. \$44.5 million Series AE refunding of BABs for East Branch Extension – Phase I Improvements was redistributed to Communications System Replacement, Edmonston Pump Refurbishment, Tehachapi East Afterbay, Perris Dam Remediation and South Bay Aqueduct Enlargement.

<sup>(5)</sup> Totals may not sum due to rounding.



The Department may issue additional Bonds in amounts substantially greater than the amounts described in this subsection to finance capital costs allocated to existing Water System Projects or to Water System Projects defined by supplemental resolutions to be adopted in the future. (See “SECURITY FOR THE BONDS – Additional Bonds.”)

## **Project Descriptions**

The following Water System Projects have been completed:

*Small Hydro Project.* The Small Hydro Project consists of two small hydroelectric powerplants, the three 11 megawatt units of Mojave Siphon Powerplant and the 3 megawatt Thermalito Diversion Dam Powerplant. The Mojave Siphon Powerplant is located at the downstream end of the Mojave Siphon of the California Aqueduct, at Silverwood Lake, ten miles north of the City of San Bernardino. The Thermalito Diversion Dam Powerplant is located at the left abutment of the Thermalito Diversion Dam on the Feather River one mile north of the City of Oroville.

*Pyramid Hydroelectric Project.* The Pyramid Hydroelectric Project consists of a portion of the first stage of the William E. Warne Powerplant, formerly known as the Pyramid Powerplant, designated by the Department for electric power generation and transmission, and conveyance facilities between the 75 megawatt William E. Warne Powerplant and Quail Lake, including Lower Quail Canal and the first stage of Peace Valley Pipeline. These facilities are on the West Branch of the California Aqueduct in the vicinity of the town of Gorman in Los Angeles County.

*Alamo Project.* The Alamo Project consists of the portion of the 17 megawatt Unit 1 of the Alamo Powerplant located on the East Branch of the California Aqueduct, approximately one mile below the Tehachapi Afterbay.

*South Geysers Project.* The South Geysers Project is located in Sonoma County, California, about 70 miles north of San Francisco. The South Geysers Project design included a geothermal generating station with a 55 megawatt turbine-generator unit, associated electrical, mechanical and control facilities, a heat dissipation system, and a 1.8-mile transmission line. The Department suspended construction of the South Geysers Project because of the lack of an adequate geothermal steam supply. In 1990, the Department sold the major equipment components for \$5.5 million and in 2004, the Department sold the plant building and the surrounding property for \$755,000.

*Reid Gardner Project.* The Reid Gardner Power Plant (“RGS”), located near Moapa, Nevada, is operated by NV Energy (“NVE”) and consists of four coal-powered generators- Units 1 through 4. Units 1 through 3 are 100 percent owned by NVE, whereas the capital ownership of Unit 4 is shared between the Department and NVE at 67.8 percent and 32.2 percent, respectively. The Department also has a 29.2 percent share of RGS facilities necessary for and common to all four units. The Participation Agreement between the Department and NVE terminates in July 2013, and the Department will cease receiving energy from the plant at that time. Upon termination, NVE is required to refund the Department’s share of undepreciated capital improvement costs of Unit 4. Meanwhile, the Department also anticipates having a continuing obligation for a yet to be determined share of environmental remediation costs related to past soil and groundwater contamination at the site. (See “POWER OPERATIONS OF THE STATE WATER PROJECT – Reid Gardner Termination and Groundwater Contamination Cleanup.”)

*Bottle Rock Facilities.* The Bottle Rock Facilities are located in Lake County, California, about 70 miles north of San Francisco. The Bottle Rock Facilities consist of a geothermal powerplant with a 55 megawatt turbine-generator unit, associated electrical, mechanical and control facilities, a heat dissipation system, and a 1.1 mile transmission line. The Department suspended operation of and mothballed the powerplant in 1990 because of the lack of an adequate geothermal steam supply and sold the powerplant in 2001 for \$1.8 million.

*East Branch Enlargement – Phase I.* The East Branch of the California Aqueduct transports water from the aqueduct bifurcation downstream of the A. D. Edmonston Pumping Plant located about 10 miles east of the town of Gorman, across the Antelope Valley and the Mojave Desert, through the San Bernardino Mountains and the cities of San Bernardino and Riverside, to Lake Perris located about 14 miles south of Riverside. The existing facilities along the East Branch include 93 miles of canal, 6.7 miles of inverted siphons, Alamo Powerplant Unit 1, Pearblossom Pumping Plant, Silverwood Lake, San Bernardino Tunnel, Devil Canyon Powerplant Units 1 and 2, Santa Ana Valley Pipeline, and Lake Perris. In 1986, Metropolitan Water District of Southern California and many of the other East Branch contractors agreed to have the Department enlarge the East Branch to an ultimate capacity of 3,149 cubic feet per second at the Alamo Powerplant/Cottonwood Chute Bypass and 2,876 cubic feet per second at Pearblossom Pumping Plant. The Department and the Contractors agreed that the enlargement of the East Branch would be done in two phases, each providing approximately half (750 cubic feet per second) of the planned capacity increase based on a 1,500 cubic feet per second enlargement. This work included an increase to the height of the canal lining, additional siphon conduits, additional pumps at the Pearblossom Pumping Plant, portions of Units 2 and 3 at the Mojave Siphon Powerplant, Units 3 and 4 at the Devil Canyon Powerplant. Construction of Phase I was completed in 1996.

*Additional East Branch Improvements.* Several additional improvements to the East Branch were constructed concurrently with Phase I of the enlargement. The improvements were needed to bring the existing East Branch up to its originally intended design capacity and to improve the reliability of the system. The major improvements include a portion of a four-foot increase in the height of the canal lining between the Alamo Powerplant and the Pearblossom Pumping Plant, and the addition of a spare pump and modification of the forebay at the Pearblossom Pumping Plant. Construction of these additional improvements was completed in 1993.

*Delta Pumping Plant Completion.* This project includes the Harvey O. Banks Delta Pumping Plant and the John E. Skinner Delta Fish Protective Facility. Originally the pumping plant was designed for 11 units, but only seven were installed initially. In 1986, the Department signed an agreement with DFW to mitigate or offset direct fishery losses caused by State Water Project pumping under which the Department provides funds for projects inside and outside of the Delta. With this agreement in place, the Department has completed the Delta pumping plant by installing an additional four pumps. The fish protective facility was also enlarged to accommodate the increased capacity. Installation of the four units and the enlargement of the fish protective facility was completed in 1992.

*Suisun Marsh Environmental Facilities.* The Suisun Marsh Environmental Facilities are designed to protect the quality of water in the Suisun Marsh on the west side of the Delta. These facilities are designed to mitigate the effects of the CVP, the State Water Project, and a portion of other upstream diversion projects. The first two of six proposed phases were completed in 1988, when the Suisun Marsh Salinity Control Gates, located at the southeast corner of the marsh, were operated for the first time. In April 1995, the Department and the Bureau stopped their planning and environmental documentation for additional western marsh facilities because the water quality objectives in the State Board's water quality standards for the Delta and the related order amending Decision-1485 will result in lower salinities in Suisun Bay and Suisun Marsh. In D 1641, the State Water Resources Control Board formally relieved the

State Water Project of its responsibility for meeting objectives at one western station (S97), converting this compliance location to a monitoring station.

*San Bernardino Tunnel Intake Structure.* A new intake tower was constructed near the southeastern shore of Silverwood Lake to replace the existing tower, which did not meet current seismic standards. Construction was completed in 1997.

*San Luis Rock Quarry.* The Department and the Bureau have acquired 689 acres of property adjacent to San Luis Dam. The property includes a rock quarry as a source of material for repair and maintenance purposes.

*Castle Rock-Lakeville Transmission Line.* Jointly owned with the Pacific Gas and Electric Company (“PG&E”) and two other utilities, the 38-mile Castle-Rock-Lakeville 230 kv transmission line provides transmission from the Geysers geothermal area where the Bottle Rock and South Geysers Projects are located. The Department has sold the South Geysers Project and the Bottle Rock Project. Currently, neither project is operational. (See “WATER SYSTEM PROJECTS – Project Descriptions – *South Geysers Project*” and “– *Bottle Rock Facilities.*”)

*Midway-Wheeler Ridge Transmission Line.* Jointly owned with PG&E, this 608 megawatt, 230 kilovolt transmission line extends 47 miles from Midway Substation to the Wheeler Ridge Substation and serves the Buena Vista, Wind Gap and Wheeler Ridge pumping plants.

*Kern Water Bank.* The Kern Water Bank was the land acquisition phase of the development of a ground water recharge and extraction facility in Kern County on the alluvial fan of the Kern River. The Department acquired approximately 20,500 acres of land for the Kern Water Bank. Under the Monterey Amendment, the land and related assets of the Kern Fan Element of the Kern Water Bank have been transferred by the Department to Kern County Water Agency, which in turn transferred such land and related assets to a joint powers authority formed by Kern County Water Agency and other local water suppliers. (See “WATER SUPPLY CONTRACT RELATED LITIGATION – Monterey Amendment Litigation” for a description of certain litigation regarding the validity of the Monterey Amendment and the agreement to transfer the land and related assets of the Kern Fan Element of the Kern Water Bank.) The Department will continue to charge Contractors under the Water System Revenue Bond amendment the amounts related to the Water System Revenue Bonds issued to finance the Kern Water Bank.

*Vista del Lago Visitor Center.* The Vista del Lago Visitor Center is located on an overlook above Pyramid Lake along Interstate 5 approximately 60 miles north of Los Angeles. The center includes educational exhibits on the importance of water supply and the development, distribution, conservation and treatment of water.

*North Bay Aqueduct – Phase II.* The North Bay Aqueduct – Phase II project completed the construction of the 27 mile North Bay Aqueduct from the Delta to Napa and Solano Counties at the northern edge of the San Francisco Bay. The project consists of 23 miles of pipeline and two pumping plants between Barker Slough on the Delta and the existing Phase I facilities at Cordelia. The project became operational in 1988.

*Project Monitor and Control System.* In July 1990, the Department installed a fiber optics communication system. This system replaced the Department’s obsolete copper wire system. This system reduced costs and increased the reliability, efficiency and capacity of the communication system. A major element of the fiber optics system was the installation of a fiber optics cable adjacent to the California Aqueduct for both commercial and State Water Project use. In 1994, the Department upgraded the backup computer for the Project Operations Control Center. The Department relocated the Control

Center in 1995. In 1997, the Department installed additional electronic control, instrumentation and communication equipment.

*Coastal Branch – Phase II.* The Coastal Branch – Phase II consists of approximately 100 miles of pipeline between the existing Phase I terminus in Kern County near Devil’s Den and a terminus located approximately 3.2 miles south of the town of Casmalia, California, on Vandenberg Air Force Base, and includes three pumping plants and related facilities and three water storage tanks. Construction was completed in 1997. This Water System Project is currently operated and maintained for the Department by the Central Coast Water Authority.

*East Branch Extension – Phase I.* The East Branch Extension facilities are being constructed in two phases. Phase I consists of new pipelines, three pump stations, a reservoir, and other appurtenant facilities between the existing Foothill Feeder downstream of Devil Canyon Powerplant and the terminus at the Noble Creek Spreading Grounds near the City of Beaumont in Riverside County. The new facilities join existing conveyance facilities constructed by the San Bernardino Valley Municipal Water District and allow the San Gorgonio Pass Water Agency to receive deliveries of State Water Project water. Construction of Phase I facilities was completed in 2003.

Reserve pump units were also added to Greenspot, Crafton Hills and Cherry Valley pump stations to provide increased pumping reliability. The preliminary work for installation of these units began in 2005 and the installation was completed in June 2008.

*East Branch Extension – Phase I Improvements.* The East Branch Extension – Phase I Improvements project includes the enlargement of the Crafton Hills Reservoir and construction of the Yucaipa Connector Pipeline. The existing reservoir will be enlarged from 85 acre-feet to approximately 220 acre-feet to provide operational flexibility, system reliability, and a reduction in energy impacts and costs. Enlargement of the reservoir will allow the Department to fill the reservoir during off-peak periods of the day. Construction of the connector pipeline will allow continued deliveries of water in the East Branch Extension while the reservoir is being enlarged and during future outages of the reservoir. Construction of the pipeline and reservoir began in 2010 and is scheduled to be completed in 2013.

*South Bay Aqueduct Rehabilitation.* The South Bay Aqueduct was constructed in the early 1960’s. After nearly 30 years of operation, it was in need of numerous repairs and rehabilitation work. It was also necessary to make improvements to the original system to accommodate environmental and operational requirements. The repairs consisted of work items such as replacement of old, deteriorating valves, repairs to pipe linings at numerous locations, complete replacement of the lining of the two steel discharge lines at South Bay Pumping Plant, and repairs to access structures that had been flooded numerous times due to their proximity to existing drainages. The improvements included adding a guard valve at all blow off structures (to allow for future valve repairs/replacements without dewatering the pipeline), adding a second air valve at all high points in the pipelines, constructing access structures at numerous locations where access manholes were buried (prior to environmental considerations related to access), and raising the tops of access structures to prevent future overtopping during high flows in drainages. The project was completed in 2004.

The following Water System Projects have not yet been completed:

*East Branch Enlargement – Phase II.* The Phase II enlargement, which will increase the capacity of Pearblossom Pumping Plant from 2010 cfs to 2876 cfs, has been indefinitely suspended at the request of the related Water Contractors. The Phase II enlargement consists of canal embankment and concrete lining; constructing additional siphon barrels; adding bays to check structures; adding two pump/motor

units and a discharge line at Pearblossom Pumping Plant; raising overcrossing structures such as bridges, pipelines, and overchutes; adding a second turbine at Alamo Powerplant; and extending underdrains.

*North Bay Aqueduct Improvements – Terminal Tanks.* The 7.2 million gallon Napa Turnout Reservoir was constructed by the Department in 1968 to deliver raw water to the Jamieson Canyon Water Treatment Plant and also served the American Canyon Water Treatment Plant. The Department replaced the then existing tank with two new 5 million gallon tanks in 2010.

*North Bay Aqueduct Alternate Intake Project.* The North Bay Aqueduct Alternate Intake Project will include the construction of a new point of diversion along the Sacramento River or its tributaries, a new pumping plant, an inline storage tank, and up to 30 miles of underground pipeline that will connect to the existing North Bay Aqueduct. The estimated capacity of the new facilities is 240 cfs. The purpose for this project is to enhance the quality, reliability and quantity of water deliveries to State Water Project Contractors while reducing impacts to endangered aquatic species. Solano County Water Agency and Napa County Flood Control and Water Conservation District receive water from the North Bay Aqueduct.

Phase I of this project included work by the Department and environmental consultants to develop required State and federal environmental documentation, acquire temporary entry permits and conduct environmental surveys leading to a Notice of Determination (“NOD”) and Record of Decision (“ROD”), to acquire project environmental permits. Work on Phase I is scheduled to be completed in 2014. Phase II of this project is expected to begin once the NOD and ROD are filed and includes acquisition of the necessary land and right of way, the design and construction of this project. Phase II is expected to be completed by December 2020.

*Communications System Replacement.* In 2004, the Department began replacing the existing communications system for the State Water Project. The new communications system equipment will be installed at the various area control centers, plants, and check structures along the aqueduct and at other various operation, administration and headquarters facilities. Leased back-up facilities will also be upgraded. This project is anticipated to be completed in 2016.

*Arroyo Pasajero Flood Control Project.* The Arroyo Pasajero Flood Control Project consists of facilities and measures designed to protect the California Aqueduct from flood waters and sediment carried by the Arroyo Pasajero Creek and the Cantua Creek Stream Group located near the town of Coalinga in Fresno County, California. This project is expected to be completed in 2015.

*Hyatt Pump-Turbine Refurbishment.* The Hyatt Powerplant is located on the Feather River near the town of Oroville, in Butte County, California. The Powerplant is located within Oroville Dam. It is an underground facility with three reversible pump-turbine units and three turbine units. This refurbishment work improved unit availability and reliability, and increased efficiencies to the highest extent possible while reducing potential environmental concerns. The major refurbishment work was completed in September 2007 and consisted of replacing the runners, wicket gates, bushings, shaft sleeves, guide bearings, and refurbishing water passages.

*Edmonston Pump Replacement.* The A.D. Edmonston Pumping Plant has 14 pump units used to pump California Aqueduct water over the Tehachapi Mountains into Southern California. The plant was designed with the capacity to convey 2.5 million acre-feet of Annual Table A Amounts (defined below) to Southern California. In recent years, the plant has been pumping near its maximum capacity; therefore, the units’ reliability and availability have become extremely critical to the objectives of the State Water Project. The main objectives of the replacement project are to increase pump reliability, availability, and efficiency while reducing maintenance needs. In August 2001, the design was started to replace the four

defective pumps. The first pump was completed in June 2007. The installation and testing of the remaining three pumps was completed in 2011.

*Delta Facilities Program.* The Delta Facilities Program consists of projects and measures in the Sacramento-San Joaquin Delta area and in the vicinity of rivers and tributaries to rivers that flow into the Sacramento-San Joaquin Delta that are designed to (1) increase water supply by increasing the efficiency of water transfer through the Delta, (2) improve water quality, and (3) reduce or mitigate for fish losses caused by pumping. The projects and measures include dredging, channel improvements, flow control structures, seismic studies and environmental mitigation measures.

*Tehachapi East Afterbay.* The Tehachapi East Afterbay Project (“TEA”) provides additional afterbay storage for the Valley String Pumping Plants (Buena Vista, Teerink, Chrisman, Edmonston). The previous Tehachapi Afterbay (Pool 42) consisted of the canal section from Porter Tunnel, which bifurcates to the West Branch to Oso Pumping Plant and to the East Branch to Alamo Powerplant and Cottonwood Chutes. The Tehachapi East Afterbay, located adjacent to the existing Tehachapi Afterbay, provides storage accessible to both the East Branch and to a lesser extent, the West Branch. The additional storage provided by the TEA reduces power costs by shifting on-peak power consumption to off-peak, increasing ancillary services capability, and providing other benefits of increased operational flexibility. Operation of the TEA began in 2006 and construction was completed in 2007. Replacement of an Antelope Valley – East Kern Water Agency turnout that was removed during construction has recently been approved. Design is underway and construction of the replacement turnout should be completed by July 2014.

*Perris Dam Remediation Program.* Perris Dam Remediation Program contains three main project components: dam foundation remediation, outlet tower retrofit/replacement, and emergency outlet conveyance extension. Each project component requires examining numerous operational and remedial alternatives, cost analyses, scheduling, cost estimating, selecting the preferred alternative, required environmental permitting and documentation, preliminary to the final design, construction, and program closeout. This program is required due to a 2005 Department study that concluded that roughly 2,300-feet of the left reach of Perris Dam’s foundation was potentially liquefiable when subjected to a maximum credible earthquake. In late 2005, the Department lowered the water level in the reservoir by about 25 feet and reduced the amount of water stored in the reservoir to about 75,000 acre-feet as the Department evaluates alternatives for repair of the dam. A subsequent 2006 Department study concluded that the latest seismic loading would also potentially subject the outlet tower to shear failure. Lastly, the construction of thousands of new homes immediately downstream of the Perris Dam requires facility improvements to channel reservoir releases to the Perris drain in an emergency event. In December 2006, the Department completed a study identifying various repair options, began additional geologic exploration along the base of Perris Dam and started preliminary design. The Department’s preferred alternative is to repair the dam to restore the reservoir to its historical level. Water stored in Lake Perris is used primarily by Metropolitan. Accordingly, Metropolitan likely would be the major contributor toward the cost of repair or replacement of Perris Dam under its State Water Contract. The Department released its draft EIR in January 2010 and final EIR in September 2011. This program is currently anticipated to be completed in 2016. However, in December 2011, an individual filed a lawsuit against the Department challenging the Department’s compliance with CEQA, including the adequacy of the EIR for the remediation program. This lawsuit could delay the remediation.

*Facilities Repair and Improvement Project.* The Facilities Repair and Improvement Project consists of reconstructions, additions and betterments to water conservation or transportation facilities existing as of January 1, 1987, and to all other facilities described in the Water System Revenue Bond Amendment of the Water Supply Contracts. (See “THE WATER SUPPLY CONTRACTS –

Amendments Providing Certain Revenues to Pay Water System Revenue Bonds.”) This project is anticipated to be completed in 2022.

*Project Planning Costs.* The Department will be reimbursed for the costs of study or planning of potential Water System Projects. Among the facilities that have been or may be studied are the Coastal Branch of the California Aqueduct; the Arroyo Pasajero Flood Control Project; the Delta Facilities Program; and additional conservation facilities. When the Department determines the actual facility to be acquired and constructed in any given case and that such facility will be financed with Bonds, such facility is designated as a Water System Project.

*East Branch Extension – Phase II.* Current East Branch Extension Phase I pumping capacity is limited to less than one-half of its total pumping capacity due to the size of the San Bernardino Valley Municipal Water District pipeline. East Branch Extension Phase II will allow 100 percent pumping capacity and will consist of approximately six miles of a new Mentone pipeline, a new Citrus pump station, a new Citrus Reservoir, an enlargement of the Crafton Hills Pump Station, and an additional pump unit for the Cherry Valley Pump Station. East Branch Extension Phase II reconnaissance level planning began in 2002. Work on the EIR and preliminary design started in 2006, final design began in 2008 and construction is anticipated to begin in 2012. Completion of the Phase II facilities is anticipated in 2015.

*South Bay Aqueduct Enlargement and Improvement.* The South Bay Aqueduct Enlargement will provide the additional capacity required to meet projected increases in water demand in the service area of Alameda County Flood Control and Water Conservation District, Zone 7. The South Bay Aqueduct Improvement will increase the existing capacity to provide the original design capacity of the South Bay Aqueduct. The South Bay Aqueduct Enlargement and Improvement work is being incorporated into a combined project to minimize overall costs and impacts. Major features include enlargement of the South Bay Pumping Plant; construction of a third discharge line and surge tank; construction of the 500 acre-foot Dyer Reservoir; seismic improvements to surge tanks 1 and 2, and modifications to the canal. Construction on the pumping plant and the discharge line began August 2006 and in 2007, respectively. Construction of Dyer Reservoir, the canal modifications and a 69 kv transmission line from Banks Pumping Plant to South Bay Pumping Plant began in 2009. Overall project work is scheduled to be completed in 2013.

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# State Water Project Facilities

## PUMPING PLANTS

Name	Number of Units	Normal Static Head (feet) (a)	Total Flow at Design Head (cfs)	Total Motor Rating (hp)
Hyatt	3	465-694	5,610	519,000
Thermalito	3	85-102	9,120	120,000
North Bay Aqueduct				
Barker Slough	9 (b)	95-120	228	4,800
Cordelia	11 (b)	110-376	138	
South Bay Aqueduct				
South Bay	9	543-563	510	27,750
Del Valle	4	0-38	120	1,000
California Aqueduct				
Banks (SWP SHARE)	11	236-252	10,670	333,000
Gianelli (SWP SHARE)	8	99-327	11,000	504,000
Dos Amigos (SWP SHARE)	6	107-125	15,450	240,000
Buena Vista	10 (b)	205	5,405	144,500
Teerink	9 (b)	233	5,445	150,000
Chrisman	9 (b)	518	4,995	330,000
Edmonston	14 (b)	1,926	4,480	1,120,000
Pearblossom	9	540	2,575	203,200
West Branch				
Oso	8	231	3,252	93,800
Coastal Branch				
Las Perillas	6	55	461	4,050
Badger Hill	6	151	454	11,750
Devil's Den	6 (b)	521	134	10,500
Bluestone	6 (b)	484	134	10,500
Polonio Pass	6 (b)	533	134	10,500
East Branch Extension				
Greenspot	4	382	70	3,900
Crafton Hills	3	613	60	4,000
Cherry Valley	2	75	32	300

(a) Amount is for plant in pumping mode.  
(b) Includes spare unit.

## POWERPLANTS

Name	Number of Units	Normal Static Head (feet) (a)	Total Flow at Design Head (cfs)	Net Dependable Capacity (MW)	Nameplate Capacity (MW)
Hyatt	6	435-694	16,950	645	645
Thermalito	4	85-102	17,400	114	114
Gianelli					
Total	8	99-327	16,960	363	424
SWP Share			190	222	
Alamo	1	115-141	1,740	15	17
Mojave Siphon	3	81-136	2,880	29	30
Devil Canyon	4	1,406	2,940	235	276
Warne	2	719-739	1,564	67	74
Castaic					
Total	7	900-1,050	20,820		
SWP Share			1,128	1,254	
Thermalito Diversion Dam	1	63-77	615	3	3
Reid Gardner, Unit No. 4 (b)					
Total	1			234	275
SWP Share					186

(a) Amount is for plant in generating mode.  
(b) Reid Gardner is a coal-fired plant. The Department will no longer receive energy after the Participation Agreement with NV Energy terminates in July 2013.

## PRIMARY RESERVOIRS and DAMS

Name	Reservoirs (a)		Dams	
	Capacity (acre-feet)	Surface Area (acres)	Structural Height (feet)	Crest Length (feet)
Antelope Lake	22,564	930	120	1,320
Frenchman Lake	55,475	1,580	139	720
Lake Davis/ Grizzly Valley Dam	84,371	4,030	132	800
Lake Oroville	3,537,577	15,805	770	6,920
Thermalito Forebay	11,768	630	91	15,900
Thermalito Afterbay	57,042	4,300	39	42,000
Thermalito Diversion Pool	13,353	320	143	1,300
Clifton Court Forebay	31,258	2,180	30	36,500
Bethany	5,070	180	121	3,940
Lake Del Valle	77,100	1,060	235	880
San Luis Reservoir/Sisk Dam SWP Storage (b)	2,027,835	12,520	385	18,600
SWP Storage (c)	1,062,183			
O'Neill Forebay SWP Storage (c)	56,433	2,700	88	14,350
SWP Storage (c)	29,500			
Los Banos	34,562	620	167	1,370
Little Panoche	5,580	190	152	1,440
Quail Lake (d)	7,580	290		
Pyramid Lake	171,200	1,300	400	1,090
Elderberry Forebay	32,480	500	200	1,990
Castaic Lake	323,700	2,240	425	4,900
Silverwood Lake/ Cedar Springs Dam	74,970	995	249	2,230
Lake Perris	131,450	2,320	128	11,600
Crafton Hills (e)			95	500

(a) Reservoir data represent design elevation, generally spillway crest level. In most cases, maximum operational levels are set 1 or 2 feet lower.  
(b) SWP share of total storage of 2,027,835 acre-feet.  
(c) SWP share of total storage of 56,433 acre-feet.  
(d) Primary reservoir only.  
(e) Primary dam only.

## AQUEDUCTS

Name	Length (miles)
Grizzly Valley Pipeline	6.0
Thermalito Power Canal and Tail Channel	3.4
North Bay Aqueduct	27.6
South Bay Aqueduct	44.6
<b>Subtotal</b>	<b>81.6</b>
Edmund G. Brown California Aqueduct (main line):	
Delta to O'Neill Forebay	66.7
O'Neill Forebay to Kettleman City (joint use)	105.7
Kettleman City to Edmonston Pumping Plant	121.0
Edmonston Pumping Plant to Tehachapi Afterbay	10.0
Tehachapi Afterbay to Lake Perris	140.0
<b>Subtotal, main line</b>	<b>443.4</b>
California Aqueduct (branches):	
West Branch	31.9
Coastal Branch	115.5
East Branch Extension	
Devil Canyon Powerplant to Greenspot	16.2
Greenspot to Noble Creek Terminus	16.4
<b>Subtotal, branches</b>	<b>180.0</b>
<b>Total</b>	<b>705.0</b>

# State Water Project Facilities

## WATER SUPPLY CONTRACTORS

- Plumas Co. Flood Control & Water Conservation District
- County of Butte
- City of Yuba City
- Napa Co. Flood Control & Water Conservation District
- Solano Co. Water Agency
- Alameda Co. Flood Control & Water Conservation District Zone 7
- Alameda Co. Water District
- Santa Clara Valley Water District
- Oak Flat Water District
- Dudley Ridge Water District
- County of Kings
- Empire West Side Irrigation District
- Tulare Lake Basin Water Storage District
- San Luis Obispo Co. Flood Control & Water Conservation District
- Kern County Water Agency
- Santa Barbara Co. Flood Control & Water Conservation District
- Ventura Co. Watershed Protection District
- Castaic Lake Water Agency
- Antelope Valley - East Kern Water Agency
- Palmdale Water District
- Little Rock Creek Irrigation District
- Mojave Water Agency
- Crestline - Lake Arrowhead Water Agency
- San Bernardino Valley Municipal Water District
- San Gabriel Valley Municipal Water District
- The Metropolitan Water District of Southern California
- San Geronio Pass Water Agency
- Desert Water Agency
- Coachella Valley Water District

● Reid Gardner Powerplant Nevada Power Company Las Vegas





