

LOCAL WATER SUPPLY DEVELOPMENT PROGRAM
INFORMATION/APPLICATION PACKAGE
FOR
DESALINATION PROJECTS
JULY 2010

PREPARED BY
THE SAN DIEGO COUNTY WATER AUTHORITY



**SAN DIEGO COUNTY WATER AUTHORITY
LOCAL WATER SUPPLY DEVELOPMENT PROGRAM**

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FOR

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**SAN DIEGO COUNTY WATER AUTHORITY
LOCAL WATER SUPPLY DEVELOPMENT PROGRAM**

I. BACKGROUND

The San Diego County Water Authority (Water Authority) was founded in 1944 to import supplemental water to the San Diego region. The Water Authority is comprised of 24 member agencies, which either directly or indirectly purchase water for use at the retail level.

The Water Authority and its member agencies are engaged in a long-term effort to diversify the regions water supplies. The Water Authority anticipates the development of approximately 40,000 acre-feet per year (AFY) of recycled water; and 11,000 AFY, or more, of brackish groundwater recovery; and 56,000 AFY of desalinated seawater, or more, within its service area by the year 2015.

In 1991 the Water Authority established the Reclaimed Water Development Fund (RWDF). The RWDF provided agencies an initial financial contribution of up to \$100 per acre-foot of recycled water produced and beneficially reused within the Water Authority's service area. In September 2005, the RWDF incentive level was increased to \$147.00/AF.

In November 2006, the RWDF Program was further modified to provide up to \$200 per acre-foot of recycled water and potable water produced from brackish or otherwise contaminated groundwater. The inclusion of funding for groundwater recovery projects necessitated a change in the Water Authority's financial incentive Program from the RWDF Program to the Local Water Supply Development (LWSD) Program.

In February 2008, the LWSD Program was again amended to expand eligibility to include seawater desalination projects and adopt program guidelines and funding principles to govern the determination of member agency financial need for seawater and brackish groundwater desalination projects.

The LWSD Program is a discretionary program of the Water Authority. After determination of eligibility, including determination of a financial need according to the program guidelines, each potential project requires the approval of the Water Authority Board of Directors.

II. PURPOSE

The purpose of the LWSD Program is to promote the development of cost-effective water recycling and desalination projects that prevent, or reduce a demand for, imported water and improve regional water supply reliability.

III. DEFINITIONS

Desalination: means an advanced treatment process designed to remove salts from brackish groundwater or seawater in order to produce potable drinking water.

Project: means the Project for production and/or delivery of desalinated Water.

Agency: means the public agency that owns and operates, or proposes to own and operate, the Project. The Agency may or may not be a member agency of the Water Authority.

Project Sponsor: is the member agency of the Water Authority whose service area is served by the Project.

End User: means each of the ultimate users or agency that purchases the desalinated water produced by the Project.

Beneficial Use: means the use of water supplied by the Project to supplement or offset imported potable-water supply demands and/or provide a water supply for industrial or commercial purposes.

Project Yield: means the actual amount of desalinated water, measured in acre-feet, which is produced by the Project in any given year, and which is used within the Water Authority's service area. Allowable Project Yield (Yield) shall exclude any water that will not reduce a demand for potable water or raw water from the Water Authority.

Project Costs: means the actual Project cost to produce an acre-foot of desalinated water beneficially used and is comprised of three components: Annualized Capital Costs, Annualized Operation and Maintenance (O&M) Costs and Annualized Replacement Costs. Project Costs exclude the cost of existing facilities and the cost of those Project components directly funded by grants or contributions.

Capital Cost Values: means the actual cost of the development of the brackish groundwater or seawater desalination and water treatment facility, the distribution system (to the point of the agency's existing distribution system or the Water Authority's aqueduct system), and the debt service associated with the construction of these facilities. The capital costs can also include costs for improvement of the member agency's distribution system that are directly attributable to receiving delivery of the desalinated water from the project.

Incentive Rate: will be recalculated annually based on the difference between eligible costs incurred (calculated as unit cost) and the Water Authority's melded (bundled) treated-water rate (including supply, treatment, storage, customer

service, and transportation components); or in the case of a purchase contract, the net unit contract purchase rate. The incentive rate will be between \$0 and \$200 per acre-foot of potable water produced or replaced over a 25-year term.

Unit Contract Purchase Rate: means the net contracted price for water purchased by the agency.

LWSD Program: means the San Diego County Water Authority's Local Water Supply Development Program.

LISA Program: means the San Diego County Water Authority Local Investigations and Studies Assistance Program

IV. ELIGIBILITY CRITERIA

To qualify for LWSD Program incentives, Agency must meet the following eligibility criteria:

1. New Water Supply

Agency must demonstrate that the Project will result in a new water supply that will reduce demands on the Water Authority for imported water. Desalinated seawater or brackish groundwater production that will not reduce demands on the Water Authority (e.g., water deliveries that reduce or replace recycled water usage) do not qualify for LWSD Program incentives. Groundwater supplies that historically did not require treatment, but now require treatment as a result of recent contamination issues, may also be eligible to receive LWSD Program incentives and will be evaluated on a case-by-case basis.

Metering devices shall be installed and owned, operated and maintained by Agency, or the Water Authority, for those deliveries wheeled through the Water Authority's aqueduct, for the purpose of measuring Yield. Each meter shall be read in accordance with the Agency's or the Water Authority's regular billing cycle for purposes of billing and accounting between the Parties to determine at the beginning of each billing cycle the quantity of desalinated water produced and delivered during the preceding billing cycle.

For water purchases, Agency shall be responsible for reporting to the Water Authority monthly at the beginning of the Water Authority's billing cycle the amount of water purchased the preceding month.

Agency shall install metering devices to determine the quantity of raw or potable water, if any, that was blended with desalinated water and delivered during each billing cycle by Agency-owned meters. Agency will be responsible for ensuring that all metering devices are properly installed, calibrated, and maintained. The

Agency shall be solely responsible for the accuracy of Agency-owned meter readings. Water Authority reserves the right to review the meter readings and may request independent meter accuracy testing. The costs of any independent meter test will be divided equally between Water Authority and Agency.

2. Financial Need

The LWSD Program provides financial incentive to member agencies to develop reliable brackish groundwater and desalinated seawater supplies that are currently more expensive than the melded cost of imported water purchased from the Water Authority. The program promotes the development of cost-effective water supply projects that prevent, or reduce a demand for imported water and improve regional water supply reliability.

Financial need will be based on a comparison of the unit cost to the agency, either the net unit cost of production and delivery, or in the case of a purchase contract, the unit net contract purchase rate, versus the Water Authority's melded (bundled) treated water rate (including supply, treatment, storage, customer service, and transportation components). For agencies using a net contract purchase price to qualify, the Water Authority will evaluate the reasonableness of the contract purchase price when compared to the costs of comparable supplies. This evaluation will also take into account the net cost of production and delivery for the Project. After consultation with the Agency, the Water Authority may adjust the net contract purchase price in determining financial need.

From this calculation of the unit cost to the Agency, financial need will be determined and an incentive rate calculated.

Once the Project has demonstrated financial need and Water Authority funding commences, Agency shall make available for inspection by Water Authority, upon reasonable advance notice, all records, books and other documents relating to the operation of the Project. Additionally, Water Authority, at its sole discretion, may conduct an annual financial review of the Project to determine whether the Project continues to meet the financial need criteria (see Section VI).

3. Project Sponsor

An agency that is not a member agency of the Water Authority must be sponsored by a Water Authority member agency (or agencies) within whose service area(s) the Project is located. The Project Sponsor will be party to any agreement approved by the Water Authority Board of Directors (Board). LWSD Program incentives will be provided as a credit on the Project Sponsor's water bill, or, at the Water Authority's discretion, a reimbursement check will be issued directly to the Agency.

4. Compliance with Regulatory Requirements and Laws

Agency shall ensure that all desalinated water produced, treated, and delivered by the Project is used in compliance with all applicable federal, state and local statutes, ordinances, regulations and other requirements. Additionally, the Agency must demonstrate that appropriate regulatory and public health permits have been, or will be, obtained.

Agency shall demonstrate that it has a permit or the legal right to extract groundwater that will be added to its water supply and distributed to its customers. The agency shall also demonstrate compliance with all applicable laws and regulations associated with the extraction, replenishment, management, treatment, and distribution of groundwater or ocean water.

5. California Environmental Quality Act

Agency shall ensure that the Project complies with the provisions of the California Environmental Quality Act (CEQA). Water Authority shall not be obligated to make any payments for Yield from any component of a Project that does not comply with CEQA requirements.

6. Technical Development

Prior to applying for LWSD Program incentives, Agency must complete a sufficient level of technical and financial planning to allow Water Authority staff to determine whether the Project complies with the eligibility criteria outlined above.

V. CALCULATION OF CONTRIBUTION RATE AND METHOD OF PAYMENT

The following conditions govern the calculation of the Contribution Rate and the payment of incentives:

1. Agreement

Agency and Project Sponsor, if applicable, must enter into an agreement with Water Authority prior to the allocation of any funds under the LWSD Program. The agreement will establish the terms governing the payment of LWSD Program incentives, the role of the Agency and Project Sponsor, liability clause, and other related matters.

The term of the agreement will be 25 years from the date the Project begins deliveries. Agency will be eligible to receive funding during each of the 25 years, or until the Project no longer qualifies to receive LWSD Program incentives. If the Project does not demonstrate a financial need in any given year, then funding will not be allocated for that specific year.

2. Maximum Contribution Rate

The Maximum Contribution Rate is currently set at \$200 per acre-foot of Yield. The Maximum Contribution Rate may be adjusted periodically by Water Authority Board of Directors, and is based upon Water Authority's actual and projected costs of acquiring additional water supplies.

3. Contribution Rate

Contribution Rate for an acre-foot of Yield will be established annually by Water Authority for each Project deemed eligible for LWSD Program incentives. Contribution Rate will be determined based on the specific financial need of Project and may be less than the Maximum Contribution Rate.

4. Unit Contract Rate

The unit contract rate shall be the weighted average rate paid by the Agency during the fiscal year.

5. Calculation of Contribution Rate

At the end of each fiscal year, Water Authority will conduct a financial review of the Project to determine differences between Project's net unit cost of production and delivery, or in the case of a purchase contract, the unit contract purchase rate; and Water Authority's melded (bundled) treated water rate (See Section VI).

6. Method of Invoicing and Payment

Agency shall invoice Water Authority monthly for the Yield, based upon the quantities billed to End Users during the previous month. Billings shall be based upon meter Agency reporting or readings at each and every connection of the Project to End User.

Contribution Rate disbursements will be paid monthly based on the actual Yield during the previous billing cycle and the Actual Contribution Rate for the Project. Incentives to the member agencies will be provided in the form of a credit on their monthly Statement of Water Deliveries and Charges. If Agency receiving the credit is not a Water Authority member agency, a reimbursement check will be issued directly to the Agency by Water Authority.

7. Eligible Project Costs

"Annualized Capital Costs" shall be computed using only the following incurred costs by the Agency for the Project:

- Design and construction management service fees.

- Planning (excluding LISA-funded planning costs), design, and construction costs of the Project facilities, including water treatment facilities, wells, pumps, conveyance pipelines, pump stations, and storage facilities, etc.
- Agency administration of Project planning (excluding LISA-funded planning costs, design, construction, and start-up costs. These costs represent a reasonable overhead allocation that must be agreed upon with the Water Authority.
- Land, right-of-way and easements for the Project.
- Environmental documentation (excluding LISA-funded costs) and mitigation measures directly related to the implementation or operation of Project and required to comply with applicable environmental permits and laws, including but not limited to the California Environmental Quality Act, National Environmental Policy Act, AB32 (Greenhouse Gas Emissions), and the California and Federal Endangered Species Acts. Environmental documentation costs shall commence with the Notice of Preparation and conclude with the filing of the Notice of Determination.
- Annual debt service expense.
- All other costs not specified in the above section shall be excluded, unless previously approved by Water Authority.
- All capital contributions (e.g. Metropolitan and Water Authority incentives, grants, fees, charges, etc.) shall be offset "or netted" against the capital cost values for the purpose of computing the Annualized Capital Costs component.

“Operation and Maintenance Costs” for the applicable fiscal year shall be computed using only the following incurred costs by Agency for Project:

- Professional consulting service fees for Project operation, maintenance and audit.
- Agency labor costs and/or contract costs (rate based on current market rate).
- Chemicals and supplies for Project operation and maintenance.
- Net electrical energy (recovery energy shall be deducted from energy purchased) for eligible facilities and distribution system operations. Water Authority shall not pay for electrical energy costs if Agency fails to install metering devices.
- Contractor services and supplies for Project facilities, operation and maintenance, and repair to maintain reliable system operation and achieve regulatory compliance.
- Monitoring required by permits, including water quality sampling and analysis of water produced by Project.
- All other costs not specified in the above section shall be excluded, unless previously approved by Water Authority.

- All Operation and Maintenance contributions shall be offset against operating cost values for the purpose of computing the Operation and Maintenance Costs component.

“Replacement Costs” shall be computed on the following basis:

- Cost estimates for replacement of major Project parts exceeding \$100,000, will be subject to internal Water Authority staff review to determine the reasonableness of the submitted cost estimate.
- Project parts identified for replacement will have met or exceeded average lifecycles for that identified replacement part.
- Salvage value of replaced parts shall be offset against replacement costs.
- All contributions shall be offset against replacement cost values for the purpose of computing the Replacement Costs component.
- All other costs not specified in the section above shall be excluded, unless previously approved by the Water Authority.

Note: Water Authority may request explanations or a review of the detailed costs included in Agency’s submittal of eligible costs, however, Water Authority’s determination as to the validity of the costs is final.

VI. ANNUAL FINANCIAL REVIEW AND RECORD KEEPING

1. Annual Review

Water Authority will conduct an annual review of Eligible Project Costs or the Unit Contract Rate to determine the Contribution Rate for the Project. Water Authority will send the appropriate reporting forms to the Agency by November 1st of each year which will require providing estimated Project Costs for the current and upcoming fiscal year. Agency will also provide actual Project Costs and or Unit Contract Rates from the prior fiscal year. These forms must be submitted to the Water Authority by January 31st of each year. For the purpose of projecting future year costs, inflation factors and interest rates will be determined by the Water Authority.

Water Authority (or its authorized agent) shall have the right to physically examine the accounting and Project records of the Agency to verify Project Costs or Unit Contract Rates no less than every three years and will require an independent audit of those records. Agency will submit all requested materials to Water Authority no later than three weeks from the date of the initial request.

Notwithstanding the formula described above, the Contribution Rate for any year may be adjusted to reflect the results of any review/audit by Water Authority of the actual Project Costs or Unit Contract Rates during previous Project operation years.

2. Record Retention

Agency shall establish and maintain accounting records of all costs incurred for the construction, operation and maintenance, and replacement of parts for the Project as described in V. 6 - Eligible Project Costs. Accounting for the Project shall utilize generally accepted accounting principles and be consistent with the terms of this Application Package.

Agency's Project accounting records must clearly distinguish all costs for the Project from the Agency's other water production, treatment, and distribution costs. These records shall also be adequate to determine project yield in order to accomplish all cost calculations contemplated within the context of the Project.

Agency shall establish and maintain accounting records of all contributions including grants that offset "Eligible Project Costs."

Agency shall collect water production data for each fiscal year of the Project and retain records of that data based on metering requirements. In addition, Agency shall collect and retain records of the total annual amount of water conveyed outside Agency's service area using Project facilities. Agency shall keep all Project records for at least three years following the termination of this Project Agreement.

Water Authority shall have the right to audit water production data relevant to the terms of any Agreement entered into for a period of three fiscal years following termination of the Project Agreement. Water Authority may elect to have such reviews/audits conducted by its staff or by others, including independent accountants or engineers, as designated by Water Authority. Agency shall make available for inspection to the Water Authority or its designee, upon 30 days written notice, all records, books and other documents related to the determination of Project Yield. Based on the results of any independent review or audit, an adjustment for over or underpayment of Project Yield for each applicable fiscal year shall be paid by Water Authority or Agency within one year of determination after such adjustment. The costs of any independent review or audit shall be equally divided between the parties.

VII. PERFORMANCE PROVISIONS

Water Authority reserves the right to terminate the Project if construction has not commenced or the Allowable Yield is not delivered by a mutually agreed upon date (subject to bi-annual review). Water Authority, after consultation with Agency, may reduce its Contribution Rate by a factor equal to the percentage shortfall of the actual Allowable Project Yield to the Agency's projected targeted Allowable Project Yield or in some other manner that reflects the realistically attainable Yield for the Project.

VIII. TERM AND AMENDMENTS

The term of the Agreement shall be for twenty-five (25) years from the date the Project commenced delivery of water to End User, unless agreed to otherwise. In the event that for any year the Contribution Rate equals more than zero, the Agreement shall not be terminated, and no funds shall be owed to Agency by Water Authority.

In the event of an Agreement breach, the Water Authority reserves the right to cease advancing current and future funds and may seek reimbursement for previously advanced funds. Additionally, the breach may prohibit the Agency from participating in any future cooperative Agreements with the Water Authority.

Agreement may be modified through bilateral agreement between the parties. Any modifications made to the Agreement shall be confirmed in writing prior to performance of the change.

IX. INDEMINITY - HOLD HARMLESS

Agency agrees to defend, indemnify, and hold harmless the Water Authority, its officers, and employees, from all damage, injury, claims, demands, losses, and liability to the extent that the same are the result of Agency conducting the Project, or the negligence or willful misconduct of the Agency or any of its officers, employees or any other person acting pursuant to its control in performing the work under this agreement.

X. PROJECT APPLICATION

It is recommended that an agency submit a completed application package prior to the start of the construction bid process. The following information and documents must be submitted as part of the LWSD Program application package:

1. A letter from the Agency's General Manager requesting funding for the Project under the LWSD Program.
2. Engineering Report (Attachment A)
3. Project Fact Sheet (Attachment B)
4. An Agency that is not a member agency of the Water Authority must also submit a letter of sponsorship from the Water Authority member agency within whose service area the Project is located (Project Sponsor).

The information required for the LWSD Program is similar to that required for Metropolitan's LRP. The same supporting information can be used for both program applications.

ATTACHMENT A

LOCAL WATER SUPPLY DEVELOPMENT PROGRAM ENGINEERING REPORT

The purpose of the Engineering Report is to verify that the Project meets all of the Qualifying Criteria. Each proposed Project is unique and, therefore, may require more or less information to support its viability for inclusion in the LWSD Program. In any case, the Engineering Report, at a minimum, must include the following:

1. The source and quality of the seawater or brackish groundwater and its conformity with water quality requirements and other pertinent regulations and permits;
2. All existing and proposed facilities which may be used to produce, treat, and convey water under the Project;
3. A 8.5" x 11" or 11" x 17" map clearly identifying Project facilities for which funding is being requested such as, seawater intake, brackish groundwater extraction wells, conveyance, and treatment facilities; and groundwater monitoring well locations;
4. Capital cost estimate delineating the cost of each Project component and other related costs necessary to complete the construction of the Project; (The cost estimate should be in enough detail to enable Water Authority staff to conduct an independent cost analysis);
5. Operations and Maintenance (O&M) cost estimate including the anticipated annual costs for manpower and administration, chemicals, power, contractor services and supplies, water quality sampling expenses, and other items required to properly operate and maintain the Project facilities and to serve customers. O&M costs for existing facilities and operations if the proposed project is an expansion of an existing facility;
6. The interest rate and term of each funding component for Project construction, (i.e., state loan programs, bonds, certificate or participation, etc.);
7. A cash flow analysis for the Project for the first 25 years of Project operation including the annual yield, projected Unit Contract Rates (if applicable), debt service, O&M costs, and contributions received from other agencies, etc. for the proposed project or project expansion;
8. A copy of the environmental document (i.e., Final Negative Declaration, Environmental Impact Report, or Notice of Exemption), certificate of

approval by the Project Sponsor, notice of determination filed with the State Clearinghouse and/or the local County Clerk;

9. A copy of pertinent permits such as National Pollutant Discharge Elimination Permit (NPDES), Wastewater Discharge, Water Reclamation, Basin Plan Amendment, etc;
10. A copy of any water purchase agreement or contract with other entities or agencies for the sale of water produced by the Project, Project operation and maintenance, and any other matters related to Project;
11. A copy of the agency's Groundwater Management plan and any project references included as part of the management plan, if applicable.

ATTACHMENT B

**LOCAL WATER SUPPLY DEVELOPMENT PROGRAM
PROJECT FACT SHEET**

I. GENERAL PROJECT INFORMATION:

A. Project Title: _____

B. Location: _____

II. CONTACT INFORMATION:

A. Project Sponsor: _____
(SDCWA Member Agency)

B. Agency: _____

C. Agency Contact
and Title: _____

D. Mailing Address: _____

E. Telephone No.: _____ Fax No.: _____

F. E-Mail Address: _____

III. PROJECT DATA:

A. Project Completion Date: _____

B. Estimated Date Project Begins Deliveries: _____

C. Maximum Yield (Acre Feet Per Year): _____

D. Engineer's Cost Estimate: _____

E. Major Proposed Funding Amounts and Sources: _____
