ENVIRONMENTAL
DEFENSE FUND

California Office
Rockridge Market Hall
5655 College Ave.
Oakland, CA 94618
(510) 658-8008
Fax: 510-658-0630

THE MONTEREY AGREEMENT PRINCIPLES:
Issues, Concerns, and Opportunities

Joint Interim Hearing of the
Senate Committee on Agriculture and Water Resources and the
Assembly Committee on Water, Parks, and Wildlife

San Jose, California
November 17, 1995

Mr. Chairmen and Members of the Committees:

My name is David Yardas. I am a Water Resources Analyst with the Environmental Defense Fund (EDF) in Oakland. I appreciate the opportunity to speak to you today on the Monterey Agreement, a set of principles agreed to by State Water Project (SWP) contractors and the Department of Water Resources (DWR) in December 1994, about two weeks prior to signing of the Bay/Delta Accord.

I especially want to thank you for responding so quickly to our request last month (in Fresno) for legislative oversight hearings on these Principles, for which a Final Program Environmental Impact Report (EIR) has already been certified (over many objections, including our own), and for which SWP contract amendments are now being implemented. We would further that request today by asking that this hearing serve as the start, not the end, of legislative oversight activities related to the Monterey Agreement principles and implementation process. I make this request for two essential reasons: first, because a large number of valid and important concerns (over and above the few I will focus on today) have been raised by groups and citizens throughout California, and it would be good if you could hear about them directly; and second, because the potential reach of these Principles demands a level of public discourse and dialogue that simply has not occurred to-date.

Let me emphasize at the outset, however, that, notwithstanding our many concerns, EDF does see considerable merit in a number of aspects of the Monterey Agreement principles. We certainly share, for example, the negotiators' stated desire to avoid protracted litigation (though their subsequent handling of the EIR process raises serious questions as to the depth of this desire); we are supportive of efforts to revise water allocation procedures and to enhance market-based transfer opportunities so as to better apportion limited SWP supplies, particularly given the foreseeable mismatch of more than 2 million acre feet between annual "entitlements" and available supplies; and we agree that targeting anticipated "surplus" revenues to specific purposes is almost certainly better than leaving those funds to DWR's general budgetary discretion.

National Headquarters

257 Park Avenue South
New York, NY 10010
(212) 505-2100

1875 Connecticut Ave., N.W.
Washington, DC 20009
(202) 387-3500

1405 Arapahoe Ave.
Boulder, CO 80302
(303) 440-4901

128 East Hargett St.
Raleigh, NC 27601
(919) 821-7793

1800 Guadalupe
Austin, TX 78701
(512) 478-5161

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But we also have a number of concerns. Among them:

1. *The closed-door nature of the Monterey Agreement negotiations.* Not surprisingly, these negotiations resulted in a set of principles featuring a host of direct and indirect agricultural and urban contractor benefits (e.g., water transfers and financial restructuring), as well as many benefits for DWR (e.g., financial resources generally, as well as the authority to construct a new Corporation Yard and Operations Center) while ignoring a host of closely-related environmental issues, concerns, and needs. We are not, of course, opposed to contractor (or even DWR) benefits per-se, but to contractor benefits which (1) will likely lead to adverse environmental consequences or which (2) are provided *to the exclusion of* related environmental benefits. (In the Bay/Delta process, for example, the notion of "equity" for all interests has been an important cornerstone throughout.) Where, we wonder, is the "equity" in these Principles?

2. *The manner in which important and legitimate questions of process and substance were ignored or cursorily dismissed in the rush to complete and certify a deficient Program EIR on the purported implications of implementing the Agreement's principles.* The Monterey Agreement EIR is fast becoming legend for it's blanket dismissal of a host of important issues and concerns. As just one example, EDF's request for detailed information on the assumptions and data which underlie the Agreement's "Payment Management Program" (see item (6), below) received the following response: "This comment raises legal, rather than environmental, issues and is outside the scope of this EIR." Of note, the same comment raised concerns about unmet Category III commitments under the Bay/Delta accord -- a legal, rather than environmental, issue??

3. *Ongoing perpetuation of the myth that DWR will someday "complete" the SWP.* Principle 12 of the Agreement includes "a reaffirmation of DWR's existing contractual obligation to make all reasonable efforts to complete the SWP." The good news here is the Final EIR's "suggestion" (as a "public controversy mitigation measure") that DWR and the contractors *not* include in contract amendments implementing the Agreement's principles any amendments that would incorporate Principle 12. But the overarching problem of unrealistic expectations and commitments remains, as does Principle 12 in the Agreement itself, along with the potential complications of deleting Article 18(b) from the subject water supply contracts (i.e., the only place where the "potential" of non-completion is at least explicitly acknowledged).

4. *The use of individual contract amendments as the principal vehicle through which the Monterey Agreement Principles will be (and are now being) implemented.* This is contrary to the signatories' pledge to work diligently and in good faith towards "a final written agreement" that could, among other matters, be reviewed by all parties of interest (who will now have to examine each and every contract amendment to understand the manner in which these Principles are implemented in fact).

5. *Important unanswered legal, financial, and environmental issues associated with the sale (or lease/option) of the Kern Fan Element (KFE) and related assets of the Kern Water Bank to "designated Agricultural contractors."* This lease/exchange arrangement (some 45,000 AF of unused SWP agricultural entitlements -- a bit more than one percent of the SWP entitlement total --

will also be "retired" as part of the deal) involves about 20,000 acres of fallowed land between Bakersfield and Elk Hills, currently in public ownership. Roughly half of that land is not used (or is unlikely to be used) for groundwater recharge purposes, but is of tremendous value to numerous listed species and serves as a cross-valley corridor for a variety of species of concern. As mitigation for prior SWP impacts and activities, DWR has agreements with the Department of Fish and Game committing to the permanent management of certain KFE lands as habitat for such species, and barring the sale, lease, or use of such lands for other purposes without the approval of DFG. How will these arrangements be handled? With what level of public review? If the handling to-date of Monterey Agreement issues is any guide, it is also highly likely (and highly unfortunate) that a lease/exchange deal will be completed prior to the completion of recovery plans now being developed for species of concern.[1]

6. *Missed opportunities for funding all or part of the state's CVPIA cost-sharing commitments, both the state's and the water contractors' Category III obligations under the Bay/Delta Accord, and long-term Bay/Delta funding overall.* A crucial aspect of the Monterey Agreement is its "financial restructuring" provisions, summarized in Exhibit A to the Agreement as the "State Water Project Payment Management Program." (A modified version of Exhibit A is attached herewith.) While some of the underlying details remain unknown (see, for example, item (2) above), the most noteworthy provisions of the Payment Management Program are as follows:

(a) $14.0 million in 1995 and $7.7 million in 1998 for a "general capital operating fund" within DWR for unspecified purposes to be made available "from bond reserves that are no longer required by bond covenants;"

(b) other "surplus" receipts (reportedly SWP revenues net of expenses, but listed as "Revenues" in Exhibit A) to be distributed approximately as follows:

(i) $3.5-15.5 million per year beginning in 1998 to a SWP "capital resources account" for unspecified purposes;

(ii) $10 million per year beginning in 1997 to a Trust Fund within DWR for use in "stabilizing payments" to SWP agricultural contractors;

(iii) $4m-30.5m per year beginning in 1997 and paid directly to SWP urban contractors for use as they direct; and

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[1] There is, of course, considerable pressure to conclude such a deal. Among other matters, "no Monterey Amendments will take effect until the Monterey Amendments of both the Kern County Water Agency and the Metropolitan Water District ... have been executed and the State has conveyed to Kern County Water Agency the property which constitutes the Kern Fan Element of the Kern Water Bank...." (Letter conveying proposed Monterey Amendments to Robert B. Almy, Water Resources Planning Manager, Santa Barbara County Water Agency, from David N. Kennedy, Director, DWR, September 29, 1995.) Of note, this letter was sent to Mr. Almy a full month prior to certification of the final EIR.

(iv) additional surplus amounts beginning in 2001 to be retained by DWR after consultation with SWP agricultural and urban contractors (only) or to be distributed first to SWP urban contractors ($2 million/year up to $19.3 million) and then to SWP agricultural (~24.7%) and urban (75.3%) contractors.

The above Payment Management Program is expected to yield substantial savings for SWP contractors (e.g., more than $119 million between 1997 and 2035 for the Central Coast Water Authority alone). Moreover, as illustrated in the attached re-work of Exhibit A, the total estimated "surplus" involves more than $1.95 billion between 1995 and 2035--an average of approximately $48 million annually--even before additional surpluses (as in (b)(iv) above) are taken into account. More than $400 million of this total will go to for SWP "capital resources"--nearly twice the State's long-term obligations under the CVPIA cost sharing agreement. And distributed contractor savings (both agricultural and urban) will total more than $1.5 billion--nearly $37 million per year, on average--or enough to finance a 1996 Bay/Delta revenue bond of $300-$400 million.[2]

In this example, we do not mean to suggest that all contractor savings could or even should be directed to environmental purposes, nor that bond funding is the only way to go. (For many environmental purposes, including supplemental water acquisitions, a secure and sustained source of dedicated annual funds will also be needed.) But in the ongoing search for Category III funds, CVPIA cost sharing funds, and long-term Bay/Delta restoration funds, it is difficult to understand why an environment greatly impacted by SWP development and operations shouldn't share in some significant portion of the Monterey Agreement's anticipated financial benefits. CVP water and power contractors are now contributing directly to Bay/Delta watershed restoration efforts through the CVP Restoration Fund; the Metropolitan Water District of Southern California is contributing directly through it's up-front commitments to Category III; what about other SWP contractors?

The above list of issues and concerns is far from exhaustive, but is indicative of the fact that, whatever their benefit, the Monterey Agreement principles leave many important questions unanswered, and ignore a host of associated environmental concerns and opportunities. Beginning with this hearing, EDF hopes that you will help to ensure that the above issues are addressed and resolved <u>before</u> irrevocable commitments to implement these Principles are made, and opportunities lost, to the detriment of all Californians.

Thank you very much; I would be happy to answer any questions.

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[2] It is our understanding that it is the position of the signers of the Monterey Agreement that the Burns-Porter Act incorporates the revenue bonding authority first established under the state CVP Act in the 1930's. If true, this authority, and at least a portion of these revenues, might be used to secure capital funds for consensus-based projects and programs under Category III immediately, and perhaps as part of an initial phase of longer-term Bay/Delta funding.

EDF 17-Nov-95

Monterey Agreement Principles - State Water Project Payment Management Program

(millions of dollars)

		Net Revenue	Capital Resources	Capital Operating Fund	Funds Available	Ag Trust	Urban	Enviro
1995		15.0	0.0	15.0	0.0	0.0	0.0	0.0
1996		7.7	0.0	7.7	0.0	0.0	0.0	0.0
1997		14.0	0.0	0.0	14.0	10.0	4.0	0.0
1998		23.0	6.0	0.0	17.0	10.0	7.0	0.0
1999		38.0	6.0	0.0	32.0	10.0	22.0	0.0
2000		39.0	6.0	0.0	33.0	10.0	23.0	0.0
2001	(a)	45.0	4.5	0.0	40.5	10.0	30.5	0.0
2002	(a)	45.0	4.5	0.0	40.5	10.0	30.5	0.0
2003	(a)	45.0	4.5	0.0	40.5	10.0	30.5	0.0
2004	(a)	45.0	4.5	0.0	40.5	10.0	30.5	0.0
2005	(a)	44.0	3.5	0.0	40.5	10.0	30.5	0.0
2006	(a)	44.0	3.5	0.0	40.5	10.0	30.5	0.0
2007	(a)	45.0	4.5	0.0	40.5	10.0	30.5	0.0
2008	(a)	45.0	4.5	0.0	40.5	10.0	30.5	0.0
2009	(a)	44.0	3.5	0.0	40.5	10.0	30.5	0.0
2010	(a)	45.0	4.5	0.0	40.5	10.0	30.5	0.0
2011	(a)	47.0	6.5	0.0	40.5	10.0	30.5	0.0
2012	(a)	49.0	8.5	0.0	40.5	10.0	30.5	0.0
2013	(a)	48.0	7.5	0.0	40.5	10.0	30.5	0.0
2014	(a)	51.0	10.5	0.0	40.5	10.0	30.5	0.0
2015	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2016	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2017	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2018	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2019	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2020	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2021	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2022	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2023	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2024	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2025	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2026	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2027	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2028	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2029	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2030	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2031	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2032	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2033	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2034	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
2035	(a)	56.0	15.5	0.0	40.5	10.0	30.5	0.0
Sum		1,954.7	418.5	22.7	1,513.5	390.0	1,123.5	-

(a) if Funds Avail > 40.5/yr, Urbans get $2.0/yr up to $19.3 w/bal to Ag (24.7%) and Urban (75.3%)

Potential Bond Proceeds based on Ag-Urban disbursements

NPV (1996)	*i*	Net Revenue	Bond Proceeds		Funds Available	Bond Proceeds
25 years	6.0%	505.6	375.0		423.9	314.4
30 years	6.0%	560.6	415.8		463.6	343.8
35 years	6.0%	601.7	446.2		493.3	365.9
40 years	6.0%	632.4	469.0		515.5	382.3

Potential bond proceeds = NPV((source/1.2) [coverage]) - 11% [1% issue, 10% reserve]

Primary Source: Monterey Agreement - Statement of Principles, Exhibit A