June 9, 2020

E. Joaquin Esquivel, Chair
State Water Resources Control Board
1001 I Street
Sacramento, CA 95814
Email: commentletters@waterboards.ca.gov

SUBJECT: **COMMENT LETTER—June 16, 2020 BOARD MEETING—DRAFT FY 2020-2021 CWSRF IUP**

Dear Chair Esquivel,

The California Association of Sanitation Agencies (CASA) and WateReuse California appreciate the opportunity to provide comments on the draft Intended Use Plan for the Clean Water State Revolving Fund. CASA's member agencies are engaged in advancing recycled water production and beneficial reuse, generating renewable energy supplies, and producing and beneficially using biosolids and other valuable resources. The mission of WateReuse California is to promote responsible stewardship of California's water resources by maximizing the safe, practical and beneficial use of recycled water.

For decades, the Clean Water State Revolving Fund has been a critical source of financing for projects that promote sustainability, enhance water resources and protect public health while ensuring such investments are affordable for rate payers. In 2015 and 2016, the program provided over $1 billion in annual funding. Unfortunately, over the last three years, the amount of funding has steadily declined, to a low of around $200 million in FY 2019-2020. We recognize that there are many reasons for this downward trend, including the transition to the Fi$cal accounting system, the challenges presented by the current pandemic, and a reduction in staffing. (The proposed IUP lists 44.2 PYs compared to 54 in FY 2015-2016.) Our associations want to work in partnership with the State Water Board to restore the program to the level commensurate with California's economic standing and to be responsive to the significant need for infrastructure, job creation and water supply.

The Reduced Financial Capability Analysis Should be Removed and the Model Assumptions Subject to Stakeholder Input

The draft IUP seeks the Board's endorsement of a 41% reduction to the annual sustainable funding capacity of the CWSRF program. While we understand the revised figure was developed with Water Board staff involvement, the rationale, assumptions and underlying drivers have not been shared with stakeholders, and the proposed change is extremely troubling to us. The prior capacity assessment called for an annual funding target of 90 to 125 percent of $1 billion annually. The proposed IUP would reduce this significantly, to 90 to 125 percent of $587 million. This runs counter to a number of statewide priorities and needs, including:

- Economic stimulus due to the severe financial impacts of COVID-19.
- The Governor's draft 2020 Water Resilience Portfolio, which calls increasing financial capacity to support recycling, reuse, and wastewater projects through the Clean Water State Revolving Fund and other state and local funding mechanisms. (Recommendation 4.1)
- The growing need for increased investment in clean water and recycled water infrastructure.

While the U.S. EPA does not require that a funding target be specified in the IUP, we agree that a funding capacity target can be a useful guide for the program, help to manage expectations and provide a measure of program effectiveness. The development of the latest financial capability analysis, however, was not transparent to stakeholders. It is important that borrowers, in addition to staff and the Board, have confidence in the soundness and legitimacy of the funding target. There has not been sufficient time to review and understand the proposed funding capacity, which from our perspective seems inconsistent with what we know of the program's financial standing and California's role as a leader.

There is also a lack of clarity regarding the assumptions and estimates that were used in the financial model. A variety of factors influence the sustainable financing capacity, from projected earnings to new capital to the time funds are encumbered. For example, the Water Board's municipal financial advisor indicated that the analysis assumed future federal clean water capitalization grants of $100 million, yet the IUP notes that for cash flow purposes, "[f]uture capitalization grants are conservatively estimated at $70 million per year." (Draft IUP footnote 9.) While we understand the emphasis on revolving capitalization after forgivable principal and administrative set asides, $70 million seems extremely conservative given the federal capitalization grant has far exceeded this total for the last 10 years. The Clean Water and Drinking Water SRFs can mutually support each other through interfund investing, combined bond leveraging, and cross security of the combined bonds. Thus, the Water Board can rely on such mutual support to enhance overall lending capacity within both SRFs.

Lending capacity is a long term, multi-year metric, and does not dictate the amount of funding under this year's IUP. Indeed, the inclusion of the rollover projects on the fundable list (which will require total funding well over the prior target of $1 billion) demonstrates that the $587 million target is not relevant for the current year. In addition, if we can identify those components which, if adjusted, could result in a higher funding capacity, we can work together to modify or influence those factors. Memorializing a 41% long-term reduction in funding capacity for such a critically important program during a time when we are working to bolster California's investments in water infrastructure and stimulate the economy should not occur unless absolutely necessary, and at a minimum, should be carefully examined and understood by all stakeholders.

For these reasons, we request that the references to the sustainable financing capacity and the annual funding target be removed from the IUP. At a minimum, the estimated sustainable financing level should be referred to as "interim" or "preliminary" in the IUP and a commitment made to allow additional stakeholder review and, if appropriate, development of a revised funding capacity analysis to guide the program over the long term.

We Recommend Funding Scenario B

As proposed, the IUP could result in the funding of only five additional projects with a score of 14 in FY 2020-2021 for a total of just over $300 million for new projects. (Scenario A) Staff recommends the Deputy Director be authorized to add an additional 18 projects with a score of 13 to the fundable list if "sufficient progress" is made in reducing the backlog. Sufficient progress is not defined and does not appear to acknowledge readiness to proceed, which leaves the applicants in limbo as to the status of new projects and might condemn the SRF to perpetually focus on a new set of delayed roll-over projects within each new IUP

The recommendation to limit the number of new projects on the fundable list appears to be driven, in part, by staffing issues and the desire to clear the backlog remaining from last year's IUP, which we fully support. Rather than leave the status of these additional projects uncertain, however, we recommend that the 18 projects that be added to the fundable list, without reducing any of the projects in scenario A to partial funding.

Partial funding is not the only way to address larger project needs. Most large projects require multiple years for construction. Not all of the funding needs to be set aside in the first year since the expenses (and corresponding request for disbursements) will also be spread over multiple years. One way to potentially free up this additional money is to identify, for large projects that scored a 14 or 13, funding that will not be needed until future years and make those funds available for other loans. The approved funding in subsequent years could then be met with future IUPs. This approach would maximize the number of projects that could be constructed this year and provide a reasonably high level of assurance to agencies with larger projects.

We recognize that Scenario B presents additional workload which exceeds the Board's current staffing resources, particularly in light of hiring limitations and other consequences of the response to COVID-19. Our associations commit to collaborate with the Board and pool resources to clear the backlog through the use of consultants paid for by a combination of administrative set-asides and project applicants. Consultants paid for by project applicants have been successfully utilized in the WIFIA program (where a fee is assessed), as well as SRF programs across the U.S. including Arizona, Indiana, Iowa, Massachusetts, Michigan, Minnesota, Missouri, Nevada, New Jersey, New Mexico, New York, North Dakota, Ohio, Rhode Island, South Dakota, Virginia, Texas, and Wisconsin At a minimum, all leveraged SRFs rely on their bond counsels and financial advisors to varying degrees to accelerate legal and financial reviews. This process can expedite the rate of project reviews and conserve limited staffing resources. In addition, relying on consultant support will free up Water Board staff to focus more of their time on assisting disadvantaged communities with their projects. DAC and SDAC projects do not require sizeable funding but do consume a significant amount of staff time.

We appreciate that the Board and staff are wary of raising expectations and of overpromising, but this is not the time to be overly conservative. As the Governor's Task Force on Business and Jobs Recovery Capital Markets and Infrastructure Subcommittee put it, the focus should be on how "the state and other California entities take advantage of low interest rates to invest in infrastructure and other capital projects, create jobs and put people back to work."

There are tools at our disposal to move through the backlog and "right the ship" without severely constraining California's investment in infrastructure that protects the environment, creates jobs, and builds the future fund through repayments. Now more than ever, the CWSRF is an incredibly important program for California – providing low interest loan monies to a large back log of water infrastructure projects. Through this process of using consultants paid for by project applicants, our associations and members are ready to partner with the Water Board to extend and expand this program's successful track record.

California Needs to Make the Most of Available Dollars Through Greater Leveraging

As noted above, the Governor's 2020 Water Resilience Portfolio expressly calls for additional leveraging of the CWSRF (cite). Across the country, it is possible to measure the dollars of financial assistance disbursed per dollar of revolving equity. Rhode Island leads U.S. states with a leveraging ratio approaching $5 of financial assistance for every $1 of equity, Other states, including New York, Ohio, Iowa and Indiana also have leveraging ratios of over $2.00. California's ratio is in the range of $1.65 to $1.00. Factors that affect this ratio include:

- Appropriating rather than borrowing state match;
- Maximizing income through higher loan rates offset by reduced coverage and reserves for lower risk borrowers;
- Providing planning and design loans to enable applicants to fully design projects and generate accurate costs rather than encumber funds for less defined projects,
- Multi-year commitments rather than encumbering estimated project costs at award date; and
- Frequent coordination with the State Treasurer to optimize investment activity.

In every communication regarding the CWSRF over the past several years, our associations have advocated greater leveraging. We are disappointed, to say the least, that we appear to be going in the opposite direction, of very conservative funding levels and scaled back expectations. We again commit to working with the Water Board to make the most of the capital available within the bounds of rating agency criteria/expectations and fiscal prudence. We continue to investigate other sources of match funds, and in the meantime request that the Water Board direct staff to fully evaluate other changes that will increase California's leveraging ratio.

The IUP Should Acknowledge the Potential for One-Time Stimulus Funding

The IUP is the business plan for the coming fiscal year. The IUP sets forth the Water Board's approach to successfully "carry out that business plan with the available financial and programmatic resources." One anticipated new resource is one time federal stimulus funding for infrastructure in late summer/early fall. While the specifics of any package remain to be worked out, the IUP should acknowledge this possibility and commit staff to coming back to the Board with an amended plan to demonstrate how the additional funding will be allocated and expedited.

Conclusion

We look forward to working with the Water Board to improve and enhance the CWSRF program. CASA and WateReuse California value our partnership with the State Water Board and share the goal of ensuring the CWSRF is predictable, robust, effective and ambitious in funding essential infrastructure for years to come.

Sincerely,

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