

**AGENDA ITEM**

**TO:** Capistrano Valley Water District Board of Directors

**FROM:** George Scarborough, General Manager

**SUBJECT:** Consideration of Project Implementation Agreement and Operating Lease Agreement with San Juan Basin Authority (Phase I of the Ground Water Recovery Plant)

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**RECOMMENDATION:**

By Motion, adopt the resolution approving the Project Implementation Agreement and Operating Lease Agreement with San Juan Basin Authority for the construction and operation for Phase I of the Ground Water Recovery Plant.

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**SITUATION:****A. Summary and Recommendation**

Phase I of the San Juan Basin Authority (SJBA) Ground Water Recovery Plant (GWRP) (the "Project") is located in and will provide benefit to the Capistrano Valley Water District (District). The Project is being implemented conjunction the SJBA, Municipal Water District of Orange County (MWDOC) and Metropolitan Water District of Southern California (MWD). The SJBA holds the water rights permit for the area while MWD is providing a subsidy for the Project through MWDOC to the SJBA.

On September 3, 2002, the Board of Directors of the District approved a Service Contract with Eco Resources, Inc.(the "Company") to design, build and operate the Project . As the sole beneficiary of the Project , the costs associated with the construction and operation of GWRP will be borne by the rate payers of the District. In order for the District and its rate payers to receive all the benefits of the Project , the District must assure that the Project be allocated necessary water rights to enable 4,800 acre-feet of production, receive the entire benefit of the MWD subsidy and be able to operate and take potable water from the Project for as long as the District deems it feasible.

A Project Implementation Agreement (Agreement) is required under San Juan Basin Authority 1998 Memorandum of Understanding (1998 MOU) in order to allocate interest in the Project water rights to each of the participating members. As the sole beneficiary of The Project , the proposed Agreement provides for the District and the City's allocated interest in the Project water rights to be 5,800 acre-feet for the purposes of extracting 4,800 acre-feet to be delivered to the District. Additionally, the

proposed Agreement irrevocably commits the subsidy described in the 1998 MWD Agreement to The Project . The proposed Operating Lease Agreement in conjunction with the Project Lease Agreement provide for the terms under which the District will be able to operate and take water from the Project for a term of 55 years. During the first 30 years, the District will make lease payments under the Project Lease Agreement to the SJBA equivalent to the debt service on the Lease Revenue Bonds (Bonds) issued by the SJBA to finance the construction of the Project . During the last 25 years, the District will make lease payments under the Operating Lease Agreement of \$1. per year. At the end of the 55 year term, the District will have the ability to renew the Operating Lease Agreement should it desire to do so.

The Project Lease Agreement is attached as part of Exhibit "A" to the Project Implementation Agreement and is a standard financing document in conjunction with the Bonds. Therefore, the Project Lease Agreement is included with the other financing documents to be considered at this meeting. Staff recommends the Board of Directors adopt the resolution approving the Project Implementation Agreement and Operating Lease Agreement.

#### B. Background

For the past two to three years, District staff has been working toward the implementation of Phase I of the San Juan Basin Authority Ground Water Recovery Plant. Prior to beginning that process, the District along with the SJBA, Santa Margarita Water District (SMWD), Moulton Nigual Water District (MNWD) (collectively the "Participating Members") entered into the 1998 MOU, which provides among other items, that prior to commencing construction of the project specified in the MOU, the Participating Members allocated interest in the specified project's water rights and water supplies will be established by a project implementation agreement among the Participating Members and SJBA. As such, the District has prepared the proposed Project Implementation Agreement for consideration by the District Board of Directors. Being the only beneficiary of The Project , the proposed agreement is between SJBA and the District and does not require approval of the other participating members.

The proposed Agreement provides among other items for the requisite allocation of interest in the water rights and commitment of the MWD subsidy to the Project. Additionally, through a Project Lease Agreement and an Operating Lease Agreement (collectively, Exhibit "A" to the Agreement), the Agreement provides for the terms under which the District will be able to operate and take water from the Project now and in the future.

### C. Agreements

Project Implementation Agreement - This agreement has been prepared in order to meet the requirements of the 1998 MOU among the Participating Members of the SJBA. The GWRP is a project of the San Juan Basin Authority. The Project lies within the City of San Juan Capistrano and will benefit the citizens of San Juan Capistrano and all other rate payers in the District's service area. As the sole beneficiary of the Project, the rate payers of the District will be asked to bear all the costs associated with the generation of the product water, however the SJBA will own and finance the Project.

The most important aspect of the Agreement is the allocation of the Project's water rights. In order for the Project to be of any value to the District, the District and the City must be allocated sufficient water rights to produce 4,800 acre-feet of water for the life of the Project. Section 2 allocates the required 5,800 acre-feet necessary to deliver 4,800 acre-feet of water to the District's potable water delivery system. Section 3 provides for no obligation for SJBA to provide make-up water should the extraction of ground water for the Project affect the District's ability to extract water from its other District-owned facilities. Lastly, Section 3 provides for immediate negotiations amongst the parties on diversions of water from the San Juan Basin in addition to the production of water from the Project. For example, this negotiation would provide for terms under which the SJBA or the District could expand the plant or groundwater wells not associated with the Project.

Section 4 of the Agreement provides for the irrevocable commitment of the MWD subsidy of \$250 per acre-foot of water delivered to the potable water delivery system pursuant to the 1998 MWD Agreement. This assures that the funds received under the subsidy will not be allocated to other projects during the term of the MWD Agreement. Under the remainder of Section 4 and Section 5, the District, as the contract operator of the SJBA, will make all major decisions and approvals including construction, operation, maintenance and repair in consultation with the SJBA.

Project Lease Agreement and Operating Lease Agreement - Due to the unique nature of this project and its interrelation to the Service Contract with ECO Resources, Inc. to design, build and operate the Project, Exhibit "A" to the Agreement is comprised of a Project Lease Agreement and an Operating Lease Agreement. Collectively, these Lease Agreements provide for the District to Lease the Project from the SJBA, operate and take water from the Project for a term of 55 years.

The Project Lease Agreement is attached as Exhibit A-1 to the Agreement and is standard project financing lease agreement normally associated with Lease Revenue Bonds. The Project Lease Agreement provides for the District to make Lease Payments equivalent to the debt service on the Bonds issued by the SJBA to finance

the project. As with all lease revenue bond financed projects, these lease payments act as security for the bonds during the term of the Project Lease Agreement. In this case, the District has the right to operate and take water from the Project for 30 years and make the appropriate lease payments. A unique aspect of this lease agreement is that should the Company default under the terms of the Service Contract and the District ultimately terminates the Service Contract for cause, the Project Lease Agreement will terminate and the Bonds will be paid by the a combination of the Parent Guarantor, Southwest Water Company and the Bond insurer. The Project Lease Agreement included with the other standard financing documents provided for Board consideration at this meeting under a separate item.

The Operating Lease Agreement is attached as Exhibit A-2 to the Agreement. The Operating Lease Agreement provides for the District to operate the Project for 55 years or until October 1, 2057. Although, the Operating Lease Agreement provides for maintenance and operations of the Project for the entire 55 years, the Project Lease Agreement governs the maintenance, operations and lease payments, etc. during the Project Lease Agreement term. At the end of 30 years or upon termination of the Project Lease Agreement under the terms of the Service Contract, the bonds will have been paid off, the SJBA will own the Project and the District will continue to operate and take water from the Project under the Operating Lease Agreement. The terms of the Operating Lease Agreement are essentially identical to those of the Project Lease Agreement but for the amount of the lease payments. The District will only pay \$1 annually to operate and take water from the Project once the Lease Revenue Bonds are retired. The Operating Lease Agreement automatically extends to coincide with term of the Property Lease between the City and the SJBA.

Property Lease Agreement - The Property Lease Agreement between the City and the SJBA is not part of the Implementation Agreement, however the Project Lease Agreement and Operating Lease Agreements are connected to the Property Lease Agreement. Essentially, the Property Lease Agreement provides for the City to lease the real property to be provided for the plant site, well sites, booster pumping station site and pipeline sites to the SJBA for purposes of the Project. Without this Property Lease, the SJBA would not be able to finance the Project and provide for the District to operate and take water. The Property Lease Agreement is for the maximum term allowed by law of 55 years. Therefore, the Operating Lease Agreement is also 55 years in length. At the end of 55 years, the Property Lease Agreement will be extended or renewed by the City, automatically extending the Operating Lease Agreement and allowing the District to operate and take water from the Project for up to another 55 years. Should the Property Lease Agreement not be renewed, the SJBA would own a Plant with no ability to access to operate it and take water. The District would be able to access the real property but would also have not ability to access the Project. The Property Lease Agreement is essential to all parties in an effort to keep

the Project operating now and in the future. The Project Lease Agreement is provided for consideration by the City Council at this meeting.

**COMMISSION/BOARD REVIEW AND RECOMMENDATIONS:**

The Water Advisory Commission (WAC) has recommended approval of The Project subject to the Project Implementation Agreement to provide for the satisfactory access to water rights, the MWD subsidy and long-term operation of the Project . The proposed Implementation Agreement provides for those items. The WAC members have received updates on the status and will receive a formal status update at their next meeting on October 22, 2002.

**FINANCIAL CONSIDERATIONS:**

Although MWD has provided a subsidy to assist in offsetting the costs of construction for the Project, the Project will result in an increase of 14% to 15% in water rates to the District in order to fully fund the Project. As discussed during the approval of Service Contract in September 2002, the cost of this project has been weighed against the alternatives and is more cost effective as well as more effective in meeting the District's goals of 50% local production and emergency storage. Without the allocation of the water rights and the ability to operate the plant for many years, the increase in water rates would not be justified. Upon completion of the first thirty years of the Project, the capital costs will have been amortized and the cost of water is projected to be much lower than imported water and well as much more reliable.

**NOTIFICATION:**

San Juan Basin Authority\*  
Fieldman, Rolapp & Associates\*  
Stradling, Yocca Carlson & Rauth\*  
Lehman Brothers\*  
Southwest Water Company\*

**ALTERNATE ACTIONS:**

1. Motion, adopt the resolution approving the Project Implementation Agreement and Operating Lease Agreement with San Juan Basin Authority for the construction and operation for Phase I of the Ground Water Recovery Plant.
2. Do not approve the resolution
3. Request additional information from staff.

**RECOMMENDATION:**

By Motion, adopt the resolution approving the Project Implementation Agreement and Operating Lease Agreement with San Juan Basin Authority for the construction and operation for Phase I of the Ground Water Recovery Plant.

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Respectfully Submitted,



George E. Scarborough  
General Manager

Attachment 1 - Resolution

The following attachment is are available for review in the City Clerks office and in the City Council Office:

Attachment 2 - Project Implementation Agreement, including Project Lease Agreement and Operating Lease Agreement

RESOLUTION NO. CVWD 02-10-15

A RESOLUTION OF THE CAPISTRANO VALLEY WATER DISTRICT AUTHORIZING AN OPERATING LEASE AND A PROJECT IMPLEMENTATION AGREEMENT WITH SAN JUAN BASIN AUTHORITY AND AUTHORIZING THE EXECUTION THEREOF AUTHORIZING CERTAIN ACTIONS IN CONNECTION THEREWITH

WHEREAS, the Capistrano Valley Water District (the "Water District") is a county water district, organized and existing under the laws of the State of California and is a subsidiary district of the City of San Juan Capistrano (the "City"); and

WHEREAS, the San Juan Basin Authority (the "Authority") and the City have approved a Property Lease by and between the City and the Authority (the "Property Lease"), pursuant to which the City will agree to lease the Property (as defined in the Property Lease) to the Authority; and

WHEREAS, the Authority and the Water District, a member of the Authority, have approved a Project Lease Agreement by and between the Water District and the Authority (the "Project Lease Agreement"), pursuant to which the Water District will agree to lease the Project (as defined in the Project Lease Agreement) from the Authority and to pay certain Lease Payments (as defined in the Project Lease Agreement) in connection with the issuance and sale of the Capistrano Valley Water District, Lease Revenue Bonds (Ground Water Recovery Project), Issue of 2002 (the "Bonds") by the Authority pursuant to a Trust Agreement by and among BNY Western Trust Company, as trustee (the "Trustee"), the Water District and the Authority (the "Trust Agreement"); and

WHEREAS, the proceeds of the Bonds will be used to finance the acquisition and construction of Phase I of the San Juan Basin Ground Water Recovery Project (the "Project"); and

WHEREAS, the Authority and the Water District desire to enter into that certain Agreement for Implementation of the Lease Agreement, by and between the Authority and the Water District (the "Implementation Agreement") and that certain Operating Lease Agreement by and between the Authority and the Water District (the "Operating Lease") for the purpose of establishing the terms of operation and ownership of the Project, the forms of which have been presented to the board of directors of the Authority at a meeting to be held on the same date as the date on which this Resolution has been adopted; and

WHEREAS, the Water District possesses all legal authority to and desires to enter into the Implementation Agreement and the Operating Lease;

NOW, THEREFORE, BE IT RESOLVED, that the Board of Directors of the Capistrano Valley Water District does hereby

1. Provide that the foregoing recitals are true, correct, and adopted.
2. Approve the proposed forms of the Implementation and Operating Lease Agreement presented at this meeting.
3. Authorize and direct the Chairperson of the Water District (the "Chairperson") and the General Manager of the Water District or his designee (the "General Manager"), acting together or separately, for and in the name of the Water District to execute each of the Implementation Agreement and Operating Lease in the form hereby approved.
4. Authorize and Direct the Chairperson, the General Manager, the Administrative Services Director and all other members, officers and employees of the Water District to execute all other documents and take all other actions on behalf of the Water District that may be necessary or advisable to carry out the transactions contemplated by the Implementation Agreement and Operating Lease.
5. Provide that this Resolution shall take effect upon adoption.

PASSED, APPROVED and ADOPTED this 15<sup>th</sup> day of October, 2002.

CAPISTRANO VALLEY WATER DISTRICT

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DIANE BATHGATE, CHAIRPERSON

ATTEST:

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MARGARET R. MONAHAN, CLERK OF THE BOARD



**ATTACHMENT #2  
PROPERTY LEASE**

**DOCUMENT ON FILE IN THE CITY CLERK'S OFFICE**