



October 27, 2016

Frank McMichael, District Manager
Ukiah Valley Sanitation District
151 Laws Avenue
Ukiah, CA 95482

SENT BY EMAIL (dm@uvsd.org) AND REGULAR MAIL

Re: Questions regarding recycled water project funding

Dear Frank:

I am responding to your letter because the City Council will not meet until November 2, 2016, and I want to respond to your questions as quickly as possible. I welcome your questions and hope to continue this discussion in an open and transparent manner so that the ratepayers in the District and the City have an opportunity to be informed about these decisions that will have a major impact on them and their sewer rates.

I have seen the letters written by the District's lawyers offering to meet and discuss possible solutions to the barrier the District's lawsuit has created, jeopardizing the receipt of the low interest loan and grant which has been reserved for the City's four phased recycled water project ("Project"). The City appreciates the District's apparent willingness to discuss the problem. The City does anticipate that this would be a first order of business for the City and District ad hoc committees, once they agree on the terms for conducting negotiations. However, the City's request that the District dismiss its lawsuit and focus, instead, on attempting to resolve its disagreements with the City through negotiations, was not proposed primarily because of the lawsuit's impact on the Project. That is certainly an important and unfortunate consequence of the litigation, but the City never proposed that the District dismiss its lawsuit until the loan was finalized and, then, refile it. Instead, the City proposed dismissing the lawsuit to focus the time and expense consumed by the litigation on resolving the District's disputes with the City. Since neither City nor District ratepayers were consulted before the District filed the lawsuit or about the District's long-term plans for providing sewer service in the Ukiah Valley, the City Council believes those negotiations should be open to the public and should produce frequent reports to City and District ratepayers on their progress.

Your letter suggests that the District Board has been ignored and not kept informed as the Project was developed. However, the City has included the District since the project's inception. The District participated in the preparation of the original RFP for the master plan of the system, helped select the

current engineering consultant, and has received staff presentations at major milestones, including the recent acknowledgement of the City's eligibility for Proposition 1A funding.

To clarify the status of the City's application for Project funding, the City has expended over \$1 million of City funds to obtain the engineered plans for the Project, certified a mitigated negative declaration under CEQA and submitted its application for \$25,564,000 from the Clean Water State Revolving Loan Fund (CWSRF) and \$9,996,000 in grants from the Water Recycling Funding Program (WRFPP) to construct Phases 1-3 of the Recycled Water Project.

According to the Program Manager for the CWSRF loan and WRFPP grant programs, the WRCB has received a complete funding package from Ukiah as shown on the Table.¹ Ukiah's Project qualifies for 1% financing and is also eligible for Prop 1 grant funding. Both funds, however, are obligated at time of contract. The District's lawsuit currently prohibits WRCB from completing its Legal and Financial Reviews. Both of these reviews are at a point that they need this issue to be resolved to complete their assessment. Once the sewer fund is secure without the burden of the lawsuit, WRCB has the numbers it needs to finalize its financial review. Its legal staff will also need to complete its review. With financial and legal approval, management will likely authorize preparation of the contract. In summary, the lawsuit has WRCB on hold.

As currently submitted to WRCB, the Project is proposed as a wastewater treatment rather than a water project to be funded by the wastewater system. Based on several communications on behalf of the District Board, the City assumed that the District would not approve participating in the funding. As a result, it adopted a Pledge Resolution as part of its application to the WRCB which only pledged to repay the loan funds in Account No. 830, which is a City-only wastewater system capital project fund. However, since the District's lawsuit will prevent finalizing the loan unless the City and the District can reach an agreement satisfactory to the WRCB, the City would like to include in those negotiations a discussion of District participation in the repayment of the loan. The Project clearly benefits both City and District ratepayers.

As a matter of law, the City owns the recycled water produced by the WWTP, but if recycled water is produced by the WWTP and financed jointly by the City and the District, any revenue produced from the sale of recycled water would be credited to the sewer system and shared by the City and the District. When Rick Kennedy was the District Manager, the District Board understood that the recycled water system is unlikely to produce significant revenue in comparison to Project costs and that the primary benefit of the system is to the wastewater system by providing an alternative to direct discharge to the Russian River. (See below answering your questions concerning how the Project will avoid these discharges.)

¹WRCB posts on its website all of the recycled water applications it has received and the requested funding amount and sources. One application allows WRCB to provide available funding from multiple loan and grant sources. The Table is posted at http://www.waterboards.ca.gov/water_issues/programs/grants_loans/docs/appstatusweb.pdf.

At your April 16th meeting Mr. White explained how the City is proposing to deal with all of the issues raised in Question 4 (UVSD video @ minutes 26-35). At that time, he explained that the proportionality of discharge, percolation, and reclamation as well as storage requirements were yet to be determined. He stated that these calculations were the subject of a forthcoming “water balance study” that was to be conducted by Carollo Engineers. Since that time, the water balance has been completed and Mr. White has offered to present its results to the Board at a subsequent meeting, but the UVSD Board declined his offer. Staff remains available to present and discuss at the request of the District.

The completed water balance shows that Phases 1-3 of the recycled water system will reduce the need for river discharge by 60%, and the addition of Phase 4 will reduce the need to discharge approximately an additional 20% for a total reduction of nearly 80%. The City plans to seek funding for Phase 4 as Phases 1-3 are being constructed. Mr. White also explained that the City’s approach for handling the remaining 20% will be to reduce the amount of inflow to the plant by addressing Infiltration and Inflow (I&I) (see UVSD video @ 27:11). In regards to disparity in the timing between inflow and irrigation demand, Mr. White explained that a major component of the project is the creation of storage (see UVSD video @ 25:40 and 31:58). Implementation of Phases 1-3 will require the construction of 66 MG of additional storage.

Item 6 in your letter asks three questions: (1) why Mr. White didn’t tell the District Board about the impact of the litigation on the Project loan as part of his presentation to the Board in April 2016, (2) why the City waited a year to indicate that an agreement with the District was a loan requirement, and (3) what type of agreement is acceptable.

The short answers are (1) the City was not told definitively by WRCB staff until June 28, 2016, that the WRCB could not enter a loan agreement as long as the District’s lawsuit was pending and specifically its cause of action to rescind the Participation Agreement and the Financing Agreement, (2) the City didn’t know it would need an agreement with the District until after June 28, 2016, and (3) a City/District agreement must provide assurances to the WRCB that the District lawsuit will not jeopardize the City’s financial ability to repay the loan.

Given your questions concerning how promptly the City has alerted the District to the impact of the lawsuit on the Project funding, I would also note parenthetically that according to your letter, the District learned of this problem from the City’s cross-complaint, filed on June 30, 2016, but the District did not offer to seek a resolution of this problem until Don McMullen wrote his letter to the City Council on September 20, 2016. I would urge the District to begin focusing on solving problems in the future rather than devoting so much effort to assigning blame for decisions that were made in the past.

Very truly yours,



Sage Sangiacomo, City Manager