

**STATE WATER RESOURCES CONTROL BOARD
BOARD MEETING SESSION - DIVISION OF FINANCIAL ASSISTANCE
JULY 15, 2008**

ITEM 7

SUBJECT

CONSIDERATION OF A RESOLUTION GRANTING AUTHORITY TO THE STATE WATER RESOURCES CONTROL BOARD'S (STATE WATER BOARD) EXECUTIVE DIRECTOR TO APPLY TO THE UNITED STATES ENVIRONMENTAL PROTECTION AGENCY (U.S. EPA) TO IMPLEMENT AN EXTENDED TERM FINANCING PROGRAM AS PART OF THE CLEAN WATER STATE REVOLVING FUND (SRF) PROGRAM

DISCUSSION

As described in the *California Water Boards' Draft Strategic Plan Update: 2008-2012*, the State Water Resources Control Board (State Water Board) is committed to addressing human health and water pollution problems associated with small, disadvantaged communities, especially in cases where these problems present an environmental injustice. Due to their small ratepayer base, small, disadvantaged communities often have difficulty affording the capital costs of wastewater improvements. One way to make projects more affordable for these disadvantaged communities is to extend the term of the financing. Increasing the term of SRF financing from 20 to 30 years reduces the annual payment by approximately 25 percent. Improving affordability may increase and accelerate the number of projects completed by small, disadvantaged communities that have a direct benefit to water quality.

The SRF Program is a joint federal/state funded program designed to help California meet the goals of the Federal Clean Water Act (CWA) (33 U.S.C.A. 1251 et seq.). The SRF Program provides below market rate financing for wastewater and water recycling system improvements, correction of non-point source and storm water pollution problems, and implementation of estuary enhancement programs. The SRF Program receives funds from U.S. EPA Federal Capitalization Grants (Federal Grants), State Bond measures, the sale of Revenue Bonds, and repayments of outstanding financing agreements.

Currently the SRF Program only finances projects for a maximum term of twenty years. CWA and the California Water Code (CWC), however, allow the Program to offer financing on longer terms if approved by U.S. EPA. Extended Term Financing (ETF) has been approved by U.S. EPA for several other states nationwide to reduce the debt service for disadvantaged communities. ETF will allow the State Water Board to give qualified applicants a Financing Agreement (FA) up to a maximum term of thirty years.

ETF will work essentially the same as the existing system from the applicant's perspective. The applicant will submit an application, receive an FA, receive disbursements, and make payments in basically the same manner as with the existing form of agreement used by the SRF Program. The interest rate for ETF will be set in the same manner as existing agreements at 50 percent of the interest rate paid by the state on the most recent sale of General Obligation (GO) bonds. The applicant will still be required to establish a dedicated source of revenue for payments, and the applicant's payments of principal and interest will be deposited into the SRF account along with payments from traditional agreements.

U.S. EPA uses eight criteria to evaluate a state's application for ETF. These eight criteria are discussed in detail in [Attachment A](#). The key criteria to obtain approval of ETF by U.S. EPA are (1) that ETF be targeted to disadvantaged communities, (2) that the financial effect on the SRF Program be limited, and (3) that the financing cannot exceed 30 years, the useful life of the Project assets, or the length of time needed to make the Project affordable for the community, whichever is less.

ETF will only be offered to small, disadvantaged communities. The definition of a small, disadvantaged community will be a community with a population of 20,000 persons or less and a Median Household Income (MHI) equal to or less than 80 percent of the statewide MHI. A small, disadvantaged community will also include a community with a population of 20,000 persons or less that pays at least four percent of its MHI toward wastewater rates. Communities with an MHI greater than 80 percent of the statewide MHI applying for ETF solely on the basis that they pay more than four percent of their MHI on wastewater rates must receive approval for ETF on a case-by-case basis at the discretion of the State Water Board. The application to U.S. EPA will also request approval for the State Water Board, upon request by the applicant, to extend the terms on existing agreements up to an additional 10 years provided the applicant meets the other criteria for ETF at the time they request refinancing of their existing SRF debt.

The criteria also require that the fund remain financially sound. A financial analysis has been performed, and is discussed in greater detail in the Fiscal Impact section below, as well as in Attachment A.

Division of Financial Assistance (Division) staff will review each project to determine the useful life of the assets and threshold at which the Project financing is affordable for the applicant. This analysis will be used to determine the maximum term of the ETF.

[Attachment B](#) contains the amendments to the Policy necessary to implement ETF. The Resolution directs that these amendments will become effective upon U.S. EPA's approval of California's ETF application.

FISCAL IMPACT

The long-term revolving nature of the SRF Program must be protected in one of two ways according to U.S. EPA: (1) ETF must not reduce over a 60-year period the projected level of funding by more than 10 percent from the level the fund would expect to offer without ETF, or (2) the SRF Program must maintain its historical average annual assistance levels or baseline.

State Water Board staff completed an analysis to determine the maximum level of ETF that can be offered so that the revolving level of the SRF Program will not decrease by more than 10 percent. The analysis projected that the SRF Program can offer about 22.5 percent of the funds available each year for ETF for the next 60 years without decreasing the available level of financing by more than 10 percent. The projection was based on the assumption that only ninety percent of available funds will be obligated each year. As an added precaution, Division staff recommends that the State Water Board limit the availability of ETF to at most 20 percent of funds yearly. This percentage will be reassessed annually in the SRF Annual Report, and could be adjusted by the State Water Board, with U.S. EPA's approval, in the future as financial conditions warrant.

In a typical year, approximately \$200 to 300 million in SRF Program funds are obligated to financial assistance. Division staff, therefore, expects that approximately \$40 to \$60 million will be available each year for ETF.

REGIONAL WATER QUALITY BOARD IMPACT

ETF should result in additional projects that address Regional Water Quality Control Boards requirements and goals.

POLICY ISSUE

1. Should the State Water Board grant authority to the Executive Director, or designee, to apply to the U.S. EPA to implement ETF as part of the SRF Program?
2. Should the State Water Board adopt the changes to the Policy, as outlined in Attachment B contingent upon approval of ETF by U.S. EPA?
3. Should the State Water Board limit the availability of ETF to 20 percent of available funds per year?

STAFF RECOMMENDATIONS

1. State Water Board staff recommends that the State Water Board grant authority to the Executive Director, or designee, to apply to the U.S. EPA to implement ETF as part of the SRF Program;
2. State Water Board staff recommends that the State Water Board adopt the changes to the Policy, as outlined in Attachment B, contingent upon approval of ETF by U.S. EPA; and
3. State Water Board staff recommends that the State Water Board limit the availability of ETF to 20 percent of available funds per year.

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STATE WATER RESOURCES CONTROL BOARD RESOLUTION NO. 2008-

GRANTING AUTHORITY TO THE STATE WATER RESOURCES CONTROL BOARD'S
(STATE WATER BOARD) EXECUTIVE DIRECTOR TO APPLY TO THE
UNITED STATES ENVIRONMENTAL PROTECTION AGENCY (U.S. EPA)
TO IMPLEMENT AN EXTENDED TERM FINANCING PROGRAM AS PART OF THE
CLEAN WATER STATE REVOLVING FUND (SRF) PROGRAM

WHEREAS:

1. The SRF Program, is a joint federal/state funded program, currently providing low-interest financing with terms of up to 20 years for projects intended to improve the quality of the state's waters;
2. The State Water Board adopted the *Policy for Implementing the State Revolving Fund for Construction of Wastewater Treatment Facilities* (Policy) on August 18, 1988, and last amended it on July 17, 2007;
3. Small, disadvantaged communities often have difficulty affording water and wastewater system improvements;
4. The Clean Water Act and the California Water Code allow the SRF Program to offer Extended Term Financing (ETF) if approved by U.S. EPA;
5. The State Water Board recognizes the lack of funding currently available to small, disadvantaged communities for wastewater projects, due to the full commitment of all available Small Community Wastewater Grant Program funds;
6. ETF may increase and accelerate the financing and completion of projects by small, disadvantaged communities by making the projects more affordable; completion of additional projects that otherwise would not be affordable should have a direct benefit to water quality;
7. The eight approval criteria outlined by U.S. EPA for an ETF will be addressed, as outlined in Attachment A in the application to U.S. EPA; and
8. The State Water Board's staff has determined that approximately 20 percent of the annual funding can be provided through ETF without decreasing the revolving level of the fund by more than 10 percent.

THEREFORE BE IT RESOLVED THAT:

1. The State Water Board grants authority to the Executive Director, or designee, to apply to U.S. EPA to implement ETF as part of the SRF Program;

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2. The State Water Board approves the amendments to the SRF Policy, identified in [Attachment B](#), contingent upon approval of ETF by U.S. EPA; and
3. Up to an average of 20 percent of the funds available annually may be used for ETF. Division of Financial Assistance staff shall annually evaluate the effect of ETF on the revolving level of the fund in the SRF Annual Report.

CERTIFICATION

The undersigned, Clerk to the Board, does hereby certify that the foregoing is a full, true, and correct copy of a resolution duly and regularly adopted at a meeting of the State Water Board held on July 15, 2008.

Jeanine Townsend
Clerk to the Board