

CHAPTER 8

# Funding Principles to Support the Coequal Goals



## ABOUT THIS CHAPTER

This chapter provides background information on federal, State of California (State), and local spending for water supply, water quality, flood management, and Delta ecosystem purposes. It proposes the development of a comprehensive finance plan to implement the Delta Plan. It also sets forth guiding principles for the development of a finance plan and proposes near-term funding for support of the Delta Protection Commission, Sacramento-San Joaquin Delta Conservancy, and the Delta Stewardship Council (Council).

A 5-year budget is included in Appendix M. And, as described in Chapter 2, successful implementation of the Delta Plan will depend upon many independent agency authorities and actions under the coordination and leadership of the Council.



# Funding Principles to Support the Coequal Goals

In establishing the coequal goals, the Delta Reform Act affirmatively reset spending priorities for the Delta ecosystem and water management. Inherent in the coequal goals is a new governance structure (primarily the Council), which the Legislature intended to have the “authority, responsibility, accountability, scientific support, and adequate *and secure funding to achieve these objectives.*” The Council was directed to develop a long-term, legally enforceable management plan for the Delta, and in implementing the Delta Plan, to “direct actions across State agencies,” in part through the establishment of an Interagency Implementation Committee. Additionally, as addressed in the preceding Delta Plan chapters, the Delta Reform Act set forth a number of policy objectives and other requirements for how the Delta Plan must be developed and what it must contain, ranging from broad guidance on types of projects the Plan should promote, to specific performance measures for evaluating progress on ecosystem restoration. Accordingly, the Council set forth several priority recommendations and regulatory policies, which together make up this Delta Plan.

The Delta Reform Act does not require the development of a financing plan for the implementation of the Delta Plan; however, given the current economic climate, recent uneven funding for water and ecosystem investment, and the critical nature of what is at stake should the coequal goals fail to be achieved, the Council affirmed the need for a financing plan and is committed to its development.

As the Public Policy Institute of California succinctly stated in its 2011 report on water management in California, “Although money alone is not sufficient for successful water

management, it is necessary” (Public Policy Institute of California 2011). In introducing any discussion on financing, particularly in the public sector, it is necessary to acknowledge the political and economic context. America is currently suffering a severe recession, and California’s economy has fared even worse. The State has experienced a multiyear budget crisis in which annual spending exceeds available revenue. As a result, financing infrastructure and new programs has become immensely challenging for State and local governments.

Today’s economic conditions may limit the ability to adequately finance a full range of water and ecosystem improvements necessary to achieve the coequal goals in the near term. However, the planning timeframe for the Delta Plan runs to the year 2100, and decisions on long-term, sustainable financing for water, ecosystem, and flood protection cannot be delayed much longer without grave and expensive consequences. A long planning horizon allows near-term foundational steps to be taken now toward improving the situation and for implementing agencies to stage actions, policies, and projects over time consistent with an adaptive management structure based on science. Additionally, some activities to implement the Delta Plan are currently funded or can be undertaken with no additional cost, and many of the actions called for in the Delta Plan are certain to result in significant long-term cost savings.

Because of the complex nature of the policy issues and of certain funding and finance methods, a comprehensive and supportable Delta Plan finance plan will take time to develop. Thorough research is needed to identify entities that

may be assessed user or stressor fees, determine appropriate levels for these fees, establish tiered fee structures, calculate the public benefits, and work through the legal implications of any financing strategy, including the practical effects of Propositions 218 and 26 on State and local financing mechanisms.

## Background

Since the CALFED Bay-Delta Program was instituted in 1995 to restore ecological health and improve water management in the Delta, significant expenditures have been made in the Delta. An estimated \$400 million has been spent annually, on average, by federal, State, and local water users.

Traditionally, the State has financed water infrastructure with general obligation bonds. These bonds were approved by the voters, and repayment is guaranteed by the State’s general taxing power. With respect to State Water Project (SWP) debt, however, even though repayment was secured by taxes, general obligation bonds were paid back primarily by the water contractors. Since 2000, California voters have authorized \$19.4 billion in water-related general obligation bonds spread over six separate bonds (LAO 2008). Several of these bonds authorize expenditures for a multitude of purposes, including assorted water projects, parkland acquisition, habitat restoration, and local assistance grants. One benefit

of financing water projects with general obligation bonds is that any expenditure made for a public purpose is repaid by taxpayers, the primary beneficiaries. Currently, remaining fund balances for active bond accounts total approximately \$2.2 billion out of the authorized total of \$19.4 billion, only a portion of which is for Delta-related spending.

Table 8-1 summarizes the current balances for general obligation bonds by individual bond act related to water, ecosystem restoration, and flood protection. It is important to note that these remaining balances are not fungible; that is, statute generally dictates the specific types of projects or programs on which funds can be spent.

Currently scheduled for the November 2014 ballot, the Safe, Clean, and Reliable Drinking Water Supply Act of 2012 would authorize, upon voter approval, the issue and sale of \$11.14 billion in general obligation bonds for financing drought relief projects, water supply reliability projects, Delta sustainability projects, water system improvements, watershed and conservation protection programs, groundwater protection and water quality projects, and water recycling projects. Key Delta projects include \$2.25 billion for protection of water supplies from catastrophic levee failure, drinking water quality improvements, levee and flood control facilities improvements, lost property tax replacement, ecosystem restoration, and contaminants reduction.

### General Obligation Bonds – California (as of January 2013)

TABLE 8-1

Bond Act (Year)	Authorized (\$ Thousands)	Committed (\$ Thousands)	Balance (\$ Thousands)
Proposition 12 (2000)	2,024,486	6,189	18,456
Proposition 13 (2000)	2,103,000	1,823,874	279,126
Proposition 40 (2002)	2,471,600	16,556	26,536
Proposition 50 (2002)	3,382,630	0	0
Proposition 1E (2006)	4,090,000	4,024,354	65,646
Proposition 84 (2006)	5,388,000	5,080,840	307,160
<b>Total</b>	<b>\$19,378,411</b>	<b>\$17,221,349</b>	<b>\$2,157,062</b>

Although general obligation bonds have been an important part of how California has funded water and ecosystem projects in the past, because of the uncertainty regarding voter approval of future bonds, a more sustainable and long-term financing approach for water, ecosystem, flood protection, and related projects is needed. As new revenue sources are developed, the use of revenue bonds may become more prevalent. For example, the SWP routinely sells and redeems revenue bonds to pay the costs of planning and construction, bond interest, and project operating expenses, as do many local agencies.

Federal-level expenditures in California in recent years have declined as grant programs for wastewater treatment in the late 1970s and 1980s expired, and flood control spending was reduced. It is likely that large federal budget deficits for the foreseeable future will preclude any increases in federal funds for California water projects.

Although State-level expenditures for water-related programs and projects in recent years have been almost entirely funded with general obligation bonds, this contrasts somewhat with the financing methods available to local agencies. Although many of these agencies have at times issued general obligation bonds and revenue bonds, it is more common for them to establish stable income streams by charging dedicated fees to ratepayers to pay the costs of infrastructure projects including water treatment and wastewater systems.

The ability of local agencies to fund flood control and stormwater projects, however, is specifically governed by the provisions of Proposition 218, approved by California voters in 1996. Under Proposition 218, direct voter approval by a majority of property owners or a two-thirds vote of the general public is required to raise funds for these purposes. Results of local Proposition 218 elections in recent years have been mixed, with some agencies gaining voter approval and others falling short of funding needed for local projects. For example, Sacramento voters successfully approved new assessments for flood control projects in 2007, but 1 year

later, voters in Orinda (East Bay Area) and Burlingame (Bay Area) failed to approve new assessments for the same purpose (Public Policy Institute of California 2011).

A companion measure, Proposition 26, approved by voters in 2010, effectively raised voting requirements for most State and local regulatory fees from a simple majority to a two-thirds majority. Regulatory fees with a broad public purpose are considered taxes and are subject to a two-thirds vote of the Legislature. Local agencies are also required to seek a two-thirds vote of the general public.

The best available information shows that total annual federal, State, and local spending on water and wastewater treatment in California is approximately \$24 billion (see Table 8-2). Operations, maintenance, and capital expenditures for water infrastructure consume significant economic resources in California. This total likely includes some overlap, but the expenditures are significant. Other sources cite higher expenditures for some of these categories. During development of the finance plan, this table will be updated to reflect the most recent data.

### Bay Delta Conservation Plan

Described in various sections of this Delta Plan, the Bay Delta Conservation Plan (BDCP) is a massive water and ecosystem public works planning process under way in the Delta. The Council supports the completion of the BDCP according to the provisions set forth in the Delta Reform Act. The scope or type of any water facility improvements, related Delta ecosystem mitigation, and other habitat improvements to be included is very preliminary at this time. The BDCP's ongoing planning costs are currently funded by State and federal water contractors. Currently available information from the BDCP indicates that, once it is completed, the first 5 years of implementation will require between \$5.7 and \$5.9 billion total for capital outlay, of which approximately \$5.2 billion is for water conveyance. Additionally, the BDCP estimates that \$3.6 billion total plus \$46 million annually will be required for Delta ecosystem

## Annual Budgets/Expenditures in California for Selected Agencies

TABLE 8-2

Agency	Budget/Expenditures		Source
	Operating (\$ Millions)	Capital (\$ Millions)	
Local cities, counties, and special districts water	10,100	2,000	California State Controller 2011a, 2011b, 2011c
Local cities, counties, and special districts wastewater	5,400	1,100	California State Controller 2011a, 2011b, 2011c
Local cities, counties, and special districts flood control	1,000	300	California State Controller 2011a, 2011b, 2011c
California Department of Water Resources	2,267	232	California Department of Finance 2012
State Water Resources Control Board	714		California Department of Finance 2012
California Department of Fish and Wildlife	381		California Department of Finance 2012
Bureau of Reclamation	300		Bureau of Reclamation 2008
U.S. Army Corps of Engineers	100	100	U.S. Army Corps of Engineers 2008
<b>Total</b>	<b>\$20,262</b>	<b>\$3,732</b>	

restoration (BDCP Steering Committee 2010). The BDCP will include a funding plan that will address estimated implementation costs and sources of funding that will be relied upon to cover these costs. The sidebar, Bay Delta Conservation Plan Costs and Existing Funding Sources, provides additional background information about the BDCP.

### Overview of Current State and Federal Delta-related Expenditures

The CALFED Bay-Delta Program was incorporated into the Council in 2010. However, some program elements endure because bond funds are dedicated by law for CALFED purposes. Additionally, the CALFED program is still referenced in federal statutes. For these reasons, an annual cross-cut budget showing State and federal expenditures for active CALFED programs and projects is developed each January.

Because the cross-cut budget includes State and federal expenditure details on all the CALFED programs, those data can be summarized to show expenditures for program elements displayed in the budget. The results are shown in Table 8-3.

## Annual State and Federal Expenditures in California by Program Element (2012–2013)

TABLE 8-3

Program Element	California	Federal	Total
Governance	\$21,145,596	\$20,490,000	\$41,635,596
Water Supply Reliability	\$161,523,833	\$18,774,000	\$180,297,833
Ecosystem Restoration	\$64,119,524	\$92,275,000	\$156,394,524
Water Quality	\$6,368,631	\$5,000,000	\$11,368,631
Risk Reduction/Levee Integrity	\$8,949,231	\$45,560,000	\$54,509,231
<b>Total</b>	<b>\$262,106,815</b>	<b>\$182,099,000</b>	<b>\$444,205,815</b>

### BAY DELTA CONSERVATION PLAN COSTS AND EXISTING FUNDING SOURCES

Potential future funding sources for the BDCP will likely compete with funding required for implementation of some elements of the Delta Plan, and for the plans and projects of State, federal, and local agencies. The Council does not consider any funding source to be solely available for the BDCP, or for any other program or plan. They are solely considered to be options at this stage.

Based on current information from the BDCP, the approximate costs of a facility and related ecosystem improvements needed for State and federal approval are approximately \$15.8 to \$16.7 billion in capital costs and an additional \$4.9 to \$5.6 billion in operating costs over the 50-year permit period. These costs are divided among the BDCP's four primary functions—water conveyance, habitat restoration, management of other stressors, and program oversight—as shown in the table below. The Council notes that preliminary cost estimates are just that: preliminary. Going forward, refined estimates will be required to complete this planning process.

#### Options for BDCP Funding

The BDCP is premised on the pledge of participating State and federal water contractors to pay the full cost of any new Delta export facility and the associated Delta ecosystem mitigation required to meet the requirements imposed on the BDCP by federal and State laws. Habitat and ecosystem restoration activities, beyond mitigation requirements, are considered to provide a general benefit to the State and should be funded accordingly.

Prior to completion of the BDCP and a full understanding of the Delta ecosystem improvements related to the BDCP, it is impossible to project the detailed funding options that might be necessary. However, it is highly likely that user fees, revenue bonds, and sources other than the State General Fund will be the primary sources of funding.

### Summary of BDCP Costs and Existing Funding Sources (\$ millions)

Program Function	Bay Delta Conservation Plan <sup>a</sup>		
	Capital Costs	Operating Costs	Total
Water Conveyance <sup>b</sup>	\$12,691	\$2,936	\$15,627
Habitat Restoration <sup>c</sup>	\$3,108–\$4,009	\$346–\$437	\$3,454–\$4,446
Other Stressors <sup>c</sup>	\$12–\$15	\$1,213–\$1,679	\$1,225–\$1,694
Program Oversight <sup>c</sup>		\$404–\$548	\$404–\$548
<b>Total</b>	<b>\$15,811–\$16,715</b>	<b>\$4,899–\$5,600</b>	<b>\$20,710–\$22,315</b>

<sup>a</sup> Over 50-year permit period

<sup>b</sup> Midpoint cost estimate

<sup>c</sup> Range of low-high estimate given

Source: BDCP Steering Committee, 2010

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## A Delta Finance Plan

The Council proposes to initiate development of a finance plan following adoption of the Delta Plan. This process will require the active participation of the Interagency Implementation Committee described in Chapter 2. Financing and funding mechanisms to be considered in developing the finance plan are included in Appendix N.

### Guiding Principles

A finance plan to fund the Delta Plan should follow these principles:

- The finance plan should first consider currently available funds that can legally support expenditures for Delta-related projects. Spending priorities should be established that address near-term funding requirements as contained in this Delta Plan.
- Implementation of the Delta Plan will undoubtedly require an array of funding sources, including new funding sources and new statutory authority. Broad-based financing and diversity in funding sources will enhance revenue stability. Likewise, State and federal funds for activities that implement the Delta Plan must be reserved for public benefits not otherwise required for project mitigation or required by law for other purposes. Appendix N describes potential funding sources.
- The Delta Plan recommends many projects that have multiple benefits; this increases opportunities to blend fund sources and builds on the tradition of past investments in multipurpose water projects with diversified fund sources.
- A clear and analytically based methodology for assessing public benefits should be evaluated and implemented.
- Targeted finance plans should be developed for major Delta Plan plans and projects (ecosystem restoration, flood risk reduction, regional water supply investments, science, administration, and water conveyance). Beneficiaries and stressors should be identified in each of these

areas, and user fees should be developed to match these stressors and beneficiaries with planned investments in each of these areas.

- Economic and financial analyses should be done as early as possible during the planning of large capital projects. This will assist agencies in the design of cost-effective projects and will help ensure that the projects are actually completed and implemented. Financial analyses should account for all of the costs of a project, both direct and indirect, including acquisition, planning, capital and interest, mitigation, science and monitoring, and operations and maintenance.

### User Fees

- User fees, including beneficiary fees and stressor fees, are essential and should be established to support the coequal goals and the implementation of the Delta Plan.
- The “beneficiaries pay” principle is a common financing approach for water projects. The challenge is to determine the beneficiaries and design a cost-allocation method scaled to the benefit.
- A companion principle to “beneficiaries pay” is “stressors pay.” Human activity that causes negative operational or environmental impacts should be assessed a fee, or otherwise charged, to repair the damage. An example of the stressors pay approach might be a surcharge on pesticides that are found to negatively impact the Delta ecosystem. Capital construction projects, whether for water reliability purposes or Delta ecosystem improvements, should be undertaken simultaneously with the development of beneficiary and user fees. Delay in establishing beneficiaries/stressors fee structures will inevitably delay any needed capital improvement projects. The development of information related to financing (such as the identification of beneficiaries and stressors, and detailed financing scenarios) should be undertaken simultaneously with the development of major capital decisions so that it can inform planning efforts.



- The finance plan should include mechanisms to ensure that user fees are legally dedicated to their intended purpose. Given State and federal budget constraints, statutory protections must be enacted to assure users that their assessments will not be diverted to other purposes.
- The finance plan should include opportunities to generate revenue when planning projects, where possible, to ensure long-term financing stability.
- To the extent possible, user fees should be based on the amount of water used or, for stressors, the volume of contaminants discharged. Tiered fee structures also should be explored where applicable.
- Long-term, stable funding approaches, such as the Delta Flood Risk Management Assessment District recommended in Chapter 7 or other beneficiary user fees, should be established to support the Delta Levees Maintenance Subventions Program, Delta Levees Special Flood Control Projects Program, and implementation of the Central Valley Flood Protection Plan.

### Near-term and Annual Funding Requirements

The following items describe activities that must be addressed and funded as soon as possible. They describe the urgent need to immediately address the steps needed to achieve the coequal goals, begin implementation of the Delta Plan, and establish annual funding for key Delta agencies:

- **Urgent expenditures for water supply reliability and ecosystem protection.** Immediate steps should be taken to protect the existing Delta water export system from flood risks and carry out ecosystem improvements being implemented pursuant to existing mitigation commitments of the SWP and the Central Valley
- Project. Those immediate needs are discussed in the various chapters of the Delta Plan.
- **Create a regional Delta Flood Risk Management Assessment District.** The Legislature should create a regional district with the authority to assess fees on Delta levee beneficiaries, including landowners, infrastructure owners, and other entities, to fund flood control protection, including levee maintenance and improvement, and emergency response, as recommended in Chapter 7.
  - **Fund a strong Delta Science Program.** Funding is needed for continued operation of the Independent Science Board, development of the proposed Delta Science Plan, the State's share of the Interagency Ecological Program, and other activities that support a strong science foundation for Delta Plan implementation. Funding for the Interagency Ecological Program should continue from participating agencies.
  - **Fund urban and agricultural water management plans.**
  - **Continue the existing operational duties imposed by the Delta Reform Act.** The Act created the Council (which includes the Delta Science Program and Independent Science Board) and the Sacramento-San Joaquin Delta Conservancy, and modified the duties of the Delta Protection Commission. Future estimated annual operating costs for these agencies are provided in Appendix M.
  - **Fees for services.** The Legislature should grant authority to the Council to assess fees to cover the costs of providing specified services related to covered actions, specifically early consultations and reviewing appeals of consistency certifications.

## POLICIES AND RECOMMENDATIONS

Administrative performance measures for the following recommendations can be found in Appendix E.

### FP R1 Conduct Current Spending Inventory

An inventory of current State and federal spending on programs and projects that do or may achieve the coequal goals will be conducted. Data sources to be used include the CALFED cross-cut budget, State bond balance reports, and the annual State budget, among others. Consideration will be given to selecting an independent agency (which could include a nongovernmental organization) to conduct the inventory.

### FP R2 Develop Delta Plan Cost Assessment

Costs will be assigned to the projects and programs proposed in the Delta Plan (Chapters 2 through 7), and sources of funding will be identified.

### FP R3 Identify Funding Gaps

Current State and federal funding gaps will be identified that are determined to hinder progress toward meeting the coequal goals.

## Timeline for Implementing Recommendations

Figure 8-1 lays out a timeline for implementing the recommendations described in the previous section.

## Timeline for Implementing Recommendations

TIMELINE		CHAPTER 8: Funding Principles to Support the Coequal Goals		
ACTION (REFERENCE #)		LEAD AGENCY	NEAR TERM 2012–2017	INTERMEDIATE TERM 2017–2025
RECOMMENDATIONS	Conduct current spending inventory (FP R1)	Council	●	
	Develop Delta Plan cost assessment (FP R2)	Council	●	
	Identify funding gaps (FP R3)	Council	●	

**Agency Key:**  
Council: Delta Stewardship Council

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Figure 8-1

## References

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