



June 25, 2003

The Honorable Governor Gray Davis
Governor
State of California
State Capitol Building
Sacramento, CA 95814

RE: Modified Quantification Settlement Agreement

Dear Governor Davis:

On behalf of the Imperial Irrigation District ("IID"), Coachella Valley Water District ("CVWD"), and the San Diego County Water Authority ("SDCWA"), the undersigned are writing to express our appreciation and gratitude for your and your staff's assistance in working with Senator Machado to assure that implementation of the Quantification Settlement Agreement ("QSA") will not preclude restoration of the Salton Sea. The purpose of this letter is to respond to Senator Machado's suggestion for a Modified QSA that would provide a three-year time period for assessment of Salton Sea restoration, enable the substitution of desalinated drainwater for the water conservation activities of the QSA, and for additional environmental contributions by the parties.

As we have mentioned on previous occasions, our three agencies believe that implementation of the IID/SDCWA and IID/CVWD QSA transfers will not interfere with any restoration plan that includes desalination of IID drain water. As we agreed at the June 16th meeting with the administration and Senator Machado, we have prepared principles under which a restoration project could substitute for the IID/SDCWA and IID/CVWD QSA transfers and propose additional environmental contributions by the parties. We summarize the principles and share some concerns that must be addressed in any subsequent discussions of this approach.

There are two basic premises underlying the attached principles. First, to substitute for QSA transfers, a restoration project must provide a credible supply source by a defined time deadline, but enable the QSA transfers to proceed as planned. We propose criteria for a trigger

that includes environmental and regulatory compliance with full permitting and firm financial commitments for a restoration project that can provide the substitute water supply, no later than the December 31, 2006 deadline proposed by Senator Machado. This deadline only allows one year for IID to start implementation of the QSA efficiency conservation projects and commence transfers to CVWD starting in year 2008. We also believe that the interests of our agencies, California and the other Basin States would not be served by postponing the water conservation and transfers under the QSA that relies on a restoration plan that would still be under preparation after the deadline.

Any substitution for QSA transfers must also assure that each party will receive substantially the same benefits and burdens as the transfers under the QSA. We propose that the Modified QSA contain specific substitution criteria: environmental and regulatory compliance, firm funding commitments, reasonable and beneficial use protection, preservation of economic equivalency, transfer protection, maintenance of water budgets, preservation of other elements of the QSA, and necessary federal concurrence.

We offer the attached principles to continue the helpful discussions we had with Senator Machado on June 16th. At that meeting, the Senator requested that we consider how to implement his idea for restructuring the current QSA to allow for a conversion to a substitute supply created by Salton Sea restoration. It is important for all to understand that the QSA is the product of multi-year negotiations, completed environmental review, and completed State Water Resources Control Board approval. In contrast, discussions of the recent Salton Sea restoration alternative with desalination have just begun, and the feasibility and environmental reviews have not yet commenced. We will continue our efforts to resolve all the issues necessary to assure that the restoration of the Salton Sea can be addressed in a manner that is consistent with the needs of the parties to the QSA.

Senator Machado also requested that the agencies offer additional environmental contributions to reduce the state funding condition precedent. The three agencies have developed the attached proposal, which would provide additional financial contributions with a present value of \$30 million. This additional contribution would reduce the state funding condition precedent to \$170 million. These contributions are based on the principle that beneficiaries contribute based on the additional supplies of water created by the QSA.

The undersigned believe that our proposals address the request of Senator Machado in allowing time for the restoration of the Salton Sea to move forward and to provide additional environmental contributions by the parties. For this proposal to be successful, the four agencies must immediately approve the March 12, 2003 QSA and related documents as modified by our

proposal. It is imperative that the four agencies meet with you and Senator Machado to complete these critical agreements to ensure water supply reliability to all of California.

Sincerely,



Steve Robbins
General Manager
Coachella Valley Water District



Maureen A. Stapleton
General Manager
San Diego County Water Authority



John Carter
Chief Counsel
Imperial Irrigation District

SR:MS:JC:njs

cc: The Honorable John Burton, Senate President Pro Tempore
The Honorable Mike Machado, Chairman, Agriculture and Water Resources Committee
The Honorable Herb Wesson, Speaker of the Assembly
The Honorable Joe Canciamilla, Chairman, Assembly Committee on Water, Parks & Wildlife
Secretary Mary Nichols, Resources Agency
Secretary William Lyons, Department of Food and Agriculture
Director Robert C. Hight, Department of Fish and Game
Acting Director Mike Spear, Department of Water Resources
Ms. Linda Adams, Governor's Office
Mr. Richard Katz, Governor's Office

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PRINCIPLES FOR MODIFIED QUANTIFICATION SETTLEMENT AGREEMENT ("MQSA")

Purpose

Senator Machado has proposed a modification of the existing Quantification Settlement Agreement of March 12, 2003 (QSA) to ensure that the potential for a Salton Sea restoration is fairly evaluated within a three-year period before substantial volumes of water are conserved by IID and transferred to SDCWA and CVWD. Under the proposal ("MQSA"), the four agencies (MWD, IID, CVWD, and SDCWA) would execute and implement the existing QSA and related agreements immediately.

The MQSA should transfer water in accordance with the existing QSA schedule. If a viable restoration program were developed by December 31, 2006 that satisfied the defined criteria below, the four agencies would agree to: (i) a substitution of desalted water made available from the Salton Sea Restoration Alternative ("SSRA")¹ for some or all of the conserved water that would otherwise be generated by IID; and (ii) the use of some or all of the State funding for the SSRA from sources including but not limited to Proposition 50, Proposition 13 and Proposition 204. Deferral of the QSA transfers for the first three years is not necessary for the following reasons:

1. There is no impact on the Salton Sea.
2. There is no identified source of substitute water that is immediately available for transfer.
3. Northern California would resist the transfer of the 60,000 acre feet of substitute water during the three years.
4. Environmental review of the QSA did not include substitute supplies during the first three years.
5. Starting QSA transfers in year 1 is consistent with expectations of the other Basin States.

The criteria provided below would allow the SSRA to be evaluated against the QSA for its sufficiency. If the criteria were satisfied, the parties would agree to the substitution of SSRA water so long as it is available for delivery before the initiation of efficiency conservation transfers under the Compromise IID/SDCWA and QSA Delivery Schedule (Exhibit J, QSA). If the SSRA were not available in a timely manner, the SSRA opportunity could still be developed in conjunction with the QSA to provide the additional water needed to fill the Colorado River Aqueduct.

Federal Concurrence

The MQSA must be acceptable to the Secretary of Interior and result in surplus water made available to California in quantities specified in the ISG.

¹ The SSRA must include the creation of transferable water consistent with the Transfer Protection criterion discussed below and restore the Salton Sea

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Criteria

To trigger the substitution of the water generated by the SSRA for that which would be created and transferred by IID, the SSRA must ensure all of the following:

- *Environmental and Regulatory Compliance.* The SSRA must be fully permitted and authorized by state and federal entities, and provide an equivalent level of protection to the parties against foreseen and unforeseen environmental consequences as contemplated by the Environmental Cost Sharing Agreement of the QSA and all applicable law.
- *Funding Commitment.* The entity responsible for the design, construction and operation of the SSRA has secured firm funding commitments for all anticipated project, environmental, regulatory and restoration costs to complete the restoration of the Salton Sea and make substitution water available over the term of the QSA.
- *Reasonable and Beneficial Use Protection.* Comprehensive determination by state and federal entities that each party's respective use of Colorado River water constitutes a reasonable and beneficial use, even if as a result of the SSRA, any party's purpose or method of existing use remains unchanged.
- *Preservation of Economic Equivalency.* The economic benefits and detriments attributable to each party under the SSRA must be generally equivalent to those provided under the QSA.
- *Transfer Protection.* The quantities, quality, duration, timing, reliability and cost of the water transferred to SDCWA and CVWD through the SSRA will be substantially similar to the transfers to those parties under the QSA.
- *Water Budgets Maintained.* The water budgets available to each of the parties will be substantially similar to those provided in the QSA.
- *QSA Preserved.* The provisions of the QSA that are not subject to the substitution of the SSRA must remain in full force and effect; e.g. canal linings, quantification.

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**Proposed Additional Environmental Contributions
by Parties to the QSA Transfers¹**

	<i>Present Value (mil)</i>	<i>Cumulative Value (mil '03\$)</i>
Original Contribution	\$43.3	\$120.6
Additional Contribution	\$30.0	\$54.6
Total	\$73.3	\$175.2

Total Environmental Contribution

	<i>Present Value (mil)</i>	<i>Cumulative Value (mil '03\$)</i>	<i>Cumulative Water Made Available by QSA</i>
IID/SDCWA/CVWD	\$48.7	\$125.2	10.0 million AF
MWD	\$24.6	\$50.0	11.1 million AF
Total	\$73.3	\$175.2	21.1 million AF

Note: MWD receives majority of water made available by QSA and pays for minority of local agency environmental contribution

Overriding Principle: beneficiary pays

Definition of Beneficiary: Any party who transfers water or receives additional water from the implementation of QSA enabled transfers and ISG surplus water. Transferee pays 100% of contribution if transferor is not compensated except for minimal O&M costs (*e.g.*, canal lining O&M reimbursement)

Definition of Additional Water Available to Beneficiary:

- IID/SDCWA (6.88 million AF)
- IID/CVWD (3.15 million AF)
- IID/MWD (water not taken by CVWD from IID/CVWD transfer)
- PVID/MWD (3.15 million AF)
- Lining Projects (3.24 million AF)
- Extension of '88 IID/MWD Agreement (1.54 million AF)
- IID and CVWD assumption of part of MWD responsibility for Indian and miscellaneous PPR's (0.65 million AF)
- ISG surplus water (2.5 million AF)

¹ Evaluated assuming 45-year initial term of QSA

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Additional QSA Environmental Fee

- Fee imposed until \$30 million ('03\$) generated
- Agricultural to agricultural transfers contributes at 2/3rd of the rate for agricultural to urban transfers

MWD Receives Majority of Water and Pays Minority of Environmental Costs

