

January 7, 2016

Hon. Kamala D. Harris
Attorney General
1300 I Street, 17th Floor
Sacramento, California 95814

Attention: Ms. Ashley Johansson
Initiative Coordinator

Dear Attorney General Harris:

Pursuant to Elections Code Section 9005, we have reviewed the proposed constitutional and statutory initiative (A.G. File No.15-0107, Amendment No. 1) that would redirect up to \$10.7 billion in previously authorized general obligation bond authority to certain water-related projects and amend the constitution to prioritize certain uses of water.

BACKGROUND

Water Sources, Infrastructure, and Uses

Sources of Water in California. Rivers originating in the Sierra Nevada Mountains and other mountain ranges in Northern California are filled mainly by rainfall and snowmelt and provide most of the state's water supply. Water available underground (referred to as "groundwater") supplies roughly a third of the state's water use and is more heavily relied on in dry years. A small share of the state's water supply also comes from other sources, such as capturing rainwater, reusing wastewater (water recycling), and removing the salt from ocean water (desalination).

Meeting the State's Water Needs. There are many demands on the state's water supply, and meeting these demands presents several key challenges. First, water is not always naturally available where it is needed, such as for the farms of the Central Valley and the population centers in the San Francisco Bay Area and Southern California. Consequently, the state's water system is designed primarily to deliver water from Northern California—where it is more plentiful—to other regions of the state. Second, the amount of water available can change widely from year to year. So, when less water is available in dry years, it can be difficult to meet the demand for water throughout the state. These demands include providing water for drinking, irrigating crops, and maintaining natural habitats—such as rivers and wetlands—for endangered species as is required under state and federal laws. However, mostly in very wet years the state can sometimes experience floods, particularly in the Central Valley. Third, water is sometimes polluted making it unsuitable for drinking, irrigating crops, or maintaining natural habitats.

In order to address these challenges, California has built various water-related projects. Some projects use natural rivers—as well as pipelines, pumping stations, and canals—to deliver water

throughout the state. These projects also include dams and other types of water storage to hold water for when it is needed. Other projects to meet the state's water challenges include treatment plants to remove pollutants from drinking water and wastewater, systems to clean up runoff from storms, and levees to prevent floods. The state has also taken a variety of actions to improve natural habitats and water quality. These include restoring watersheds (an area of land that drains into a body of water) by reintroducing native plants and animals. The state has also provided water to rivers when needed by fish.

Beneficial Uses of Water in California. The California Constitution requires that the water resources of the state be put to beneficial use as much as possible, and that the waste or unreasonable use of water be prevented. Other laws and court decisions guide interpretations of what constitutes a beneficial use of water. Federal, state, and local government agencies allocate water based on this legal framework. Balancing these beneficial uses of water is complex, and agencies weigh such factors as water rights, public health concerns, and environmental factors. There are three main types of beneficial uses:

- ***Domestic Uses.*** Beneficial domestic uses include supplying drinking water and water for industrial purposes.
- ***Agricultural Uses.*** Beneficial agricultural uses include supplying water for livestock and irrigation of crops.
- ***Environmental and Recreational Uses.*** Beneficial environmental uses include supplying water to sustain fish populations and habitat. Beneficial recreational uses include supplying water for boating and aesthetic enjoyment such as for wild and scenic rivers.

Roles of Various Governments in the Water System. The state, federal, and local governments play important roles in providing clean and reliable water supplies. Most spending on water programs in the state is done at the local level, such as by water districts, cities, and counties. In recent years, local governments have spent approximately \$26 billion per year to supply water and to treat wastewater. About 80 percent of this spending is paid for by individuals as ratepayers of water and sewer bills. In addition, local governments pay for projects using other sources, including state funds, federal funds, and local taxes. While most people get their water from these public water agencies, about one-sixth of Californians get their water from private water companies.

The state runs programs to (1) conserve, store, and transport water around the state; (2) protect water quality; (3) provide flood control; and (4) protect fish and wildlife habitat. The state provides support for these programs through direct spending, as well as grants and loans to local government, nonprofit organizations, and privately-owned water companies. (The federal government runs similar programs.) Funding for these state programs usually comes from bonds and fees.

The 2014 Water Bond (Proposition 1). On November 4, 2014, voters approved a water bond measure—Proposition 1. The proposition provides a total of \$7.5 billion in general obligation bonds—\$7.1 billion in new general obligation bonds and \$425 million in redirected general obligation bonds that were previously approved by voters—for various water-related programs. One of the larger allocations of the \$7.5 billion is \$2.7 billion to pay up to half of the cost, with certain exceptions, of new water storage projects including dams and projects that replenish groundwater. This funding can only be used to cover costs related to the “public benefits” associated with storage projects, including restoring habitats, improving water quality, reducing damage from floods,

responding to emergencies, and improving recreation. Local governments and other entities that rely on the water storage projects would be responsible for paying the remaining project costs. Projects have to provide measureable improvements to the Sacramento-San Joaquin Delta ecosystem or to the tributaries to the Delta.

High-Speed Rail

Voters Approved Funding for High-Speed Rail in 2008 (Proposition 1A). In November 2008, voters approved Proposition 1A, which authorizes the state to sell up to \$9.95 billion in general obligation bonds for the development and construction of a high-speed rail system. Of this amount, \$9 billion is available to support planning, engineering, and capital costs for the system. The remaining \$950 million in bond funds is available for capital improvements to existing passenger rail service—specifically, intercity, commuter, and urban rail systems. The bond funds authorized in Proposition 1A require a match of at least 50 percent from other funding sources such as the state, federal, and local governments, or the private sector. A total of about \$5 billion in Proposition 1A funds have been appropriated to date with a total of about \$1 billion of bonds sold to date (leaving about \$8.9 billion in unsold Proposition 1A bond funds).

Federal Funds for High-Speed Rail. The California High-Speed Rail Authority (HSRA), which is responsible for planning and constructing the high-speed rail system, has received \$3.5 billion in federal funds for planning, engineering, and construction of high-speed rail in the Central Valley, which require matching state funds. All of the federal funds have been appropriated to HSRA, which began construction of the high-speed rail system in the Central Valley in 2014 using these funds. Currently, about \$670 million of the federal funds have been spent. Of the remaining \$2.8 billion in unspent federal funds, about \$1.9 billion is available to the state through September 30, 2017. The roughly \$900 million in remaining federal funds must be spent before December 31, 2018, under the terms of the current federal agreement.

PROPOSAL

This measure amends the State Constitution to prioritize reasonable and beneficial public uses of water and redirects up to \$10.7 billion in general obligation bond funds approved by the voters under Proposition 1 and Proposition 1A to certain water-related projects.

Constitutional Amendment to Prioritize Reasonable and Beneficial Uses of Water. The measure amends the State Constitution to prioritize the reasonable and beneficial uses of water. Under the measure, “the public interest in assuring the highest priorities of beneficial use and water conservation, as a public benefit and to satisfy the public trust, shall be first, domestic use, and second, irrigation use through the development and maintenance of surface water and groundwater storage facilities.”

Redirects Bond Funds From Propositions 1A and 1. This measure redirects up to \$10.7 billion in general obligation bonds from Propositions 1A and 1 to certain water-related projects (discussed more below). Specifically, the measure would redirect up to \$8 billion in unsold Proposition 1A bond funds for high-speed rail. The remaining bond funds above this amount would continue to be available for the state’s high-speed rail project.

In addition, the measure redirects up to \$2.7 billion authorized under Proposition 1 for new water storage projects including dams and projects that replenish groundwater. The requirements

under Proposition 1 that the funding could only be used to cover costs related to the public benefits associated with the storage projects would no longer apply.

Measure Allocates Bond Funds to Certain Water-Related Projects. The measure creates the 2016 State Surface Water and Groundwater Storage Facilities Fund (fund), established in the state Treasury. The Proposition 1 and Proposition 1A bond funds redirected pursuant to the measure would be deposited in the fund and allocated to water projects as follows:

- ***New Construction of Surface Water Storage Projects (\$4.2 Billion).*** The measure provides \$4.2 billion for new construction of surface water storage projects and specifies that the proposed Sites Reservoir (in Colusa and Glenn Counties) and Temperance Flat Reservoir (in Fresno and Madera Counties) projects are eligible for such funding.
- ***Projects to Increase Surface Water Storage Capacity (\$900 Million).*** The measure provides \$900 million to increase the surface storage water capacity of existing facilities and specifies that San Luis Reservoir (in Merced County) and Shasta Dam (in Shasta County) projects are eligible for such funding.
- ***New Construction of Groundwater Storage Facilities (\$2 Billion).*** The measure provides \$2 billion for construction of new groundwater storage facilities to recharge existing groundwater aquifers.
- ***Modernization of Existing Facilities (\$2.2 Billion).*** The measure provides \$2.2 billion for modernization of existing surface and groundwater storage facilities.
- ***Remaining Funds Reserved for Future Spending.*** Unexpended proceeds of bonds after the completion of the projects identified above are reserved for future spending for public benefits resulting from construction of local surface water and groundwater projects.

Measure Establishes State Water Authority. The measure creates the State Water and Groundwater Facilities Authority (Authority) within the Department of Water Resources. The Authority would consist of nine regionally selected members. The Authority would be exclusively responsible for authorizing the development of plans and construction of the water storage and groundwater storage projects funded by the measure.

FISCAL EFFECTS

Effect on State Debt Costs. Redirecting up to \$10.7 billion in bond funds from previously approved measures would not significantly increase or decrease the state's anticipated debt payments, assuming these bonds would have been sold in the future to support high-speed rail (as authorized under Proposition 1A) and water-related projects (as authorized under Proposition 1).

Possible Effects on Receipt of Federal Funds. The measure would affect the amount of federal funds that would come into California for high-speed rail and water-related projects. On the one hand, as described above, high-speed rail has already received \$3.5 billion in federal funding, which may not fully be drawn down if this measure passes. On the other hand, state and local water agencies might be able to draw down more federal funding for water-related projects mainly because of the higher overall amount of funds available for these purposes. The amount of additional funding for water-related projects is unknown and would depend on the specific projects selected, as well as

the amount of federal funds available. In total, the net effect of the measure on federal funds is unknown.

Other Fiscal Effects on State and Local Governments. The measure amends the State Constitution to prioritize *first* the domestic uses of water, and *second*, irrigation as the highest priorities for beneficial water use. As a result, some existing state laws that guide the use of water might be inconsistent with the Constitution if the measure passes. Determining which laws are inconsistent with the proposed constitutional provision and how to apply these laws likely would need to be decided by the courts. Depending on the outcome of any such cases, state and local governments could be required to change how various water-related projects are operated and how water is allocated. To the extent that water is allocated differently, there could be some fiscal effects, such as some water agencies paying higher or lower amounts for water. The resulting net impact from the above fiscal effects on state and local governments is unknown.

The fiscal effects of the measure on the state would also depend on whether the state continued to pursue a high-speed rail project in the future. For example, if the state were to pursue a high-speed rail project, the state would require additional funding to complete the project. On the other hand, if the state were not to continue with such a project, it could (1) achieve significant savings by relieving the need for future state funding for the project and (2) result in the state being required to repay federal funds. However, the state might need to fund other transportation projects to replace the capacity that the high-speed rail system would have provided.

Summary of Fiscal Effects. This measure would have the following fiscal effects:

- No significant increase or decrease in the state's anticipated debt payments from the redirection of up to \$10.7 billion in bonds from previously approved measures, assuming these bonds would have been sold in the future absent this measure.
- Unknown net fiscal effects on state and local governments due to measure's changes to how water is prioritized in the State Constitution, as well as potential changes to funding levels available for capital projects.

Sincerely,

Mac Taylor
Legislative Analyst

Michael Cohen
Director of Finance