



Topic: **Reservoir Committee Agenda Item 2.2** **2020 August 21**

Subject: **Funding Credit and Reimbursement Policy Implementation**

Requested Action:

Approve updated Funding Credit and Reimbursement Policy (Policy).

Detailed Description/Background:

When the Reservoir Committee was formed, one of the requirements included the development of this Policy to ensure equity among participants and be an important component to the rebalancing process. The initial Policy went through a thorough development and review process and was approved by the Authority in August 2018. A revised Policy is now required as the Authority continues to progress into new phases of the project.

A subgroup of the Joint Budget and Finance Committee was convened to review the current Policy and develop draft revisions as needed to reflect the status of the current Sites Project. The Subgroup developed a working draft revised Policy and examples of applying the draft Policy which were reviewed and commented on by the Joint Budget and Finance Committee during their July 10, 2020 meeting. A revised draft was prepared based on the comments received and discussed at the July Reservoir Committee and Authority Board meetings.

Comments from these meetings were incorporated into a revised draft which was reviewed by Authority General Counsel and then by the Joint Budget and Finance Committee. Attachment A provides the revised Policy for consideration of approval.

The most significant changes being proposed in the revised Policy from the current Policy are:

- Revisions to Section 6 "Participation Priority" include the addition of two new priority rounds. A revision was also made to clarify the application of "Last in / First Out" approach should the available participation be reduced below the amount of participation by Project Agreement Members.
- Revisions to Section 10.3 "Limitation on Reimbursements" provides additional clarity to when the Authority would make reimbursement payments.
- The new Section 14 "Provision for Buy-in After Phase 1" was added to specify the requirement that additional or new participation pay the equivalent funding of prior phases upon executing the Project Agreement.
- The new Section 15 "Provision for Phase 2 Rebalancing and True-up Process" was added to provide a process for Project Agreement Members to change their level of participation at the conclusion of each incremental Phase 2 Project Agreement. The provision is similar to the Phase 1 True-up with the exception of Class 2 Water conversion.

In response to comments received subsequent to last month's review by the Reservoir Committee, additional revisions were made to expand the application of the policy to Phase 2, provide flexibility for allowing incremental Project Agreements and associated participation changes, recognize federal and State participation and clarify/specify previous provisions and requirements.

Prior Action:

July 22, 2020: Reviewed and commented on the Working Draft Funding Credit and Reimbursement Policy Revisions.

August 16, 2018: The Credit Reimbursement Policy was approved.

June 25, 2018: The status was discussed with direction provided to the Ad Hoc Finance and Economics Work Group.

Fiscal Impact/Funding Source:

The Policy's requirement to reimburse Project Agreement Members for partial or complete withdrawal from the Project would be funded by new revenue for the "Buy-in" payments received from an existing Project Agreement Members that increase their amount participation or from new/returning Project Agreement Members initiating participation. Reimbursement payments would only be made once the Reservoir Committee and Authority Board determine that funds are available to make such payments without impacting the implementation of the Project.

Staff Contact:

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Attachments:

Attachment A: Funding Credit and Reimbursement Policy.

Sites Reservoir Project, Phase 1 & 2 Funding Credit and Reimbursement Policy

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APPENDIX A – Participating Members and Respective Priority

Status: **Adopted by Authority**
Purpose: **Rev1 – Phase 2**
Caveat:
Notes:

Preparer: **S. Brown**
Checker:
QA/QC:

Phase: **1** Version: **1D5**
Date: **2020 August 3**
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1. PURPOSE OF POLICY

The Sites Project Authority (Authority) has adopted bylaws¹ that establish use of a Cost Development Model to track each participating agency's funding contributions and anticipated funding requirements as the Sites Reservoir Project (Project) is developed.

The purpose of this Funding Credit and Reimbursement Policy (Policy) is to establish the rules and procedures for contributing funds for the Project that will be used to inform the Cost Development Model as the project advances. The specific objectives of the Policy are to define the provisions and terms for:

- Defining contribution credit to participating agencies (Project Agreement Members, see **Section 3.8**) for having contributed funds to advance the Project;
- Defining allowable conditions for the use and/or reimbursement of credit;
- Providing an equitable exchange in participation levels between Project Agreement Members; and
- Defining the process for recalculating the equivalent cost basis among Phase 1 Project Agreement Members for Class 1 and Class 2 water².
- Defining the process for recalculating the equivalent cost basis for future phases of the project that are funded on a "cash call" basis.

It is the intent of this Policy to ensure that all Project Agreement Members will each have paid the same amount on an equivalent cost basis as the Project advances.

The Policy only applies to contributions from Project Agreement Members and is not intended to be used to determine the value or priority of Federal or State Funding.

2. ADMINISTRATIVE

2.1 Role of the Authority and Reservoir Committee

Through its Bylaws, the Authority considers this process to be a foundational part of advancing the Project. Development of the terms of this Policy has been undertaken by the participants in each phase of the Reservoir Project Agreements (Reservoir Committee). Acceptance of this document by the Authority is required before this Policy can be implemented.

2.2 Amendments to this Policy

It is the Authority's intent that this policy be updated as needed (i.e. is a "living" document) to ensure the Project is implemented equitably, efficiently and cost-effectively. The Authority may

¹ November 21, 2016 Amended and Restated Bylaws of the Sites Project Authority for Phase 1 of the Sites Reservoir Project, Section 3.9.

² Participation in voting and funding is based on a Members' participation as measured in acre-feet that is used to apportion the project's development costs. Until the completion of Phase 2, the annualized volumes of water that could be released from storage can't be finalized until the Project has acquired the prerequisite permits needed for construction and operations and both state and federal agencies have committed to fund their equitable share in the Project.

amend this Policy to reflect changes to the funding structure for the Project (e.g. separate participation in water storage versus water supply). Any amendment to this Policy will not reduce or increase any participant's contribution credit (as defined below) for having contributed funds to advance the Project.

2.3 Precedence of Documents

This document is subordinate to both the Authority's and Reservoir Committee's governance documents. Should a conflict exist, the Authority's Joint Exercise of Powers Agreement - including the Bylaws - shall take precedence, followed by the Reservoir Committee's sequential Reservoir Project Agreement for each phase of the Project (Requirements).

Further and in keeping with the *Mission and Project's Primary Goals* established in Phase 1³, should a conflict exist between this document and any Reservoir Project Agreement, which may include the terms and conditions for the interim finance plan, the Reservoir Project Agreements shall control, and this document shall be amended to remove the conflict.

2.4 Document Revision History

A record of approved changes to this document shall be recorded in this section, starting with its original approval for use, which is revision 0.

<u>Rev.</u>	<u>Effective Date</u>	<u>Status of Authorizing Action</u>
0	August 20, 2018	Approved by Reservoir Committee and adopted by the Authority.
1	TBD	Revised to include Phase 2 considerations.

3. DEFINITIONS

The following definitions are used in this Policy:

- 3.1. "Class 1 Water" Water supply reserved for Project Agreement Members based on 50% of the total average annualized volume of water released from storage (250 TAF⁵).
- 3.2. "Class 2 Water" Additional 170 TAF⁴ of water supply that may be available to Project Agreement Members, of which the State of California and/or the United States Government will be given the first right to acquire for ecosystem and water quality "public" benefit(s).
- 3.3. "Contribution Credit" The accumulated funding provided by a Project Agreement Member for both Class 1 and Class 2.

³ Refer to Exhibit B of the Phase 1 Reservoir Project Agreement, General Requirements.

⁴ These acre footage values are based on original project yield projection at the onset of Phase 1 in 2016 and are subject to change throughout the duration of the project.

- 3.4. “Equivalent Cost Basis” The equivalent cost per acre-foot for Class 1 water established by the Reservoir Committee.
- 3.5. “Equivalent Required Funding” The amount of funding required by each Project Agreement Member at the Phase 1 True-up event (**Section 13**) equal to the Equivalent Cost Basis times the Project Agreement Member’s participation in Class 1 water.
- 3.6. “Fully Subscribed Project” Full participation in the total amount of Class 1 Water available. The amount of Class 1 Water available is equal to the total water made available by the Project less the amount of water reserved for federal and state investment in the Project. The associated amount may change between the end of Phase 1 and end of Phase 2. Further, it is contemplated that in Phase 2, consideration will be given to shift from the current delivery-based method (FOB Holthouse Reservoir) to a storage-based method.
- 3.7. “Funding Obligation” A Project Agreement Member’s semi-annual pro-rata share of funding required. The Authority may elect to waive any Project Agreement Member from a semi-annual obligation by excluding that particular Project Agreement Member’s participation in the Project when determining the basis for the pro-rata share of the remaining Project Agreement Members.
- 3.8. “Project Agreement Member” Any agency or entity that has executed a Project Agreement and not withdrawn from the project.⁵
- 3.9. “Good Standing” Meeting the requirements to actively participate in the Project according to Section 8.1 of Authority’s Bylaws.
- 3.10. “Participation” A Project Agreement Member’s elected participation rate expressed in terms of acre-feet of average annual water supply, or other metric utilized to determine the pro-rata share of funding required from each Member.

⁵ Ibid, Section 7.3 for membership types. A list of current Project Agreement Members is provided in Exhibit A1 of the Phase 1 Reservoir Project Agreement.

Project Agreement Members to change their participation. These changes will become the basis for the Phase 1 True-Up.

- 5.6 As the Project advances, each additional phase of the project will require Project Agreement Members to commit funding through execution of a new Project Agreement. Changes in participation may be allowed at the conclusion of each phase, subject to the credit and reimbursement conditions established by this Policy.

6. PARTICIPATION PRIORITY

As more or less Class 1 Water becomes available, each Project Agreement Member's allocation of Class 1 and/or Class 2 Water may be impacted based on the priority assigned to its participation in the manner provided below. Should the level of participation need to be reduced, the reduction will occur on a "last in / first out" basis. Each Project Agreement Member will be assigned a priority based on the following criteria:

- Round 1 Priority: Founding members of the Authority who also elected to execute the Phase 1 Reservoir Project Agreement. Project Agreement Members in this round received Class 1 Water.
- Round 2 Priority: New members of the Authority seated prior to the 2016 on-boarding process who elected to execute the Phase 1 Reservoir Project Agreement. Project Agreement Members in this round received Class 1 Water.
- Priority 2.1: Existing members of the Authority seated prior to the 2016 on-boarding process, who had executed the Phase 1 Reservoir Project Agreement, and who elected to change their participation quantities in advance of the August 1, 2016 deadline that closed the On-boarding process. These changes were approved by the Authority on June 13, 2016.
- Round 3 Priority: Additional participation beginning with the 2016 On-Boarding process and extending through execution of a funding agreement with the State. Project Agreement Members in this round receive either:
- 1) For Public Water Agencies: A combination of Class 1 and/or Class 2 Water dependent upon the availability of Class 1 Water; or
 - 2) For Non-Member Participating Parties: Mutual Water Companies who submitted a request to participate as part of the 2016 On-Boarding process received Class 2 Water.

Note that a rounding error in the original allocation of Class 1 and Class 2 water was found November 2017. The correction to the rounding error was applied retroactively to Priority 3 participants.

The following sub-priority within Round 3 will be based on the date that additional participation is established, which is the date the Phase 1 Reservoir Project Agreement was authorized to be executed by the Project Agreement Member.

- Priority 3.1 Prior to executing the Phase 1 Reservoir Project Agreement, 10,000 acre-feet of Class 1 Water became available and was allocated to those Project Agreement Members who had initially agreed to accept fractional shares of Class 1 and Class 2 totaling the amount requested in their On-boarding letter of intent. For each of these Project Agreement Members, the result was a reduction in Class 2 water and a corresponding increase in Class 1 Water.

- Priority 3.2 Prior to executing the Phase 1 Reservoir Project Agreement, Project Agreement Members who requested to increase their participation received Class 2 Water.

- Priority 3.3 California Water Service request during the 2016 On-Boarding process requiring CPUC approval before executing the Reservoir Project Agreement.

- Priority 3.4 Metropolitan Water District of Southern California elected to not specify an acre-ft as the basis of their participation in the 2016 On-Boarding process, but subsequently requested to participate in Class 2 Water through execution of the Reservoir Project Agreement.

- Priority 3.5 After Project Agreement Members had executed the Phase 1 Reservoir Project Agreement, 6,285 acre-feet of Class 1 Water became available after April 28, 2017 that was allocated to those Project Agreement Members who had initially agreed to accept fractional shares of Class 1 and Class 2 totaling their participation amount (Priority 3). Project Agreement Member's in this priority received a pro-rata share of the Class 1 Water and a corresponding decrease in their Class 2 Water.

- Priority 3.6 After Project Agreement Members had executed the Phase 1 Reservoir Project Agreement, an additional 6,285 acre-feet of Class 1 Water became available after May 31, 2017 that was allocated to those Project Agreement Members who had initially agreed to accept fractional shares of Class 1 and Class 2 totaling their participation amount (Priority 3.0). Project Agreement Member's in this priority received a pro-rata share of the Class 1 Water and a corresponding decrease in their Class 2 Water.

- Round 4 Priority: Additional Phase 1 participation following execution of the funding agreement with the State. Project Agreement Members in this round would only receive Class 2 Water unless participation changes result in the availability of Class 1 Water.

This round will also include additional Class 1 Water required to maintain the minimum participation threshold from water agencies located in the Sacramento River Hydrologic Region (see **Section 7**).

Note that no participation changes or new participation occurred during Phase 2A. All Project Agreement Members that signed the Phase 2 Project Agreement in April 2019 continued their level of participation through August 2020.

- Round 5 Priority: This round includes additional participation from existing or new Project Agreement Members following the completion of Phase 2A and prior to execution of the Phase 3 Project Agreement. Sub-priority within this round will be established as follows:
- Priority 5.1 Additional or new participation from agencies in the Sacramento River Hydrologic Region. This priority was established to encourage Northern California participation (**Section 7**).
 - Priority 5.2 Additional participation from existing Project Agreement Members.
 - Priority 5.3 New participation from prior Project Agreement Members that completely withdrew during a prior phase of the Project.
 - Priority 5.4 New participation from agencies that have not participated in prior phases of the Project.
- Round 6 Priority: New or additional participation during the development and execution of the Phase 3 Project Agreement.

Any established priority will be forfeited commensurate with a reduction in participation. Priority is only valid for the participation commitment under the active Project Agreement, less any amount subtracted as a result of a reduction in participation or Project withdrawal.

Additional rounds may be established by the Authority Board as the Project develops. The current list of priority participation is included in Appendix A.

7. PROVISION FOR ENCOURAGING NORTHERN CALIFORNIA PARTICIPATION

The Authority desires to maintain a minimum threshold for participation by agencies within the Sacramento River Hydrologic Region equal to approximately 25% of the total water supply. Should the participation from Project Agreement Members in this region drop below the threshold, the Authority may solicit additional interest from Project Agreement Members or agencies that are not currently participating in the Project, both of which are located in the Sacramento River Hydrologic Region. The additional participation will be established within the current round of priority at the time the Project Agreement is executed (**Section 6**).

8. CREDITING POLICY FOR ADVANCE FUNDING

The Crediting Policy describes the process of how Contribution Credit is earned by each Project Agreement Member by fulfilling its funding obligations. Funding obligations will be established through the Authority's annual budgeting process and will be apportioned to Project Agreement Members based on their respective participation. Each Project Agreement Member will accumulate Contribution Credit equal to its cumulative funding for both Class 1 and Class 2 participation throughout all phases of the project.

9. USE OF CONTRIBUTION CREDIT

Contribution Credit will be utilized to determine any payment or reimbursement due as result of the following events:

- Withdrawal or reduction in Project participation, as further described in **Section 11**; or
- True-up of Class 1 Cost Basis and Retirement of Class 2 participation, as further described in **Section 13** and **Section 15**.

10. REIMBURSEMENT POLICY FOR CONTRIBUTION CREDIT

The Authority will provide reimbursements under the following conditions.

10.1. Reimbursements from Rebalancing Process

Based on the results of the Rebalancing Process (**Section 13** or **Section 15**), the Authority will reimburse certain Project Agreement Members for excess Contribution Credit. The Authority will only reimburse such members once all payments have been received from Project Agreement Members that owe additional funds as a result of the Rebalancing Process.

10.2. Reimbursements from Withdrawal from Participation

A Project Agreement Member partially or completely withdrawing their participation in the Project will be reimbursed for its accumulated Contribution Credit up to the extent of its withdrawal based on the Provision for Withdrawal (**Section 11**). The Authority will provide such reimbursement once all payments have been received from Project Agreement Members electing to increase participation to offset the withdrawn participation.

10.3. Limitation on Reimbursements

Notwithstanding the applicability of any term or condition of this policy regarding withdrawal, in no event will the Authority be required to provide any reimbursement payment until the Authority determines that such payment will not have an adverse impact on the financial viability or overall implementation of the Project. Partial reimbursement payments may be made based on available funding with the remaining amount maintained as a liability for the Authority to pay at such time sufficient funding exists. As funding from new participation (**Section 14**) becomes available, the Authority may pay down the liabilities on a pro-rata basis following the order in which the liabilities occurred (e.g. Phase 1 liabilities are paid prior to Phase 2A liabilities).

10.4. Reimbursements due to Project Termination

In the event that the Project cannot be completed or in the event the Authority terminates the then active Reservoir Project Agreement, the Authority will disperse any available Project funds according to the participation percentages as defined in the current version of the then active Reservoir Project Agreement.

11. PROVISIONS FOR WITHDRAWAL FROM PROJECT

11.1. Withdrawal or Reduction Before the Start of Phase 2 Obligations

A Project Agreement Member may reduce or completely withdraw its participation relative to Class 1 and/or Class 2 Water within the window associated with Assumption 4.5 and the Phase 2A Reservoir Project Agreement (Dated April 1, 2019). In order to maintain equity among all Project Agreement Members, all changes in Project participation will be accommodated through the provisions of the Phase 1 True-Up Process (**Section 13**).

11.2. Withdrawal or Reduction During Phase 2

A Project Agreement Member may reduce or completely withdraw its participation at the conclusion of each incremental funding obligation during Phase 2 (e.g. Phase 2A, Phase 2B, etc.). In order to maintain equity among all Project Agreement Members, changes in Project participation will be accommodated through the provision of the Phase 2 True-Up Process (**Section 15**) at the conclusion of each incremental funding obligation.

11.3. Withdrawal or Reduction Before the Start of Phase 3 Obligations

Following Phase 2, Project funding will most likely involve debt issuance and require full financial commitment by Project Agreement Members for Phase 3 and Phase 4. Consequently, the last opportunity for a Project Agreement Member to withdraw or reduce participation under this policy will be prior to execution of the Phase 3 Reservoir Project Agreement. In order to establish equity prior to debt issuance, all final changes in Project participation will be accommodated through the provision of the Phase 2 True-Up Process (**Section 15**).

12. PROVISION FOR CLASS 2 CONVERSION TO CLASS 1 PRIOR TO THE TRUE-UP PROCESS

Prior to the Phase 1 True-up Process (**Section 13**), the conversion of Class 2 Water will occur only when additional Class 1 Water becomes available. Project Agreement Members with Class 2 participation will be allowed to convert their Class 2 Water in order of highest to lowest priority.

The cost for each Project Agreement Member to convert its Class 2 to Class 1 will be equal to the difference between the Class 1 and Class 2 funding obligations on a per acre-foot basis, multiplied by the quantity (acre-feet) of Class 2 being converted to Class 1.

13. PROVISION FOR REBALANCING PHASE 1 PARTICIPATION AND TRUE-UP OF THE CLASS 1 COST BASIS

At the conclusion of the Phase 1 Rebalancing Process, the Authority will establish the final amount of Class 1 Water available for participation and establish an equivalent cost basis per acre-foot (the True-Up Process). The final Phase 1 participation will be established as follows:

- The minimum threshold for participation from agencies in the Sacramento River Hydrologic Region (**Section 7**) will be considered prior to the conversion of Class 2.

- Any voluntary change in participation shall be fully recognized prior to the calculation of conversion of Class 2 Water to Class 1 Water.
- Class 2 will be converted to Class 1 in order of highest to lowest priority until the final amount of Class 1 participation is fulfilled. The cost to convert Class 2 Water shall be paid by each member separate from the determination of the Equivalent Required Funding for Phase 1. Funding associated with Class 2 conversion will be included in the Project Agreement Member's cumulative Contribution Credit.
- Any remaining Class 2 participation will be retired. Project Agreement Members with retired Class 2 Water will be placed on a stand-by list for future participation based on their original priority.
- Should the total amount of Class 1 participation be less than the amount available, the Authority will solicit interest from current Project Agreement Members for additional participation. If the additional Class 1 participation is still available, the Authority will solicit interest from other non-participating agencies.

An equivalent cost basis per acre-foot will be established for all Project Agreement Members at the conclusion of Phase 1 as follows:

- The Equivalent Cost Basis for Class 1 participation has been established by the Project Reservoir Committee as \$48.50 per acre-foot.
- The Equivalent Required Funding for each Project Agreement Member will be the Equivalent Cost Basis multiplied by the Project Agreement Member's Class 1 participation at the end of Phase 1.
- If the Equivalent Required Funding is greater than the Project Agreement Member's cumulative Contribution Credit, a true-up payment will be due from the Project Agreement Member to the Authority equal to the Equivalent Required Funding minus the Member's cumulative Contribution Credit.
- If the Equivalent Required Funding is less than the Project Agreement Member's cumulative Funding Obligation, a reimbursement will be due from the Authority to the Project Agreement Member equal to the Project Agreement Member's cumulative Contribution Credit minus its Equivalent Required Funding.

14. PROVISION FOR BUY-IN AFTER PHASE 1

During Phase 2, if Class 1 Water is available, existing or new Project Agreement Members may increase their participation. In order to maintain equity among Project Agreement Members, additional participation carries a "buy-in" cost equal to the equivalent cost basis at the time that new or additional participation is requested. The equivalent cost basis has been established by the Reservoir Committee as:

Phase 1: \$48.50 per acre-foot
Phase 2A: \$60.00 per acre-foot
Total: \$108.50 per acre-foot

Additional increments may be added as the project progresses through Phase 2.

The buy-in cost for additional/new participation is equal to the Equivalent Cost Basis per acre-foot multiplied by the amount of additional/new participation requested less any reimbursement liability due from the Authority from prior withdrawal/reduction in participation. The buy-in payment will be invoiced upon execution of the Reservoir Project Agreement.

The additional/new participation will be assigned the current round of priority at the time the Reservoir Project Agreement is executed (**Section 6**).

The Authority may, but shall not be obligated to, utilize the buy-in payments to reduce any outstanding reimbursement liabilities from prior phases.

15. PROVISION FOR PHASE 2 REBALANCING AND TRUE-UP PROCESS

At the conclusion of each incremental Phase 2 agreement, the Authority will declare any change to the Fully Subscribed Project and Project Agreement Members will identify their preferred Participation moving forward in the Project.

With respect to the Fully Subscribed Project, any available Class 1 water will be offered according to the Round 5 sub-priorities (**Section 6**). Project Agreement Members that increase their participation and new Project Agreement Members must “buy-in” to the Project at the current Equivalent Cost Basis (**Section 14**).

With respect to the Fully Subscribed Project, if the total preferred Participation exceeds the Fully Subscribed Project, Project Agreement Members with a proposed participation increase will only receive a pro-rata share of their proposed increase. If the total preferred Participation still exceeds the Fully Subscribed Project, the Participation of Existing Project Agreement Members will be reduced on a “last in / first out” basis according to the participation priorities (**Section 6**) and on a pro-rata basis within the same priority or sub-priority.

Once the final participation is established for each incremental Phase 2 Project Agreement, true-up payments and reimbursements will be determined for each Project Agreement Member:

- The Equivalent Required Funding at the completion of each incremental Phase 2 Project Agreement will be the Equivalent Cost Basis multiplied by the Project Agreement Member’s participation.
- If the Equivalent Required Funding is greater than the Project Agreement Member’s cumulative Contribution Credit, a true-up payment will be due from the Project Agreement Member to the Authority equal to the Equivalent Required Funding minus the Member’s cumulative Contribution Credit.
- If the Equivalent Required Funding is less than the Project Agreement Member’s cumulative Funding Obligation, a reimbursement will be due from the Authority to the Project Agreement Member equal to the Project Agreement Member’s cumulative Contribution Credit minus its Equivalent Required Funding.

16. FAIR SHARE FUNDING SUMMARY

The Authority will prepare a funding summary upon completion of Phase 1 to document each Project Agreement Member's funding contributions, equivalent cost basis and Contribution Credit. The Phase 1 Participant Ledger will summarize the conversion and/or retirement of Class 2 Water and the true-up of the Class 1 cost basis at the end of Phase 1.

The Participant Ledger will be updated to document changes in Participation, Priority and Equivalent Cost Basis for each Project Agreement Member through completion of Phase 2.

Appendix A – Participating Members and Respective Priority