Meeting: **Sites Joint Authority Board & Reservoir Committee Workshop**

Subject: **Plan of Finance #2 – Finance & Governance Alternatives**

Location: Click here to join the meeting

Call in: **1-888-404-2493**

Code: **794 877 128#**

Board Chair:	Fritz Durst (Reclamation District 108)
Board Vice Chair:	Jeff Sutton (Tehama-Colusa Canal Authority)
Res Comm Chair:	Jeff Davis (San Gorgonio Pass Water Agency)
Res Comm Vice Chair:	Bill Vanderwaal (Reclamation District 108 & Dunnigan Water District)
Treasurer:	Jamie Traynham (Davis Water District)

Notice: Pursuant to Executive Orders N-25-20 and N-33-20, issued by Governor Newsom on March 12, 2020, and guidance by the California Department of Public Health dated March 11, 2020, this meeting will be conducted by teleconference. The public may attend the meeting and offer public comments by phone, using the call-in number above. Members of the Committee will participate by teleconference from other locations.

AGENDA

Friday, April 23, 2021 9:30 am – 12:00 pm

NO ACTION or DECISION WILL BE TAKEN

ROLL CALL & CALL TO ORDER:

9:30 **Welcome, Overview, Introductions — Fritz Durst, Jeff Davis, Jerry Brown, Charles Gardiner**

Workshop objectives:

- Receive guidance and direction on the financing alternatives (Attachment A).
- Receive guidance and direction on the framing of Guiding Principles and Preliminary Terms for local agency participation (Attachment B).
- Receive guidance and direction on long-term governance and delegation timing.
- Identify home board information needs.

9:40 **Review Background and Context for Project Financing — JP Robinette**

- Review decision timelines for 2021 and 2022-2023.
- Review progress and guidance to date.

➢ **Discussion:** *Clarifying questions.*

9:50 **How do we pay for it? Financing Alternatives – JP & Doug Montague (Attachment A)**

- Review preferred financing plan and alternate approaches.
- Review approaches for managing financing risks for lenders, the JPA, and Participants.
- Review options and variations for payment obligations.

- **Discussion questions:**
  a. *Are the financing alternatives feasible?*
  b. *Are there other financing alternatives that should be explored?*

10:35 **What do we get? Guiding Principles and Preliminary Terms – JP (Attachment B)**

- Introduce structure of Guiding Principles and Preliminary Terms for local agency participation.
- Identify key terms for development in the current phase.

- **Discussion question:**
  a. *What principles are critical to flesh out before the next round of funding?*

11:00 **How do we make decisions? Governance and Delegation Principles – Jerry & Charles**

- Existing Governance: Review existing structure and bylaws
- Phases of the Project: Review the triggers for revised responsibilities, liabilities, and obligations.

- **Discussion Questions:**
  a. *Is the current governance structure and delegation sufficient for future decisions?*
  b. *Does it need to evolve? If so, when?*
  c. *What do your home boards need to know about future governance and decision-making to execute the successor agreement?*

11:50 **Wrap up and Next Steps – JP & Charles**

- Action items and homework.
- Workshop 3.
- Home board information needs.

12:00 **Adjourn**

ADJOURN

ADA COMPLIANCE: Upon request, Agendas will be made available in alternative formats to accommodate persons with disabilities. In addition, any person with a disability who requires a modification or accommodation to participate or attend this meeting may request necessary accommodation. Please make your request to the Board Clerk, specifying your disability, the format in which you would like to receive this Agenda and any other accommodation required no later than 24 hours prior to the start of the meeting.

This meeting will be recorded.

Sites Project Financing Alternatives Technical Memorandum

I. Introduction

The purpose of this technical memorandum is to provide an analysis of the financing alternatives that may be available for the funding of future Sites Reservoir (the "Project") costs. The memorandum also addresses the key credit structuring decisions that must be made prior to securing external financing.

II. Sites Reservoir Project

The Sites Project Authority (the "Authority") was formed in 2010 to facilitate the development, construction and operation of the Sites Reservoir. Since the formation of the Authority, significant progress has been made in the advancement of the Project including the securing of State funding as well as a USDA loan for a significant portion of Project costs.

Projected Cost – In 2018, the Project underwent a value planning exercise that both reduced the size of the Project and simplified its engineering and construction requirements. The result was a significantly less expensive project and potentially a shorter construction period. Sites staff and consultants are currently finalizing updated Project cost estimates that reflect the new project configuration as well as updated permitting, design, engineering and construction cost estimates. These updated cost estimates are expected to be available in May 2021.

Planning and Construction Schedule – The Project construction schedule will be driven primarily by the time required to secure environmental permits and water rights. Based on current planning estimates, permits and water rights should be secured by mid-2023 and Project construction should begin approximately in mid- to late-2024. Project completion and the beginning of operations is projected by 2030. Should there be delays in securing permits or water rights, the Project construction schedule will need to be adjusted accordingly.

III. Project Participant Pool

The Reservoir Committee comprises the participant pool for the Project (the "Participants" or "Reservoir Committee Members"). The Reservoir Committee is very diverse and includes small agricultural districts as well as large urban water wholesalers. The agricultural participants are primarily located in the Sacramento Valley ("North of Delta") while the urban participants are downstream and south of the Sacramento-San Joaquin Delta ("South of Delta").

The North of Delta Participants are generally small and have not incurred public debt and are, therefore, not rated by any of the nationally recognized credit rating agencies. Many are so small and have such limited customer bases that they are likely not ratable. North of Delta Participants currently comprise 43% of the Reservoir Committee Members and 25% of total Project subscriptions.

The South of Delta Participants are generally larger, urban and are rated by one or more of the rating agencies. The South of Delta Participants comprise 57% of Reservoir Committee Members and 75% of total Project subscriptions.

The following table provides information regarding the current participation levels and credit ratings of the Reservoir Committee Members. Participants with credit ratings are highlighted in blue.

Sites Participants	Credit Ratings (Moody's/S&P/Fitch)	Acre Foot Participation	Percentage Participation
Antelope Valley-East Kern WA	A1/AA/NR	500	0.3%
Carter MWC		300	0.2%
City of American Canyon	NR/AA/NR	4,000	2.4%
Coachella Valley WD	NR/AA+/AAA	10,000	6.0%
Colusa County		10,000	6.0%
Colusa County WD		10,073	6.0%
Cortina WD		450	0.3%
Davis WD		2,000	1.2%
Desert WA	NR/AA/NR	6,500	3.9%
Dunnigan WD		2,972	1.8%
Glenn-Colusa ID		5,000	3.0%
Irvine Ranch WD	Aa1/AAA/AAA	1,000	0.6%
La Grande WD		1,000	0.6%
Metropolitan Water District of SC	Aa1/AAA/AA+	50,000	29.8%
Reclamation District 108		4,000	2.4%
Rosedale-Rio Bravo WD	NR/A/NR	500	0.3%
San Bernardino Municipal WD	NR/AAA/NR	21,400	12.8%
San Gorgonio Pass WA		14,000	8.4%
Santa Clara Valley WD	Aa1/AA/AA+	500	0.3%
Santa Clarita Valley WA	NR/AA/AA-	5,000	3.0%
Westside WD		5,375	3.2%
Wheeler Ridge - Maricopa WSD		3,050	1.8%
Zone 7 WA	NR/AA+/AA+	10,000	6.0%
Total		**167,620**	**100.00%**

From a credit perspective, 48% of Reservoir Committee Members have credit ratings and these Participants account for 65% of total Project subscriptions. The two Participants with the largest Project subscriptions both have credit ratings and together account for 43% of total Project subscriptions. We will discuss later the strengths and challenges presented by the composition of the Project credit pool.

It should be noted that it will be in the Project's best interest for unrated Participants that may be able to secure an "A" rating from one of the credit rating agencies to begin exploring the process for requesting an underlying issuer rating from a rating agency. If more Participants are rated, it may improve the likelihood of securing financing or lower the cost of interim or permanent financing for the Project overall.

IV. Funding Already Secured

As mentioned earlier, the Authority has made meaningful progress in securing funding for a significant portion of Project costs and currently pays a portion of Project development costs with funding from both State and federal sources.

State Proposition 1 – The Authority aggressively pursued, and in 2018 was awarded, State Proposition 1 ("Prop 1") funding for the Project from the California Water Commission. The initial Prop 1 award from the Water Commission was for $816 million, some of which (approximately $12.5 million) has already been used for planning and permitting costs. With the withdrawal of other projects that received Prop 1 awards, the Authority has received a commitment from the State for an additional $20 million in Prop 1 monies bringing the total award amount to $836 million. The majority of the Prop 1 funding will be available for general Project design and construction costs, once permitting and water rights are secured.

USDA Rural Development Loan – In 2018, the Authority pursued and received approval for a USDA Rural Development Community Facilities loan to be used for the construction of the Project's canal intertie facilities. This type of USDA loan is only available to communities with populations of less than 20,000 and the Project's eligibility is therefore, tied to the participation of the smaller, rural Project Participants. The loan can be used for the reimbursement of up to $449 million of qualified facility construction costs including the refinancing of short-term canal intertie construction debt once the intertie is completed. The loan, if utilized, will have an interest rate that is the lesser of 3.875% or the USDA loan rate determined at the time of the closing of the loan. The USDA loan rate would be 2.25%, if the loan closed today. The USDA also leaves open the possibility of refinancing the loan in the future, if interest rates decline after the loan closing. The loan can have a term of up to 40 years. The USDA loan has a requirement that in the event of a Participant default on loan payments, the remaining Participants will be required to make up the debt service shortfalls, subject to a limit of 25% of each Participant's own debt service obligation. With the 2019 reconfiguration of the Project, the location and cost of the canal intertie facilities has changed but it is anticipated that the Authority will still be able to utilize the majority of the available loan amount, if it is advantageous to do so.

Federal Funding – While the Authority has not yet received a commitment of federal WIIN Act monies, it continues to receive modest funding from the U.S. Bureau of Reclamation ("Reclamation") for Project-related studies (e.g., Congressional appropriations totaling $6 million and $13.7 million in Fiscal Years 2020 and 2021, respectively). The Authority and Reclamation typically split the Congressional appropriations. The Authority is working with Reclamation now to determine how the $13.7 million appropriated for FY 2021 will be split between the two entities. The Authority is continuing its discussions with Reclamation regarding future WIIN Act commitments and other forms of federal funding.

V. Funding Still Needed

Cash Calls - While progress has been made in securing State and federal funding commitments for the Project, the majority of this funding will not be available until the Project is permitted and has secured water rights. Until this occurs (currently projected to be mid-2023), it is expected that Project Participants will continue to be responsible for funding Project development costs from internal sources or "cash calls". The Authority continues to evaluate the level of cash calls required to fund future critical path activities. The most recent estimate of the cash call needed for 2021 is $150 per acre-foot of Project subscription and the estimate for the 2022 cash call is $200 per acre-foot. The Authority is also evaluating whether the cash calls should cover set periods of time or should be driven more by the achievement of critical path landmarks.

Interim Financing - Once Project permits and water rights are secured, the Authority and the Participants will have the option of continuing to fund the balance of pre-construction costs through cash calls or to secure external financing for these costs. Assuming the Participants decide to pursue external borrowing for the balance of pre-construction costs, the Authority could pursue either a public sale of securities or a direct line of credit with a commercial bank.

Bank Line of Credit - Given the inherent complexity involved with educating potential lenders or investors regarding a pooled credit with dozens of participants the majority of whom are not rated, we recommend pursuing a direct placement of debt for interim financing rather than a public sale that would require educating hundreds of investors as well as the rating agencies. This was the approach the Authority took when it solicited lending proposals from banks in late 2018. While the Authority cancelled the solicitation before proposals were received, there was significant bank interest in the Project. If most of the key credit questions that existed in 2018 are answered before the next solicitation (e.g., permitting, water rights, composition of the borrower pool, etc.) the level of bank interest should be even higher. We have continued to brief a number of the key banks on the progress of the Project to maintain their interest and generate a feeling of "ownership" in the Project's success. A bank line of credit in the current market would cost approximately 1.50%-1.75%, based on recent discussions with banks potentially interested in providing a line of credit to the Authority. Given that the Authority is some time away from formally soliciting bank proposals, current modelling projections incorporate a conservative assumption of 3% for the cost of a bank line.

WIFIA Loan for Interim Costs – While a bank line of credit may be the most conventional source of financing for Project costs once cash calls have ended and before Project construction begins and long-term bonds are issued, it may also be possible to use the proceeds of a federal Water Infrastructure Finance and Innovation Act ("WIFIA") loan to finance these costs. The Authority is considering applying for a WIFIA loan in the upcoming application cycle this spring. We will provide more details regarding WIFIA loans in our discussion of long-term financing options later in this document.

Interim Financing Will Be Binding – Because interim lenders will want to understand and evaluate the mix of credits involved in the Project pool of borrowers before making a lending decision, they will require some level of certainty regarding which Participants will be obligated for the loan. Lenders will also be evaluating the likelihood of the Authority securing long-term financing to refinance or pay off the bank line of credit. Therefore, Participants executing Project Agreements that will be in effect during the interim lending period will be obligated to continue with the Project through completion. Participants will only be able reduce their participation or exit the Project in the future if there is another Participant or an Authority and bank-approved new participant that is willing to assume their interim financing obligations.

Long-Term Financing – After all permitting, planning and design is complete but before Project construction contracts can be awarded, the Authority will need to identify the sources of funding for construction. Some of the funding will come from already identified State and federal sources such as Prop 1 funds, USDA loan proceeds and potentially WIFIA loan proceeds. While these sources of funding may cover construction costs for the first several years, eventually the Authority will need to secure additional long-term financing from the capital markets. The most common form of long-term borrowing for projects such as the Sites Project is the public sale of long-term tax-exempt municipal bonds.

Fixed Rate Bonds – Fixed rate bonds pay interest semi-annually at a fixed interest rate and would be structured with annual maturities to provide Participants with level annual debt service. Participants will be required to remit their share of semi-annual debt service payments to the Authority six months or more ahead of the date that the Authority makes its debt service payments to bond investors or interim lenders (i.e., if the Authority has to make a debt service payment to bond investors/lenders annually on December 1^{st}, Participants will be required to remit their share of that December 1^{st} payment six months in advance on June 1^{st} each year). The fact that the interest rate on the bonds does not change makes all future annual debt service obligations known and will aid Participants in budgeting and setting rates and charges. The final maturity of long-term bonds is customarily 30 years but could be as long as 40 or more years. Interest accrues on the total amount of bonds issued even if the proceeds of the borrowing are not spent for several years. However, unspent bond proceeds can be invested until needed, thereby partially offsetting the impact of the interest being paid on the bonds. The Authority's current modeling projections assume a fixed rate bonds cost of 5%, whereas current rates are closer to 3.5%.

The Authority would also use either the proceeds of a WIFIA loan or long-term bonds to refinance the interim bank line of credit once Project construction begins. In order for the Authority's bonds to be tax-exempt there are IRS rules that limit the time that the Authority will have to spend bond proceeds on Project costs. This will need to be factored into the plan of finance along with other factors to determine the most efficient borrowing plan.

Other long-term financing vehicles including variable rate securities will also be available to the Authority and may be utilized to meet specific objectives but for the purposes of this memorandum we will leave them for discussion at a future time.

At the appropriate time, Project staff and its financial consultants will also evaluate the economics of purchasing municipal bond insurance for long-term bonds sold for the Project. Municipal bond insurers provide insurance that guarantees the timely payment of bond principal and interest on bonds in the event the borrower fails to make timely payment. The decision whether to purchase bond insurance will depend on whether the reduction in the Authority's borrowing cost that results from having the insurance is greater than to the cost of the bond insurance.

WIFIA Loans – In 2014, Congress enacted the Water Infrastructure Finance and Innovation Act ("WIFIA"), a low-cost loan funding program to be administered by the United States Environmental Protection Agency ("EPA"). WIFIA authorizes the EPA to issue long-term, low-interest loans or loan guarantees to a wide variety of water and wastewater infrastructure projects. WIFIA financing is broadly available to public, private, and mixed public-private entities and the EPA can enter into loans ("WIFIA loans") to fund qualifying projects for up to 49% of the total cost of the project. Selected projects demonstrate a broad range of projects that the WIFIA Program can finance, including wastewater, drinking water, stormwater, and water recycling projects.

The WIFIA Program offers loans with low, fixed interest rates and flexible financial terms which can provide savings to borrowers and their customers. Importantly, a single, fixed, interest rate is established at closing for the loan. This means that a borrower may receive multiple disbursements over several years at the same fixed interest rate which is locked at loan closing. This functionality can allow borrowers to utilize a WIFIA loan as an interest rate hedge in a rising interest rate environment and as such, provides borrowers with diversity and flexibility in their funding source as they contemplate future capital projects.

Moreover, another key benefit of a WIFIA Loan is that the interest rate locked at loaning is not impacted by the borrower's credit or loan structure. All borrowers benefit from the AAA Treasury rate, regardless of whether they are rated AA or BBB, and the WIFIA Program does not charge an interest rate dependent on specific financial terms or covenants.

Eligible project costs include development-phase activities (i.e., planning, feasibility analysis, environmental review, permitting, and preliminary engineering and design work); construction, reconstruction, rehabilitation, and replacement activities; acquisition of real property; environmental mitigation; construction contingencies; equipment; capitalized interest necessary to meet market requirements; reasonably required reserve funds; capital issuance expenses; carrying costs during construction and WIFIA application and credit processing fees. Further, prospective borrowers may request that costs incurred prior to receipt of the WIFIA Loan be included as part of eligible project costs. Previously incurred costs must be directly related to the development or execution of the project including preliminary design, right-of-way acquisition, and NEPA compliance related costs. The WIFIA Program approves such requests on a case-by-case basis.

The WIFIA loan program has the following key program features:

- Minimum project size of $20 million for large communities
- Minimum project size of $5 million for small communities (population of 25,000 or less)
- Maximum portion of eligible project costs that WIFIA can fund is 49%
- Subject to EPA approval, costs incurred, and in-kind contributions made prior to receipt of a WIFIA loan, may count toward the 51% of project costs to be funded by non-WIFIA dollars
- Total federal assistance may not exceed 80% of a project's eligible costs
- WIFIA and SRF funding can be used to co-finance a project
- Maximum final maturity date is 35 years from "substantial completion" of a project
- Maximum time that repayment may be deferred after substantial completion of the project is five years

The interest rate must be equal to or greater than the US Treasury rate of a similar maturity at the date of closing, a requirement that EPA implements using the Treasury rate plus .01%. This rate can be locked in at closing, even if loan disbursement is deferred until later in the process of project implementation. A WIFIA Loan with a weighted average life of 22 years would have a rate of 2.38% based on current market rates. For purposes of modeling, we have used a 3.50% assumed rate for WIFIA loans.

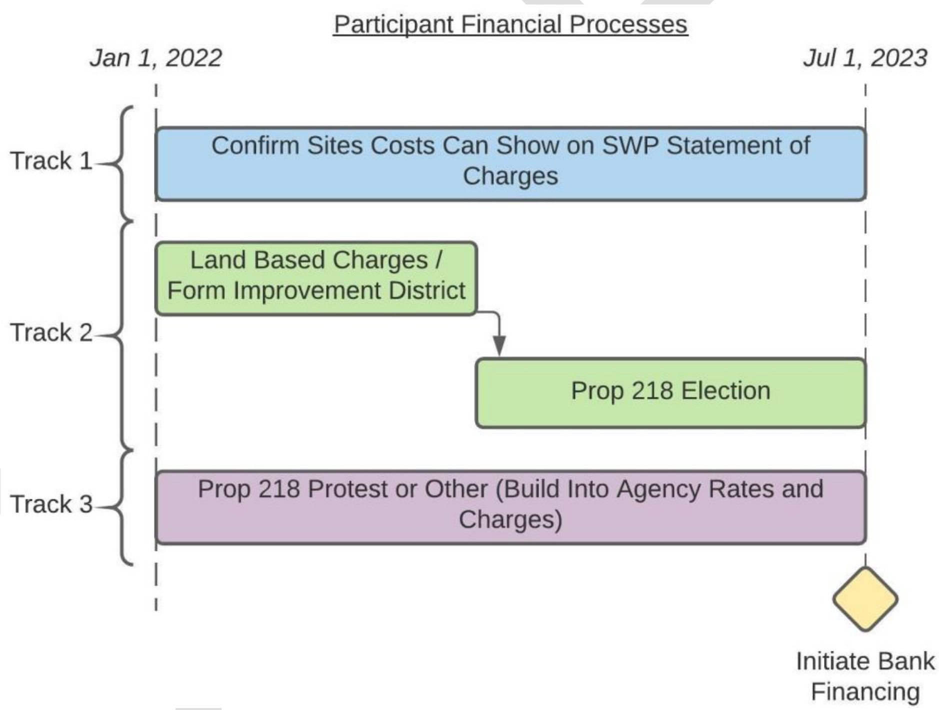
There are a number of meaningful benefits to WIFIA funding for the Project, primarily its flexibility with regards to structure, repayment timing, and the incremental funding flexibility with reduced rate risk resulting from the Authority's ability to lock-in an interest rate at the time the WIFIA loan closes. Moreover, the ability to use WIFIA funds for planning, permitting, and design costs, as well as for previously incurred project costs would be valuable to the Authority.

The Authority should consider when it will require funds for the Project when deciding when to make its WIFIA loan application. Typically, the EPA announces the funding round in April with borrowers required to submit a Letter of Interest ("LOI") by July. Borrowers are notified in October/November if they have been selected to submit a full application, and it typically takes borrowers 3-6 months to complete a full application. Once the application is submitted, it takes the EPA a minimum of 6 months to conduct due diligence, develop loan documentation, and execute a WIFIA Loan. Based on MDA's experience with other clients that submitted LOIs and were invited to apply in previous WIFIA rounds, the process to apply and then close a WIFIA loan can range from 8-12 months or more, depending on the borrower and the complexity of the project.

The Authority will also need to decide the size of WIFIA loan it will be requesting and if it will plan to split its WIFIA loan request into two smaller loans (one to fund early Project costs and one later in the construction process) to improve the likelihood of securing loan approval.

VI. Options for Securing Revenue to Meet Debt Service Obligations

As detailed in a technical memorandum prepared by the Project Financing Team in January 2021, there are three potential Participant sources of funds that can be used to meet the anticipated future financial obligations relating to the Project: (1) include the costs of the Project on the Participant's DWR State Water Project Annual Statement of Charges, (2) levy benefit assessments or other land based charges on land located within a Participant's boundaries, or (3) incorporate the costs into current water rates and charges.



The sources of funds available to a specific Participant will depend on the legal organization of the agency and powers attributable to it, the nature of its customer base (wholesale vs. retail) and whether all customers of the agency will be participating in the Project or only a subset. We believe most Participants will have available to them at least one of these sources of funding, with the implementation of each funding approach having its own legal requirements, timing requirements and critical path. We also believe that most Participants will be able to treat their Project debt service obligations as an operating expense (similar to the State Water Project and Central Valley Project contracts). This is generally the highest priority of payment obligations for the Participants. The critical path for implementing any of these sources of funding will likely be 12-18 months. Participants should begin planning now so that their required processes are complete before revenues need to be collected. As noted earlier, Participants will need to plan so that payments for debt service obligations can be remitted to the Authority at least six months before the Authority's debt service payments are due to lenders and/or bond investors.

Funding Through State Water Project Statement of Charges – Track 1

Several Project Participants that are also participants in the State Water Project have indicated a desire to have their share of Project costs billed and collected through their DWR State Water Project Annual Statement of Charges. Monies collected by DWR on behalf of the Project through a Participant's Statement of Charges would then be transferred to the Authority for payment of the respective Participant's Project obligations. Discussions between DWR and the State Water Contractors regarding the process for including Project costs in DWR's Statements of Charges are in progress.

If the Statement of Charges approach to securing revenues does not end up being possible, Participants that have been planning on the approach will need to assess their position and determine if one of the other revenue-raising approaches outlined below is workable for them.

Funding Through Special Benefit Assessments – Track 2

A second option for financing the costs of the Project is to levy special benefit assessments or other land-based charges on parcels of land located within a Participant's boundaries. This option may appeal to Participants that wish to have Project costs billed and collected through the property tax roll and secured by the real property of customers or those Participants that have less than all the customers in their service area participating in the Project.

Participants interested in this approach will need to comply with Article XIIID of the California Constitution. Article XIIID provides substantive and procedural requirements on the increase of any "fee" or "charge" levied by a local government upon a parcel of real property or upon a person as an incident of property ownership, including specific procedural requirements applicable to special benefit assessments. Under Article XIIID, an assessment for special benefits requires the preparation of an engineer's report, notice and the distribution of ballots to the public, a public hearing and an affirmative vote of a majority of the votes received (counted and weighted in accordance with Proposition 218) before the assessment can be imposed.

In addition, an assessment is only permitted to be imposed if there is a "special benefit" to the property that is over and above the benefits conferred upon the general public at large. General enhancement of property value, by itself, does not constitute a special benefit. Any assessment must be proportional to the benefit actually received by a parcel and the assessment may not exceed the proportional benefit.

The specific procedural requirements of Article XIIID need to be taken into consideration by a Participant when developing a financing plan and timeline if the Participant decides to fund its costs through a special benefit assessment. Article XIIID requires that the proposed assessment be supported by a detailed engineer's report prepared by a registered professional engineer certified by the State of California. The engineer's report must identify the parcels to be assessed, distinguish between general benefits and special benefits (only special benefits are assessable), and apportion the costs of the project to each specially benefitted parcel according to the proportionate special benefit of each parcel. Generally, these reports take 6-9 months to prepare including procuring an assessment engineer, so the time and costs involved must be considered by the Participant.

Participants will be required to mail notice to the record owner of each parcel subject to the proposed assessment at least 45 days prior to the mandatory public hearing regarding such proposed assessment. The notice must include specific information including the reason for the assessment, the basis upon which the amount of the proposed assessment was calculated, the duration of payments, the time, place and date of the public hearing to consider objections and protests to the proposed assessment, among other requirements. The notice must also include the assessment ballot, which is the ballot used by property owners to favor or oppose the proposed assessment. The ballots are counted at the public hearing, and the proposed assessment cannot be imposed unless the assessment ballots favoring the assessments exceed the assessment ballots opposing the assessment. The weight of a ballot is determined according to the proportional financial obligation of the property owner.

It should be noted that the preceding is a general summary of the Proposition 218 procedural requirements relating to the imposition of a special benefit assessment. Proposition 218 does not provide independent authority to levy an assessment. Such authority must be granted elsewhere in the California Code. As a result, there may be procedural requirements associated with approving an assessment that are not summarized above.

If less than all of the property within a Participant's boundaries will participate in the Project, it may be advisable to create an improvement district for purposes of imposing the land-based charge. While each Participant's formation statute will vary, typically either a petition process or election process is necessary to create an improvement district. The terms and requirements of such creation will need to be incorporated into the Participant's financing timeline.

Funding Through Current Water Rates and Charges – Track 3

Certain Participants may decide to meet the planned annual debt service obligations of the Project through increases in the current rates and charges they apply to their water users. Similar to the funding through special benefit assessments described earlier, for Participants that provide retail water to their water users, any rate increases to existing water rates or charges will need to comply with the protest provisions of Proposition 218, specifically Article XIIID. As noted previously, Article XIIID provides substantive and procedural requirements on the increase of any "fee" or "charge" levied by a local government upon a parcel of real property or upon a person as an incident of property ownership. As a result, the Participant providing retail water will need to provide written notice of the proposed increase to the record owner of each identified parcel upon which the increased rate or charge is to be imposed and hold a public hearing regarding the potential increase. The public hearing must be held at least 45 calendar days after the mailing of the notice. The increase will be subject to the majority protest provisions of Article XIIID, meaning that if a majority of owners of the identified parcels file written protests against the proposed increase, the increased rate or charge cannot be imposed.

Rates and charges charged by Participants that provide wholesale water to their customers are not subject to the provisions of Article XIIID because such rates and charges constitute the price charged by the wholesaler to retail suppliers for the water provided, and not charges to persons or properties as an incident of property ownership. However, wholesale Participants may have other statutory rate setting requirements applicable to them.

For Participants considering this option, their governing boards must be briefed on Project progress, educated regarding the benefits of the Project and the near-term and long-term financial obligations the agency will be undertaking and ultimately, the board must take formal action approving each new funding agreement for the Project. In addition, Participants should consider whether increased rates or charges are a palatable option for their customers.

VII. Credit Drivers

Before the Authority can access the credit markets for either interim or long-term Project financing, there are a number of key credit structuring decisions that will need to be made. These decisions have the potential to not only affect the cost of borrowing for the Project but may, in some cases, affect the Authority's ability to access the capital markets.

While the credit and security requirements of lenders and long-term debt holders will not be known until the Authority actually undertakes a bank solicitation or a bond offering, we have received some informal feedback from potential bank lenders regarding the requirements they are likely to have in order to provide the Authority with an interim financing line of credit. This feedback has informed our discussion of the following key credit issues.

Who Will be Obligated to Repay Debt

The diversity in size and financial strength of the members of the Reservoir Committee (i.e., the Participants), as well as the number of agencies involved, creates both opportunities and challenges to the structuring of a marketable credit for the Project. At least one of the rating agencies views pooled credits with 20 or more participants, such as the Project, as stronger than smaller pools, due to the credit diversification. However, given that 12 of the 23 water districts involved in the Project do not have credit ratings from any of the three primary rating agencies (Standard & Poor's, Moody's Investors Service and Fitch Ratings), investors will be uncomfortable purchasing the Project's securities unless the stronger, rated agencies participating in the Project are obligated for a significant portion of the Project debt. This being said, there are several possible ways to structure the Project credit that could be pursued and may be acceptable to commercial lenders and long-term bond investors.

Single Finance Plan – The strongest credit that the Authority can present to the capital markets is one in which all Participants participate together in each financing. It would provide the Authority with the least complex approach to coordinating borrowing activities for the Project and would provide the unrated Participants with the fewest obstacles to accessing the capital markets. Under this approach, the Authority would be responsible for issuing all debt for the Project on a schedule to accommodate initial construction as well as necessary repairs and replacements and future capital improvements.

The Authority debt would be secured by water storage and water supply service contracts ("Service Contracts") with Reservoir Committee Members. Amounts owed by the Reservoir Committee Members under the Service Contracts would include fixed and variable operation and maintenance expenses, repairs and replacements, capital improvements and Authority debt service.

As discussed earlier, amounts owed by Reservoir Committee Members under the Service Contracts would likely be considered as an operation and maintenance expense of each Reservoir Committee Member's water system and would therefore, be high priority payments for each agency.

The Service Contracts would provide some limited level of "step up" to protect the Authority and Authority debt holders from defaults by other Reservoir Committee Members (similar to the State Water Project contracts). Step-up provisions are discussed in more detail below.

Multiple Finance Plans - This approach would have the same characteristics as a single finance plan except that the Authority would issue debt under two or more financing plans with each finance plan corresponding to similarly rated groups of Reservoir Committee Members. For example, the Authority could issue one series of debt secured by Service

Contract payments from Reservoir Committee Members rated A- or better. The Authority could then issue a second series of debt secured by Service Contract payments from Reservoir Committee Members rated less than A- or those which are unrated.

The Authority would be obligated under the Service Contracts to coordinate all debt issuance under the various financing plans to assure that debt proceeds were available to pay for initial construction costs allocable to all Reservoir Committee Members on a timely and pro-rata basis.

Service Contract step-up provisions would also apply if there are multiple finance plans and obligations would cross all debt series.

While multiple finance plans may have appeal and advantages to some Participants, this approach would likely be more complicated to implement. This is partly because the large, Wall Street banks we have briefed have indicated that they are not likely to be able to offer credit to a pool that only includes the unrated Participants, unless there is some form of credit enhancement provided by the rated Participants to improve the security of the financing for the unrated Participants. Therefore, it may be worthwhile to begin outreach to regional and community banks that already have business and lending relationships with the smaller Participants to determine their level of interest in providing funding directly for the unrated Participants, as an alternative to solely working with the larger, Wall Street banks for financing. Another possible way to organize multiple finance plans is by location and Project infrastructure utilization (e.g., North of Delta Participants and South of Delta Participants).

Pay-As-You-Go - Under the Pay-As-You-Go approach, a Reservoir Committee Member with sufficient credit worthiness could opt out of Authority financing for the initial Project construction in return for agreeing to provide to the Authority its pro-rata share of capital costs allocable to the Reservoir Committee Member under the Service Contract in order to maintain the Project construction schedule.

Payments for these capital costs would be due prior to the date the Authority posts a preliminary offering document for each Authority debt issue for initial construction costs.

Amounts owed by the Reservoir Committee Member under the Service Contract would include fixed and variable operation and maintenance expenses, repairs and replacement and capital improvement and Authority debt service for repairs and replacements and capital improvements other than initial construction costs.

As in both prior scenarios, amounts owed by the Reservoir Committee Member under its Service Contract would be payable to the Authority as an operation and maintenance expense.

Service Contract step-up provisions related to Authority debt would also apply to pay-as-you-go Reservoir Committee Members.

Note that if Participants elect to pursue Pay-As-You-Go self-financing rather than participate in the Authority financings, any self-financings should be completed concurrently with any Authority financings to eliminate the risk that not all construction funding will be available when needed.

What Happens If There are Project Shortfalls

As stated in the Joint Exercise of Powers Agreement, the Authority's primary purpose is to pursue the development and construction of the Project in order to increase and develop water supplies, to improve the operation of the State's water system, and to improve the environment. The Authority has established a number of central values which guide its mission, including the principle of shared responsibility for shared benefits. A unique aspect of the Project is the level of partnerships and the spirit of collaboration by a broad coalition of Participants and stakeholders to advance this vital project. As such, it behooves the Authority to consider how it will handle a situation in which a Participant has a shortfall in fulfilling its share of financial obligations related to the Project. This is particularly important for banks considering interim lending to the Authority or for investors evaluating the Authority's long-term bonds who will pay considerable attention to established security provisions that address what happens if one or more of the Participants fail to make debt service payments on a timely basis.

Project Sufficiency Pledge - It is likely that a key provision of the Project credit will be the commitment of all Participants to a Project sufficiency pledge of some nature which will cover any shortfall in Project debt service and ensure the Project's continued viability should a Participant be unable to make their share of debt service payments. Participants have agreed that the Project's sustainability is paramount and complying with sufficiency obligations of this sort will help ensure that future. Moreover, this type of commitment will give investors comfort that in the event that a Participant is unable to meet its financial obligations for some reason, the remaining Participants will meet their obligations for them. This type of sufficiency pledge can take the form of the establishment of a liquidity reserve to ensure there are funds on hand to cover any shortfalls. Subject to input from lenders and the rating agencies, it may be possible to fund this reserve in one of two ways. It could be funded by all Participants at the outset of the Project with an agreement to replenish the reserve fund if it is ever drawn upon or it could be structured such that Participants that opt not to fund their share of the reserve upfront would instead pledge to provide cash in the future when needed to cover shortfalls. In return for pledging sufficiency commitments or by funding a Project liquidity reserve, Participants would receive the Project entitlements forfeited by the defaulting Participant.

Regardless of the structure of the liquidity reserve, the rating agencies and investors will still expect creditworthy, rated Participants to be required to cover a high percentage of scheduled annual debt service. The current Project participation by rated Participants is 65%.

Banks have indicated that a Project sufficiency pledge by Participants would be required whether the Authority uses a single finance plan or multiple finance plans and would also be required of "pay-as-you-go" Participants. All Participants would be required to comply with sufficiency obligations/commitments to ensure Project durability in the event that there are Participants who fail to meet their obligations.

Project Sufficiency Waterfall - It may be possible to structure the Project Agreements with a "waterfall" of options before Participants are asked to comply with their previously agreed upon Project sufficiency pledge. A basic outline of this type of waterfall arrangement is below:

> Waterfall Triggering Event: Project Participant defaults on its debt obligation for the Project.
>
> **Step 1**: Notify Participants of the default and allow them to volunteer to meet the debt service obligations as well as the sufficiency obligation of the defaulting Participant in exchange for receiving the defaulting Participant's Project entitlement (60 days for Participants to volunteer).
>
> **Step 2**: If there are no Participant volunteers, the Authority can seek outside entities interested in joining the Project to assume the defaulting Participant's obligations and entitlements. Outside entity has to be acceptable to the Authority, Reservoir Committee and the bank to be approved to step in (60 days for Authority to identify external entity to step in).

Step 3: If no acceptable outside entities agree to step in, all non-defaulting Participants comply with their agreed upon sufficiency pledge to either pay their share of the debt service shortfall or pay their proportional share of the replenishment of the liquidity reserve if it has been drawn upon to cover a defaulted payment (60 days for non-defaulting Participants to fulfill pledge if no external entity identified).

Given feedback from the banks, failure to include a Project sufficiency pledge in the Project Agreements will reduce the likelihood of securing financing and will increase costs. Lack of a Project sufficiency pledge may also jeopardize the Authority's ability to secure a WIFIA loan as the EPA may view it as a credit weakness.

Take-or-Pay vs. Take-and-Pay - Discussions with municipal market participants regarding the credit requirements of the capital markets for a project such as the Sites Project lead us to recommend that the Authority structure its Participant agreements based on the take-or-pay principal rather than the take-and-pay concept. The take-or-pay principal is the concept of each Project Participant having a contractual obligation to pay for its predetermined share of the Project's capital costs (i.e., bond debt service and other related costs) regardless of Project performance (i.e., amount of water actually stored or availability of water for delivery). This contrasts with the take-and-pay principal in which Project Participants' payments are contingent on the Project performance (i.e., payment is for actual water storage or water delivered). Take-or-pay Project Agreements will be a cornerstone of the credit.

Participation Off-Ramps – In Project Agreements executed to date, Participants have had the ability to reduce their participation level in the Project or exit the Project completely ("off-ramps") and, through "rebalancing" receive reimbursement for their past investments in the Project from the remaining Participants. While this rebalancing has been somewhat problematic, since the source of Project funding to date has been cash calls, this accommodation to downsizing or exiting Participants has been a policy matter for the Authority and the Reservoir Committee. However, once the Authority secures either interim or long-term external financing, these off-ramps will not be possible and Project Agreements will need to reflect this. This is because lenders and investors will want certainty regarding the Participants and their participation levels before committing to lend or invest.

VIII. Feasibility Hurdles/Risks

As mentioned earlier, there are a number of critical path milestones that must be met and decisions that must be made that will affect both the willingness of Project Participants to remain involved in the Project as well as the ability of the Project to secure external financing. These include but may not be limited to the following:

DWR Statements of Charges – If DWR and the Authority conclude that the Project's costs can be billed to participating State Water Contractors through DWR's annual Statement of Charges process, the Contractors may be able to bill for Project-related costs using their court-validated local property taxing authority. This would improve the credit characteristics of the participating State Water Contractors for Project purposes and could enable these Participants to avoid putting Sites charges on the monthly water bills of their customers. Several Participants have indicated that the ability to use the DWR billing process may determine whether or not they can participate in the Project.

Federal Participation – As discussed earlier, in addition to State participation in the Project, it is unclear how much federal participation there may be or in what form it may come (e.g., grants, loans or delivered Project components). At this point, commitments for federal participation in the Project consist of the $449 million USDA Rural Development loan that was secured by the Authority in 2018 and $24 million of Bureau of Reclamation grants for Project-related studies. If there is a future federal commitment to participate, it is likely to require a "rebalancing" or reduction of the participation levels of the existing Participants, due to the smaller reservoir that is currently being contemplated. On balance, we believe that federal participation in the Project would be viewed by the credit markets as a positive. The Authority and its legal and financial advisors will work to assure that the potential tax and other consequences of federal participation in the Project are understood and that decisions made by the Authority regarding federal participation will be informed decisions.

Litigation – While joint powers authorities such as the Authority have broad authority under State law, the Authority will still need to determine with its legal advisors if the Authority should be validating its authority to sell Project-related debt. Legal validation of bonding authority is often a protracted process that affects project timelines. If there is any litigation outstanding related to the Project that has the potential to jeopardize project permitting, water rights, construction or financing, it will be very difficult to secure interim or permanent financing.

Delays – It should also be noted that, even if it is determined that no validation of Project debt is required or recommended by counsel, any sale of public debt will still be subject to the risk of litigation based on legal and environmental claims and could therefore be delayed by court action. These delays could impact the Authority's ability to proceed with the Project and to refinance its interim debt with long-term debt, if interim lending if utilized. The risk of delays will need to be carefully assessed and disclosed to potential interim and permanent lenders.

Permitting – Interim lenders would be concerned about lending to the Authority prior to all environmental permits being in place as this potentially transfers some of the risk associated with the Project to the lenders themselves. This is not to say that lenders will not consider lending in these circumstances, but fewer banks would consider doing so and they would likely require higher interest rates and stricter lending terms. For this reason, the Authority does not plan to proceed with external financing until all key permits have been secured.

Water Rights - Securing of water rights for the operation of the Project is obviously essential for Project feasibility. In 1977, DWR filed claims for surplus water rights on a number of rivers in the State thereby potentially giving the State a priority claim on the water rights if and when needed. This pool or reserve of water rights rests with the State (not DWR specifically) and is controlled by the State Water Resources Control Board. The Authority has petitioned the State Water Resources Control Board for a portion of these reserved water rights to supply the water needed for the operation of the Project. Project staff estimates that these water rights will be secured by mid-2023. Similar to assuming environmental and permitting risks discussed above, interim lenders would have difficulty lending prior to the securing of the needed water rights as it would require them to assume the risk that the water rights will eventually be successfully secured. Therefore, similar to the issue lenders would have with lending before Project permits are secured, the Authority does not plan to proceed with external financing until water rights have been secured.

IX. Additional Guidance

This memorandum has provided information regarding the finance structuring issues that the Authority and the Reservoir Committee will need to evaluate and address as they prepare to interface with commercial lenders, long-term bond investors, rating agencies, the EPA (WIFIA loan program) and others regarding the Project's creditworthiness. As these internal discussions progress in the months ahead, there are several actions that the Project Financing Team could be taking that may help inform the Authority and Reservoir Committee discussions and decisions. We pose these questions for your consideration and future discussion.

- Should the Project Financing Team continue discussions with major banks to maintain their interest in the Project and to stay informed of their likely lending requirements?

- Would there be value in having the Project Financing Team engage in discussions on behalf of the smaller agricultural Participants with regional or specialty banks or other lenders that have a history of lending to smaller or agricultural entities to assess the availability and estimated cost of credit?

- Should the Project Financing Team work to further develop and refine the concept of a Sufficiency Pledge and Liquidity Reserve and test these concepts with potential lenders?

Draft Sites Reservoir Benefits and Obligations Contract Guiding Principles and Preliminary Terms

Preamble

The Sites Reservoir Project (the Project) is a proposed 1.3-1.5 million acre-foot off-stream reservoir located approximately 10 miles West of the town of Maxwell, California. The Project includes development and operation of infrastructure including necessary dams, pipelines, pump stations, power transmission lines, and other facilities needed to provide new water supply and storage. The Project will utilize existing conveyance facilities to divert water from the Sacramento River for storage in the reservoir and for deliveries. The Project will provide public benefits including environmental water supply, recreation, and regional flood control benefits. The Project will provide non-public benefits to participating water agencies including water storage and water supply benefits.

The Project is being developed by the Sites Project Authority (the JPA), a public agency formed in 2010 through execution of a Joint Exercise of Powers Agreement (the JPA Agreement) whose members are public agencies in the Sacramento River Watershed. The JPA Agreement and associated Bylaws identify requirements and obligations for membership in the JPA and allow for Project Agreements to govern funding and participation in any project the JPA undertakes. The JPA may also enter into agreements with other agencies for the purposes of developing the Project (see Related Agreements).

The Project is being developed in phases including (1, *complete*) formation and state funding award, (2, *in progress*) certification of environmental impact report and statement and acquisition of key permits, (3) final design and right-of-way acquisition, (4) construction and commissioning, and (5) project close-out and operations.

The JPA has entered into Project Agreements for the development of the Project through Phase 2 with JPA members and non-members who meet the requirements set forth in the JPA's Bylaws, referred to as Participants. The Project Agreements establish a Project Agreement Committee, the Reservoir Committee, made up of all Participants.

It is anticipated that beginning in Phase 3 and/or upon the initiation of project financing, the Project Agreements may take the form of a Sites Reservoir Benefits and Obligations Contract (the Contract). The purpose of this document is to establish guiding principles and preliminary terms to help guide development of the Contract between the JPA and the Participants (where the JPA and Participants are collectively referred to as "the parties").

There are several details that still need to be finalized for a full and complete agreement to be reached; however, the parties believe this document represents their mutual understanding of the allocation of project benefits, costs, risks, financing obligations, and ownership obligations. The parties agree to work cooperatively and in good faith to follow the guiding principles outlined herein and resolve any new issues identified later to establish the Contract by approximately Summer 2023, prior to initiating Project financing. This document is a work in progress and will need to be aligned with the final adopted Plan of Finance. Addressed principles include:

- Roles and Responsibilities
- Project Assets and Ownership
- Beneficiary Pays
- Financing
- Leasing of Storage and Sales of Water
- Minimum Contract Term, Successor Agreements, and Changes

Related Agreements

The Participants acknowledge that the JPA plans to enter into Agreements for the Administration of Public Benefits with various agencies of the State of California and to enter into an agreement with the Bureau of Reclamation for federal government funding of a portion of the Project in exchange for certain, defined benefits. While these state and federal agencies will not be party to the Contract, they are playing crucial roles in providing some Project funding and in administering public benefits. The JPA will strive to proportionately share Project risks, obligations and benefits within these agreements consistent with the JPA's overall "beneficiary pays" principle.

The Participants also acknowledge that the JPA is negotiating Facilities Use Agreements for use of the Glenn-Colusa Irrigation District (GCID) Main Canal, fish screen and pump station; the Tehama Colusa Canal Authority (TCCA) canal, fish screen and pump station; and the Colusa Basin Drain and associated facilities ("Partner Facilities").

Principles and Preliminary Terms

1. Roles and Responsibilities

1.1 The JPA will act as the developer and operator of the Project and is responsible for obtaining input from the Participants to help guide its decisions.

1.1.1 As the developer, the JPA is responsible for obtaining the required Project Water Right(s), securing the Project Site and any deeds claims or associated property rights, acting as the lead agency with regard to complying with CEQA / NEPA requirements, obtaining Project permits, evaluating funding options, collecting funds for payment of Project capital costs during construction (including debt service and reserves), entering into agreements needed to support development of the Project, and overseeing Project design and construction.

1.1.2 As the operator, the JPA will be responsible for: allocating water to and from storage in accordance with the Storage Principles (or its successor) and requests from individual Participants, the terms of the Contract, and with the Project Water Right(s); operating, maintaining, and replacing Project Facilities; permit compliance; collecting funds for payment of Project capital costs (including debt service and reserves), operations, maintenance, replacement and administrative / management costs; and all other functions related to administration of the Project and the Project Agreements.

1.2 The Participants are responsible for: covering Project costs (except for those obligations covered by grants, by Agreements for the Administration of Public Benefits with various agencies of the State of California, or by federal agreements); assuming certain Project risks and obligations as will be described in the Contract; and providing input to the JPA regarding Project funding, governance, and risk management.

1.2.1 As it relates to covering Project costs, the Participants are responsible for using their individual authorities (authority to establish and collect rates, taxing authority etc.) to ensure reliable cashflow to the JPA to provide for the timely payment of Project costs (including debt service and reserves).

1.2.2 As it relates to assuming certain Project risks and obligations, the parties agree that the Participants must have the opportunity for meaningful input into the definition and management of those risks and obligations. For clarity, risk management decisions that will significantly affect Project costs and / or Participant's risk exposure will require **[input from the Participants / concurrence from Participants as indicated by a majority of shares]**. For example, any decision to expand the Project scope to include significant purchase of property downstream of the dam as a means of mitigating flooding or dam failure risk would fall into this category.

1.2.3 As it relates to providing input to the JPA more broadly, the Participants are all individual members of the Sites Reservoir Committee (and its workgroups) established by the JPA to undertake specific work activities for the development of the Sites Reservoir Project.

1.3 Future Changes to Roles and Responsibilities. The parties acknowledge that the parties may agree to future changes in the roles and responsibilities between the JPA and Participants. Such changes may be considered at major Project milestones such as the time the water right is secured, at the time of financing; and completion of Project construction, as examples.

2. Project Assets and Ownership

2.1 The land on which Project facilities are sited, physical features of the Project (excluding Partner Facilities, and the water right(s) will be owned by the JPA.

2.2 Each Participant's interest in the Project is represented by its allocation of storage capacity and its right to a proportionate share of Sites water available that is diverted to storage ("capacity share").

2.2.1 Within certain constraints, storage capacity allocations and the associated rights to Sites water shares will be considered saleable assets.

2.2.1.1 The Participants agree that any sale of a Participant's storage allocation cannot result in a change to the Project's bond rating or otherwise pose any risk to Project financing, and may be subject to the approval of the financing entity(ies) depending on the terms of any financing agreement. The sale of a Participant's share will be approved by the JPA.

2.2.1.2 Possibly Add / Discuss: Any constraints on pricing sales, priority of who is offered shares for sale, and that any Participant selling its storage allocation will receive payment "net" of any payments owed the JPA.

2.3 Possibly Add: Quantify rights to water supply and storage allocations for individual Participants.

3. Beneficiary Pays

3.1 The parties agree that, in principle, Project costs should be allocated consistent with the flow of Project benefits and obligations. For clarity, this means that a Participant receiving benefits from the Project or from a Partner Facility agrees to pay a pro-rated share of all costs of the Project and, if applicable, of the Partner Facility consistent with the Cost Allocation Framework (to account for which Participants use which facilities) developed by the JPA with input from the Participants.

3.2 Project Costs include all costs of Project development (i.e. land, water rights, permits), design, construction, debt service, operation and maintenance, major renewals and replacements, and administrative costs.

3.2.1 Project fixed costs (excluding fixed costs associated with Partner Facilities) will be allocated between all Participants based on their percent share of Project storage (excluding any storage allocated to federal and California state agencies).

3.2.2 Project variable costs (excluding variable costs associated with Partner Facilities) will be allocated based on the estimated annual amount of water moved into and out of storage by each Participant as a percent share of the total annual amount of water moved into and out of storage. At the end of the year a true-up process will be used to align estimated and actual quantities of water moved.

3.3 Partner Facility Costs. The parties recognize that certain Partner Facilities are needed to realize Project benefits but that not all Participants need to use all of the Partner Facilities. Partner Facility costs will be allocated to Participants based on actual use based on wheeling rates established in the Facilities Use Agreements.

3.4 Possibly Add: Quantify cost allocations for individual Participants based on the beneficiary pays principle.

4. Financing

4.1 The parties agree that the JPA will issue debt to fund all or a portion of the Project capital costs at such time that the JPA has secured the water right and has otherwise made sufficient progress such that the JPA, as advised by the Reservoir Committee, has determined that long-term debt issuance is warranted.

4.2 The parties further recognize that significant benefits to the Project as a whole would result from group financing (i.e., lower interest rates, **[other]**) and that financing entities may impose conditions on the financing that will likely impact each of the Participants. The parties agree to continue to evaluate group financing along with other financing methods beneficial to the project.

4.2.1 Group Financing and Ratings of Individual Participants

4.2.1.1 Not all of the Participants are rated by recognized credit rating agencies and are therefore unable to lend their rating to a group financing. Therefore, in order for group financing to be viable, the financing will need to be based on the rating of a significant subset of those Participants that are rated. To the extent that an unrated Participant may be able to obtain a rating of "A" or better, the parties agree that such Participants are encouraged to do so.

4.2.1.2 The parties acknowledge that those Participants lending their rating to a group financing are taking additional risk and the parties agree to explore means to offset this risk.

4.2.2 Obligations of "Pay Go" Participants to Support Project Financing.

4.2.2.1 The parties also recognize that some Participants may wish to obtain their own financing or to pay Project costs as they are incurred out of available revenues ("pay-go").

4.2.2.2 "Pay-Go" Participants also recognize that they will receive an indirect benefit from Project group financing in that it provides a greater assurance there will be a sufficient number of Participants to assure viability of the Project.

4.2.2.2.1 "Pay-go" may be allowed as long as it does not materially adversely affect the ability to finance the Project.

4.2.2.3 "Pay-go" Participants also recognize the JPA's need for reliable cash-flow to fund Project design and construction. Therefore the "Pay-go" Participants will commit to fund reserves through early payment in order to reliably meet their funding obligations.

4.2.3 In order for group financing to be viable, financing entities have indicated they will require any financing agreement to include a "Project Sufficiency Pledge". All Participants will need to agree to these obligations, even if they select a "pay-go" option.

4.3 Possibly Add: Quantify debt-service and other financial obligations for individual Participants.

5. Leasing of Storage and Sales of Water

5.1 Participants may share or lease their Storage Allocation with other Participants and with other entities. The terms of sharing or leasing are at the discretion of the Participant who is a party to the storage or lease agreement but must not negatively impact other Participants, Project operations or financing. Any sharing or leasing of will be coordinated with the JPA so that proper Project operations and water accounting can be maintained. A Participant may not transfer or assign any of its rights or obligations as part of any sharing or leasing agreement.

5.2 Participants may sell water held in their Storage Allocation to other Participants or other entities. The terms of sales of water held in a Participant's Storage Allocation are at the discretion of the Participant but must not negatively impact other Participants, Project operations or financing. Any sale of water held in a Storage Allocation will be coordinated with the JPA so that proper Project operations and water accounting can be maintained. A Participant may not transfer or assign any of its rights or obligations as part of any sale of water. The receiving entity must either have sufficient available Storage Allocation to store the water or release the water upon purchase.

5.3 Possibly Add / Discuss: Any priority, pricing constraints, or obligations related to the sales of water supply or leasing of storage to Participants or non-Participants.

6. Minimum Contract Term, Successor Agreements, and Changes

6.1 The parties agree that the term for the Contract will, at a minimum, coincide with the length of the financing agreement and will contain provisions for extensions.

6.2 The parties further acknowledge that it will be necessary to develop successor agreements and that the Contract will detail the process and timeline for developing, negotiating and agreeing to such successor agreements.

6.3 Possibly Add / Discuss: Project offramps at different milestones during the Project's development.

6.4 Possibly Add / Discuss: Changes in the regulatory environment and permit conditions.