



July 18, 2018

Mr. Mike Markus, P.E.
General Manager
Orange County Water District
18700 Ward Street
Fountain Valley, CA 92708

Subject: Proposed Poseidon Seawater Desalination Project at Huntington Beach

Mike:

In your email to the Producers on July 13, 2018, you explained that, in your view, the OCWD Board had only requested input from the Producers regarding the proposed term sheet between OCWD and Poseidon Resources. Your email arrived after the Producers had already developed, over the course of two meetings, an approach through which input from the Producers could be provided to the OCWD Board. We were disappointed that the Producers' efforts to provide input on the Poseidon project, as a group, were rejected and replaced by four questions regarding the revised term sheet. At tonight's meeting, we will be requesting that the OCWD Board table this item so a dialogue can begin with the Producers regarding the proposed Poseidon project.

At this time, engagement with the Producers is difficult at a policy level since only a few retail water agencies have adopted a formal position regarding the Poseidon proposal. That fact does not preclude a detailed two-way discussion among the water managers from the Producer agencies and OCWD. In the absence of policy positions, it is more appropriate to limit these discussions to non-policy items – of which there are many. For example, staff from water agencies are very qualified to debate the projected annual average rate increase of rates charged by the Metropolitan Water District of Southern California (MWD). Why not include the Producers in the discussion regarding MWD's future rates? This does not reduce the OCWD Board's authority to make the final selection, but it seems a more informed decision – especially when this assumption will dictate whether Poseidon water will ever be less expensive than MWD water – will be a better decision.

The Groundwater Producer Agencies managers met on June 13 to discuss the OCWD Board's request for input from the Producers. At that meeting we developed an approach that consisted of OCWD staff facilitating a mini-survey of the Producers based on questions developed together. In response to a request for potential questions, individual agencies sent in what amounted to 55 questions for consideration at the July 11 Producers meeting. OCWD staff even

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provided nine questions as a starting point for our discussions. The list of 55 questions is attached to this letter as Exhibit "A".

In my experience, OCWD is at its best when it works in partnership with its Producer agencies. This cannot happen without meaningful dialogue. To make that dialogue productive requires that OCWD recognize the unique traits of the Producer agencies, while developing solutions that benefit the Basin. At tonight's OCWD Board meeting, I will once again be requesting that OCWD table the term sheet discussion in lieu of addressing the concerns of IRWD and the other Producer agencies. I will also request that the Board clarify that it is interested in receiving input from the Producers and that we work together to fairly and accurately ascertain this input.

On a separate but related note, it would benefit OCWD and the Producers to request that Poseidon provide a written statement that it understands and accepts the non-binding nature of the term sheet, the associated discussions and analyses taking place. If OCWD does not already have a statement like this from Poseidon, could you please make this request of Poseidon? Many of us would be interested in Poseidon's response.

Please provide a copy of this letter to each of your Board members in advance of tonight's Board meeting. I look forward to working with you on this matter.

Sincerely,



Paul A. Cook, P.E.
General Manager

Enclosure

EXHIBIT "A"

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OCWD Groundwater Producers Poseidon Term Sheet Questions

1. Is the Metropolitan Water District of Southern California (MWD) unreliable? MWD, who built the Colorado River Aqueduct, was instrumental to build the State Water Project, build the Diamond Valley reservoir, is the leader on the twin tunnels, and water recycling in partnership with the LA county Sanitation District, unreliable? Has the MWD ever failed us?
2. Why would we want to pay more for desalinated water than imported water from MET? With the cost differential, shouldn't we import more water and put it in the ground, save money, fill the basin, and have plenty of water for the next drought at a lower price?
3. The new proposed Term Sheet shortens the agreement length from 50 years to 30 or 35 years. Therefore, after 30 or 35 years the desalination plant will be owned by OCWD. This sounds like a good deal; however, under what conditions will that plant be transferred to OCWD? Will the maintenance and repairs be kept up to date or would the plant be completely dysfunctional due to lack of maintenance and repairs?
4. When will the updated OC Reliability Study be available for review? Have any of the parameters changed from the initial study (i.e., decreased reliability of the SWP before WaterFix built ((goes to availability of imported water for GW recharge)); QSA full implementation/uncertainty re: Salton Sea; Lake Mead shortages; likelihood of sustained extreme conservation ~.4-.5MAFY over time)?
5. Is there a value/subsidy being provided by MET for the increased reliability provided by the Poseidon project?
6. What does the term "economic return" starting in Year 15 mean? Is the "economic return" tied to maintenance, repair and rehabilitation costs/conditions in the plant?
7. Will there be parameters set (and validated by an outside party on a regular basis) to determine the operational condition and asset value of the plant during the term of the agreement?
8. What are the cost of the distribution facilities in AF?

9. **Term Sheet Question** - Do you approve that one agency would benefit more than the rest due to the treatment plant location?
10. **Term Sheet Question** - Based on the anticipated increase in RA, what is your agency's monthly residential bill increase will be based on 5/8 meter and 15 units of use in today's dollar? OCWD to provide the anticipated RA in today's dollar based on the today's project cost analysis.
11. **Term Sheet Question** - Is your agency willing to subsidize other agency for the good of all producers?
12. **Project Question** - Would your agency support a water supply alternative study? Considering lower water demands, GWRS Final expansion, Cal WaterFix, Cason Plant, recycling, new conservation laws and others.
13. **Project Question** - Do you consider Desalination as an insurance policy?
14. **Project Question** - Do you agree that using of desal water for spreading or injection (except for the sea water barrier) is not a good use of the water?
15. **Project Question** - Would you favor a smaller capacity project/plant?
16. **Project Question** - Would you support placing the project on a county-wide ballot?
17. As described during the June 13th Producers Meeting, OCWD may consider a CPTP type program. Implementation of a CPTP program could increase the BPP for inland Producers. Increasing the BBP for inland Producers may facilitate the need for the Producers to construct additional production and/or distribution facilities. Based on an evaluation conducted in 2017, a permanent increase in the BPP to 86% could require a significant increase in capital spending. Who will be expected to pay for these improvements? Has this potential capital cost been factored into the cost-benefit-analysis? Are any of these costs included in the \$350 / acft distribution/conveyance allowance? Would this result in any 'stranded capital' for Producers?
18. Would usage of Poseidon water require OCWD to pump more GWRS water to the forebay? Can existing basins handle this additional GWRS water? Would additional basins be required?

19. Please clarify cost-benefit of utilizing Poseidon water at barrier wells. Using Poseidon water for recharge/barrier wells does not appear to be an efficient use of such expensive water. What is the cost-benefit of using this water to defer other improvements? What were the assumptions? Payback period?
20. For the cost impacts to OC Basin / Producers shown in the Board presentation, did those number assume that OCWD would take all 56,000 ac-ft of water? How would these numbers be impacted if South County retailers committed to a specified amount of water? How much water could realistically be assumed for this estimate? How much water could be conveyed to South County through existing infrastructure?
21. We are assuming that the annual O&M cost (including membrane replacement cost, which might be high) is included in the estimated unit cost (e.g., in the \$1,916/af for the 30-year deal). Please provide a more detailed breakdown for the various components making up the stated unit cost (Debt Service + O&M + Energy + R&R). Please also provide a more detailed breakdown for the assumptions/components that make up the stated \$350/af place holder for the Distribution System (Debt Service + O&M + Energy).
22. The estimated MWD LRP subsidy of \$475/af is good for 15 years. The increase in the unit cost after LRP is over should be more clearly identified on the 30-yr and 35-yr unit cost graphs.
23. Has OCWD considered how this project would help filling the water supply gaps identified in the OC Reliability Study? How much benefit/reliability would this project provide if Cal WaterFix is constructed?
24. What happens if it becomes too costly for Poseidon to continue operating the project? Would OCWD step in and take over prior to the 30-yr (or 35-yr) term?
25. Do you believe that MWD will run out of water at some point during the next 30 years?
26. Do you believe that OCWD should replace reliable water from MWD with a more expensive supply from the Poseidon Project, as required by MWD to receive LRP subsidies?
27. Do you believe that a \$100 to \$250 per AF increase in the RA is an acceptable cost for benefit(s) related to OCWD's participation in the Poseidon Project?

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28. Do you believe that the Producers should subsidize Huntington Beach getting water at a discount from the Poseidon Project?
29. Should individual Producer agencies be allowed to opt out of the costs and any benefits associated with the Poseidon Project?
30. Do you believe that recharging water from the Poseidon Project (direct or in-lieu) would be more cost effective than recharging water available from MWD or from the GWRS?
31. Do you believe that it is appropriate to assume that MWD's rates will increase at 4.1%?
32. Do you believe that OCWD and the Producers should bear any risk associated with the Poseidon Project including electricity costs?
33. Do you believe that the cost of water from the Poseidon Project should be capped at the cost of MWD water?
34. Do you believe that OCWD should perform a comprehensive study of alternatives prior to considering executing a term sheet for the Poseidon Project?
35. Do you believe that a 30 year take-or-pay contract with Poseidon Resources will be the most cost-effective water supply reliability alternative available to OCWD?
36. Should OCWD develop more cost effective reliability projects before committing to the Poseidon project?
37. Do you believe that OCWD should finalize its plan for distributing water received from the Poseidon project before continuing discussions with Poseidon on a term sheet?
38. Should OCWD pursue the Poseidon project if it will negatively impact OCWD's credit rating?
39. Do you think that MET will not be able to provide current delivery levels nor increase levels over the next 20 to 40 years as normal operation?
40. What are the political ramifications from steep RA increases if OCWD fully participates in this project.

41. As far as MET reliability do you believe that any catastrophic event in the MET system would be significant enough where it would not be up and running within 2-4 weeks.
42. Import supply is 25% of most producers total water production. This year it will be 23%. Will a one month outage of MET be manageable without Poseidon water?
43. Do you believe that there is a possibility that this project would hinder the ability for OCWD to take potential Carson Plant water that would not be subject to allocations?
44. Is OCWD's proposed partnership with Poseidon stepping beyond OCWD's core purpose and mission?
45. Is the Poseidon project the right project for the OCWD GW Basin at the right price?
46. Should OCWD and or MWDOC prepare a supply/demand balance analysis for the proposed baseline water resource?
47. Considering the proposed cost per acre foot, should any portion of the treated water from the proposed project be used for direct recharge or barrier water for the groundwater basin?
48. If used for barrier or direct recharge should the cost comparison for this resource be using fully treated Met water?
49. Is MWD's water supply to our basin unacceptably unreliable? If so, how would you characterize this condition in general terms? For example, one answer might be MWD's supply is unreliable three years out of ten.
50. Should the cost comparison for the feasibility of the HB Desalination Project use the cost of fully treated (T1) MWD rates?
51. Should a decision be made on the proposed terms sheet without knowing the full cost of the project including conveyance?
52. Should there be in-basin funding for a project that will benefit non-basin retailers?
53. Will the quality of the proposed desalinated water be higher, lower or neutral compared to other sources currently in use in the OCWD service area?

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54. Do you think the new state legislation on water conservation mandates will impact demands in the future?

55. Should OCWD continue to finance studies and analysis on the proposed project with its replenishment assessment and other revenues derived from the OCWD GW Producers?