



MEMORANDUM

TO: City Council

FROM: Matthew Downing, City Manager
Bill Robeson, Assistant City Manager/Public Works Director
Nicole Valentine, Administrative Services Director
Shannon Sweeney, City Engineer
Shane Taylor, Utilities Manager

SUBJECT: Discussion of City Water Supply, Central Coast Blue, and Future Resources; and Consider Approval of a Budget Adjustment Request

DATE: April 9, 2024

SUMMARY OF ACTION:

Since 2021, the City of Arroyo Grande has been committed to augmenting the regional water supply, most recently by participating in a Joint Powers Authority (JPA) with the Cities of Grover Beach and Pismo Beach to recycle wastewater through the Central Coast Blue (CCB) project. Since then, significant progress has been made toward that goal. Recent financial updates regarding funding availability and implementation cost necessitate City Council review. Staff recommends a budget adjustment to pay for costs in FY 2023-24, presents this discussion of the City's water supply, and seeks Council input on next steps.

IMPACT ON FINANCIAL AND PERSONNEL RESOURCES:

The JPA Cost Sharing Agreement obligates the City to pay for 25% of the total costs of the CCB Project. The City of Pismo Beach will pay 39% of the costs and the City of Grover Beach will pay 36% of the costs. The range of estimated CCB Project costs increased from \$85-\$112 million in 2022 to \$134-\$159 million in 2024, with most of the escalation attributed to inflation. The last review of the City's Water Rates incorporated the CCB Project construction cost estimate at \$93 million.

Based upon the JPA Cost Sharing Agreement, the City currently owes approximately \$409,000 in pre-construction costs to the City of Pismo Beach, with an estimated \$105,200 the remainder of FY 2023-24. A budget adjustment totaling \$514,200 from the Water Enterprise Fund Balance is needed to fund the City's share of the CCB project pre-construction costs for FY 2023-24.

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RECOMMENDATION:

- 1) Receive and file a discussion of City water supply and future water resources;
- 2) Approve a budget amendment totaling \$514,200; and
- 3) Provide direction as necessary.

BACKGROUND:

The City of Arroyo Grande has evaluated its water supply and demand several times. The [2021 Water Supply Alternatives Study Update](#) references and summarizes previous work, including the 2004 City of Arroyo Grande Water Supply Alternatives Study. That report analyzed seventeen water supply alternatives the City could implement to increase water supply and meet future demands. The 2021 report is included as Attachment 1. One of the main recommendations of that report is continued participation in a regional recycling project as a source of an additional permanent water supply, such as Central Coast Blue (CCB).

CCB is a regional recycled water project. The Project has been a multi-agency effort between three of the four Northern Cities Management Area agencies (the Cities of Arroyo Grande, Grover Beach, and Pismo Beach) to construct a regional recycled water project that will enhance supply reliability by injecting advanced purified water into the Santa Maria Groundwater Basin (SMGB). The Project will reduce vulnerability to drought and seawater intrusion by creating a seawater intrusion barrier and supplementing the naturally occurring groundwater.

The inception of a recycled water project began in 2014 with the San Luis Obispo County Regional Recycled Water Strategic Plan. This concept was further augmented in 2015 with the Pismo Beach Recycled Water Facilities Planning Study and in 2016 with the South San Luis Obispo County Sanitary District Recycled Water Facilities Planning Study. A final environmental impact report and preliminary attentional report were completed in 2021.

On [March 23, 2021](#), the City Council considered a proposed CCB Operating Agreement. After receiving public comment and conducting discussion and deliberation, the City Council approved the Operating Agreement and adopted Statements of Overriding Considerations and a Mitigation, Monitoring, and Reporting Program.

On [September 14, 2021](#), the City Council discussed eight preliminary water supply alternatives and directed staff to complete an analysis of these potential water supply alternatives. On [November 23, 2021](#), the City Council received the [2021 Water Supply Alternatives Study Update](#). The recommended long-term water supply alternative in that report was continued participation in a regional recycling project such as CCB, as a source of additional permanent water supply.

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On [January 11, 2022](#), the City Council approved a [Water and Wastewater Rate Study](#). The study proposed a water rate increase of 6.4% beginning on April 19, 2022, and increases each January 1 through 2026 to provide sufficient revenue for ongoing operations as well as participation in the CCB project. The water rates include the City's full costs to participate in CCB without additional grant funding based on the estimated costs at that time, which are shown in Table 1:

Table 1 – CCB Total Cost Incorporated in the 2021 Water & Wastewater Rate Study

Pre-Construction Costs	\$ 8,288,607
Construction Phase Costs	\$ 43,407,577
Total Costs	\$ 51,696,183

On [January 25, 2022](#), the City Council authorized entering into a Cost Sharing Agreement with the other JPA participants and applying for financial assistance to the State's Clean Water State Revolving Fund.

On [September 14, 2022](#), the first joint City Council meeting called for in the Cost Sharing Agreement was held. At that meeting, the City Councils and the public received an update from the Project's design and engineering consultant regarding the Project components and purpose, preliminary design of the Advanced Treatment Facility, updated cost estimates, grant funding opportunities and awards, and permitting requirements. At this meeting, the total construction cost estimates for the Project increased to \$93 million.

On [September 27, 2022](#), the City Council approved the CCB JPA Agreement, creating the CCB Regional Recycled Water Authority (CCBRRWA), and appointed Mayor Ray-Russom to be the City Council's representative CCBRRWA Board of Directors. On June 5, 2023, a second joint City Council meeting was held. At that meeting, the City Councils and the public received an update from the CCBRRWA General Manager and the Project's design and engineering consultant that included a Status Report and Project Update. Additionally, a Report was presented on alternatives and considerations to advance local hiring for construction of the CCB Project, while no formal action was taken.

On [August 8, 2023](#), the City Council authorized staff to apply to the Environmental Protection Agency (EPA) for a Water Infrastructure Finance and Innovation Act (WIFIA) loan to fund the City's share of CCB project costs, incur costs related to the application, and appropriated \$55,000 from the Water Enterprise Fund Balance to support these actions. The total construction costs used for the WIFIA loan were estimated at \$93 million, of which \$39 million would be paid by grants and \$54 million would be financed by Arroyo Grande, Grover Beach, and Pismo Beach. Arroyo Grande's share of CCB is 25% and, after adding the City's estimated preconstruction payments of \$2 million, the City would need to finance up to \$14.3 million for the remaining portion of preconstruction

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and construction costs. During the WIFIA application process, the City had a 10-year proforma completed by Tuckfield and Associates to confirm current Water Rates were sufficient to sustain the construction cost increase with current rates and into the future. The 10-year proforma analysis stated that in FY 2026-27 through FY 2029-30 water rates would need to increase by 9% each year.

The CCBRRWA Board of Directors met on [March 18, 2024](#), at which time they received an update on the Project. The project update included discussion related to Water Supply Conditions, Funding and Financing, and Project Costs.

Water Supply Conditions

Current water supply conditions for the CCB Partner Agencies have improved since the 2019 to 2022 historic drought, experienced Statewide. Lake Lopez is at capacity, groundwater levels are at a 10-year high, and State Water Project allocations are at 30 percent as of March 22, 2024. While the recurrence of drought conditions in the future is likely, this temporary improvement in water supply conditions has afforded the CCB Partner Agencies the opportunity to revisit and refine the Project delivery strategy to provide the most cost-effective project to the ratepayers.

Funding and Financing

In January 2024, the State Water Resources Control Board (“State Board”) Division of Financial Assistance informed the City of Pismo Beach that the \$15 million Water Recycling Funding Program Grant awarded in September 2023 would be reduced to \$5 million. This reduction is part of a Statewide effort to address the State budget deficit and is not unique to CCB. All ten projects initially awarded Water Recycling Funding Program (WRFP) Grants in the State Board’s FY 2023-24 Clean Water State Revolving Fund Intended Use Plan are facing grant reductions. The \$10 million grant reduction has resulted in a significant funding gap that will necessitate revisions to the Project funding plan and the overall funding and financing strategy. It is important to note that the remaining \$5M of the WRFP Grant is at risk until secured by an agreement with the State Board.

Project Cost

Construction costs for water and wastewater projects continue to increase throughout the State, especially for water reuse projects employing specialized treatment technologies with extensive mechanical and electrical distribution equipment. This reality has increased the estimated CCB Project costs since the last cost estimate was prepared. The range of estimated CCB Project costs increased from \$85-\$112 million in 2022 to \$134-\$159 million in 2024, with most of the escalation attributed to inflation and supply chain issues. The Project team has been exploring opportunities for cost reduction through value engineering and collaborative delivery methods. Additionally, efforts are being made for each Partner Agency to conduct a water supply strategy evaluation along with project management efforts that include pursuit of additional funding, a temporary

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pause to detailed design and permitting, re-evaluation of the Project implementation schedule, and analysis of value engineering and collaborative delivery options to reduce overall Project cost.

Additionally, CCBRRWA staff and Project consultants have dedicated significant time and resources over the past several months to respond to questions and concerns from community members and Project stakeholders. This increased interest in the CCB Project, coupled with limited staff resources, has led the Project team to identify the need to implement a more robust communications strategy, including the potential for the support of a professional community engagement firm. This would require additional preconstruction costs to the City not previously anticipated.

ANALYSIS OF ISSUES:

The CCB project design involves injecting recycled water into the basin at key locations near the seawater interface (Project) to help address the threat of seawater intrusion. Phase 1 of the Project proposes to treat wastewater from the City of Pismo Beach to an advanced purification level to create approximately 900 acre-feet of additional water per year. This new developed water would be injected into the basin at key locations to help ensure that a sufficient barrier exists within the basin to keep seawater from flooding into the aquifer and contaminating the wells used by the NCMA parties. As a result, the Project will support the City's ability to rely on groundwater to supply water to its residents and businesses into the future. The Project could secure an estimated 225 acre-feet per year of reliable groundwater for the City.

As identified above, each of the Partner Agencies will be evaluating their individual water supply strategies in light of the changing conditions surrounding the region's water supply and the Project's financial changes. This discussion is to evaluate the City's water supply strategy.

Water Supply and Demand

In an ever-changing, semi-arid climate like California, cities must evaluate and plan for water supply and demand scenarios over a variety of time periods. One strategy for meeting long-term water supply needs is conservation. Significant conservation has already been accomplished by Arroyo Grande residents and businesses.

Current conditions do not negate the need to prepare for future potential drought conditions similar to the ones experienced from 2013 to 2022. In December 2022, storage in Lopez Lake was depleted to 22% of capacity, approximately 10,800 acre-feet. These levels neared the point where no further water from Lake Lopez could be delivered for municipal supply, even with the conservation achieved. Had the drought extended one more year, the City would have been forced to rely solely on its groundwater supply, which was similarly depleted. Accordingly, the City should consider water supply options during this current period in order to capitalize on this recent period of significant precipitation.

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Short-, Mid-, and Long-Term Options

2023 and 2024 rains have filled Lopez Lake and, through active management, have secured the City's water supply needs for at least approximately seven years. In light of this, there are no additional short-term options needed to be considered at this time.

If drought conditions occur in the mid-term of approximately 7 to 12 years, staff have identified three potential options for City action:

1. Implement progressively severe conservation measures to maintain water supply for as long as possible. This is seen as a standard action previously implemented and would be one of the first actions recommended at the appropriate time in a future drought scenario.
2. Temporary Purchase of State Water from Oceano Community Services District (OCSD). This option was exercised in 2009 when the City and OCSD entered into a five-year agreement for 100 acre-feet per year Oceano water supply be delivered to the City. The cost was 105% of the Lopez water cost at the time. The ability to pursue this option in the future will depend on OCSD's needs, availability, and willingness.
3. Purchase State Water from San Luis Obispo County. The Department of Water Resources recently modified rules for the purchase and exchange of State Water. San Luis Obispo County (SLOC) and Central Coast Water Authority (CCWA) recently entered into an agreement for the exchange of State Water supply for pipeline capacity. Because of these changes, the City has an opportunity to potentially participate in the purchase of a portion of that water in future times of need, should this be of interest to the City Council now or in the future.

As stated previously, California is an ever-changing, semi-arid climate. As responsible stewards of public resources, the City needs to continue working towards long-term water resiliency because multiple-year drought conditions will occur again. CCB has been the City's and region's best long-term water supply option. In light of recent years of significant rain, and with loss of grant funding and increased project cost estimates, this affords the City and Partner Agencies the opportunity to continue evaluating the Project implementation schedule, potential additional phasing, opportunities for additional grant funding, potential for additional project partners, and analysis of value engineering and collaborative delivery options to reduce overall Project cost.

Water Rates Status

The current water rates and the 10-year proforma completed in August 2023 show that the current and future water rates could sustain the CCB project at the estimated \$93 million construction cost. With the updated estimates project costs totaling in the range of \$134 - \$159 million, the 10-year proforma would need to be updated once cost estimates have been updated with value engineering and an updated timeline for construction to begin work has been completed. To date the City has spent \$2,006,027, as shown in Table 2 below:

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Table 2 – Expenditures spent towards the CCB Project

Expenditure Programs	FY 2017-18 through FY 2021-22	FY 2022-23	FY 2023-24	CCB Total
CCB JPA O&M	-	19,645	83,528	103,173
Land Purchase - Calvin Court	-	50,181	-	50,181
CCB Pre-Construction Costs	302,637	1,550,036	-	1,852,673
	302,637	1,619,862	83,528	2,006,027

The current FY 2023-24 did not include additional funds for the CCB project because the original intent was to include all FY 2023-24 costs for pre-construction as part of the WIFIA financing. With this updated Project information, financing will not be completed in FY 2023-24. Accordingly, a budget amendment totaling \$514,200 for FY 2023-24 pre-construction costs is requested for approval from the Water Enterprise fund, bringing the Project total to \$2,520,227, as shown in Table 3 below:

Table 3 – Expenditures spent towards the CCB Project with the Proposed Budget Adjustment

Expenditure Programs	FY 2017-18 through FY 2021-22	FY 2022-23	FY 2023-24	CCB Total
CCB JPA O&M	-	19,645	83,528	103,173
Land Purchase - Calvin Court	-	50,181	-	50,181
CCB Pre-Construction Costs	302,637	1,550,036	514,200	2,366,873
	302,637	1,619,862	597,728	2,520,227

Next Steps

Dependent upon any direction provided by the City Council, staff will continue engaging with Partner Agencies to deliver a cost-effective project resulting in a reliable water supply for the City’s Water Supply.

ALTERNATIVES:

The following alternatives are provided for the Council’s consideration:

1. Approve the budget amendment;
2. Do not approve the budget amendment; or
3. Provide other direction to staff.

ADVANTAGES:

Approving the budget amendment and pursuing water supply strategies as outlined have the following advantages:

- Demonstrates the City’s commitment to reliable water supplies.
- Recent rains have provided relief to immediate water supply needs but do not eliminate the need to continue working towards long-term water supply reliability.
- Recent improvements to the City’s immediate water supply provides time to determine next best steps.

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- Work already completed by the JPA supports future water reliability projects.
- Some elements of the CCB project, constructed in a phased manner, can continue working towards the long-term needs while considering current budget limitations.
- Using work to date, project framework could be developed that can support a modular solution in short order, should environmental situations change more rapidly than anticipated.
- Continues progress using the momentum of the JPA structure and regional framework already established.

DISADVANTAGES:

Approving the budget amendment enables the City to pay costs already incurred as a participant in the JPA. However, this expenditure will not result in project completion or any increase in water supply. The CCB project as originally scoped has exceeded existing and anticipated funding. At this time, project completion as currently designed appears untenable. However, some grant funding has already been secured. There may be value in determining how such funding may be applied to elements associated with a long-term, permanent, reliable regional water supply.

ENVIRONMENTAL REVIEW:

This recommended course of action is not a project subject to the California Environmental Quality Act (CEQA) because it has no potential to result in either a direct, or reasonably foreseeable indirect, physical change in the environment. (State CEQA Guidelines, §§ 15060, subd. (c)(2)-(3), 15378.)

PUBLIC NOTIFICATION AND COMMENTS:

The Agenda was posted at City Hall and on the City's website in accordance with Government Code Section 54954.2.

ATTACHMENTS:

1. 2021 Water Supply Alternatives Study Update