

**STATE OF CALIFORNIA
CALIFORNIA REGIONAL WATER QUALITY CONTROL BOARD
CENTRAL COAST REGION**

STAFF REPORT FOR OFFSITE MEETING OF June 9, 2004

Prepared May 27, 2004

ITEM NUMBER: 3

**SUBJECT: Use of Nonprofit Organizations as Settlement Fund Holding Vehicles
and Discussion of a Regional Board Conservation Program**

SUMMARY

Over the past seven years the Central Coast Regional Water Quality Control Board has repeatedly made use of nonprofit organizations to hold and manage funds from various settlements, usually associated with mitigation requirements for illegal discharges or other impacts to water quality. We have learned a great deal during these years about how to set up these funds most effectively, and we discuss in this document some lessons learned from past settlements and suggestions for future approaches that may maximize our overall effectiveness.

We also discuss a new idea: a Regional Board Conservation Program, which would focus available funds on high priority, beneficial Board approved projects, while maximizing our efficiency and effectiveness. This would be accomplished by directing some:

1. existing unallocated Regional Board settlement funds,
2. future settlement funds, and
3. future funds from administrative civil liabilities and mandatory minimum penalties,

toward specific Conservation Program objectives, through a single (or a few select) coordinating nonprofit organization(s).

DISCUSSION

Several of the major settlements from the past seven years are described below to provide some historical perspective on the use of nonprofits for settlement management. A summary table of current and historical SEPs is provided as attachment one. Key observations relate to the role the selected nonprofit plays in managing the

fund, the fees that are charged, whether the funds have been leveraged, and resulting staff work load.

1997 – P G & E Diablo Canyon Settlement

\$2.5 million out of a total of \$14.2 million of this settlement was held as a long-term endowment at the San Jose State Community Foundation to support the State Mussel Watch Program. The Foundation has served in a fiduciary capacity only. Funds were not restricted for use in the Central Coast Region only, and have typically been spent to support a number of long-term monitoring sites up and down the state. The entire Mussel Watch program was in dire financial straits at the time. Our Board recognized the value of this statewide program, and took advantage of this settlement opportunity to do something for the good of the statewide water quality program by steering this money to Mussel Watch. Three of the program's sites fall in our Region. Funds have also been spent to upgrade equipment and facilities at the Mussel Watch laboratory, and to develop new analytical techniques for newly emerging chemicals. The fund balance in the most recent annual report (March 2003) was \$2 million. This fund is entirely managed by the California Department of Fish and Game and represents little work for staff. A statewide committee consisting of staff from the State Board and coastal Regional Boards convenes periodically to provide input into fund use.

From this same settlement, the Regional Board (and PG&E – a settlement requires the agreement of both parties) designated \$3.66 million for the Bay Foundation of Morro Bay to implement the Morro Bay National Estuary Program (NEP) Comprehensive Conservation and Management Plan. Pursuant to the Consent Decree, the fund is to be fully spent by 2007. In this case, the

intended use of the funds coincided closely with the nonprofit's mission. The Bay Foundation charged no fees for holding the funds, and only reimburses themselves for bookkeeping and accounting costs. Because staffing was available through the NEP to plan and implement projects, this fund requires little oversight on the part of staff (we approve fund use through participation on an Executive Committee, and Executive Officer approval). This fund has been used very effectively to leverage millions of additional dollars into the program. For example, the Hollister Ecological Reserve, a 580 acre land purchase on Chorro Creek which restores 1.5 miles of floodplain and riparian habitat, was purchased for \$5.2 million, of which only about \$195,000 of settlement funds were needed. \$2.7 million in settlement funds have been allocated toward a total of \$17 million in projects. The fund balance as of March 2004, was \$3.1 million (the original settlement amount of \$3.66 M has increased in value to \$5 M).

1998 – Guadalupe UNOCAL Settlement

Approximately \$15.6 million from the UNOCAL settlement associated with pollution at the Guadalupe Oil Field was deposited into a settlement trust held by the National Fish and Wildlife Foundation (NFWF). NFWF charged an initial fee of \$313,079 to establish the account, and an annual fee of approximately \$37,000 to administer it. It serves in a fiduciary capacity only, and we are currently negotiating an increase of the annual administrative fee. The settlement required several criteria be considered in funding of projects, and subsequently, the Board adopted a list of seven criteria for the evaluation of mitigation project proposals. These criteria include: geographic nexus; water quality; hydrocarbon pollution; region-wide project application; degree of fund leveraging; and institutional stability of the project proponent. Staff has been very involved in managing this fund. No funds were set aside initially for staffing, but for the past two years we have used settlement funds to off-set the large staff workload. Recent Board decisions to fund a watershed coordinator position will alleviate much of this problem, particularly for projects associated with the agriculture industry. Initially, projects were selected through a general Request for Proposals. Cumulatively, \$130 million in requests were received; of these, nine projects totaling

approximately \$8.5 million were funded. Last year, the Board approved the Guadalupe Fund Blueprint for expenditure of funds targeted toward nonpoint source-related discharges in the greater Guadalupe Oil Field/lower Santa Maria River area. The Blueprint utilizes a much more targeted approach to project scoping and solicitation in order to use the funds more effectively to achieve our water quality goals.

One of the nine initially funded projects established a \$2 million endowment for the Central Coast Ambient Monitoring Program (also maintained by NFWF). This fund has proved an invaluable tool for our monitoring program, to overcome some of the financial hurdles associated with state contracting delays and unpredictable budgets. Only interest is spent from this account; approximately \$75,000 per year is used to hire samplers and data management support, to cover laboratory analytical costs when state lab contracts are not available, and to purchase monitoring equipment. This income supplements state SWAMP funds of approximately \$300,000 per year.

1998 – Avila UNOCAL Settlement

\$1 million of the UNOCAL settlement associated with pollution in the Avila Beach area was deposited into a settlement trust held by the San Jose State University Foundation (SJSUF). SJSUF serves in a fiduciary capacity only; it charged an initial fee of \$20,000 and an annual fee of 2% of total remaining funds. Projects funded from this settlement were screened through the same seven criteria used for the Guadalupe settlement. These criteria include: geographic nexus; water quality; hydrocarbon pollution; region-wide project application; degree of fund leveraging; and institutional stability of the project proponent.

Staff has been very involved in managing this fund and the associated projects. No funds were set aside initially for staffing, and the contracts associated with this fund represent a significant workload for staff. Projects were selected through a general Request for Proposals. Because of the limited size of the Avila Fund, the Fund was fully encumbered in contracts. Forty project proposals were received in response to the RFP, totaling more than \$4 million in requests. Twelve projects totaling approximately \$1.0 million were

authorized for funding by the Board. Unlike the Guadalupe Fund, the Avila fund was fully encumbered with mitigation project contracts, so no funds were available for subsequent contract management.

2000 – Moss Landing Power Plant NPDES Permit

The Moss Landing Power Plant NPDES permit includes a requirement that Duke Energy provide \$7 million for mitigation of cooling water impacts in the Elkhorn Slough. Although this is not a "settlement" per se, the outcome is relevant to this discussion. The Elkhorn Slough Foundation manages these funds, and has successfully leveraged the original \$7 million into approximately \$21 million (in the bank). These funds are used to acquire lands adjacent to and upstream of the Elkhorn Slough and Moro Cojo Slough, and to do restoration work within the Sloughs and surrounding watershed. The Elkhorn Slough Foundation follows established criteria and goals set by the Regional Board and has proved to be an excellent program. Individual projects are implemented relatively quickly and efficiently, with minimal time demands on Regional Board staff. Thousands of acres have been purchased, and hundreds of acres of Slough habitat are being restored and protected.

2003 – PG&E Moss Landing Settlement

This \$5 million settlement was in response to backflushing of hot water into Moss Landing Harbor by PG&E, former owner of the Moss Landing Power Plant (Duke Energy settled for \$250,000 for violations over a much shorter period of time). The funds are held by the Community Foundation for Monterey County. The Foundation charges 1.5% or \$15,000 per year, whichever is greater, to manage the Fund. The Consent Judgment provided staffing oversight costs (\$250,000 to be used over the next five to seven years). \$950,000 was paid into a fund for CCAMP to conduct monitoring activities in the Monterey Bay area. The remainder of the settlement established \$2.85 million for project implementation and \$950,000 for associated nonpoint source monitoring activities. These funds target priority problems affecting Elkhorn Slough and tributary watersheds identified through the Bay Protection and Toxic Hotspot Cleanup Plan and the

Monterey Bay National Marine Sanctuary's Action Plan for Agriculture and Rural Lands. Project criteria require a minimum 25% match. A number of specific project criteria have been developed, including demonstration of the ability to reduce pollutants to target waterbodies. The Community Foundation has so far played an active role by helping to arrange for meetings and by participating in the Technical Advisory Committee. Foundation staff was recently selected to coordinate the upcoming Request for Proposals process and assist staff with administration of projects.

NonProfits and Waiver Monitoring

The Regional Board will be considering the Agricultural Conditioned Waiver issue at the July meeting. Monitoring is a condition of such waivers. However, individual monitoring by growers is relatively expensive. As an alternative, a cooperative program has been proposed which allows growers to contribute funds to a centralized monitoring organization to conduct monitoring on a waterbody scale, rather than on a farm field scale. Regional Board staff is looking into using some of the above PG&E and Unocal Guadalupe funds, in combination with grants from Proposition funds available through the State Board, to help establish this monitoring entity (e.g., through a non-profit organization). The entity would work with the agricultural community and Regional Board staff to develop a monitoring dues schedule, collect and hold such dues, administer the monitoring program, and initiate limited monitoring prior to full implementation of the agricultural waiver monitoring program. Such an organization also could work on behalf of the agricultural community to seek future grant funds to help reduce program costs, negotiate bulk rates for laboratory costs, and facilitate needed research to address any new questions which might arise as a result of monitoring. The organization can also collect existing high quality monitoring data from other monitoring programs and submit it in lieu of new monitoring to reduce overall program costs.

We have also considered establishment of a similar program for monitoring the cumulative

and individual impacts of timber operations. Timber harvests don't lend themselves to the same model as has been established for agricultural waiver monitoring, in that harvests are located in multiple small watersheds, individual operations may be very small, and the total number of operations is small compared to the agricultural industry. However, there are other watershed-scaled monitoring efforts that may be able to tie in to efforts to assess impacts of timber activities. An example of this is the Integrated Watershed Restoration Program (IWRP) being implemented by the Coastal Conservancy in several watersheds in the Santa Cruz area. We will discuss the various options at our timber/sediment workshop, including the idea of a fee (e.g. by board foot harvested) for a cooperative monitoring program for sediment in the timber areas of Santa Cruz County. Such a program could also employ the services of a non-profit as discussed already, or an association representing timber harvesters, in order to carry out the monitoring program, in collaboration with other monitoring activities in the area.

Lessons Learned

Some of the key lessons that we have learned from the last seven years of managing settlement funds and the associated mitigation contracts include:

- It is important to incorporate a component of time/money for staff costs associated with the development, implementation, and management of mitigation contracts, within the original settlement. We have learned that the staffing costs associated with fund management can be significant, and upfront accommodation of these costs is desirable.
- Some funds have resulted in far less staff work than others; those held and managed by local nonprofits directly involved in restoration programs have generally been well-spent, well-leveraged, and have resulted in relatively low staff burden. In lieu of this, staff burden can be reduced by hiring of coordinator positions, as that is being done now for the Guadalupe and Moss Landing funds. This coordinator position

can be built in with the settlement (2003 Moss Landing) or developed as a "project" by staff after the settlement (Guadalupe).

- Foundation costs and level of involvement are highly variable. Annual costs can range from 1% or less to 3% or higher; others may charge a one-time flat fee of 10% or more. Fees do not necessarily correlate closely to level of involvement or quality of service provided.
- Centralization of funds to one or a few locations (e.g., community foundations) allows for: 1) Decreased staff effort directed toward dealing with multiple fund management groups; and 2) Better leveraging position to negotiate lower fund management costs.
- Utilization of project scoping approach (as used with Guadalupe and Moss Landing) is a more efficient model for targeting priority water quality problems than the open Request For Proposal approach used previously.
- Nonprofits can be used effectively for implementing innovative approaches to monitoring and other water quality activities. Multiple contributions to a single entity from settlements or dischargers (in fulfillment of monitoring obligations) can provide more efficient, effective use of those resources. Nonprofit organizations can let contracts efficiently, can hire support staff, can seek outside funding, and can otherwise provide support that is difficult to obtain within the State system. Staff intend to further the development of nonprofit relationships as we seek practical solutions to our water quality problems.

Regional Board Conservation Program

This item also discusses a new idea: establishment of a Conservation Program. The Conservation Program would establish a list of pre-approved supplemental environmental projects (SEPs) that dischargers could fund in lieu of paying

administrative civil liabilities. Dischargers that settle disputes could also agree that settlement funds will fund these SEPs. This will provide the greatest possible benefit to water quality over the long term via permanent preservation of beneficial uses of water throughout the Central Coast Region. This goal would be accomplished by allowing the use of some future settlement funds, and some future funds from administrative civil liabilities (including mandatory minimum penalties), to fund specific Conservation Program projects. An outline of the proposed objectives follows:

1. Establish conservation buffer zones around priority water bodies (rivers, streams, estuaries, wetlands) via conservation easements, purchase, agreements, or other mechanisms. Buffer zones would be defined such that human activity is limited for the purpose of protecting water quality. This specific objective would include performance criteria, such as the establishment of defined buffer zones along fifty percent of the Region's priority water bodies within twenty years.
2. Provide funding for projects that directly support conservation buffer zones, such as larger watershed scale conservation projects, permanent implementation of best management practices (such as out-of-stream water supplies for ranching operations), habitat restoration, and performance monitoring (limited, streamlined efforts, such as presence/absence surveys), etc.

These funds would not be used for general staff work, general studies, planning, or similar administrative work, or to fund any programs of the Regional Board (such as CCAMP). The purpose is to direct these funds toward permanent, on the ground preservation of habitat and beneficial uses, which in turn maximizes water quality in those protected areas.

There is a multitude of worthy projects that could be considered for funding. The conservation program proposal is designed to provide a preferred option for dischargers to direct settlement funds (from enforcement or mitigation cases). One of the most important influences on a

stream, lake, or near shore coastal water is the use of the adjacent land. A network of permanent conservation zones in these areas will provide an important buffer between the waterway and various land uses that are the source of pollutants. The buffers themselves may also serve as improved riparian habitat, with all the associated water quality habitat benefits (shading, insects for fish food, cover for fish, bank stabilization, added flood plains, wildlife support, etc.). In recent years staff and the Board have focused on non point sources from land uses such as agriculture (including grazing), timber harvests, and grading. Conservation buffer zones could provide a major benefit to water quality in water bodies affected by these land activities.

Program Efficiency

Projects would be carried out by established non-profit conservation organizations in the Central Coast Region, and leveraging Conservation Program funds to the greatest extent possible. The Enforcement Policy encourages matching funds and leveraged projects. Coordinating efforts with successful conservation organizations minimizes the need for additional staff resources.

The funds for this Conservation Program could be held and managed by a single, professional, non-partisan, non-profit financial management organization, such as a Community Foundation. This approach would minimize the number of accounts and complexity of oversight. In the alternative, funds could go to a few such organizations. We could use one in the north and one in the south, for example. Using one organization would minimize staff time, but using organizations geographically closer to the "violation area" and funded project area might be perceived as beneficial.

Funds Derived from Enforcement Actions and Settlement Cases

In response to certain types of violations, the Regional Board occasionally assesses Administrative Civil Liabilities, including mandatory minimum penalties, in enforcement cases. The Regional Board can consider Supplemental Environmental Projects (SEPs) as a way for responsible parties to comply with enforcement actions. The State Board policy

regarding enforcement actions and the use of SEPs is described in the Water Quality Enforcement Policy - February 19, 2002. SEPs used to satisfy all or part of Administrative Civil Liability actions, or part of mandatory minimum penalty actions, must meet specific criteria described in the Enforcement policy. This proposal would establish a candidate SEP that dischargers or responsible parties could elect to fund to comply with the Regional Board's enforcement action (in whole or in part, depending on the type of enforcement action).

Administrative Civil Liability Orders that direct payment of monies to the Conservation Program would specify the particular project(s) and milestone(s) that the payment would fund. For example, an order could specify that a particular deposit will pay for 25% of a preliminary site assessment to determine the feasibility of acquiring a particular conservation easement. Orders directing funds to the Conservation Program would have to meet all other requirements for SEPs (Enforcement Policy, Section IX.B-E), including the nexus requirements and the requirement for the successful completion of SEP milestones. In the previous example, the Regional Board could reserve jurisdiction to amend the order and redirect the funds to another project if the preliminary site assessment was not completed within a stated period of time.

The dedicated account would include specific criteria for implementing high priority projects. The criteria and the priority projects would be subject to review and approval by the Board prior to any deposits to fund a particular project or any expenditure of funds from the dedicated account. Once the criteria and priority projects are approved by the Board, the Executive Officer will approve expenditures from the dedicated account to implement the approved projects. The criteria will include a scope of work, milestones, and performance goals (and this language would be mirrored in the enforcement action order for specific cases). This approach would result in one set of criteria and priorities.

The benefit of this funding mechanism would be to assure efficiency and accuracy in allocating funds toward high priority, Regional Board approved projects. The Regional Board adopted criteria would be attached to the dedicated account so that

funds could only be used for the described purpose. With the dischargers' consent, ACL orders could direct funds to an already approved project, without the discharger having to go through the difficult, time consuming, and repetitious process of finding and developing projects on their own (sometimes through multiple Regional Board hearings). This approach eliminates the many repeated efforts by dischargers and would greatly reduce Regional Board time and staff time spent on each case.

The Regional Board also periodically negotiates settlement agreements with responsible parties. Funds from these settlements range from thousands to tens of millions of dollars. Future settlement agreements could allow settlement funds to be deposited in the candidate SEP to fund Conservation Program projects. Again, this minimizes Regional Board time and staff time, and assures that the funds are directed toward the highest priority Board approved projects. The same Regional Board approved criteria would apply to the use of these settlement funds.

If a project funded through the Conservation Program meets the requirements of any existing SEP fund that was established by a prior settlement agreement (e.g., the Guadalupe Oilfield or PG&E Elkhorn Slough settlements), the entity carrying out the project could also apply for additional funding from the SEPs.

Performance Monitoring

Performance monitoring would be done to assure that specific goals and objectives are achieved. Staff would also provide regular reports to the Regional Board, including financial status and progress toward meeting the specific goals and objectives of the Conservation Program and the progress of specific projects.

CONCLUSION

This item discusses the Regional Board's historic and current efforts to manage funds from several settlement and enforcement cases, and the lessons we have learned to make such management most effective. It also describes the use of nonprofits as a tool for developing more effective monitoring.

This item also discusses establishment of a Conservation Program for the purpose of providing the greatest possible protection for beneficial uses over the long term (in perpetuity). The most beneficial long-term goal is the establishment of conservation buffer zones around high priority water bodies. The mechanism for implementing the Conservation Program would be a dedicated account funded by enforcement actions and settlement cases.

The goals, objectives, and performance monitoring associated with the Conservation Program would be in compliance with the Enforcement Policy, so that responsible parties could deposit funds directly to the dedicated account as a compliance option provided that each ACL Order meets all applicable requirements of the Enforcement Policy and each settlement agreement meets all applicable nexus requirements. The Conservation Program would assure that limited available funds and staff resources are directed to the highest Regional Board priority projects in an efficient manner.

The dedicated account could be managed and held by a single non-profit, professional financial management organization, or a few similar organizations. Using only one such organization allows for a single quarterly financial statement and minimizes the confusion of having many separate funds that must be tracked.

RECOMMENDATION

Staff looks forward to discussing the Conservation Program concept with the Regional Board. The next step will be for staff to draft agreement with a non-profit entity that will establish the dedicated account. Staff will also draft a more detailed description of the goals, objectives, priorities, implementation plan, and specific projects for Board approval (an action item for a future meeting).

ATTACHMENTS

1. SEP Summary Table