



Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

FROM: Kerrie Romanow
Nanci Klein

SUBJECT: SEE BELOW

DATE:

Approved

Date

12/4/20

COUNCIL DISTRICT: 4

SUBJECT: COOPERATION WITH SOUTH SAN FRANCISCO BAY SHORELINE PROJECT, COST SHARE AGREEMENT WITH VALLEY WATER, DECLARATION OF SURPLUS, TRANSFER OF LEGACY LAGOONS 16-19, AND TRANSFER OF SHORELINE PROJECT EASEMENTS

RECOMMENDATION

- (1) Adopt a resolution authorizing the City Manager, or his designee, to:
 - a. Negotiate and execute a funding agreement with the Santa Clara Valley Water District (“Valley Water”), a Special District created by the Legislature of the State of California, for the Regional Wastewater Facility’s (“RWF”) payment of project betterment costs for the South San Francisco Bay Shoreline Project (“Shoreline Project”), in the amount of \$2,000,000, or half of total project betterment costs, whichever is less, subject to the appropriation of funds; and
 - b. Declare the Legacy Lagoons 16-19 property (portion of APN 015-31-051) as “exempt surplus land” to the needs of the City pursuant to Cal. Gov. Code §54221(f)(1)(D); and
 - c. Negotiate and execute an agreement for the transfer of the “exempt surplus land” of the Legacy Lagoons 16-19 property to Valley Water (portion of APN 015-31-051) in accordance with Cal Gov. §54221(f)(1)(D) and San Jose Municipal Code §4.20.080; and
 - d. Negotiate and execute an agreement for the transfer of project easements to Valley Water for Shoreline Project access, construction staging, and levee protection on RWF lands in exchange for compensation to be established by an appraisal completed by Carneghi, Nakasako, and Associates; and
 - e. Negotiate and execute all other necessary documents to effectuate the transfer of the Legacy Lagoon 16-19 property and related project easements.

OUTCOME

Acceptance of this recommendation will facilitate the development of the South San Francisco Bay Shoreline Project (“Shoreline Project”), including realigning the project to include the Legacy Lagoons 16-19 property. The San José-Santa Clara Regional Wastewater Facility (“RWF”) will cooperate with all aspects of the project, including:

- RWF to pay for half of Shoreline Project betterments, up to \$2,000,000, to construct certain facilities beneficial to the RWF, in a cost share arrangement with Santa Clara Valley Water District (“Valley Water”).
- RWF to transfer Legacy Lagoons 16-19 to Valley Water in exchange for up to 35 acres of mitigation credit to meet the 401 Certification issued by the California Regional Water Quality Control Board, San Francisco Bay Region pursuant to Order No. R2-2019-0026 dated August 28, 2019.
- RWF to grant certain project easements for access, staging, and levee protection, subject to final project design, at appraised value.
- RWF to cooperate with the Shoreline Project to provide immediate, short-term access to the Pond A18 property via a license agreement. Valley Water would take possession of Pond A18 either through negotiation of a sale at fair market value, or through a friendly condemnation proceeding. Staff will return to Council for resolution of the transfer of ownership for Pond A18.

The City of Santa Clara City Council, as a co-owner of the RWF facility, must also authorize the recommendations in this Memo and the Treatment Plant Advisory Committee (“TPAC”) will review the proposed recommendation on December 10, 2020. Staff will include a verbal report on TPAC discussion on December 15 in order for the RWF to proceed with the above steps.

EXECUTIVE SUMMARY

The City of San Jose and the RWF support and are ready to move forward with the Shoreline Project. There are significant benefits to the RWF in the U.S. Army Corps of Engineers’ (“USACE”) initiative to redesign the Shoreline Project to include Legacy Lagoons 16-19, including benefits for compliance with the Regional Water Board’s 2019 Legacy Lagoons “Clean Up” Order. The recommended actions in this memo are necessary to ensure the USACE continues with this redesign work and addresses outstanding project requirements.

Regardless of project design outcomes, the RWF must sell the Pond A18 property to Valley Water for the Shoreline Project to be constructed. City staff is asking for Council guidance before completion of negotiations to ensure staff is pursuing viable approaches to the negotiation for Pond A18. City staff hopes there is a successful conclusion on price for the sale of Pond A18. Staff also supports Valley Water’s use of a friendly condemnation proceeding, where by the property can be immediately transferred to Valley Water and the fair market value of the

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property would be determined later in order to ensure timely initiation of the Shoreline Levee project.

BACKGROUND

The City of San José is the administering agency for the RWF and co-owner of the RWF with the City of Santa Clara. As the administering agency for the RWF, the City is responsible for the acquisition and disposition of real and personal property which the City determines to be reasonably necessary for treatment plant purposes. Pond A18 consists of approximately 856 acres of land area contiguous to the RWF (included as Attachment A), and Legacy Lagoons 16-19, consisting of approximately 38.49 acres of land in the RWF area (included as Attachment B).

The South San Francisco Bay Shoreline Project is a congressionally authorized project sponsored by the USACE together with Valley Water and the California State Coastal Conservancy (“CSCC”) to manage flood risk and ecosystem restoration along the South San Francisco Bay. Within the South Bay region, the Alviso area was identified as the first phase, because of the high potential for flood damage, including possible damage to homes, businesses, and the RWF. Phase One of the South San Francisco Bay Shoreline Project proposes to build a new flood-protection levee along existing salt pond levee alignments, including the RWF’s Pond A18. An estimated \$177.2M in funding has been authorized by Congress for the construction of the Shoreline Project with a projected completion date of December 2025.

The RWF is a critical asset in Santa Clara County and property in the Shoreline Levee Study area and is an important partner in the success of the Shoreline Project. In order to proceed with the construction of the Shoreline Project, Valley Water, as the local partner with USACE, must acquire the fee property interest in Pond A18 as well as agree to certain easements necessary to the project. The intended use of Pond A18 in cooperation of this project shall be for wetlands and environmental mitigation. The USACE is currently redesigning the Shoreline Project with an updated alignment to include the Legacy Lagoons 16-19 property in addition to Pond A-18 to further expand the acreage for tidal habitat restoration. There are numerous benefits to the RWF from this realignment, described in more detail in the Analysis section later in this Memo. The Shoreline Project and related subjects (e.g., Legacy Lagoons Cleanup, trails) were presented at TPAC on numerous occasions, as key developments occurred, over the past five years.

In 2015 and 2017 respectively, the Treatment Plant Advisory Committee (“TPAC”) and the San José City Council directed that staff begin negotiations with Valley Water for the transfer of Pond A18 to facilitate the construction of the Shoreline Project consistent with the criteria set forth below:

1. Need for coordination and concurrence of the City of Santa Clara, as co-owner of the RWF.

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2. Confirmation that the value of the shoreline levee to the RWF is equivalent to fair market value of the proposed property.
3. Transfer of property to the Valley Water to be triggered upon award of the design contract by U.S. Army Corps of Engineers. However, if construction was unable to commence by January 1, 2021, Valley Water would need to pay the RWF the fair market value of Pond A18.
4. Inclusion of provisions that the levee crossing of Artesian Slough would not interfere with the RWF's current operation and preserve the RWF's current ability to discharge into the Bay as permitted under the National Pollutant Discharge Elimination System permit.
5. If construction of the levee required investment in capital or operational costs to RWF sooner than otherwise expected, the Shoreline Project would equitably share the burden of those costs.
6. Consideration of the RWF's capital expenditures for the repair of both gate structures on the pond that have occurred as a result of the delays on the Shoreline Project.
7. Finalization of the levee alignment and confirmation that any costs associated with a change in alignment will be borne by the Shoreline Project.
8. Resolution of the RWF's Waste Discharge Requirement for the management of water quality in Pond A18. This regulatory obligation should not be the RWF's after the property is transferred, but this is not an automatic action that happens concurrent to title transfer.

On November 22, 2019, the City received an offer from Valley Water for the purchase of Pond A18 and certain easements for \$13,778,000, based on Matt Watson of Carneghi-Nakasako & Associates' appraisal report dated September 21, 2018. Staff retained Ron Garland of Garland & Salmon and Terry S. Larson of Smith & Associates to conduct reviews of Mr. Watson's appraisal of Pond A18 and the related easements. Mr. Garland indicated Valley Water's appraisal for Pond A18 was very conservative, but per the scope of his review, did not produce an opinion of value. Mr. Larson agreed with Mr. Watson's appraised values of the easements. Valley Water offered \$53,000 for the easements. However, the easements necessary for the project are not fully defined yet and will need to be finalized before completing the transaction.

Per the direction of TPAC during the February 13, 2020 meeting, City of San José and City of Santa Clara staff collaborated to deliver a counteroffer to Valley Water on March 6, 2020 in the amount of \$22,477,000 for the fair value of Pond A18 and payments to reasonably offset the additional operational and capital cost to the RWF resulting from the Shoreline Project. This counteroffer did not include the value of project easements to be transferred as final easement requirements were not defined at the time.

Staff subsequently brought the Shoreline Project to City Council on April 14, 2020 and was authorized to continue negotiations for an agreement with Valley Water for the sale of Pond A18 and related easements to support the Shoreline Project consistent with the criteria directed by

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TPAC and Council as described above. Pond A18 was also declared as surplus to the needs of the City at this Council meeting, consistent with prior TPAC recommendation.

On April 21, 2020, Valley Water delivered a response to the City of San José and City of Santa Clara's counteroffer, increasing their original offer by \$108,000 to \$13,886,000 and recommended that the City of San José and City of Santa Clara commission their own appraisal to substantiate a fair market value for the pond.

Staff commissioned a restricted appraisal report from Valbridge Property Advisors ("Valbridge"). A restricted report limits the appraisal analysis presented in written form. Instead, this analysis was delivered to RWF and Valley Water staff via an oral presentation. This report style was agreed to by all parties because it expedited delivery of the appraisal. Valbridge valued Pond A18 at \$29,000,000. Valbridge noted that Valley Water's appraisal, which they based their offer on, did not account for the property's change in market conditions over time or the changing supply and demand characteristics for bay wetland properties suitable for habitat mitigation. Over time, the supply of potential bay wetland mitigation properties has declined significantly as lands are used for mitigation credits and this has caused the value of these lands to increase.

After discussions including Valley Water and Valbridge, Valley Water provided the RWF a "verbal" offer of \$16,300,000 for Pond A18 in November 2020. Setting aside any additional mitigating costs such as the related easements and other similar factors, Valley Water's offer is still approximately \$12,700,000 under the value Valbridge appraised Pond A18.

ANALYSIS

Valley Water's current offer of \$16,300,000 for Pond A18 is significantly below fair market value and staff does not recommend selling the property at that price. The recommended actions address significant areas of cooperation with the Shoreline Project and will allow the project work to proceed, including USACE redesigning the project to include Legacy Lagoons 16-19, pending resolution of project access and staging logistical requirements.

As RWF and Valley Water have not yet agreed to a sale price for Pond A18 itself, the Shoreline Levee partners could continue to negotiate and reach agreement on a sale price for Pond A18 or if a mutual agreement cannot be accomplished Valley Water could proceed to acquire ownership of Pond A18 through a formal "friendly" condemnation action filed in Superior Court. Acquiring Pond A18 through condemnation proceedings is Valley Water's backstop if the parties cannot come to an agreement on the price of Pond A18, and will provide the Shoreline Project immediate possession and access to Pond A18 enabling work on the project to proceed while the parties continue to negotiate and/or proceed with friendly condemnation. The Court would determine Fair Market Value. As previously noted, RWF staff will work with the Shoreline

Project to allow project access via a license agreement to Pond A18 as required in the short term and cooperate with Valley Water seeking possession of the Pond A18 property through condemnation proceedings.

Key Benefits of Realignment

The USACE has currently paused design work on the realignment design work for the Shoreline Project until the RWF and Valley Water come to terms of agreement on remaining real estate issues. USACE has indicated they will revert to original project designs that do not include Legacy Lagoons 16-19 if terms of cooperation are not reached soon. This would have significant negative impacts on the RWF as key project benefits are contingent on the realignment, through loss of a “1 to 1” mitigation ratio, and loss of a four-year delay to a clean-up order for Legacy Lagoons, described below.

A. '1 to 1' Mitigation Ratio for Legacy Lagoons Clean-up Wetland Mitigation

The Water Board issued a Clean Water Act Section 401 Water Quality Certification for the Legacy Lagoons Cleanup Project (“401 Certification”) on July 11, 2020 that requires mitigating 60 acres of impacted wetlands resulting from the entire Legacy Lagoons Cleanup Project which is being completed pursuant to an Order. The Water Board has granted to RWF, in writing, a beneficial 1-to-1 mitigation ratio for the project, which limits total mitigation credit obligations to 60 acres. However, this mitigation ratio is contingent on USACE redesigning the Shoreline Project to include Legacy Lagoons 16-19. The Water Board would likely require a 2-to-1 acreage ratio for this Order, so without the realignment, the RWF would likely be obligated to produce 120 acres of wetland mitigations. The RWF estimates its on-site capacity to mitigate wetlands at up to 118 acres.

B. Four-year Delay to the Legacy Lagoons Phase Two Clean-up Order

The Water Board issued an order obligating the RWF to complete the Phase 2 cleanup of the Legacy Lagoons by November 30, 2023. Per a letter dated September 1, 2020, the Water Board agreed to extend their Order No. R2-2019-0026, for an additional four years past the Order due date, until November 30, 2027. This delay is contingent on the USACE redesigning the Shoreline Project to include Legacy Lagoons 16-19. This delay would address any potential conflicts between the construction schedules of the Legacy Lagoon Phase 2 Cleanup and the Shoreline Project and defers the cost to ratepayers for the cleanup work.

Shoreline Project Mitigations to RWF Cost Impacts

All parties are working to finalize all other required components of the project including but not limited to: designation of areas for construction staging, terms of access for easement areas, liability for construction impacts to RWF regulatory compliance and plant infrastructure, payment of Shoreline Project betterment costs, sequencing of construction for other projects taking place at the RWF over the Shoreline Project timeline, managing operation of newly

constructed flood control structures to preserve the flow of RWF effluent into the bay, and necessary security fencing for the plant. Written resolution and mitigation of these issues from the USACE and Water Board is a prerequisite for transfer of the project easements authorized in this action.

Overview of Recommended Actions

A. Shoreline Project Betterments Cost Sharing (Recommended Action 1.a)

Certain modifications to the Shoreline Project to accommodate the RWF are classified as “Betterments”, which the USACE will construct as part of the project, but requires the local sponsor of the project, Valley Water, to reimburse expenses for. The USACE has included two betterments based on RWF comments to the project designs. RWF agrees to reimburse Valley Water for project betterment payments to the USACE in an amount not to exceed \$2,000,000, or half of total Betterment costs. These costs will incur once the project begins, which is anticipated to begin in 2023-2024. The USACE has agreed to limit Betterment costs to those approved by the RWF, for an engineered ogee spill-way to allow effluent to overflow the shoreline levee when the shoreline gates are closed, and an engineered tie-in to allow the proposed RWF outfall channel effluent/flood walls to more easily connect into the shoreline levee when it is constructed in future years.

B. Transfer of Legacy Lagoons 16-19 Property to Valley Water (Recommended Actions 1.b and 1.c)

Transfer of the 38.45-acre Legacy Lagoons property is necessary for the Shoreline Project’s realignment and for the RWF to maintain the 1 to 1 mitigation. The RWF will transfer the property for the consideration of up to 35 acres of wetland mitigation credit according to the 401 Certification issued. The RWF commissioned an appraisal that determined the highest and best use of the property to be for use as mitigation credits. Accordingly, the value of the mitigation benefits received for the transfer of the property is determined to be fair market value consideration for the property. Declaration of the property as exempt surplus land is necessary to effectuate the transfer.

C. Transfer of Shoreline Project Easements (Recommended Actions 1.d and 1.e)

RWF agrees to grant final Shoreline Project easements to Valley Water related to access, construction staging, and levee protection. Easements will not be defined until the USACE’s final design is complete, but the RWF agrees to grant final easements provided they are consistent with Valley Water and USACE’s written commitment to mitigate impacts due to Shoreline Project access and activities. The RWF will grant the easements in exchange for compensation to be established by an appraisal completed Carneghi, Nakasako, and Associates (by Matt Watson, if available). Mr. Watson, through Carneghi, was engaged by Valley Water previously to appraise Shoreline Project easements, and the parties agree that Carneghi will establish the fair market value of any future easements to transfer.

Staff have determined that the recommended actions bring significant value to the RWF because of the above described benefits of the Shoreline Project's realignment and the Shoreline partner's actions to mitigate the cost impacts to the RWF. With resolution of the recommended actions, the partners have essentially completed all other necessary work for the success of the Shoreline Project, except for agreement on the price of Pond A18.

CONCLUSION

The RWF is a key structure and property in the Shoreline Levee Study area and is an important partner in the success of the project. To enable the local partners to proceed with the construction of the Shoreline Project, the RWF must cost-share USACE project betterments, and must transfer property interests in Legacy Lagoons 16-19 and related project easements.

The cost of mitigating wetland impacts is a significant incentive to work with the USACE to commit to the project realignment and include Legacy Lagoons 16-19 in the Shoreline Project. USACE has indicated that if the recommended actions aren't approved, they will stop work on the redesign and revert to the prior plans. If this were the case, per the contingencies in the Water Board's commitments, the RWF would lose up to 35 acres of wetland mitigation credit from Legacy Lagoons 16-19 and the promise of a 1 to 1 mitigation ratio for Legacy Lagoon clean-up. Loss of the 1 to 1 mitigation ratio could potentially cause significant additional expense to the RWF.

The Shoreline Project will benefit the RWF, surrounding cities, and residents of the South Bay. The parties agree on all aspects of the Project, except for the fair market value of Pond A18 itself. Staff recommend that the City proceed with the transfer of Legacy Lagoons 16-19 and related easements to Valley Water, entering into a cost-share arrangement with Valley Water for payment of Shoreline Project betterments, and to continue to negotiate for a fair market price on Pond A18 or, in the alternative if negotiations are unfruitful, allowing working with Valley Water on a condemnation proceeding that will allow for immediate possession use of Pond A18 while allowing the courts to determine the proper value of Pond A18.

EVALUATION AND FOLLOW-UP

Upon City Council's approval of the recommendations, staff will enter into documents necessary to effectuate the transfers of Legacy Lagoons 16-19 and related project easements and a cost share agreement with Valley Water. Should Valley Water provide staff with a new offer for purchase of Pond A18, staff will return to Council with either a recommendation to accept the offer, or to decline and pursue just compensation in the condemnation process. In addition, once the project begins, staff will bring forward necessary budget actions to appropriate up to \$2

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million for the betterment costs either as part of a future City Council memorandum or budget process.

CLIMATE SMART SAN JOSÉ

The recommendation in this memo aligns with one or more Climate Smart San José energy, water, or mobility goals.

PUBLIC OUTREACH

This memorandum will be posted on the City's Council Agenda website for the December 15, 2020 Council Meeting.

COORDINATION

This memorandum was prepared in coordination with the City Attorney's Office and the City Manager's Budget Office.

COMMISSION RECOMMENDATION/INPUT

This memorandum is scheduled to be heard at the TPAC meeting on December 10, 2020. Staff will deliver an oral summary of TPAC's recommendation during the December 15 City Council meeting.

FISCAL/POLICY ALIGNMENT

This project is consistent with the City Council-approved strategy to support management of flood risk and enhance ecosystem restoration in South San Francisco Bay by supporting the development of the Shoreline Levee project. This project is also consistent with the budget strategy principle of focusing on protecting our vital core services.

COST SUMMARY/IMPLICATIONS

1. AMOUNT OF RECOMMENDATION/COST OF PROJECT: Up to \$2,000,000

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2. COST ELEMENTS OF AGREEMENT/CONTRACT: Up to \$2,000,000
3. SOURCE OF FUNDING: Fund 512 – San José / Santa Clara Treatment Plant Capital Fund.
4. FISCAL IMPACT: Property betterment is estimated to cost up to \$2,000,000 and would be funded by the San Jose / Santa Clara Treatment Plant Capital Fund (Fund 512). It is anticipated that the project will begin in 2023-2024. Once the estimated costs are determined and the project begins, actions to appropriate funds for the betterment costs will be brought forward for City Council approval either through a future City Council memorandum or part of a future budget process. Revenue from the sale of property subsequent to this agreement will go into the San Jose / Santa Clara Treatment Plant Income Fund (Fund 514). The included recommendations also have long term fiscal impacts for the RWF by reducing potential operating and capital cost increases that these recommendations mitigate. Additional explanation of the project’s long-term fiscal impacts on the RWF related to various regulatory requirements and mitigated capital costs are included in the Analysis section of this memorandum.

CEQA

PP20-006, Determination of Consistency with the San José/Santa Clara Water Pollution Control Plant Master Plan Final EIR (Resolution No. 76858).

/s/

KERRIE ROMANOW
Director of Environmental Services

/s/

NANCI KLEIN
Director of Economic Development

For questions, please contact Napp Fukuda, Assistant Director, Environmental Services, at (408) 793-5353 or Kevin Ice, Senior Manager, Real Estate Services, at (408) 535-8184.

Attachments:

Attachment A - Pond A18

Attachment B - Legacy Lagoons 16 - 19

Attachment A
Pond A18



**Attachment B
Legacy Lagoons 16-19**

