



OFFICE OF
INSPECTOR GENERAL
U.S. DEPARTMENT OF THE INTERIOR

THE BUREAU OF RECLAMATION WAS NOT TRANSPARENT IN ITS FINANCIAL PARTICIPATION IN THE BAY DELTA CONSERVATION PLAN



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INSPECTOR GENERAL
U.S. DEPARTMENT OF THE INTERIOR

Memorandum

SEP 07 2017

To: Alan Mikkelsen
Acting Commissioner, Bureau of Reclamation

From: Mary L. Kendall 
Deputy Inspector General

Subject: Final Evaluation Report – The Bureau of Reclamation Was Not Transparent in Its Financial Participation in the Bay Delta Conservation Plan
Report No. 2016-WR-040

This memorandum transmits our final report detailing our evaluation of the Bureau of Reclamation's (USBR's) financial assistance agreements for the State of California's Bay Delta Conservation Plan (BDCP).

We found that USBR understated the full cost of its participation in the BDCP by \$50 million and subsidized the Federal Central Valley Project (CVP) water contractors' share of BDCP costs. Beginning in 2009, USBR allowed certain CVP water contractors to make large advance payments for CVP operation and maintenance (O&M) activities. These advance payments created a surplus of Water and Related Resources appropriations intended for CVP O&M activities that USBR used to fund its financial assistance agreements with the State for BDCP activities. USBR did not obtain an opinion from the Office of the Solicitor on the legal sufficiency of this practice until 2014, six years after it began.

We also found that USBR could not provide analysis or documented evidence to support its determination that \$50 million paid to the State would be nonreimbursable, and therefore not repaid to the U.S. Treasury. Finally, we found that USBR did not expend funds under its third financial assistance agreement with the State in accordance with the authority delegated to the Commissioner under the Fish and Wildlife Coordination Act because the funds were not used to plan, design, or construct projects to create or improve instream habitat.

We include four recommendations to address the weaknesses in USBR's policies and procedures that allowed these events to occur. USBR did not concur with our recommendations, but agreed that it would no longer provide funds to the State for future BDCP efforts unless appropriated funds are specifically requested for that purpose.

Based on USBR's June 14, 2017 response to our draft report, we consider Recommendations 1, 2, and 4 to be resolved and implemented. We consider Recommendation 3 unresolved and not implemented and are referring it to the Assistant Secretary for Policy, Management and Budget for resolution.

If you have any questions regarding this memorandum or the subject report, please contact me at 202-208-5745.

The legislation creating the Office of Inspector General requires that we report to Congress semiannually on all audit, inspection, and evaluation reports issued; actions taken to implement our recommendations; and recommendations that have not been implemented.

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Results in Brief

We evaluated the Bureau of Reclamation's (USBR's) financial assistance agreements for the State of California's Bay Delta Conservation Plan (BDCP) to determine whether USBR fully disclosed to the U.S. Congress and other stakeholders the cost of its participation in BDCP efforts, whether USBR had legal authority to convert funds from reimbursable to nonreimbursable purposes, and whether USBR expended funds in accordance with its legal authority for its financial assistance agreements.

We found that USBR did not fully disclose to Congress and other stakeholders the \$84.8 million cost of its participation in the BDCP efforts, including its subsidizing of the Federal Central Valley Project (CVP) water contractors' share of BDCP costs. According to State law and the memorandum of agreement between the parties involved with the BDCP, CVP water contractors and State water contractors were responsible for splitting the cost of the BDCP. USBR, however, contributed 64 percent of the CVP water contractors' share, or 33 percent of the total funding for the BDCP through June 30, 2016.

We also found that although USBR reported the funds it requested and received from Congress under the California Bay-Delta Restoration appropriation for the BDCP, it did not report \$50 million derived from an appropriation, available for other general purposes, that it also used for the BDCP. USBR obtained this \$50 million over a 7-year span by using a complex, obscure process that was not disclosed in the annual congressional budget justifications, Office of Management and Budget Calfed Bay-Delta certified annual financial reports, or numerous briefing documents on BDCP issues and status prepared by USBR for senior management officials.

In the process, USBR also decided that the \$50 million in appropriated funds was used for a nonreimbursable purpose, meaning the cost was absorbed by the Federal Government rather than being repaid by CVP water contractors. Had USBR used the appropriated funds for reimbursable CVP operation and maintenance, the purpose for which the funds were originally requested, the costs would have been repaid by CVP water contractors. We found that USBR was unable to provide documentation or analysis supporting its determination that these funds were nonreimbursable, and we question USBR's interpretation of this legal authority.

Finally, while USBR had the legal authority to enter into financial assistance agreements with California Department of Water Resources (DWR) to the extent funds were used to plan and design a project to improve fish and wildlife habitat, we found that USBR's use of funds under its third financial assistance agreement with DWR was inconsistent with the authority delegated to the Commissioner under the Fish and Wildlife Coordination Act because these funds were not used to plan, design, or construct projects to create or improve instream habitat.

We make four recommendations to address the weaknesses in USBR's policies and procedures that allowed USBR not to disclose to Congress and other stakeholders that \$50 million in Federal funds was being used for the BDCP and that these funds would not be returned to the U.S. Treasury as expected.

USBR did not concur with our recommendations, but we consider the basic objectives of Recommendations 1, 2, and 4 to have been achieved because (1) USBR will no longer provide funds to DWR for future BDCP efforts unless appropriated funds are specifically requested for that purpose, (2) USBR's nondisclosure to Congress and other stakeholders of the full cost of its participation in the BDCP has been disclosed through our report, and (3) USBR's submission of inaccurate annual Calfed Bay-Delta certified financial reports has now been disclosed through our report. Further, we believe USBR's commitment regarding appropriated funds for the BDCP is acknowledgement of the validity of our findings that the actions it took to fund BDCP planning costs and subsidize CVP water contractors were neither transparent nor consistent with the "beneficiaries pay" principle underlying Reclamation Law.

We consider Recommendations 1, 2, and 4 to be resolved and implemented. We consider Recommendation 3 to be unresolved and not implemented and are referring this recommendation to the Assistant Secretary for Policy, Management and Budget for resolution.

Introduction

Objective

The objective of our evaluation was to answer the following questions:

1. Did the Bureau of Reclamation (USBR) properly disclose to the U.S. Congress and other stakeholders¹ the cost of its participation in the Bay Delta Conservation Plan (BDCP) planning efforts?
2. Did USBR have legal authority to convert Water and Related Resources (W&RR) appropriations² from reimbursable to nonreimbursable purposes?
3. Did USBR expend funds in accordance with the legal authorities for its financial assistance agreements?
4. Did USBR have the legal authority for its financial assistance agreements with the California Department of Water Resources (DWR)?
5. Did USBR properly account for funding and ensure that participation in the BDCP did not adversely affect repayment of the Federal investment in the Central Valley Project (CVP)?
6. Did USBR have legal authority to redirect appropriations to the State for BDCP planning purposes?

Our findings relative to the first four questions are discussed in the “Findings” section of this report. For Question 5, we determined that USBR’s accounting for advance operation and maintenance (O&M) payments did not adversely affect the repayment of the CVP. Finally, for Question 6, we did not find sufficient evidence that USBR violated appropriations law in providing funding for its financial assistance agreements with DWR for the BDCP, including its use of the advance O&M payments. See Appendix 1 for the scope and methodology of this evaluation.

Background

The Sacramento-San Joaquin Delta is a significant ecosystem located east of the San Francisco Bay and just south of Sacramento, CA. It is a habitat for hundreds of aquatic and terrestrial species, some of which are unique to the region. The Delta is also an ecosystem in steep decline. It has been altered by a system of manmade levees, reservoirs, and dredged waterways constructed to support farming and urban development and to provide flood protection for local cities. In addition, the natural water flows in the Delta have been altered by the operation of the California State Water Project (SWP) and USBR’s CVP, which deliver water supplies for 25 million Californians and municipal, industrial, and agricultural uses in the San Francisco Bay Area, the Central and San Joaquin Valleys, and

¹ We consider stakeholders to include the Office of Management and Budget; Federal, State, and local agencies; water contractors; nongovernmental organizations; and the general public.

² W&RR appropriation funds are for the management, development, and restoration of authorized water and related activities, including the operation, maintenance, and rehabilitation of USBR projects.

Southern California. In this declining ecosystem, several fish species have dropped in numbers to the point where Federal regulators have stepped in to protect them by limiting Delta water deliveries to SWP and CVP water contractors.

Both the Federal and State governments have declared that current conditions in the Delta are unsustainable and that action is needed to protect critical habitat and secure reliable water supplies. The BDCP is a State-led, collaborative effort to address these needs. California authorized the BDCP in 2009 with passage of the Sacramento-San Joaquin Delta Reform Act of 2009 (Delta Reform Act). This law was subsequently codified in the State Water Code, and § 85089 specifies that the SWP and CVP water contractors, which are beneficiaries, are responsible for arranging for paying the cost of BDCP environmental reviews, planning, design, construction, and mitigation activities.

As originally conceived, the BDCP would identify and implement strategies to improve the overall ecological health of the Delta and to move fresh water through or around the Delta. Water supply reliability was to be enhanced by constructing new facilities to divert water for SWP and CVP water contractors north of the Delta, near Sacramento, and convey the water around or under the Delta to existing SWP and CVP pumping facilities 30 miles to the south. Ecosystem improvements were to be achieved by restoring and protecting up to 150,000 acres of habitat and by improving water flow conditions in the Delta. See Appendix 2 for a snapshot of the BDCP as of May 2014.

In March 2009, USBR's then-Director of the Mid-Pacific Region signed a memorandum of agreement (MOA) with DWR and other parties, including the SWP and CVP water contractors. The MOA established roles and responsibilities to facilitate the funding and planning for completing the BDCP and related environmental studies, the cost of which was estimated at \$140 million. Between March 2009 and July 2015, USBR awarded three financial assistance agreements to DWR for BDCP activities. In March 2009, USBR awarded a \$51.8 million financial assistance agreement to DWR to fund the completion of general planning studies, preliminary engineering, and environmental compliance documentation required for the BDCP. USBR subsequently awarded two additional financial assistance agreements to DWR—one in December 2009 for \$4 million and one in July 2015 for \$17.9 million—to fund the continued development and recirculation of draft environmental compliance documentation for the BDCP.

In December 2014, after a draft environmental impact statement/environmental impact report (EIS/EIR) was completed and public comments were received and addressed, the Governor of California announced a significant change in direction of the BDCP. The re-envisioned BDCP planning efforts were directed to a newly proposed preferred alternative, which the State refers to as California WaterFix. This alternative focused on the construction of new water conveyance facilities,

the cost of which is currently estimated at \$15 billion, to be repaid by SWP and CVP water contractors participating in WaterFix. WaterFix, however, eliminates the restoration and protection of up to 150,000 acres of habitat as an integrated component of the BDCP. WaterFix proposes only to restore approximately 15,600 acres of habitat to mitigate the impacts of constructing the new intakes and Delta tunnels. See Appendix 3 for a snapshot of the BDCP preferred alternative, WaterFix, as of June 2016.

As of June 30, 2016, total funding provided for the BDCP was approximately \$257.3 million,³ of which USBR contributed \$84.8 million. USBR provided funding through its in-kind services⁴ (\$15.4 million) and through financial assistance agreements (\$69.4 million). Funds for these financial assistance agreements came from—

- W&RR appropriations (\$50 million);
- California Bay-Delta Restoration appropriations (\$15.4 million); and
- the American Reinvestment and Recovery Act (\$4 million).

³ DWR reported to us that total funding contributed was approximately \$253.1 million, including \$80.6 million contributed by USBR. We found that USBR provided an additional \$4.2 million, and therefore adjusted DWR's number to \$257.3 million.

⁴ In-kind services are costs incurred by USBR to accomplish BDCP activities, such as salaries, contracts, and legal services.

Findings

USBR did not fully disclose to Congress and other stakeholders that it contributed \$84.8 million to the BDCP or that it subsidized 64 percent of the CVP water contractors' share of the cost. In addition, USBR Mid-Pacific Region officials determined that \$50 million in payments to DWR under three financial assistance agreements for BDCP activities was nonreimbursable, meaning the cost would not be repaid to the Federal Government by CVP water contractors. Finally, USBR did not expend funds under the third financial assistance agreement in accordance with the authority delegated to the Commissioner under the Fish and Wildlife Coordination Act (Coordination Act).

USBR Disclosure of BDCP Costs Not Transparent

USBR Did Not Disclose That It Subsidized CVP Water Contractors' BDCP Costs

Under State law and the MOA between parties involved with the BDCP, CVP water contractors were responsible for paying 50 percent of BDCP costs. The MOA also contained language that allowed USBR to subsidize the CVP water contractors' share. USBR used the language in the MOA to contribute 33 percent of all funding for BDCP planning efforts (64 percent of the CVP water contractors' responsibility); CVP water contractors contributed only 18 percent, while SWP water contractors contributed 47 percent (see Figure 1). We found no evidence that USBR's subsidy was ever disclosed in annual budget justifications or financial reports, and USBR officials could not give a valid rationale for providing the subsidy.

BDCP Funding Sources (In Millions)

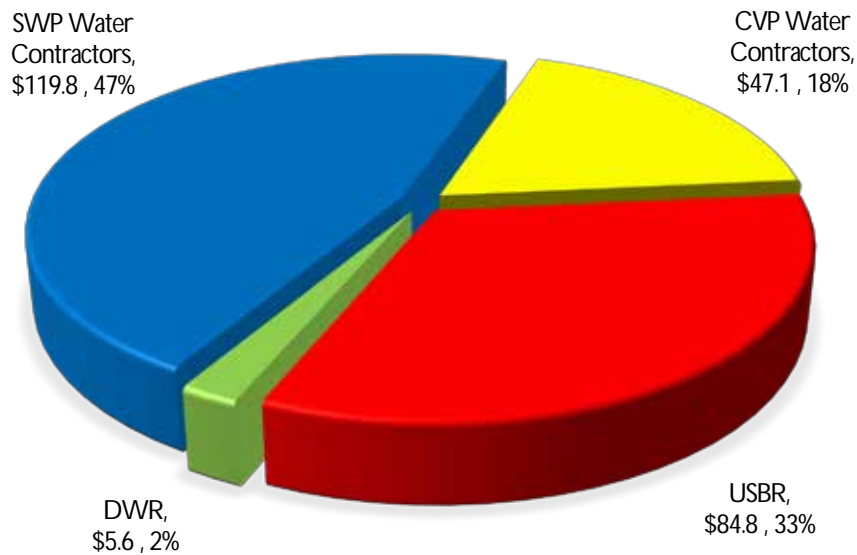


Figure 1. BDCP participant contributions through June 2016.

The Delta Reform Act, a California statute, mandates that SWP and CVP water contractors are responsible for all costs of the BDCP, including environmental review, planning, design, construction, and mitigation activities. The law specifically states:

Construction of a new Delta conveyance facility shall not be initiated until the persons or entities that contract to receive water from the State Water Project and the Federal Central Valley Project or a joint powers authority representing those entities have made arrangements or entered into contracts to pay for . . . costs of the environmental review, planning, design, construction, and mitigation . . . required for the construction, operation, and maintenance of any new Delta water conveyance facility.

The Delta Reform Act recognizes the long-standing principle underlying Reclamation law⁵ that the beneficiaries of an improvement or project pay for that improvement or project. In December 2011, the State of California's Governor Brown and then-Secretary of the Interior Salazar reinforced the applicability of this principle to the BDCP in a joint press release that states: "It is important to note that the Delta Reform Act of 2009 requires the beneficiaries of the project to pay for the planning process."

⁵ Reclamation law is a term used to refer to the total body of public laws governing the reclamation program, beginning with the Reclamation Act of 1902, and including all laws amending and supplementing the Act.

Acknowledging both the Delta Reform Act requirement and the “beneficiaries pay” principle, Section III of the MOA signed by USBR’s former Mid-Pacific Regional Director stated: “Participating SWP contractors and CVP contractors have agreed among themselves that the costs of the [BDCP] Planning Phase should be shared initially on an equal 50-50 basis.” The MOA goes on, however, to state that any in-kind services contributed by USBR, and any funds USBR provides to DWR via a financial assistance agreement, would be credited toward the participating CVP water contractors’ 50 percent contribution. It was this language in the MOA that allowed USBR to subsidize CVP water contractors’ BDCP payment obligation and, in the process, contradict the long-standing “beneficiaries pay” principle. USBR could not provide us with a rationale for its decision to subsidize CVP water contractors, other than the water contractors asked USBR to pay.

USBR Did Not Disclose the Full Cost of Its Participation in the BDCP

USBR altered its standard funding process for CVP O&M activities to help fund its financial assistance agreements with DWR for BDCP activities. In doing so, USBR obscured the source of its funding and the total cost of its participation in the BDCP. Specifically, USBR supplemented its BDCP activities with \$50 million derived from funds appropriated for “water and related resources” and authorized for application to reimbursable CVP O&M activities and other purposes.

Beginning in 2009 and continuing through 2015, USBR executed agreements with up to five CVP water contractors to modify the terms of their existing water service contracts. CVP water service contracts require water contractors to pay up to 2 months of estimated O&M costs in advance to USBR. USBR’s agreements modified the contracts of willing CVP water contractors to allow them to make advance payment of up to 1 year of estimated O&M costs. Under the modified contracts, any advanced funds were deposited into a designated USBR liability account to be used for certain CVP O&M activities that would otherwise be paid for with W&RR appropriations requested from and provided by Congress for this and other purposes.

USBR continued to request W&RR appropriations for reimbursable O&M activities of the Delta and Miscellaneous Divisions of the CVP in its annual budget justifications. Advance O&M payments from CVP water contractors under the terms of the water service contracts that USBR had modified then created a surplus of W&RR appropriation funds that USBR was able to use to make payments to DWR under the financial assistance agreements for BDCP environmental studies. These payments were then credited toward the CVP water contractors’ share of the BDCP costs, per USBR’s MOA, and not reimbursed to the U.S. Treasury. USBR’s modified process is illustrated and compared to its standard CVP O&M funding process in Figure 2. The funding amounts in this chart are for illustrative purposes and do not represent actual amounts for any particular year.

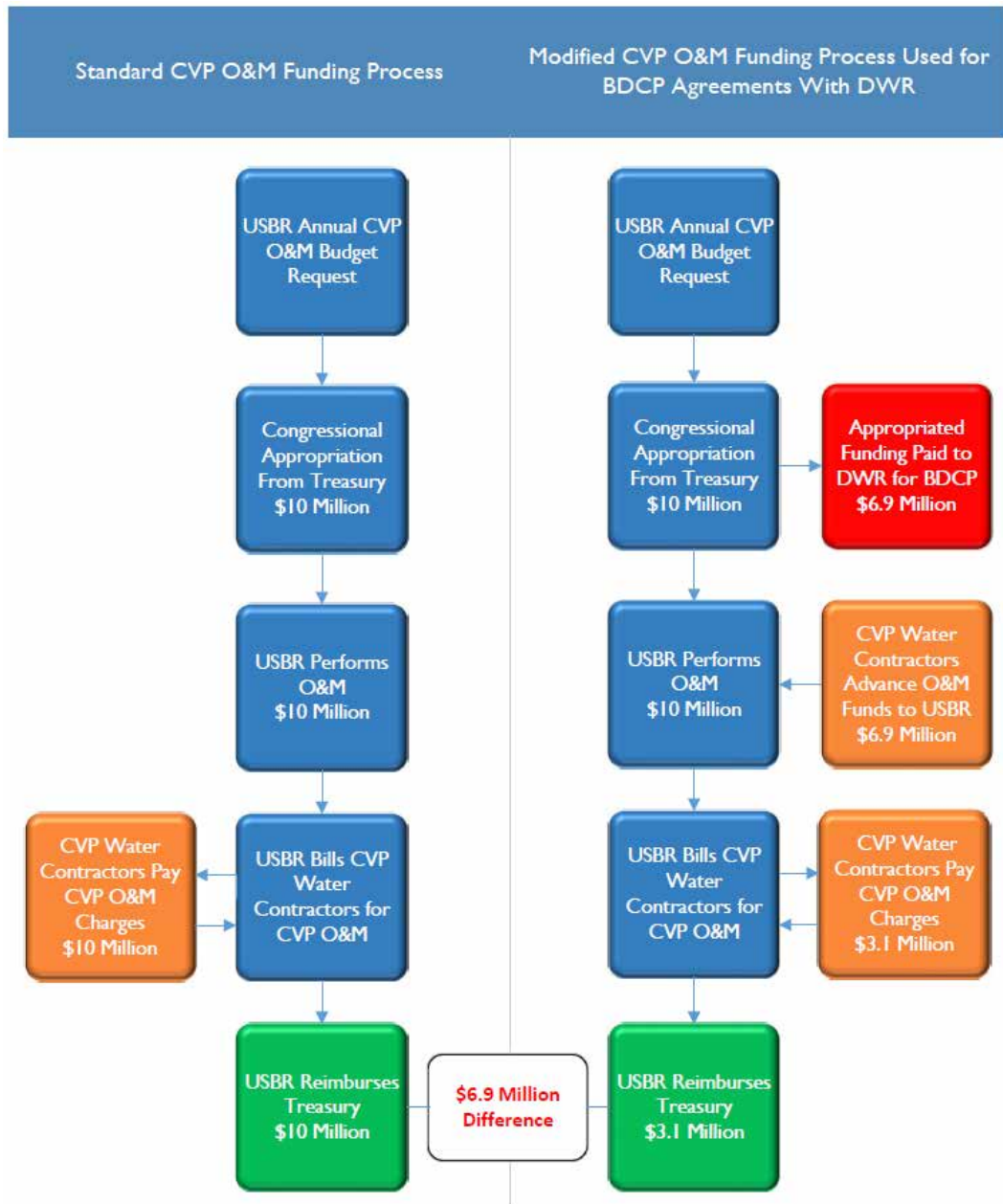


Figure 2. Comparison between USBR's normal use of appropriations to fund CVP O&M activities and USBR's use of the advance O&M process to obtain funding for the majority of its participation in the BDCP. The funding amounts in this chart are used to represent the process in fiscal years 2009 – 2015, but are not actual amounts for any particular year.

This modified CVP O&M process obscured the total amount USBR contributed to BDCP efforts. In its annual budget justifications for fiscal years 2009 through 2015, USBR requested funding specifically for its agreements with DWR for BDCP environmental studies through the California Bay-Delta Restoration appropriation. USBR supplemented the funding it requested with \$50 million in

W&RR appropriations Congress provided for purposes including CVP O&M activities and did not disclose that it was doing so.

We found evidence that Mid-Pacific Region officials were concerned about transparency and the risks of their long-term use of the advanced O&M funding process. USBR developed a discussion document (dated September 16, 2014) for Mid-Pacific Region officials that included the following concerns:

- None of the W&RR appropriation funding used for the BDCP was included in any of USBR's budget requests to Congress.
- USBR historically stated it could not obtain advance CVP O&M funding directly from water contractors (USBR referred to this as "taking CVP O&M off-budget"), but USBR had, in fact, done so for 5 years to fund its BDCP payments to DWR.
- Future inquiries and inferences about USBR's use of the advance O&M funding process might occur as a result of the growing difference between USBR's budget requests for BDCP and its BDCP expenditures.
- The advance O&M funding process was not transparent.

It was not until November 21, 2014, 6 years into USBR's use of this funding process and immediately prior to awarding the third financial assistance agreement to DWR, that the current Mid-Pacific Regional Director requested and received concurrence from the Commissioner to use this process. On November 24, 2014, the Office of the Solicitor determined that the Region's use of this funding process was legally sufficient, based on an understanding of the process obtained through meetings with Mid-Pacific Region officials.

We also found that USBR did not disclose to Congress through available mechanisms that the majority of its BDCP expenditures were funded from appropriations available for CVP O&M. In particular, we noted that the Calfed Bay-Delta Authorization Act⁶ requires the Director of the Office of Management and Budget to submit a financial report to congressional appropriation committees, certified by the Secretary of the Interior.

The Calfed financial report assists the President in considering the necessary and appropriate level of funding for each of the agencies in carrying out its responsibilities under the Calfed Bay-Delta Program. To do so, the Calfed financial report displays proposed budgets for all Federal agencies for the upcoming fiscal year and provides a detailed accounting of all funds used by all Federal agencies responsible for implementing the Calfed Bay-Delta Program during the previous fiscal year.

⁶ Pub. L. No. 108-361, "Title I – California Water Security and Environmental Enhancement, Sec. 106. Crosscut Budget." The California Bay-Delta Restoration appropriations used for the BDCP are authorized by the Calfed Bay-Delta Authorization Act.

When reporting its annual budget request and prior year expenditures, USBR did not include the \$50 million it obtained from the W&RR appropriation and used for the BDCP. USBR only reported the funding it requested and received from the California Bay-Delta Restoration appropriation for the BDCP.

USBR's Deputy Commissioner of Operations told us that budget guidance for the Calfed financial report was prospective in nature and did not allow for the reconciliation of the difference between USBR's budget request and expenditures for the BDCP. We did not attempt to evaluate the reported limitations, but nonetheless note that by not including USBR's expenditure of W&RR funds, the Calfed Bay-Delta certified annual financial reports submitted from fiscal years 2009 through 2017 understated USBR's BDCP costs by \$50 million. Moreover, USBR's total contribution of \$84.8 million for its participation in BDCP environmental studies and planning activities on behalf of CVP water contractors was not fully disclosed to Congress and other stakeholders.

Recommendations

We recommend that USBR:

1. Fully disclose to Congress and other stakeholders the cost of its participation in the BDCP efforts by identifying and reporting all appropriated funds requested and used for the BDCP in its future annual budget justifications and Calfed Bay-Delta certified annual financial reports; and
2. Report to the Office of Management and Budget and Congress that the Calfed Bay-Delta certified annual financial reports submitted from 2009 through 2017 understated USBR's BDCP costs by \$50 million.

Funds Granted to DWR Not Repaid to the Federal Government

Mid-Pacific Region officials created accounting codes that classified payments under USBR's financial assistance agreements with DWR for BDCP activities as nonreimbursable. This means that the \$50 million in appropriations Congress provided for expenses including CVP O&M that USBR diverted to DWR for BDCP activities was absorbed by the Federal Government. Had the financial assistance agreements been considered reimbursable, USBR would have billed CVP water contractors for the amounts paid to DWR, similar to USBR's process for recouping the cost of providing CVP O&M funding (see "Standard CVP O&M Funding Process," Figure 2).

The forms used to create the accounting codes for the financial assistance agreements with DWR indicated the costs were being incurred for "investigation

and study” activities to benefit fish and wildlife not specific to any project and cited Pub. L. No. 92-149, which provides that the cost of investigations and surveys related to potential USBR projects not authorized for construction is nonreimbursable. The forms made no reference to the section of the law being relied on, nor did they contain any details justifying the use of this legal authority. Mid-Pacific Region officials told us they considered the cost of the BDCP to be nonreimbursable because they were for investigation and survey of potential USBR projects or divisions or units of USBR projects not yet authorized for construction.

As previously discussed, the BDCP is a State-led, collaborative effort authorized by the State of California under the Delta Reform Act. We are not aware of any effort or plan by USBR to seek congressional authorization to construct features of the BDCP as a new project or unit of the CVP. In fact, USBR’s Director of Program and Budget told us that the BDCP may never be authorized for construction, and if authorized, it will be a State project not a Federal project.

We concluded that the BDCP environmental review and planning activities were being performed to address the impacts of operating the SWP and CVP, and were therefore related to the existing Federal project rather than a potential new project or unit. We, therefore, question the classification of these costs as nonreimbursable and believe that the \$50 million in appropriated funds used to make the payments to DWR should have been repaid by CVP water contractors rather than absorbed by the Federal Government.

Mid-Pacific Region officials provided us with their guidelines⁷ for making the determination that BDCP costs were nonreimbursable. The Region’s guidelines describe the basic principles and procedures for determining the reimbursability or nonreimbursability of program activities, including a decision process table with steps and descriptions. The guidelines also require that program managers identify the specific authority and document the basis for a determination of reimbursability or nonreimbursability. Regional officials told us that the regional ratesetting manager’s signature on the accounting codes forms was the evidence documenting that they adhered to the decision process shown in these guidelines. Mid-Pacific Region officials, however, were unable to provide any documentation or analysis supporting their determination that \$50 million in appropriated funds be absorbed by the Federal Government rather than repaid by CVP water contractors.

We consider USBR’s controls for making such a significant financial decision to be inadequate, because the decision was made at the regional level with the highest approval level being that of the Mid-Pacific Region budget officer. We believe that senior USBR officials—including, but not limited to, the Regional Director and the Director of Program and Budget—should review and concur

⁷ Regional guidelines, titled “Business Practices Guidelines for Determining Reimbursability of Program Activities,” dated February 2002.

with financial determinations of such significance. Concurrence should be based on a thorough vetting of supporting documentation and analysis prepared by regional officials.

Recommendation

We recommend that USBR:

3. Develop and implement policies and procedures to ensure regional determinations that funds will be spent for nonreimbursable purposes are (1) adequately documented by a clear, accurate, and thorough analysis of the legal basis for the determination, and (2) reviewed and approved by the Regional Director and the Director of Program and Budget.

Funds Not Expended in Accordance With Delegated Authority

We found that USBR had the legal authority to enter into financial assistance agreements with DWR to the extent funds were used to plan and design a project to improve fish and wildlife habitat. We also found that USBR used funds for these purposes in accordance with its delegated authority for the first and second financial assistance agreements with DWR. We found, however, that USBR's use of funds under its third financial assistance agreement with DWR was inconsistent with the authority delegated to the Commissioner under the Coordination Act because these funds were not used to plan, design, or construct projects to create or improve instream habitat.

The Coordination Act authorizes the Secretary to provide assistance for “the development, protection, rearing, and stocking of all species of wildlife, resources thereof, and their habitat.” The Coordination Act delegation of authority (255 DM 1) allows USBR to provide financial assistance to create or improve instream habitat of any Federal reclamation project. The Delta Reform Act identifies two coequal goals to be accomplished by the BDCP, namely—

- providing a more reliable water supply for California; and
- protecting, restoring, and enhancing the Delta ecosystem.

These statutory authorities provide the basis for efforts to complete the BDCP and the associated EIS/EIR.

USBR awarded the first and second financial assistance agreements to DWR in 2009 to fund the completion of environmental planning studies and environmental compliance documentation required for the BDCP. Funds provided by USBR under these agreements resulted in the draft BDCP and associated EIS/EIR

released in 2013. The draft BDCP proposal identified 22 specific conservation measures that included new water delivery facilities in the north Delta to secure water supply availability, as well as ecosystem measures to restore or protect up to 150,000 acres of habitat and address other stressors to fish and wildlife in the Delta. Based on the scope of the ecosystem measures, we concluded that the environmental planning work performed under USBR's first and second financial assistance agreements was reasonably associated with a project to improve fish and wildlife habitat.

In December 2014, the Governor of California announced a significant change in the direction of the BDCP, adding a new preferred alternative called California WaterFix. This preferred alternative eliminated the ecosystem measures to restore and protect 150,000 acres of habitat as an integrated component of the BDCP. Instead, California WaterFix's new intakes and tunnels would reportedly offer operational flexibility to the CVP and SWP by allowing the projects to take water in the north Delta, improving overall ecological conditions in the south Delta for endangered species by creating more natural water flow patterns and improving water quality conditions. As a result of the addition of California WaterFix as the new preferred alternative, the State was required to revise and recirculate drafts of the BDCP EIS/EIR.

The \$17.9 million financial assistance agreement USBR awarded to DWR in July 2015 was for preparation of the recirculated draft environmental documents and finalization of the EIS/EIR, with WaterFix as the new preferred alternative. USBR included a statement in the agreement that "funding the completion of the final EIS/EIR is necessary as each task and resource area determination is integral to a comprehensive understanding of the project, its benefits, and impacts." In other words, the agreement asserted that the entire EIS/EIR needed to be completed to see all of the potential benefits of the project.

USBR's assertion does not appear to be consistent with the Department's delegation order, which in pertinent part, only authorizes the Commissioner to provide financial assistance, regarding the construction and/or continued operation and maintenance of any Federal reclamation project, to plan, design, and construct projects to create or improve instream habitat. Given that the preferred alternative identified in the final BDCP EIS/EIR eliminated the key ecosystem measures to restore and protect habitat, we conclude that USBR did not expend funds under the third financial assistance agreement in accordance with this authority.

Recommendation

We recommend that USBR:

4. Prior to funding any additional Federal financial assistance for the BDCP, make a written determination that grants are for an authorized purpose and consistent with delegated authority.

Conclusion and Recommendations

Conclusion

The State of California and USBR have agreed that action is needed to protect critical Bay-Delta habitat and secure reliable water supplies for 25 million Californians. Responding to this need, the State authorized the BDCP and specified that all costs of planning, designing, constructing, and operating features associated with the BDCP would be borne by SWP and CVP water contractors as beneficiaries of a more secure water supply. We found that USBR went to great lengths to fund the State's BDCP efforts and to subsidize CVP water contractors and that USBR's actions were not transparent.

USBR did not fully disclose to Congress and other stakeholders that a total of \$84.8 million in Federal funds was used to help pay for the planning costs of the State of California's BDCP. USBR also did not disclose that it used these funds to subsidize 64 percent of the CVP water contractors' share of the State's planning costs and could not provide us with any explanation of why it did so. In addition, USBR financed its participation in the BDCP efforts by using a complex process that was not transparent to stakeholders. Further, USBR made a determination at the regional level, without sufficient analytical documentation, that \$50 million in Federal funds was nonreimbursable, resulting in these funds not being repaid to the Treasury. Finally, USBR did not expend funds under its third financial assistance agreement with DWR in accordance with the authority delegated to the Commissioner under the Coordination Act because the funds were not used to plan, design, or construct projects to create or improve instream habitat.

On July 21, 2017, DWR certified the final BDCP EIS/EIR and filed its Notice of Determination. USBR is expected to issue its own Record of Decision soon. California WaterFix remains the agencies' preferred alternative. Construction of facilities estimated to cost at least \$15 billion will therefore depend substantially upon reaching agreements with SWP and CVP water contractors to pay for these facilities, as current State law requires. We are concerned that the absence of transparency displayed by USBR during the planning phase of the BDCP will be perpetuated in the future. We therefore made four recommendations to address the weaknesses in USBR's policies and procedures that allowed USBR not to disclose to Congress and other stakeholders that \$50 million in Federal funds was being used for the BDCP and that these funds would not be returned to the Treasury as expected.

Recommendations and Summary of USBR's Response to Our Draft Report

On June 19, 2017, USBR provided a response to our draft report. The response was signed by the Acting Commissioner on June 14, 2017, and by the Acting Assistant Secretary for Water and Science on June 16, 2017. Based on this response, we consider Recommendations 1, 2, and 4 resolved and implemented and Recommendation 3 unresolved and not implemented. We will refer Recommendation 3 to the Assistant Secretary for Policy, Management and Budget for resolution. See Appendix 4 for the full text of USBR's response; Appendix 5 lists the status of each recommendation.

We recommend that USBR:

1. Fully disclose to Congress and other stakeholders the cost of its participation in the BDCP efforts by identifying and reporting all appropriated funds requested and used for the BDCP in its future annual budget justifications and Calfed Bay-Delta certified annual financial reports.

USBR Response: USBR did not concur with Recommendation 1 or our related findings about USBR's nondisclosures to Congress and other stakeholders regarding BDCP participation costs and subsidies. USBR stated that it disclosed its decision to subsidize CVP water contractors in an October 2013 response to a September 20, 2013 letter from seven congressional representatives. USBR further stated that the reason it did not concur was that it has determined that appropriated funds that USBR does not specifically request for purposes of the BDCP will not be provided to DWR for future BDCP efforts.

OIG Reply: We do not consider USBR's proposed action regarding the use of appropriated funds for the BDCP to be fully responsive to our recommendation because USBR did not agree to include all appropriated funds used to date in its annual Calfed Bay-Delta certified financial report. Even though USBR did not concur with our recommendation, we believe the recommendation's basic objective has been achieved because (1) USBR will no longer provide funds to DWR for future BDCP efforts unless USBR has specifically requested appropriated funds for that purpose, and (2) USBR's nondisclosures have now been disclosed through our report. Accordingly, we consider Recommendation 1 to be resolved and implemented.

We take issue with USBR's claim that the letter it sent to seven congressional representatives represents adequate disclosure of its use of W&RR appropriations and its agreement to subsidize CVP water contractors. First, the date of the letter USBR provided was February 26,

2014, not October 2013. Second, USBR's reference to this letter implies that it was the first time that USBR advised anyone in Congress that it had funded development of the BDCP from W&RR appropriations in addition to the specific appropriations it requested from the California Bay-Delta Restoration Fund. We consider this significant because this letter is dated almost 5 years after USBR signed the MOA that committed it to subsidizing CVP contractors and began using the modified CVP O&M process to obtain additional funds for this purpose. Third, and most significantly, the letter does not disclose, as USBR claims, its decision to subsidize CVP water contractors. In its letter, USBR reported that it had obligated approximately \$63.2 million through fiscal year 2013 for activities to support the BDCP and identified the amounts and sources of all of the funds it used, but USBR did not acknowledge that it used these appropriated funds to pay BDCP planning costs that were the responsibility of CVP water contractors.

We also noted that USBR's response to our draft report did not provide a valid reason for subsidizing CVP water contractors. USBR stated that it had agreed to the MOA language that committed it to subsidizing CVP contractors with the intent to further the goals of the BDCP and to complete the required planning studies and environmental documents. As we pointed out in our report, USBR's actions contradicted the mandate of the Delta Reform Act, the "beneficiaries pay" principle underlying Reclamation law, and the then-Secretary's position on the applicability of the "beneficiaries pay" principle, as stated in the December 2011 press release. In its response, USBR ignored these guiding laws and principles and did not explain its legal basis for ignoring them. USBR's stated intent to further the BDCP planning effort is not, in our opinion, a valid reason for using Federal appropriations to pay costs that were the responsibility of CVP water contractors.

2. Report to the Office of Management and Budget and Congress that the Calfed Bay-Delta certified annual financial reports submitted from 2009 through 2017 understated USBR's BDCP costs by \$50 million.

USBR Response: USBR did not concur with Recommendation 2, and its response to this recommendation did not directly address our concern that the annual Calfed Bay-Delta certified financial reports provided to Congress since 2009 are inaccurate. USBR did reference the responses it made to Recommendation 1 and Finding 1, stating that "the information in the budget crosscut reflects the best information available at the time of transmittals" and that "it was not known at the time of the budget justification whether or not the CVP water contractors would advance CVP O&M funds for the fiscal year; nor was it known whether reimbursable or nonreimbursable appropriated dollars would be earmarked for the program."

OIG Reply: We do not consider USBR's proposed action regarding the use of appropriated funds for the BDCP to be fully responsive to our recommendation because USBR did not agree to include in its annual Calfed Bay-Delta certified financial reports all of the appropriated funds used to date. Even though USBR did not concur with our recommendation, we believe the recommendation's basic objective has been achieved because (1) USBR stated elsewhere in its response that it will no longer provide funds to DWR for future BDCP efforts unless USBR specifically requests appropriated funds for that purpose, and (2) USBR's submission of inaccurate annual Calfed Bay-Delta certified financial reports has now been disclosed through our report. Accordingly, we consider Recommendation 2 to be resolved and implemented.

In its response to our draft report, USBR stated that it appropriately reported expenditures related to the BDCP through its annual financial statements and that it did not consider its decision to convert funds as an understatement for reporting purposes. USBR also mentioned again that its response to the September 20, 2013 letter from seven congressional representatives fully disclosed the total cost of its participation in the BDCP. As we stated in our reply for Recommendation 1, we take issue with USBR's reference to this letter because USBR responded to only seven Congressional representatives and sent the letter almost 5 years after it committed to subsidizing CVP water contractors. Most significantly, the letter did not disclose, as USBR claims, its decision to subsidize CVP water contractors. Instead, USBR reported the total amount it obligated as of fiscal year 2013 (\$63.2 million) for activities to support the BDCP and identified the amounts and sources of all of the funds it used.

Our report describes the unusual nature of the 2009 contractual arrangement USBR created to help fund its financial assistance agreements with DWR for BDCP activities. It also describes how USBR used this arrangement for 7 successive years to obtain \$50 million from W&RR appropriations without ever mentioning in its annual budget justifications or the Calfed Bay-Delta certified annual financial reports it submitted to Congress that it was using these funds for BDCP purposes. Finally, our report demonstrates how USBR's contractual arrangement was used to direct W&RR appropriations to DWR for BDCP purposes and reduce CVP O&M reimbursements to the U.S. Treasury in the process.

USBR did not dispute the accuracy of our portrayal of the financing process it created and used for the BDCP, nor did it provide evidence that Congress and the public were routinely advised of its use of annual W&RR appropriations for BDCP purposes.

3. Develop and implement policies and procedures to ensure regional determinations that funds will be spent for nonreimbursable purposes are (1) adequately documented by a clear, accurate, and thorough analysis of the legal basis for the determination, and (2) reviewed and approved by the Regional Director and the Director of Program and Budget.

USBR Response: USBR did not concur with Recommendation 3. USBR asserted that its decision to determine that CVP O&M appropriations were suitable and appropriate to nonreimbursable purposes for the BDCP was made in good faith and that funds granted to DWR via financial assistance agreements were properly vetted, reviewed, and awarded. USBR also stated that the cost authority forms it used to classify payments to DWR as nonreimbursable were prepared in accordance with the Mid-Pacific Region's guidelines for determining reimbursability and that the forms were reviewed and approved by all levels required per the guidelines. Finally, USBR stated that it sought approvals at many levels and that the Regional Director that signed the first MOA in March 2009 was aware of the financial implications of his actions.

OIG Reply: We consider Recommendation 3 unresolved and not implemented and will refer it to the Assistant Secretary for Policy, Management and Budget for resolution.

USBR did not provide documentation to substantiate that the Regional Director who signed the 2009 MOA was aware that \$50 million in W&RR appropriations provided for reimbursable CVP O&M expenses would be diverted to DWR for BDCP activities and classified as nonreimbursable costs. As discussed in our report, USBR did not provide evidence that regional officials documented their basis for a determination of nonreimbursability when cost authority forms were prepared and approved.

We consider USBR's controls for making such a significant financial decision to be inadequate because the decision was made at the regional level, with the highest approval level being that of the Mid-Pacific Region budget officer. We believe that senior USBR officials—including the Regional Director and the Director of Program and Budget—should review and concur with financial determinations of such significance, and that concurrence should be based on a thorough vetting of supporting documentation and analysis prepared by regional officials.

4. Prior to funding any additional Federal financial assistance for the BDCP, make a written determination that grants are for an authorized purpose and consistent with delegated authority.

USBR Response: USBR did not concur with Recommendation 4 or our finding that funds were not expended under the third financial assistance agreement in accordance with USBR’s delegated authority. USBR stated that funds were used to plan and design instream habitat improvements including fish passage screening facilities. USBR stated that it did not concur with our recommendation because it has determined that appropriated funds that are not specifically requested for purposes of the BDCP will not be provided to DWR for future BDCP efforts.

OIG Reply: We do not consider USBR’s proposed action regarding the use of appropriated funds for the BDCP to be fully responsive to our recommendation because USBR did not explain how its cited legal authority allowed USBR to fund the entire EIS process for the WaterFix project as a whole. Even though USBR did not concur with our recommendation, we believe the recommendation’s basic objective has been achieved because USBR stated in its response that it will no longer provide funds to DWR for future BDCP efforts unless appropriated funds are specifically requested for that purpose. Accordingly, we consider Recommendation 4 to be resolved and implemented.

In its response to our draft report, USBR argued that WaterFix will improve fish habitat and conditions because specific operational criteria will be implemented for flows that create a more favorable habitat, and an additional point of diversion will be added, which will lower the impact of diversions on fish species. USBR stated that new operational criteria associated with WaterFix will assist species by creating a “net ecosystem benefit.”

We noted that USBR’s claim of a “net ecosystem benefit” appears to be challenged by the Environmental Protection Agency’s January 18, 2017 comments on the final EIS (FEIS) for WaterFix. For example, the EPA stated the following:

The FEIS continues to predict that water quality for municipal, agricultural, and aquatic life beneficial uses will be degraded and exceed standards as the western Delta becomes more saline. Significantly, the FEIS’ conclusions regarding the impacts to aquatic life remain unchanged from those of the SDEIS [Supplemental Draft Environmental Impact Statement], predicting substantial declines in quantity and quality of aquatic habitat for 15 of 18 fishes evaluated under WaterFix preferred operations.

The point of our finding is that USBR’s grant of \$17.9 million under the third financial assistance agreement went to fund completion of the entire EIS process for the whole WaterFix project, not just to planning the

habitat-improvement-related portions of the project, such as fish screens. In its response to our draft report, USBR did not address how the delegation order and the *Fish and Wildlife Coordination Act* authorize funding the entire EIS process for the WaterFix project as a whole.

Appendix 1: Scope and Methodology

Scope

Our evaluation objective was to answer the following six questions focusing on the Bureau of Reclamation's (USBR's) legal authority for its financial assistance agreements with the California Department of Water Resources (DWR) and whether Federal appropriations were properly used and accounted for and disclosed to the U.S. Congress and other stakeholders:

- Did USBR properly disclose to Congress and other stakeholders the cost of its participation in the Bay Delta Conservation Plan (BDCP) planning efforts?
- Did USBR have legal authority to convert Water and Related Resources appropriations from reimbursable to nonreimbursable purposes?
- Did USBR expend funds in accordance with the legal authorities for its financial assistance agreements?
- Did USBR have the legal authority for its financial assistance agreements with DWR?
- Did USBR properly account for funding and ensure that participation in the BDCP did not adversely affect repayment of the Federal investment in the Central Valley Project?
- Did USBR have legal authority to redirect appropriations to the State for BDCP planning purposes?

To answer these questions, we researched the purpose and statutory authority for USBR's participation in the BDCP, evaluated the statutory authorities for USBR's use of three financial assistance agreements for the program, and reviewed the source and application of program funds. We conducted our evaluation from April 2016 to November 2016.

We conducted our evaluation in accordance with the Quality Standards for Inspection and Evaluation as put forth by the Council of the Inspectors General on Integrity and Efficiency. We believe that the work performed provides a reasonable basis for our conclusion and recommendations.

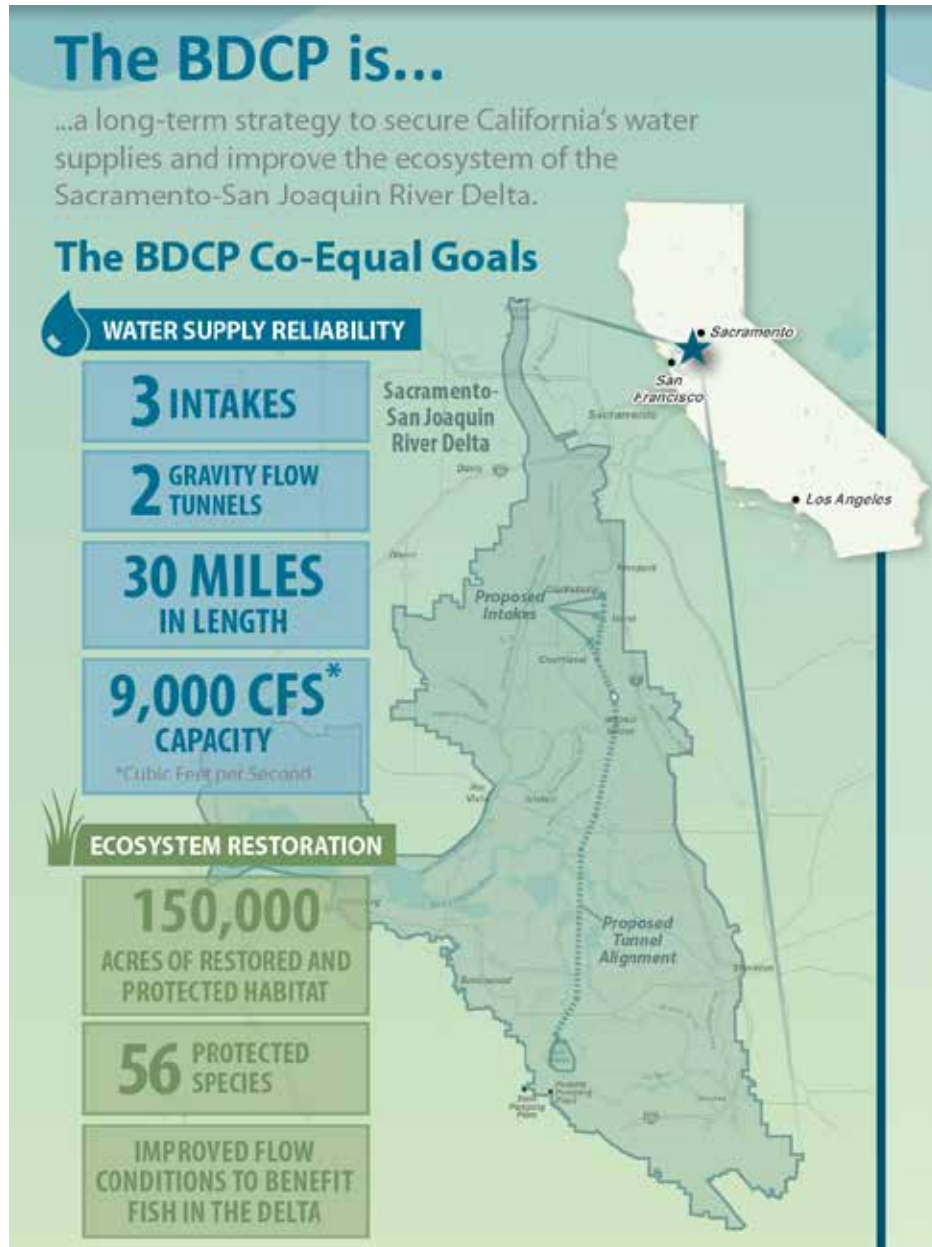
We reviewed internal control documentation and processes for providing financial assistance. We did not include a review of USBR's information system controls as the primary objective of our review was to determine whether USBR had legal authority to enter into a financial assistance agreement with DWR. We relied on computer data provided by USBR, but our scope did not include verifying the data.

Methodology

To accomplish our objectives, we—


- gathered background information on the BDCP through subject plans; budget documents; environmental planning documents; and prior reports, including those from the Office of Inspector General, U.S. Government Accountability Office, and California Legislative Analyst’s Office;
- identified and reviewed departmental and Bureau policies related to financial assistance;
- identified and reviewed laws related to the BDCP and the financial assistance agreements;
- obtained and reviewed financial assistance agreements, including modifications and related documents;
- coordinated with our Office of General Counsel regarding legal authorities for the financial assistance agreements and financial activities;
- obtained legal reviews prepared by the Pacific Southwest Regional Office of the Solicitor related to the BDCP and financial assistance agreements;
- interviewed officials representing USBR; the Washington, DC, and Pacific Southwest Regional Offices of the Solicitor; and DWR about the BDCP and financial assistance agreements;
- obtained and reviewed other agreements and contracts, including those for advance operation and maintenance (O&M) payments, related to the BDCP;
- identified and analyzed funding sources for the financial assistance agreements; and
- obtained and analyzed USBR’s water rate-setting schedules and accounting of O&M costs and payments for Westlands Water District to gain an understanding of the process and its effect on project repayment.

Appendix 2: Bay Delta Conservation Plan Fast Facts, as of May 2014



BDCP Co-Equal Goals of Water Supply Reliability and Ecosystem Restoration, 2014. Source: BDCP website, http://baydeltaconservationplan.com/Libraries/Dynamic_Document_Library/BDCP_Fast_Facts.sflb.ashx

Appendix 3: California WaterFix Fast Facts, as of June 2016




WATER DELIVERY UPGRADE

2 tunnels up to 150' below ground designed to protect California's water supplies from sea level rise, earthquakes, floods and levee failure.

3 new northern intakes, each with 3,000 cubic-feet per second (cfs) capacity, located farther upstream, closer to higher quality water, where impacts to fish habitats are lower.

Gravity-fed tunnels to move water naturally and more efficiently with reduced harm to fish.



IMPROVED RIVER FLOWS AND ECOSYSTEM HEALTH

Reinstate a more natural direction of river flows in the south Delta, minimizing harmful reverse flows caused by powerful pumps.

Continue to meet San Francisco Bay outflow requirements to protect against salt water intrusion and improve the overall health of the Delta ecosystem.

New location away from habitat of endangered species with advanced fish screens that protect even the smallest species.

As of June 2016, California WaterFix will include two tunnels and three intakes to deliver up to 9,000 cfs and restore more natural river flows. Source: California WaterFix website, http://cms.capitoltechsolutions.com/ClientData/CaliforniaWaterFix/uploads/CWF_FastFacts5.pdf

Appendix 4: Bureau Response

The Bureau of Reclamation's response to our draft report follows on page 28.

All response attachments have been reviewed, included in the assignment working papers, and will be shared with the Department.



United States Department of the Interior

BUREAU OF RECLAMATION

Washington, DC 20240

IN REPLY REFER TO:

84-27410

3.1.3

MEMORANDUM

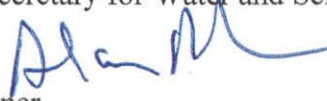
To: Office of Inspector General
Attn: Assistant Inspector General for Audits, Inspections, and Evaluations

Through: Scott Cameron
Acting Assistant Secretary for Water and Science



JUN 16 2017

From: Alan Mikkelsen
Acting Commissioner



JUN 14 2017

Subject: The Bureau of Reclamation's Response to the Office of Inspector General (OIG)
Draft Report, *The Bureau of Reclamation Was Not Transparent in its Financial Participation of the Bay Delta Conservation Plan*, Report No. 2016-WR-040

The OIG in its May 3, 2017, draft report, *The Bureau of Reclamation Was Not Transparent in Its Financial Participation in the Bay Delta Conservation Plan*, requested that Reclamation inform the OIG of the planned course of action to address and implement the recommendations in the subject report. The requested information is attached.

If you have any questions or require additional information, please contact Elizabeth Cordova-Harrison, Director, Mission Support Organization, at 303-445-2783.

Attachment

cc: Assistant Secretary – Water and Science
Attn: Kerry Rae

94-00010 (AShepet)

84-27000 (SDeMarco), 84-27400 (KConnolly), 84-27410 (PClemens, BAlbery),

84-27410 (AHartman, MDiem), 84-52100 (KKarlovits, SKelly),

MP-110 (DGray, SMay)

(w/att to each)

The Bureau of Reclamation's Response to the
Office of Inspector General (OIG) Draft Evaluation Report
The Bureau of Reclamation Was Not Transparent in its
Financial Participation in the Bay Delta Conservation Plan
Report No. 2016-WR-040

May 2017

General Comments: Reclamation responses to the OIG Notice of Potential Findings and Recommendations (NPFRs) are included herein. As importantly, Reclamation is providing background information to offer additional context regarding its participation in the Bay Delta Conservation Plan (BDCP).

In 2006, Reclamation, in coordination with the California Department of Water Resources (DWR) and several state and federal water contractors, started planning efforts to implement a comprehensive strategy for restoring ecological functions of the Delta and improving water supply reliability in the State of California. The initial approach focused on the development of a conservation plan, referred to as the BDCP, which would include modifications to the State Water Project (SWP) by adding intakes in the north Delta and would preserve and restore substantial amounts of land in the Delta for the protection of various endangered and threatened species, as well as other "special status species." Seven years later, the Draft BDCP and Draft Environmental Impact Report/Environmental Impact Statement (EIR/EIS) were released together for public review in December 2013. The Draft EIR/EIS analyzed and disclosed the potential environmental effects associated with the proposed BDCP and 14 other action alternatives.

Based largely on extensive public comments received on the Draft EIR/EIS and Draft BDCP Reclamation and DWR issued a Partially Recirculated Draft EIR/Supplemental Draft EIS in July 2015 that included three new alternatives. As part of this document, Reclamation and DWR introduced Alternative 4A—known as California WaterFix. Although Alternative 4A was announced as the new CEQA (California Environmental Quality Act) proposed action and the National Environmental Policy Act (NEPA) proposed action and preferred alternative (a federal designation that was not attached to any of the alternatives presented in the Draft EIR/EIS), all other alternatives are still under consideration by Reclamation until a Record of Decision is signed.

In summary, California WaterFix includes new water conveyance facility construction including three new intakes on the Sacramento River with state-of-the-art fish screens to prevent fish entrainment, two underground tunnels, new conveyance facility operation in coordination with operation of existing CVP/SWP Delta facilities, maintenance of the existing facilities and newly constructed facilities, implementation and maintenance of mitigation and conservation measures, and required monitoring and adaptive management activities including future water operations. Once in the tunnels, water would flow by gravity to the south Delta and on to an expanded Clifton Court Forebay and existing Central Valley Project (CVP) and SWP pumping plants. Implementation of this alternative would include operation of both new and existing water

conveyance facilities, thereby enabling joint management of north and south Delta diversions in better concert with fish migratory patterns. The habitat restoration elements of BDCP evolved into California EcoRestore to advance and restore at least 30,000 acres of critical habitat in the Sacramento – San Joaquin Delta. Reclamation continues to coordinate and is currently heavily involved with leadership roles with our partners in the Fremont Weir Adult Fish Passage Modification, Knights Landing Outfall Gate, and Yolo Bypass Salmonid Habitat Restoration and Fish Passage Project while coordinating extensively on other activities.

As importantly, Reclamation strongly recommends a point of clarification with respect to the following language as written in OIG’s report under Background Information (page 5); specifically, the OIG states:

“The reenvisioned BDCP planning efforts were directed to a newly proposed preferred alternative, which the State refers to as California WaterFix. This alternative focused on the construction of new water conveyance facilities, the cost of which is currently estimated at \$15 billion, to be repaid by SWP and CVP water contractors.”

The current position of the Bureau is only CVP water contractors participating in California WaterFix will be obligated to recovery of capital costs.

Recommendation 1: *Fully disclose to Congress and other stakeholders the cost of its participation in the BDCP efforts by identifying and reporting all appropriated funds requested and used for the BDCP in its future annual budget justifications and Calfed Bay-Delta certified annual financial reports.*

Reclamation’s Response: Non-concur. Per P.L. 108-361, the CALFED (now known as the California Bay-Delta Restoration) Federal Crosscut (also referred to as the CalFed Financial report) is included in the President’s Budget each year, in which funding is based on the President’s request. Budget justification documents are not designed for requests for (nor disclosures of) reimbursable versus non-reimbursable funds, rather they are justifications for requests for discretionary appropriations.

The information in the budget crosscut reflects the best information available at the time of transmittals. The budget justifications are done in the January/February time for the next fiscal year. The advance CVP O&M funding received by Reclamation (from specific CVP water contractors) was an annual action that occurred in September just before the beginning of the next fiscal year. Therefore, it was not known at the time of the budget justification whether or not CVP water contractors would advance CVP O&M funds for the fiscal year; nor was it known whether reimbursable or non-reimbursable appropriated dollars would be earmarked for the program.

The final funding for the DWR agreements was done in FY 2015 and Reclamation hasn’t provided any more funds to DWR. The final California WaterFix EIS/EIR has been published as of December 2016. The FY 2018 Budget has just been released and the California (CA) Bay-Delta Restoration for CA WaterFix (\$3 million) includes the following text “Reclamation’s efforts towards CA WaterFix are solely funded through

the Bay-Delta Appropriations.” This language is included to disclose that Reclamation will not be realigning appropriated dollars from other sources for CA WaterFix purposes.

Reclamation contends all actions it took with respect to the BDCP were done with good faith and were as transparent as possible during the process. However, Reclamation agrees in principle with the aforementioned recommendation and has strived to improve this process with respect to accurate budget activity plans (BAPs) and comprehensive annual reports. Nonetheless, the purpose of non-concurrence as stated above is specific to the fact that Reclamation has currently determined appropriated funds that are not specifically requested for this purpose will not be provided to DWR for future BDCP efforts.

Finding 1: USBR did not disclose that it subsidized CVP Water Contractor’s BDCP costs.

Reclamation’s Response: Non-concur. Reclamation disclosed its decision to subsidize CVP water contractors for BDCP costs. In October 2013, Reclamation responded to a letter dated September 20, 2013, from Representatives John Garamendi, George Miller, Doris Matsui, Mike Thompson, Jerry McNerney, Jared Huffman, and Ami Bera to Secretary of the Interior Sally Jewell seeking information regarding Federal funding for the Bay Delta Conservation Plan. Within the response, Reclamation fully disclosed that approximately \$30.6m was funded from Water and Related Resources (W&RR), \$28.6m was funded from the California-Bay Delta Restoration Fund and \$4m from the American Recovery and Reinvestment Act (ARRA) (Attachment 1). This topic was also part of questions submitted to Reclamation by the House Natural Resources Committee’s Subcommittee on Water and Power, and it was very clear from the wording of Reclamation’s response to a Question for the Record (QFR), finalized later in October of that same year, that this agreement was fully understood.

Reclamation entered into Financial Assistance Agreements (FAA) with DWR to ensure the completion of general planning studies, preliminary engineering, and environmental documents for the BDCP that are required by State and Federal laws allowing Reclamation to participate in implementing actions that conserve species and restore associated habitat in the delta.

Reclamation disclosed in the FAA and in a Memorandum of Agreement (MOA) its funding to DWR and the mutual agreement among all parties that in-kind services provided by Reclamation would be credited toward the participating CVP contractors’ 50 percent contribution. Additionally, Reclamation disclosed that any funds provided to DWR via a FAA with Reclamation would also be credited towards the CVP contractors’ portion of the BDCP Planning Phase costs. These agreements were entered into in good faith with the intent to further the goals of the BDCP in completing the required planning studies and environmental documents. The FAA and the MOA both included language stating that the information included within the agreements were subject to audit; thereby, notifying all participating parties that the information would be disclosed as required. Reclamation’s actions to credit CVP contractors for in-kind services and for funds provided to DWR via a FAA was not intended to be covert or obscure.

Finding 2: USBR did not disclose the full cost of its participation in the BDCP

Reclamation's Response: Non-concur. In the aforementioned letter dated October 2013, Reclamation responded to a letter dated September 20, 2013, from Representatives John Garamendi, George Miller, Doris Matsui, Mike Thompson, Jerry McNerney, Jared Huffman, and Ami Bera to Secretary of the Interior Sally Jewell seeking information regarding Federal funding for the Bay Delta Conservation Plan. Within the response, Reclamation fully disclosed total cost to date for Reclamation's participation in the Bay Delta Conservation planning efforts (Attachment 1).

Responsible Official: Mid-Pacific Region Director, David Murillo

Recommendation 2: *Report to the Office of Management and Budget and Congress that the Calfed Bay-Delta certified annual financial reports submitted from 2009 through 2017 understated USBR's BDCP costs by \$50 million.*

Reclamation's Response: Non-concur. Reclamation appropriately reported expenditures (costs) related to the BDCP through its annual financial statements. Specifically, as stated in Reclamation's response to Recommendation 1, Finding 1 and Finding 2, Reclamation disclosed its decision to convert funds from reimbursable to non-reimbursable. It is important to note that Reclamation does not consider its decision to convert funds as an understatement for reporting purposes. As previously mentioned, budget documents are not designed for requests (nor disclosures of) reimbursable versus non-reimbursable funds, rather they are justifications for requests for discretionary appropriations.

As importantly, the rationale for Reclamation's decision is covered in the applicable financial agreements (Attachment 2) and further expanded upon in responses herein. Reclamation is authorized to award such agreements as stated in the Fish and Wildlife Coordination Act. Moreover, as OIG indicates in their report (page 13) Reclamation had the authority to enter into financial agreements to the extent the funds were used to plan and design a project to improve fish and wildlife habitat. As indicated by OIG, they consider two (2) of three (3) financial agreements in question to meet this purpose. Reclamation has consistently identified such project purposes as non-reimbursable, hence its decision to convert as previously stated. Where OIG and Reclamation fundamentally differ is in regards to the OIG assessment on the remaining agreement. Reclamation strongly supports its assertion that all funds expended in these agreements were used to plan and design instream habitat improvements including fish passage screening facilities. Further detail to include rationale and support is expanded upon in Reclamation's response to Findings 3 and 4 below.

Responsible Official: Mid-Pacific Region Director, David Murillo

Finding 3: Funds Granted to DWR Not Repaid to the Federal Government

Reclamation's Response: Non Concur. As previously stated, Reclamation asserts that its decision to determine Central Valley Project Operation and maintenance appropriations were suitable and appropriate to non-reimbursable purposes for the Bay Delta Conservation Plan and was made in good faith. Funds granted to DWR via financial assistance agreements were properly vetted, reviewed, and awarded appropriately.

Recommendation 3: *Develop and implement policies and procedures to ensure regional determinations that funds will be spent for nonreimbursable purposes are (1) adequately documented by a clear, accurate, and thorough analysis of the legal basis for the determination, and (2) reviewed and approved by the Regional Director and the Director of Program and Budget.*

Reclamation's Response: Non-concur. Reclamation's Water and Related Resources appropriation is not classified by reimbursable and non-reimbursable, it is the activity or function that defines reimbursability.

In 2002, the Mid-Pacific Region developed Business Practices Guidelines (Guidelines) in determining the reimbursability of program activities. The Guidelines supplement but do not replace related Department and Reclamation policies or directives and standards (Attachment 3). In accordance with the Guidelines, Reclamation developed Budget Activity Plans (Activity Plan) for the Bay Delta Conservation Plan (Attachment 4). Activity Plans were completed annually by the Bay Delta Office Activity Manager, Program Manager and the Regional Budget Officer as part of the budget formulation process. It was preliminarily determined that the Bay Delta Conservation Plan activity would be classified as non-reimbursable. Corresponding cost authority forms were subsequently prepared, as outlined in the Guidelines, supporting the determination of non-reimbursable with reference to P.L. 92-149. These forms were reviewed and approved by all levels required per the Guidelines.

In addition to following Guidelines, in November 2014 Reclamation has a memo from the Solicitor (Attachment 5) explaining appropriation legal sufficiency and the Regional Director sent a memo to the Commissioner. The memos provide context supporting Reclamation's decision to convert Central Valley Project Operation and maintenance appropriations from reimbursable to non-reimbursable purposes for the Bay Delta Conservation Plan.

Reclamation had to seek approval at many levels. The Regional Director signed the first Memorandum of Agreement in March 2009 and was aware of the financial implications. There was a strenuous process to engage the stakeholders for BDCP and internal Reclamation processes to track funding. The final year of the agreement to provide funding to DWR was FY 2015.

Responsible Official: Mid-Pacific Region Director, David Murillo

Finding 4: Funds Not Expended in Accordance with Delegated Authority.

Reclamation's Response: OIG states Reclamation's third financial assistance agreement with DWR was

"inconsistent with authority delegated to the Commissioner under the Coordination Act because the funds were not used to plan, design, or construct projects to create or improve instream habitat."

Non-concur. Funds were used to plan and design instream habitat improvements including fish passage screening facilities.

The California WaterFix operational criteria will improve habitat and improve fish conditions in the south Delta through the implementation of specific operational criteria for flows that create more favorable habitat as well as adding an additional point of diversion that will lower the impact of diversions of fish species. Currently, all exports of Sacramento River water require pulling flows across the Central and South-Delta towards the pumping facilities in an unnatural flow pattern that changes the habitat. The California WaterFix adds a point of diversion on the Sacramento River. Current South-of-Delta facilities owned by Reclamation and DWR create entrainment issues for federally-listed species such as Delta Smelt and Chinook salmon. New operational criteria associated with WaterFix will assist species by limiting entrainment and creating a net ecosystem benefit.

The California WaterFix includes a state of the art positive screening facility on the new points of diversion. Current facilities use behavioral screen that does not exclude 100 percent of fish. Current facilities use salvage operations that require direct intervention and handling to truck fish back to a suitable migration path.

Although this preferred alternative is not an HCP (Habitat Conservation Plan), it does create ecosystem benefits. All alternatives evaluated benefit the South Delta habitat and ecosystem by taking stress off the existing water export facilities and reducing entrainment through modified and optimized operations associated with the new North Delta facilities coming online as a result of WaterFix implementation. As such, Reclamation had authority to enter into the Agreement with DWR.

Planning studies are critical in meeting the requirements of the program and need to be considered and are included in the delegated authority. The initial approach for BDCP called for a Habitat Conservation Plan (HCP). Planning processes exist, in part, to explore alternatives and would ideally provide insights that may improve an approach. It is not pragmatic to receive an answer that maximizes fish and wildlife benefit before performing the study. NEPA requires us to consider a range of alternatives. Excluding an alternative would leave us legally vulnerable. Specifically, to arguments that the government was pre-decisional. The finding as currently written would limit potential alternatives.

As importantly, WaterFix does, in fact, improve instream habitat. Although more habitat improvements would have occurred as a result of the HCP, invalidating use of the Fish and Wildlife Coordination Act based on a standard that anything less than the maximum amount proposed does not qualify would prohibit exploring alternatives that may meet other purpose of the action agency. The standard would preclude any study that may benefit fish and wildlife that finds such action infeasible or undesirable. Reclamation's only option would be to cease funding the development of all fish and wildlife projects due to the risk that a project may not be feasible after a thorough exploration, which may result in violation of the delegated authority for the Fish and Wildlife Act unless Reclamation built a project.

Alternative 4A Operation Criteria - Improved Flow Habitat

During the development of Alternative 4A, one of the more difficult challenges involved identifying proposed operations that provide an appropriate balance between exports and ecological issues in the Delta. Alternative 4A includes operating criteria to address San Joaquin River migratory fish survival, April-May Old and Middle rivers (OMR) flows, and Fall X2 (which is a criteria related to Delta smelt survival). This operational scenario also includes an operable barrier at the head of Old River—all of which are intended to improve flow habitat and migratory fish survival. California WaterFix further adds *additional* criteria for spring outflow and new minimum flow criteria at Rio Vista from January through August for the benefit of fish and improved flow habitat.

For additional context, Reclamation recommends OIG considers Chapter 3 of the Final EIR/EIS for in-depth discussion and analysis of Alternative 4A operational criteria.

Meeting Requirements of the Coordination Act

As stated in the Agreement, both the HCP/NCCP and the non-HCP/NCCP alternatives include the development of a new water conveyance facility that will include new intakes on the Sacramento River that convey water through tunnels southward approximately 30 miles to Clifton Court Forebay. These new intakes are anticipated to reduce the environmental risks of water pumping at existing south of Delta (SOD) facilities (the Jones and Banks pumping plants). Existing pumping at SOD facilities has been curtailed in recent years partly as a result of the risk of entrainment of endangered fish species, specifically Delta smelt. Thus, the placement of new intake facilities in the north Delta would allow further operational flexibility of the CVP and SWP, creating the ability of the projects to take water in the north Delta, and improving overall ecological conditions in the south Delta for endangered species by reducing exports at the Jones and Banks pumping plants and creating more natural flow patterns.

Recommendation 4: *Prior to funding any additional Federal financial assistance for the BDCP, make a written determination that grants are for an authorized purpose and consistent with delegated authority.*

Reclamation's Response: Non-concur. On July 30, 2015, Reclamation entered a Cooperative Agreement (Agreement) with DWR. The following section of the Section 7(a) of the Fish and Wildlife Coordination Act (FWCA) authorizes Reclamation to award this financial assistance agreement:

Section 6 F. (2) Fish and Wildlife:

The regional directors and the Director, Management Services Office, are delegated the authority pursuant to the Fish and Wildlife Coordination Act (16 USC 661-666c); Section 5 of the Endangered Species Act of 1973 (16 USC 1534); and Section 7(a) of the Fish and Wildlife Act of 1956[16 USC 742f(a)] to take the following actions, either directly or by providing financial assistance to non-Federal parties (255 DM 1.1.B.). Authority to award financial assistance agreements for projects associated with off-site locations [Paragraph 6.F.(2)(b)] is limited to the regional directors and Director, Management Services Office. The authority of the regional directors and Director, Management Services Office to award financial assistance agreements for all other projects authorized by this delegation can only be re-delegated to designated grants officers.

(b) plan, design, construct, and monitor, including acquire lands or interest therein as needed, instream habitat improvements, including but not limited to fish passage screening facilities at off-site locations (as negotiated on privately owned lands and facilities not associated with a Reclamation project.)

Reclamation will continue efforts to ensure sound written documentation reflecting decisions made are at the appropriate level of authority and are consistent with authorized project purposes. The purpose of non-concurrence as stated above is specific to the fact that Reclamation has currently determined appropriated funds that are not specifically requested for this purpose will not be provided to DWR for future BDCP efforts.

Responsible Official: Mid-Pacific Region Director, David Murillo

Appendix 5: Status of Recommendations

Recommendation	Status	Action Required
1, 2, and 4	Resolved and implemented	None.
3	Unresolved and not implemented	<p>USB: Reconsider recommendation and provide a plan for completing the action, including target dates.</p> <p>OIG: Refer recommendation to the Assistant Secretary for Policy, Management and Budget for resolution.</p>

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