



San Jacinto River Authority

ADMINISTRATIVE OFFICE
P.O. Box 329 • Conroe, Texas 77305
(T) 936.588.1111 • (F) 936.588.3043

February 9, 2010

The Honorable Robert Nichols
P.O. Box 12068
Capitol Station
Austin, Texas 78711

Dear Senator Nichols:

Thank you for the kind words in your letter of February 4, 2010. The staff, management and Board of Directors of the San Jacinto River Authority have invested an enormous amount of time, expense and effort, both recently and over the decades, to put the Authority in a position to be able to respond positively, economically and timely to the water shortage that faces all of Montgomery County and to offer the County the very best solution to this potential crisis. We apologize in advance for a lengthy response, but your letter does, indeed, raise a number of questions and issues that deserve full and candid responses.

In order to fully respond to your letter, it is necessary that we first point out again the purposes and objectives of our proposed countywide groundwater reduction plan ("GRP"). The entire County is facing a regulatory restriction that, if not timely addressed, could halt growth and development abruptly and destroy the economic viability of all of Montgomery County, not just certain areas, cities or communities. It is important to note that such regulatory restriction has been imposed by the Lone Star Groundwater Conservation District ("LSGCD"), a political subdivision of the State of Texas created by the Texas Legislature and approved by the voters of Montgomery County for the purpose of managing our shared groundwater resources. As part of the regulated community impacted by the LSGCD's rules, the Authority's countywide GRP program is offered as an option for other regulated Large Volume Groundwater Users ("LVGUs") to achieve and maintain compliance with such rules.

The Authority's countywide GRP is the most efficient, economical and timely solution for all of Montgomery County to achieve compliance. No one has offered any plan or evidence to the contrary. The Authority can produce the lowest cost and most efficient plan for compliance with the LSGCD rules by: (i) combining the Authority's water rights and resources, the administrative, technical, construction and operational experience of the Authority, and the ratepayer base of the entire County; (ii) eliminating the unnecessary middleman of regional water authorities and their associated costs and bureaucracies; (iii) using the demonstrated success of the principle of overconversion of heavily populated areas; (iv) taking advantage of the population concentration patterns already existing in the County; (v) running a non-profit operation and supplying water at the lowest costs available in the Houston region; and (vi) treating all water users in the same manner, whether they be a city, a MUD or special district, a

LAKE CONROE DIVISION
P.O. Box 329
Conroe, Texas 77305
(T) 936.588.1111
(F) 936.588.1114

WOODLANDS DIVISION
P.O. Box 7537
The Woodlands, Texas 77387
(T) 281.367.9511
(F) 281.362.4385

HIGHLANDS DIVISION
P.O. Box 861
Highlands, Texas 77562
(T) 281.843.3300
(F) 281.426.2877

private utility, an investor owned utility, a non-profit water supply corporation, an irrigator, an HOA or other type of user, and without advantage or disadvantage based on size, demand or geographical proximity to either Lake Conroe or any treated surface water pipelines. But to achieve the lowest cost to all ratepayers in Montgomery County, it is essential to not permit fragmentation of the plan by certain users at the expense of the other users in the County.

If the County succumbs to this division, geographically or politically, the most developed areas of the County will succeed, while the less developed, less financially able and most remote areas of the County will suffer permanent damage. For example, our estimates show that a large LVGU, like Conroe, or an LVGU situated on or near Lake Conroe, may be able to construct a stand alone system to withdraw, treat and distribute surface water and achieve a blended surface water and groundwater cost that is not wildly in excess of the costs estimated by the Authority for participants in the plan, but the City of Magnolia, for example, would experience costs that are two to three times higher. Similar results can be expected throughout the less developed portions of Montgomery County, while the larger, more affluent areas of the County would experience much more modest surface water costs and would avoid pumpage fees altogether (thereby eliminating a critical economic incentive for conservation). Such a system would also result in a patchwork of distribution lines controlled by local interests that could also stifle access to water by smaller LVGUs. For these reasons, the Authority has offered this plan as a solution for the whole County, based upon a pooled, lower unit cost to all, but is unwilling to participate in a piecemeal dismantling of the plan by those who have invested nothing to develop these water resources but nevertheless seek proximity or size advantage to the detriment of the remainder of the County.

As you remind us in your letter, the water available in Lake Conroe is limited and will not last the County indefinitely. Accounting for existing long-term sales of water out of Lake Conroe to Entergy, there remains something less than 100,000 acre-feet per year of permitted firm yield out of Lake Conroe (including water purchased from Houston). Depending upon the level of conservation achieved over the coming years (which historically can be expected to reduce per capita consumption by no more than 15%), this supply should last the County for 30 to 40 years. If the Authority were to allow piecemeal purchases of firm raw water by non-participants, the participants in the plan would be disadvantaged by (i) the loss of the water sold and the acceleration of costs necessary to bring in additional water supplies, (ii) the reduction in the ratepayer base over which to spread plan costs, and (iii) the loss of groundwater pumpage fees that would otherwise be paid, thereby increasing costs to the participants. Since the participants will be paying fees to reserve this water for future use, the GRP contract reserves and commits these firm supplies to the participants and results in the Authority having no firm water for sale to non-participants. However, until this water is needed for use by the participants, it may be sold on a short-term, interruptible basis to non-participants. Under the GRP contract, the revenue to the Authority for any interruptible water sold to non-participants is applied first to reimburse the participants for any fees paid to reserve that water, so it should be apparent why the Authority would want to have the first opportunity to make such short-term sales, rather than Houston. The obvious public purpose served is to reduce the cost of water supply to the participants.

With these principles in mind, we offer the following responses to your questions:

1. *What is the public benefit to the citizens in Montgomery County of prohibiting a Large Volume Groundwater User (LVGU) from purchasing water from Houston, in any particular year, if the SJRA chooses not to use the entire balance of Houston's portion of Lake Conroe's yield?*

The public purpose and benefit is described in the preceding introductory paragraph. It is to capture potential revenues from short-term water sales for the benefit of the fee paying participants in the plan in order to lower their costs, rather than to allow Houston to derive revenues from sales to non-participants when Houston has already been paid reservation fees for the water by the plan participants. The Reserved Quantity of water in Section 2.2 of the Houston water sales contract is the same as the interruptible water discussed above. Further, it is our understanding of the rules of the LSGCD that reliance by an LVGU upon an interruptible supply of water will not satisfy the requirements for an approvable groundwater reduction plan.

The Authority was urged by you and our entire elected political leadership in Montgomery County, including all of those who now wish to criticize the Authority for creating a "monopoly", to secure this water from Houston for Montgomery County. In addition, the need to acquire this water from Houston for use in the Authority's countywide GRP was clearly documented in the Water Resources Assessment Plan ("WRAP") prepared by the Authority on behalf of itself and almost every other LVGU. The Authority, and no one else, has committed its financial resources to accomplish this objective on terms that benefit the countywide plan and its participants. That is precisely what the GRP contract and the referenced provisions of the Houston contract do. We fail to see how we could responsibly do otherwise.

2. *Under what circumstances would SJRA allow Houston to sell a portion of the unclaimed water to a LVGU in Montgomery County?*

For the reasons discussed in our response to question 1, above, SJRA can foresee no circumstances where it would be beneficial to the plan participants to allow Houston to capture revenues that would otherwise inure to the benefit of the plan participants.

3. *What practical incentives exist in SJRA's GRP to implement significant water conservation projects?*

The GRP contract promotes conservation through economic means, but further enforcement of conservation measures must come from the LSGCD or LVGUs providing retail service. The Authority agrees with you that any such additional conservation measures should be supported. In addition, the GRP contract allows reuse of groundwater-based effluent without restriction and reuse of treated surface water where legally possible, and allows the Authority the ability to include reuse projects in its GRP and to help underwrite the costs of such projects where they will benefit all participants.

The GRP contract contains the most practical and commonly used form of conservation incentive---the economics of pumpage fees to equalize the costs of groundwater and surface water such that it is equally feasible to convert or overconvert to surface water where practical, or to remain on groundwater where not practical. The contract also includes the Authority's commitment to support and promote conservation, including reuse projects, in circumstances where it is beneficial to the plan participants to do so. However, it was discussed at length at the recent water summit that a wholesale provider of water, such as the Authority, is in the least effective position to enforce conservation because it cannot curtail water deliveries at the consumer level to achieve compliance. This type of enforcement must necessarily be done by a regulatory authority, such as the LSGCD, or the LVGU providing retail services.

This portion of your letter appears to treat reuse projects and conservation measures interchangeably. Reuse may serve as an additional source of water supply, but reuse alone does not necessarily reduce water demands. Inasmuch as reuse represents a water supply strategy that would extend the useful life of the water in Lake Conroe and lead to groundwater usage reductions, the GRP contract provides the opportunity for the Authority to assist in financing some or all of the costs of reuse projects that are beneficial to the participants as a whole.

Your interpretation of the GRP contract to create disincentives to conservation and "additional fees" for indirect reuse projects overlooks the express terms and definitions in the contract. Under the contract, a participant pays pumpage fees based on groundwater pumped and surface water fees for treated surface water actually received, if any. The term "Water" is defined specifically to mean treated surface water delivered through the project. Consequently, in Section 3.04 of the contract that you cite, if a participant reuses its groundwater (with or without additional conservation measures), or simply achieves reduced groundwater pumpage through its own conservation education or enforcement efforts, that participant has the greatest incentive the Authority can offer---avoidance of pumpage fees on the conserved or reused groundwater. Section 3.04, correctly applied, simply means that to the extent that a participant receives any additional credits (over and above the avoidance of pumpage fees) that may be offered by the LSGCD in the future which result from receiving treated surface water from the project, then those credits are transferred to the Authority for the benefit of all participants (since they, collectively, have helped to underwrite the costs of providing that surface water at an economical cost), but only to the extent of the treated surface water actually supplied.

As to Section 4.12(c) of the GRP contract, this provision is simply a recognition that surface water supplied from either the Authority's or Houston's water rights in Lake Conroe are subject to reuse restrictions in order not to prejudice the reliability of prior downstream water rights or environmental flow requirements. By definition, these restrictions do not apply to a participant's direct or indirect reuse of its own groundwater.

Section 4.12(b) of the contract which you cite only comes into play after a participant begins taking treated surface water from the project. Since treated surface water must be delivered to participants at a constant rate (with variations in demand being met with

increased or decreased groundwater pumpage by participants), each participant must be prepared to take, and must actually take, this minimum daily amount (the “Contract Quantity”). A participant beginning a reuse project, after being previously committed to take a minimum Contract Quantity, cannot then reduce that Contract Quantity without the consent of the Authority (so as to effectively “balance” the surface water and groundwater usages of all participants as a whole and maintain compliance with the LSGCD rules). Instead, a participant must further reduce the groundwater usage of the participant. This is both necessary to manage and coordinate a program of overall groundwater reduction and entirely consistent with the objective of groundwater reduction.

4. *Does SJRA support indirect reuse projects which allow communities to utilize excess water in Lake Conroe?*

It is not now, and has never been, the position of the Authority that the wastewater discharges into Lake Conroe constitute part of its permitted yield. If the Authority wished to make such a claim, it would first have to file a permit application with the TCEQ and go through the necessary hearings and administrative proceedings. The Authority has not done so, and the source of this information is simply wrong.

That being said, the Authority and all water rights holders in Lake Conroe and downstream are certainly aware that wastewater discharges derived from groundwater sources help to make the permitted yield of Lake Conroe more firm. Since the County as a whole and the levels in Lake Conroe are dependent to some degree on the firmness of the yield of Lake Conroe, the Authority would do a disservice to the County and its plan participants by supporting efforts by non-participants to reuse groundwater-based effluent which would otherwise be discharged into Lake Conroe when that reuse plan is (i) only feasible if supplemented by the purchase of additional surface water from Lake Conroe that has been committed to the participants through the payment of reservation fees, and (ii) seeks to avoid the payment of pumpage fees applicable to plan participants.

As to MUDs 8 and 9, the Authority has spent a great deal of time and resources discussing our concerns about this so-called “reuse” plan with their various representatives, including some three hours of discussion in the last two weeks. This plan is entirely dependent on the Authority’s willingness to (i) allow MUDs 8 and 9 to utilize the assets and properties of the Authority and Houston, namely Lake Conroe, to store their effluent, albeit only for a short period of time (but not to transport it, as is the case in indirect reuse projects using the bed and banks of the rivers and streams of the State), (ii) permit the construction of a raw water intake structure within the property rights of the Authority on Lake Conroe, and (iii) dilute and “cleanse” their effluent by means of the stored water in Lake Conroe in order to make it marketable to their customers. This is a novel, but inappropriate, attempt to treat a structural reservoir financed, operated and maintained by others in the same fashion as the natural bed and banks of a river or stream of the State.

We believe that this is not at all a common practice, but is simply an effort to avoid the costs of building on-site storage for their effluent and the payment of pumpage fees as a participant in the plan. If these costs borne by other LVGUs can be avoided by MUDs 8 and 9 through using the property rights and water resources of others, then it is no wonder that it might seem to be economical to MUDs 8 and 9. A substantial share of the costs of storage that would otherwise be encountered in a true, direct reuse project is being borne by others without any compensating payment. This appears to the Authority to be reuse in name only and proximity exploitation that harms the rest of the County and must be recognized for what it is. If this proposed project is multiplied several times over to include other similarly situated Lake Conroe area LVGUs, the impact on the storage capability and the available water in and yield of Lake Conroe for serving the rest of the County could be substantial. For these reasons, the Authority is not persuaded that it should consent to the application by MUDs 8 and 9 to the TCEQ to use Lake Conroe in such a fashion, and for the reasons discussed earlier, the Authority has advised MUDs 8 and 9 that it has water to sell to a non-participant only on an interruptible basis, but the Authority is hopeful that MUDs 8 and 9 will join the GRP and seek approval of their project as a participant.

5. *Does SJRA encourage the exploration of options besides the SJRA's GRP?*

All LVGUs in Montgomery County have had nearly four years to exhaustively study all available options. To the Authority's knowledge, no LVGU, except the Authority, has made any serious effort to develop alternatives or to put forth an alternative plan until the very recent "discovery" of the "reuse" and "brackish water" alternatives. The Authority developed its plan in open meetings with 201 of the 203 LVGUs through the WRAP process. The results are public information accessible on the Authority's website. These last minute options have been conceived in virtual privacy and are each accompanied by a demand for another delay in the implementation of the LSGCD groundwater reduction rules. In view of the millions of dollars being expended each year by LVGUs to drill additional wells and to rehabilitate existing wells, the Authority is not persuaded that further delay (rather than the development of a feasible alternative) is wise.

As discussed above, the Authority supports true recycling and reuse efforts. The Authority considered and dismissed brackish water as a viable countywide alternative some two years ago for a variety of reasons. The quantity, quality and reliability of brackish water resources throughout Montgomery County are not known, and disposal of the brine residue from brackish water treatment by deep well injection presents serious economic, environmental and permitting obstacles. However, this is not to say brackish water is not feasible for a particular LVGU, but this option should have been investigated by those LVGUs long ago.

6. *What studies have been done to predict the economic impact of lower lake levels?*

In the months preceding Judge Sadler's water summit on September 28, 2009, there were many unfounded assertions of the dire consequences that would result from the use of Lake Conroe water for its intended purpose. Since the water summit, the Authority has

received almost no further questions or expressions of concern about Lake Conroe levels, including at the January 14, 2010, GRP presentation at the Lone Star Convention Center, but we have received a number of expressions of appreciation for making this data available in an easy to understand fashion. We are also aware of recent efforts by certain special interest groups and individuals to undermine the efficacy of the Authority's data in this regard, but, once again, no one has come forward with any credible, scientific data to the contrary.

Prior to the water summit, the Authority sought a proposal for an economic impact study from a major Texas university for the purpose of quantifying and comparing the effects of a countywide economic Armageddon resulting from a shortage of water supply to sustain the growing economy of Montgomery County, and the periodic and temporary effects of fluctuations in lake levels 30 or more years from now resulting primarily from inevitable acts of nature and only peripherally from usage of water in Lake Conroe. The proposal received by the Authority for the study was, unfortunately, incorrect in scope and quite expensive and did not offer a timely completion date. Based upon the successful results of the water summit, the Authority's Board of Directors chose to take no further action on pursuing this study. Fortunately, however, the Authority was informed about the disastrous effects of a water shortage by a thorough study on the subject prepared by the Texas Water Development Board, entitled "Socioeconomic Impacts of Unmet Water Needs in the Region H Water Planning Area." We are not aware of any studies commissioned by any other LVGU concerning the enormous impact of lake level fluctuations, but should you learn of any such efforts, we would appreciate your sharing such information with us.

7. *Would the SJRA consider selling surface water to an entity not participating in its GRP?*

The Authority's position on this question and the principles supporting our position are discussed at length above and need not be repeated here. However, we are intrigued by the balance of your letter. You began by reciting that you had been asked a number of questions that needed answers. It appears that you have been hearing a great deal of the same rumors and innuendo that we only hear about indirectly.

As regulatory deadlines approach, it is only natural that the general anxieties about the changes we all face to our past, wasteful practices in the use of inexpensive groundwater will grow. But the Authority is also acutely aware of the organized and well-funded efforts of certain special interest groups and individuals to delay and undermine this project by misinformation and rumors and by attacking the integrity of the Authority, its plan and contract, and its Board, staff, consultants and supporters, without having made any prior effort to investigate or offer any constructive alternatives, except those which serve their special interests at the expense of the County as a whole.

Some examples of this campaign, as well as the matters referred to in five of the last six paragraphs of your letter, deserve specific and categorical responses at this time:

- A. The Authority has not told any engineer or consultant that they may not investigate or consult with any LVGU or regulatory agency about brackish water.
- B. The Authority has taken no position on whether any underlying brackish water aquifers in Montgomery County are or should be subject to regulation by the LSGCD. That is a matter for the LSGCD, not the Authority.
- C. All LVGUs have had years to fully explore the available options, including the purchase or reservation of water from the Authority, Houston, the Trinity River Authority or the Brazos River Authority; the importation of groundwater; the development of brackish water; reuse or recycling; conservation; rainwater harvesting, etc. To our knowledge, none except the Authority have done so in a serious manner. The Authority has taken no options off the table. Rather, the lapse of time and inaction by those who now complain most loudly have done so.
- D. The Authority has invested more than 15 years and tens of millions of dollars (but not one dollar of taxpayer money) in acquiring, developing, rearranging and contracting for sufficient local water resources to meet the coming water shortage and to offer these resources to the entire County on a non-profit basis and at the lowest possible cost. Until very recently, the Authority was urged by our elected leaders and by written support from some 85% of the LVGUs in Montgomery County to develop this plan and to secure all available water in Lake Conroe for use in Montgomery County. Now that we have done so, with no financial or other assistance from any other LVGU, except token WRAP preparation fees, the special interests cry "monopoly" and seek to carve up the plan for provincial, political or financial gain.
- E. By virtue of its Woodlands Division's non-profit operation of the groundwater supply system serving the 100,000 or so Montgomery County citizens in The Woodlands, the Authority is, indeed, the largest LVGU in the County. But by pooling this ratepayer base with the entire County and reducing the unit costs of groundwater reduction compliance to all LVGUs, it is Montgomery County, not the Authority or The Woodlands, that receives the greatest benefit. If the Authority was seeking to secure a special benefit to The Woodlands, it would have simply converted The Woodlands the minimum 30% to surface water, consumed all of its water rights in Lake Conroe doing so, ignored the opportunity to acquire additional water supplies available from Houston in Lake Conroe (which were coveted by North Harris County users) and left the remainder of the County to fend for itself. This would have been the path of highest return, lowest risk and lowest cost to the Authority. Instead, the Authority is attempting to do that which is right and equitable to all LVGUs, not what is easy.
- F. Any LVGUs that believe that groundwater reduction should not apply countywide, or to them in particular, should take their concerns to the LSGCD. As stated above, the Authority does not make the rules, but like all LVGUs, must comply with them.
- G. We have no doubt that there are some LVGUs who wish to construct and "control" their own systems, using surface water from the Authority. We have yet to see a plan

for doing so that does not seek to take special advantage and to shift the costs of compliance to others who often are less able to bear those added costs.

- H. The Authority is committed to providing water to all LVGUs in the County who wish to participate in our plan and share the burdens of compliance uniformly on the exact, same basis and terms as are applicable to the Authority's Woodlands Division. We cannot support the special or provincial interests who wish to distribute costs unevenly, or that favor urban interests over suburban or rural interests, or that pit different areas of the County against each other.
- I. The GRP contract is not perpetual, but as is the case with any long-term, multi-phase capital project, financing of the project requires that the contract continue at least until all debt is retired. Indeed, we have received a number of complaints that the contract is not perpetual. Consequently, the contract includes a clause for continuing service following the expiration of the contract term.
- J. There is nothing unprecedented about a river authority or large city in Texas taking a leading role in securing water resources for the future of their areas when others fail to act. You need only look to Houston, Dallas, Fort Worth, the Trinity River Authority, the Brazos River Authority and others for examples on a much larger scale of this type of vision and leadership in water resource management.
- K. Special mention should be made of the most recent rumor that the Authority has made a "special" agreement with The Woodlands that is more advantageous than the GRP contract. This is patently false and appears to be designed to inflame the old politics of North County versus South County. Anyone familiar with the public records should know that the MUDs in The Woodlands own no water wells, are not LVGUs and, therefore, are not eligible to enter into the GRP contract. The Authority, through its Woodlands Division, is the LVGU serving The Woodlands. As such, the Authority (who cannot contract with itself) has committed in the GRP contract to be subject to the same requirements, terms and payments as all other LVGUs. Comparison of a 1975 vintage operating contract between the Authority and a Woodlands MUD is like comparing an apple to an orange and announcing that they are different.
- L. The Authority's willingness and ability to offer this plan are based on (i) the needs of the County as a whole, (ii) the mission and purpose of the Authority to develop and beneficially apply the water resources of the San Jacinto River basin for the greatest public benefit, and (iii) the hard work and dedication of the past and present management, staff and Boards of Directors of the Authority. The Authority has fairly, objectively and constructively represented the interests of all of Montgomery County for more than 70 years, without political bias, ego, territorial prejudices or the influences of special interests. Montgomery County does not benefit from Balkanizing the County in the face of a common, countywide crisis. We believe that the Authority has acted as a good steward of water resources, as is our mission.

When the special interests arrive, it is not surprising to hear inflammatory terms such as “monopoly” or “conflict of interest” or “lack of accountability” or other similar vague terms. Since these interests invariably seek special advantage or benefit, at the expense of the remainder of the County, they cannot openly justify their positions and must seek to disrupt all other alternatives.

We remain confident that the Authority’s plan is the best possible plan for Montgomery County, and we will continue to defend it against all who wish to dismantle, delay or destroy the County’s best opportunity to meet its water supply challenges. We thank you for the opportunity to set the record straight on these matters, and with this additional information, we hope to have your support of this essential program.

By this letter, we are urging all LVGUs who believe as we do to make known their support to their elected officials.

Yours very truly,



R. Gary Montgomery
President, Board of Directors

- cc: Governor Rick Perry
Lt. Governor David Dewhurst
Attorney General Greg Abbot
Congressman Kevin Brady
Senator Tommy Williams
Representative Brandon Creighton
Representative Rob Eissler
Representative John Otto
Montgomery County Judge and Commissioners Court
City of Conroe Mayor and City Council
City of Cut-n-Shoot Mayor and City Council
City of Magnolia Mayor and City Council
City of Panorama Mayor and City Council
City of Stagecoach Mayor and City Council
City of Willis Mayor and City Council
San Jacinto River Authority Board of Directors
Lone Star Groundwater Conservation District Board of Directors
Texas Water Development Board
Texas Commission on Environmental Quality
All Montgomery County LVGUs (by e-mail)