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September 24, 2007

ADMIN. DEPT.
EVMWD

SEP 25 2007

RECEIVED

VIA OVERNIGHT MAIL
Sean Gallagher, Director
Energy Division
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102

Re: Lake Elsinore Advanced Pumped Storage ("LEAPS") Project –
California Environmental Quality Act Lead Agency

Dear Mr. Gallagher,

Best Best & Krieger, LLP acts as general counsel to the Elsinore Valley Municipal Water District (the "District") which is involved in the process of preparing an Environmental Impact Report as Lead Agency for the District's Lake Elsinore Advanced Pump Storage project ("LEAPS"). The District's Board President and General Manager appreciated the opportunity to meet with you recently to discuss the LEAPS project. The District was formed in 1950, and its service area includes over 97 square miles. The District has approximately 38,000 water and wastewater customers and a \$48 million annual budget. The District initiated its efforts to study, entitle and license its LEAPS project in the early 1990s in conjunction with the District's efforts to reclaim and stabilize Lake Elsinore.

As you know, the District and The Nevada Hydro Company, Inc. ("NHC") entered into a Development Agreement dated May 15, 1997, which contemplated a license application with the Federal Energy Regulatory Commission ("FERC"), in docket P-11504, for a pump storage project described in a preliminary permit application in that docket ("P-11504 Development Agreement"). However, no license application was ever filed and the preliminary permit expired. On February 21, 2001 FERC issued to the District a preliminary permit in docket P-11858, for a proposed pumped storage project, utilizing Lake Elsinore as lower reservoir, and appurtenant transmission. On February 2, 2004, the District and NHC filed as co-applicants for a license, pursuant to the preliminary permit in docket P-11858, for the LEAPS project, including a 500-MW pumped storage facility (utilizing Lake Elsinore as lower reservoir) and a 500 kVA transmission line interconnecting the systems of San Diego Gas & Electric Company and Southern California Edison Company. We understand that NHC has made certain agreements

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with MSPDC, a wholly-owned subsidiary of Morgan Stanley, under which the Company, a newly organized entity, will jointly continue the development of LEAPS and into which MSPDC will contribute certain capital investments to fund the development.

You have requested additional information regarding the District's status as Lead Agency for the LEAPS project. The purpose of this letter is to provide a more detailed description of the LEAPS project, and explain why, in light of the District's role in implementing the project, the District is an appropriate agency to conduct environmental review for the project. Finally, this letter is intended to clarify that the District remains open-minded regarding the possibility of sharing lead agency duties as permitted by CEQA.

As you know, the LEAPS project will require the construction and operation of a reservoir and hydroelectric power generation facility near Lake Elsinore, California. It will also require construction of a transmission line to connect the hydroelectric facility to the rest of the Southern California power grid. The project will include a lined upper reservoir in the hills immediately above Lake Elsinore, two parallel high-pressure water conduits, an underground powerhouse, and about 30 miles of 500-kV transmission line connecting the project to existing Southern California Edison and San Diego Gas and Electric transmission lines.

The District is both a proponent and future operator of the LEAPS project. In addition to obtaining the required regulatory approvals, the District's role in the LEAPS project will require it to provide water for the hydroelectric facility, maintain water quality to levels necessary for the project's continued operation, and maintain surface water elevation in Lake Elsinore. In order to accomplish these tasks, the District will be required to take further discretionary actions related to the project, including, but not limited to, actions related to the project's water supply and water-related operations. Because of its role as a proponent and operator of the LEAPS project, the District is best situated, both practically and legally, to be the lead agency for the project.

The California Environmental Quality Act ("CEQA") defines a lead agency as "the public agency which has the principle responsibility for carrying out or approving a project which may have a significant effect upon the environment." (Pub. Res. Code, § 21067.) "If the project will be carried out by a public agency, that agency shall be the lead agency even if the project would be located within the jurisdiction of another public agency." (Cal. Code Regs. tit. 14 ("State CEQA Guidelines"), § 15051(a); see also *Friends of the Eel River v. Sonoma County Water Agency* (2003) 108 Cal.App.4th 859 [as the lead agency under CEQA, a water agency had an obligation to discuss in its environmental impact report a pending Federal Energy Regulatory Commission proposal which might curtail the project's water sources].)

With regard to what constitutes a "project", CEQA clearly states that a project is "the whole of an action, which has a potential for resulting in either a direct physical change in the environment, or a reasonably foreseeable indirect physical change in the environment, and is . . . an activity directly undertaken by any public agency." (Cal. Code Regs. tit 14 ("State CEQA Guidelines"), § 15378(a) [emphases added].) Indeed, both CEQA and case law make it clear that segmenting or piece-mealing a project into smaller portions for purposes of environmental

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analysis is generally forbidden. (See, e.g., State CEQA Guidelines, § 15378; *Christward Ministry v. Superior Court* (1986) 184 Cal.App.3d 180; *Kings County Farm Bureau v. City of Hanford* (1990) 221 Cal.App.3d 692.)

The District's obligations as proponent and future operator of the LEAPS project make it the public agency with principle responsibility for carrying out the project, and therefore the appropriate lead agency. Additionally, even though the District will not have a direct role in the operation of the transmission line component of the project once it is complete, as lead agency, CEQA requires the District to analyze the project as a whole, and to avoid dividing it into its individual hydroelectric and transmission line components. Accordingly, the District is the appropriate lead agency for the entire LEAPS project.

Recognizing its obligations as the lead agency, the District publicly released a June 1, 2006 CEQA Notice of Preparation of an Environmental Impact Report clarifying both that the District is the appropriate lead agency, and that the LEAPS project consists of hydroelectric and transmission line components. Additionally, as a project proponent, the District applied to the FERC for a license to construct and operate the LEAPS project. Following FERC's release of a Draft Environmental Impact Statement, which jointly analyzed the hydroelectric and transmission components of the project, the District submitted comments to FERC reiterating that the transmission line component of the project is appurtenant to the hydroelectric component and, as such, both components must be analyzed together.

Finally, although the District is the appropriate lead agency for the LEAPS project, the project will be located within multiple jurisdictions, and will require approvals from numerous other public agencies – including, we understand, an approval from the Public Utilities Commission. These other public agencies will be responsible agencies within the meaning of CEQA. (See Pub. Res. Code, § 21069.) In this role, each agency will have the opportunity and duty to review all of the District's CEQA documents, including the District's Environmental Impact Report, and to participate in the environmental review process as appropriate. (See State CEQA Guidelines, § 15050, subd. (b).) Should the Public Utilities Commission, however, prefer to take a more direct and active role in assisting with the environmental review for the LEAPS project, CEQA does provide that two agencies with a substantial claim to the lead agency role may “by contract, joint exercise of powers, or similar devices” agree to use “cooperative efforts” in fulfilling lead agency responsibilities as co-lead agencies. (State CEQA Guidelines, § 15051, subd. (d).) A preliminary draft co-lead agency agreement providing for such cooperation between the District and the Public Utilities Commission is enclosed herewith for your consideration.

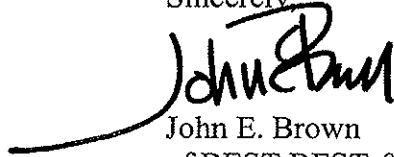
In conclusion, because of its responsibilities as a proponent and future operator of the LEAPS project, the District is the appropriate lead agency under CEQA to analyze the project's potential environmental effects. Nonetheless, and consistent with CEQA's intent, the District would be pleased to coordinate or cooperate with other agencies – including the Public Utilities Commission – to complete the environmental review process and produce a Draft Environmental Impact Report that is as thorough and accurate as possible.

LAW OFFICES OF
BEST BEST & KRIEGER LLP

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We appreciate your attention to this matter, and hope the analysis contained in this letter addresses your concerns regarding the District's role as lead agency for the LEAPS project. If you have any questions or comments regarding the contents of this letter, the enclosed sample co-lead agency agreement, or the District's role as lead agency, please feel free to contact me.

Sincerely

A handwritten signature in black ink, appearing to read "John E. Brown". The signature is written in a cursive style with a long horizontal stroke extending to the left.

John E. Brown
of BEST BEST & KRIEGER LLP
Counsel, Elsinore Valley Municipal Water District

Enclosure

cc: Ronald E. Young, District General Manager
President and Board of Directors

MEMORANDUM OF UNDERSTANDING

Between

ELSINORE VALLEY MUNICIPAL WATER DISTRICT

And

STATE OF CALIFORNIA PUBLIC UTILITIES COMMISSION

This MEMORANDUM OF UNDERSTANDING (MOU) is hereby entered into by and between the Elsinore Valley Municipal Water District, hereinafter referred to as the District, and the State of California Public Utilities Commission, hereinafter referred to as the CPUC. The District and CPUC are hereinafter referred together as the Parties.

A. **PURPOSE:**

The District and its co-applicant The Nevada Hydro Company, Inc. have proposed the construction and operation of a reservoir and hydroelectric power generation facility near Lake Elsinore, California. The facility will require the construction of a transmission line to connect the hydroelectric facility to the rest of the Southern California power grid. The facility will include a lined upper reservoir in the hills immediately above Lake Elsinore, two parallel high-pressure water conduits, an underground powerhouse, and approximately 30 miles of 500-kV transmission line connecting the facility to existing Southern California Edison and San Diego Gas and Electric transmission lines. Collectively, these facilities are known as the Lake Elsinore Advanced Pumped Storage Project (the "LEAPS Project") and are the subject of a pending application for a Federal Energy Regulatory Commission ("FERC") license and a United States Forest Service Special Use Authorization (FERC Project No. p-11858).

The District, as the applicant for LEAPS Project approvals and the "public agency which has principal responsibility for carrying out" the LEAPS Project, is the appropriate lead agency for purposes of completing environmental review under the California Environmental Quality Act. (Pub. Res. Code, § 21067; 14 Cal. Code Regs., § 15050.) As lead agency, the District has determined that an Environmental Impact Report ("EIR") must be prepared in accordance with CEQA to analyze the potential environmental impacts of the LEAPS Project. In furtherance of this decision, the District publicly circulated a Notice of Preparation to interested agencies, organizations, and individuals in June 2006.

Recently, the CPUC has asserted that it has similar but more limited approval authority over certain aspects of the transmission line component of the LEAPS Project – specifically, the potential issuance of a Certificate of Public Convenience and Necessity ("CPCN"). As CEQA requires that "the whole of an action" be analyzed in a single environmental document, it is neither practical nor

permissible to segment the LEAPS Project into transmission and non-transmission components for purposes of allowing the CPUC to independently analyze the transmission component of the LEAPS Project. (14 Cal. Code Regs., § 15378.)

As permitted by CEQA, the purpose of this MOU is to provide a framework for cooperation between the District and the CPUC to work together as co-lead agencies in preparing and completing a joint EIR which analyzes the LEAPS Project in compliance with CEQA (Public Resources Code section 21000), the State CEQA Guidelines (California Code of Regulations, title 14, section 15000 et seq.), the local CEQA guidelines of the District and – if applicable – of the CPUC, and all other applicable laws, orders, regulations, directions, and guidelines. (14 Cal. Code Regs., § 15051(d) [“An agreement may provide for cooperative efforts by two or more agencies” to fulfill lead agency duties].) Work would include, but is not limited to, environmental and technical information collection, analysis and reporting. Should the decision be made to approve the LEAPS Project, this Memorandum of Understanding continues the cooperation during construction of the Project for the purpose of implementing and/or monitoring mitigation measures developed through the CEQA process. This cooperation serves the mutual interest of the Parties and the public in that the cooperative efforts of the District and the CPUC will efficiently provide a complete and accurate EIR for the public’s review. In consideration of the above premises, the Parties agree as follows:

B. AS CO-LEAD AGENCIES, DISTRICT AND CPUC SHALL:

1. Be jointly responsible for ensuring compliance with the requirements of CEQA and its implementing regulation, along with all other applicable laws, and shall be responsible for the scope and content of the EIR prepared for the LEAPS Project;
2. Cooperate in assembling mailing lists of interested agencies, organizations, and individuals for purposes of providing notices under CEQA or other laws and for soliciting input and distributing the notices, the Draft and Final EIR, and any other documents as required by law;
3. Cooperate in completing any required consultation with interested or affected public agencies including but not limited to the California Department of Fish and Game, the United States Fish and Wildlife Service, the California State Historic Preservation Officer, and interested Native American Tribes;
4. Solicit, review, and, if acceptable to both Parties, approve an environmental services contract for the preparation of a Draft EIR and all supporting technical studies through a qualified Contractor;

5. Assume joint responsibility for the costs and expenses associated with the environmental services contract and the preparation of the Draft EIR and all technical studies;
6. Reserve the rights to review and revise, at their respective options, selected sections of the Draft and/or Final EIR, as appropriate. It is anticipated that the District's efforts under this Section will focus on the LEAPS Project's pumped storage and pipelines facilities, water quality, water supply, public utilities, and impacts specific to the communities around Lake Elsinore. It is further anticipated that the CPUC's efforts under this Section will focus on the LEAPS Project's transmission and power station facilities, and impacts to utility systems and the State's energy distribution grid. As to all other impacts, the District and CPUC shall coordinate their efforts to complete environmental analysis.

C. THE PARTIES MUTUALLY AGREE AND UNDERSTAND THAT:

1. Schedule of Deadlines. The District and the CPUC intend to proceed with the completion of a Draft EIR and for the LEAPS Project by the end of December 2008. The LEAPS Project is a high priority project for both the District and the State. Both Parties will attempt to meet this timeframe. The Parties agree to prepare a detailed schedule for the completion of the environmental review of the LEAPS Project, and agree to modify and reach final agreement on the details of such schedule – which will include specific dates establishing the deadlines for expected deliverables from the Contractor, as well as deadlines for the District and the CPUC to respond to all materials provided by the Contractor – within one month after the Parties approve an environmental services contract hiring a Contractor for the preparation of the LEAPS Project EIR and technical studies.
2. Contractor Selection. The CPUC will prepare and notice a Request for Qualifications (RFQ) for the preparation of the EIR in accordance with State contracting requirements. The Parties shall evaluate the qualifications and proposals of the prospective EIR contractors based on the RFQ evaluation criteria. The Parties shall have mutual responsibility for final selection of the Contractor. The selection process will be governed by provisions of the CPUC contracting procedures and California law. If for any reason, a change in the Contractor or subcontractor becomes necessary, the District and CPUC will jointly engage in selection procedures for a new Contractor.
3. Agency Project Representatives. For the purpose of coordinating the responsibilities of the Parties for the preparation of the EIR for the LEAPS Project, the persons listed below are the designated Agency Project Representatives of the Parties. Actual delivery of written notice to the following representatives, or such substitute representatives as the

respective Parties may hereinafter designate, shall constitute notice to that organization. The principal contacts for this instrument are:

District Project Representative: Ronald E. Young, General Manager
Elsinore Valley Municipal Water District
P. O. Box 3000
31315 Chaney Street
Lake Elsinore, CA 92531-3000
Phone: (951) 674-3146

Facsimile: (951) 674-9872

CPUC Project Representative: -----**To Be Added**-----

4. Regular Consultation between Parties. The successful preparation of the EIR requires complete and full communication between the Parties. It is the duty of the Agency Project Representatives to ensure close consultation throughout the EIR preparation and review process. Accordingly:
- (a) The Agency Project Representatives shall keep each other advised of the developments affecting the preparation of the Draft EIR. Toward this end, and to ensure close consultation and coordination, the Agency Project Representatives shall conduct conference calls at least once every two weeks and shall meet face-to-face at least once every two months.
 - (b) In the event that either Agency Project Representative is unable to participate in any such regularly scheduled conference call or meeting, an alternate shall be delegated to represent that Agency Project Representative's party in said call or meeting.
 - (c) CPUC recognizes the need for the District to work directly with the Contractor with regard to water quality, water supply, local environmental impacts, and pumped storage facility analyses. The District will keep CPUC informed of these discussions and will involve CPUC when appropriate.
 - (d) The District recognizes the need for the CPUC to work directly with the Contractor with regard to electricity grid, energy facilities, power house, and transmission facilities analyses. The CPUC will keep the District informed of these discussions and will involve the District when appropriate.
 - (e) Consistent with existing laws and regulations, the Parties agree to share all relevant information.

- (f) Any and all media releases and/or public mail-outs shall be made with the joint approval and at the direction of the District and the CPUC.
5. Scope and Content of EIR. The District, CPUC, and the Contractor shall jointly schedule and conduct any required scoping meetings with the public and other agencies at the beginning of the process. These meetings will be held to determine the areas of public and agency concerns pertaining to the proposed LEAPS Project, and guide the Parties in scoping the EIR. The Agency Project Representatives shall determine (with approval, if necessary, from the signatories to this MOU or their delegates);
- (a) the scope and content of the EIR for the Project to ensure that the requirements of the various federal and state statutes are met and that the statutory findings required of the District and the CPUC for their respective decision on the Project can be made;
 - (b) whether the work performed by the Contractor is satisfactory, and if not, how best to correct the deficiencies in the work; and
 - (c) the division of responsibilities among the Parties and any cooperating responsible or trustee agencies.
6. Administrative Draft EIR. The District and CPUC shall review the administrative Draft EIR and provide comments to the Contractor in writing. The District and/or CPUC may request revision of the administrative draft with further agency review.
7. Draft and Final EIR. The District, CPUC, and the Contractor shall jointly schedule and conduct public meetings to receive comments on the Draft EIR during the public review period. The Contractor will receive and log written comments submitted on the Draft EIR during the public comment period. The Contractor will prepare preliminary responses. The District and CPUC will review the responses for accuracy and identify any necessary revisions before they are incorporated into the Final EIR. The Final EIR will be prepared and reviewed in the same manner as the Draft EIR.
8. Consultation with Other Agencies. The District and CPUC reserve the right to consult directly, without notice or report, with other Federal, State, and local officials during the preparation of the EIR to ensure objectivity and compliance with CEQA. The Parties will immediately notify each other and the Contractor if matters discussed at any such consultation will require significant changes in the development of the EIR or require significant costs pursuant to this Memorandum of Understanding.
9. Privileged and Confidential Information. The District, CPUC and the Contractor will, upon request, share procedures and underlying data used in developing submitted sections of the Draft and/or Final EIR including,

but not limited to, final reports, subcontractor reports, and interviews with concerned private and public parties, whether or not such information is contained in the working papers or the Draft or Final EIR. The Parties intend that information that is otherwise protected from disclosure under the attorney-client privilege, work-product privilege, and deliberative process privilege and/or any other applicable privilege may be exchanged without waiving or compromising such privileges or doctrines. The Parties agree that privileged information received from the other Party shall be treated and maintained as confidential to the extent allowed by federal and state laws, regulations and policies. Parties agree to label as "Confidential" documents that they believe are privileged and should not be disclosed. Neither Party will disclose privileged information received from the other Party, regardless of whether it is labeled "Confidential," without first notifying other Party.

10. Effective Dates. This MOU is executed as of the date of the last signature and is effective through December 31, 2012, or the date on which all appeals and litigation filed in connection with approval of the LEAPS Project have been fully resolved, whichever date is earlier, at which time it will expire unless extended.
11. Modification. Modifications to this MOU shall be made by mutual consent of the Parties, by the issuance of a written instrument, signed and dated by all Parties.
12. Termination. Any of the Parties, in writing, may terminate this MOU in whole, or in part, at any time before the date of expiration upon 30 days' written notice to the other party. During any such 30-day waiting period, the Parties will actively attempt to resolve any disagreement between them. In the event of termination of this MOU, if the preparation of an EIR is still required, both the District and CPUC shall have access to all documentation, reports, analyses and data developed by the Contractor.
13. Rights and Responsibilities of Parties. This MOU sets forth the Parties' rights and responsibilities for preparing the Project EIR, and for subsequent activities related to the document. This MOU in no way restricts the District or the CPUC from participating in similar activities with other public or private agencies, organizations, and individuals. This MOU does not authorize the transfer of funds between Parties. Each Party is responsible for its own acts and omissions in connection with activities undertaken pursuant to this MOU.

THE PARTIES HERETO have executed this instrument:

Elsinore Valley Municipal Water District

California Public Utilities Commission