



Memorandum

TO: TREATMENT PLANT
ADVISORY COMMITTEE

FROM: John Stufflebean

SUBJECT: McCARTHY PROPERTY

DATE: 12-03-09

Approved

Date

This memorandum responds to the request made by the Treatment Plant Advisory Committee at its October 2009 meeting for information regarding the Plant's interests in the McCarthy Property in Milpitas. Specifically, the Committee asked staff and the City Attorney's Office to respond to the following questions:

1. What rights did the Plant purchase and what was the purchase price? What would the rights be worth now if the Plant were to agree to release the rights?
2. What is the potential for monetary liability to homeowners for damages if development is allowed to occur before the solar drying operation is discontinued?
3. What is the impact on the water recycling project that we are trying to get done, if we try to move forward now with discontinuing the solar drying operation at the same time? Does there need to be prioritization, or can we do both? What are the potential rate increases associated with doing these projects separately at the same time?
4. Could an assessment district be formed on the McCarthy property to provide a funding source for all or a portion of the costs associated with discontinuing the solar drying operation? Is there some way to shift costs associated with that project to the developer or either the developer or the homeowners over time, for a portion of the cost, or must all of the costs be paid for through rates?

Written answers to questions 1 and 3 are provided below. The City Attorney's Office will provide verbal response at the TPAC meeting on questions 2 and 4.

Question 1. What rights did the Plant purchase and what was the purchase price? What would the rights be worth now if the Plant were to agree to release the rights?

As a result of a settlement agreement in 1998 between the City of San Jose and the McCarthy property owners, the City purchased a 50-year deed restriction (through 2048) on 140 acres of McCarthy Ranch property, to exclude "odor sensitive uses" (residential, lodging, or other such overnight uses.) The City's purchase also included a 6 acre strip of land located along Coyote Creek, and within 500 feet of the Plant's biosolids drying beds, including a house located on that property. The purchase price for the entire transaction was \$6 million and required the house to be leased back to McCarthy for a term of five years at \$800 per year for use by farm laborers working on McCarthy lands. The \$6 million purchase price was budgeted and paid for out of

Treatment Plant funds. The house is currently planned for demolition at a cost of \$200K due to its unsafe and poor condition. The current property zoning with the deed restrictions, allows the development of uses such as commercial, retail or industrial uses.

The City has not obtained an appraisal of the fair market value of the deed restriction or the 6 acre strip of land. However, the value of the deed restriction to the Plant is more than just the original \$6 million paid, because any valuation must consider the cost impact to the Plant of allowing residential so close to the biosolids drying area, while it is still in operation. The deed restriction was purchased to prevent residential development in such close proximity to the current open air dewatering and drying operation and staff continues to believe that residential use of such property is incompatible with the Plant's interest, as long as the open air operation is in use.

Plant Master Plan work to date indicates that the earliest timeframe for permanently changing the biosolids drying process is 10 to 12 years. Until that time, the Plant would continue to use open air drying for its biosolids and reuse the material as Alternate Daily Cover at the nearby Newby Island Landfill, where the Plant has a contract for reuse for the next 10 years, and it is anticipated that, subject to renegotiation with Newby Island, the Plant could continue with landfill disposal until the landfill closes or regulatory changes prevent use for biosolids as Alternate Daily Cover. It should be noted that if the deed restriction remains in place, the Plant would not need to begin planning to change the biosolids process due to concern with conflicting residential uses for many years.

Current dewatering, drying and disposal of biosolids cost the Plant \$3.5 million/year. The Plant Master Plan project has assumed that open air drying will be phased out over the next 30 years. In response to the request from TPAC members on what it would cost to accommodate the request to release property restrictions sooner than the Master Plan time frame, staff has worked with the Plant Master Plan consultants to develop an alternative approach to discontinue open air dewatering and drying operations in a shorter, three to four year, time frame. This approach, which consists of contracting out the solids dewatering operation, is estimated to cost the Plant \$13 million per year for a period of 10 to 12 years. This approach represents a \$9.5 million per year increase in biosolids processing and reuse. The cost to the Tributary agencies would be in proportion to their O&M cost share agreement. It should also be noted that this would be an interim solution that has a life expectancy of 12 years. The Plant Master Plan consultants have given initial estimates of over \$500 million in capital costs alone to convert to a permanent alternative biosolids processing and disposal technology, with the earliest time frame for completing such conversion being 10 to 12 years.

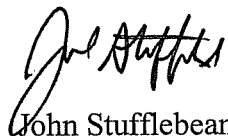
Question 3: What is the impact on the water recycling project that we are trying to get done, if we try to move forward now with discontinuing the solar drying operation at the same time? Does there need to be prioritization, or can we do both? What are the potential rate increases associated with doing these projects separately at the same time?

As indicated above, the Plant Master Plan project has assumed that open air drying will be phased out over the next 30 years. Given that biosolids technologies are still evolving and many

treatment plants in the Bay area and nation are facing significant and costly decisions regarding biosolids treatment and reuse options, a final cost analysis is not yet available for what future technologies may be needed. The current estimate for discontinuing open air solar drying is over \$500 million in capital costs alone with significant increases in operating costs. Pilot testing will be needed in order to determine the most efficient and cost-effective treatment technologies. Based on the current operations (4 year cycle in the drying beds), need for environmental review of alternatives, need for pilot testing and the significant cost, it will take a minimum of 10 to 12 years to discontinue solar drying. Acceleration of the project would incur the costs described above to accomplish discontinuation of the open air drying operation sooner and therefore result in higher operations and maintenance costs sooner.

The funding for the Plant's share of the Advanced Water Treatment Project of \$11 million has been allocated in the Plant's existing 5-year CIP. A new project to discontinue open air drying sooner than completion of the Plant Master Plan would need to be prioritized within the ongoing needs. Although San Jose does not set the sewer rates for the tributary agencies, the potential rate impact of the new project on San Jose rate payers would be significant and it is assumed the same would be true for the tributary agencies.

Staff will be prepared to respond to questions and concerns at the TPAC meeting on December 10, 2009. The City's Attorney Office will be verbally answering the legal questions on which the Committee requested information. For further information, please contact Dale Ihrke, Deputy Director, at 945-5198.



John Stufflebean

Director, Environmental Services