

**UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
ENVIRONMENTAL FINANCIAL ADVISORY BOARD**

January 10, 2005

Mr. Stephen L. Johnson
Deputy Administrator
United States Environmental Protection Agency
1200 Pennsylvania Avenue, NW
Washington, DC 20460

Re: Innovations in Watershed Financing

Dear Mr. Johnson:

The Environmental Financial Advisory Board (EFAB), through its Non-Point Source Financing Workgroup, has been looking at innovative ways to finance the wide variety of improvements needed to restore watershed health. We have undertaken this project based on our conclusion that financing infrastructure and related natural resources projects to improve and restore watershed health presents a major challenge for EPA, the states, municipalities, and watershed management groups. We believe that there is a huge potential for maximizing available financing for watershed management by informing and training watershed managers, coordinators and groups to overcome the multiple financing challenges they face in getting coordinated projects underway.

Since the early 1990s, the EPA's Environmental Finance Team (EFT) in the Office of the Chief Financial Officer has explored ways to encourage innovative and effective financing of important environmental projects. In the course of EFAB's recent review of ongoing activities, we became aware of the Office of Water's recent creation of the Sustainable Finance Team in the Office of Wetlands, Oceans and Watersheds (OWOW). The Team's charter is broad enough to encompass most of the concerns that EFAB has identified to meet the challenge and potential noted above. We have reviewed the Team's ambitious and well-targeted work plan, which gives EPA an excellent start on implementing the goal of assisting watershed groups and managers to increase their knowledge and use of all available financing tools.

We would like to urge you to continue to support and, in certain areas, expand work in the area of non-point source financing, including the work of OWOW's Sustainable Finance Team. For its part, EFAB is willing to assist and supplement the work of the Team and others with financial expertise and other contributions.

In addition to the excellent work they are already undertaking, there are a few areas where we would like to see the Agency and its Sustainable Finance Team focus its efforts, with appropriate contributions from EFAB's Non-Point Source Workgroup and other experts in the area, including the EPA-supported, university-based, Environmental Finance Center Network (EFCN). These include:

- a. Continue to develop a new paradigm for watershed-based finance that moves from a limited grant-funded approach to a portfolio strategy that builds partnerships and targets public funds, private financing and other resource contributions from a range of potential sources. The Team has properly emphasized leveraging financing and funding at local, regional, state levels, i.e., government programs, business investment decisions, bank loans. A roundtable involving representatives from states, localities, financial institutions, businesses, nonprofits and others to explore the full range of possible financing options and partnerships would be a good beginning. EFAB is considering convening such a roundtable, and will work with the Office of Water and the Office of the Chief Financial Officer to help stage and facilitate this effort.
- b. Expand training for watershed groups, managers and coordinators in the use of innovative financing and funding tools and of local resources and networks to increase financing and funding options. The greatest sources of innovation in assembling a portfolio of nontraditional, nongovernmental and leveraged financing are likely to be at the watershed level. Increasing the capacity of watershed groups and managers to identify and develop these sources will be crucial to long-term success. The EFCs and others are working on this issue, and in Region 10, for example, the EFC's Plan2Fund watershed financing tool and Directory of Watershed Resources represent two excellent foundations for much-needed training. These are tools that not only help watershed groups do the right things, but also make the best use of the limited time that volunteers at the local level can commit to meeting local watershed goals. Existing training capacity through the Association of State and Interstate Water Pollution Control Administrators (ASWIPCA), the Council of Infrastructure Financing Authorities (CIFA) and other groups should be utilized and expanded.
- c. Develop additional case studies to provide practical experiences and lessons learned for watershed managers. The EFCs and other university watershed and finance centers should be asked to contribute case studies to an EPA database.
- d. A complementary approach you may want to consider is to encourage or require recipients of EPA watershed grants to receive training in financing tools and approaches like the EPA Watershed Academy distance learning module on watershed financing or other learning tools.

EFAB believes that these approaches are well in line with Enlibra principles, such as putting markets before mandates, recognizing true benefits and costs, and pursuing solutions that transcend political boundaries. Watershed financing offers the kind of challenge where Enlibra principles can work, and the EFAB/EFCN/EFT team can add value to the efforts of the Agency and its Sustainable Finance Team in this regard.

The Board thanks you for the opportunity to provide our comments and recommendations to you. We hope they will promote activities that will support the vital work of watershed groups and managers in restoring and enhancing the nations water quality.

Sincerely,

Lyons Gray, Chair
Environmental Financial Advisory Board

A. Stanley Meiburg
Executive Director

cc: Charles E. Johnson, Chief Financial Officer
Benjamin H. Grumbles, Acting Assistant Administrator, OW
Diane Regas, Director, OWOW

March 15, 2005

Lyons Gray, Chair
A. Stanley Meiburg, Executive Director
U.S. Environmental Protection Agency
Environmental Finance Advisory Board
Washington, D.C. 20460

Dear Mr. Gray and Mr. Meiburg:

Thank you for your letter of January 10, 2005, to the Environmental Protection Agency (EPA), regarding innovations in watershed financing. I appreciate the Environmental Finance Advisory Board's (EFAB) Non-Point Source Financing Workgroup's efforts to foster innovative watershed finance mechanisms. I also applaud EFAB's efforts to enhance collaboration among EPA's environmental finance efforts, including the Office of the Chief Financial Officer's (OCFO) Environmental Finance Program and Environmental Finance Center (EFC) Network and the Office of Wetlands, Oceans, and Watersheds' (OWOW) Sustainable Finance Team. We plan to continue our investments in the area of innovative watershed finance and welcome your assistance in these efforts.

Before turning to your recommendations, I want to express EPA's continued commitment to developing innovative mechanisms to fund watershed protection and restoration. As you note, EPA has taken numerous steps to address this challenge, such as establishing OCFO's Environmental Finance Program and OWOW's Sustainable Finance Team. These groups build the capacity of watershed organizations to develop innovative finance mechanisms by conducting finance workshops, developing funding databases, and producing finance planning tools. EPA also continues its investment in the Clean Water and Drinking Water State Revolving Funds. In recent years, the Clean Water and Drinking Water State Revolving Fund (CWSRF) program has provided about \$4 billion annually to fund water quality protection projects for wastewater treatment, non-point source pollution control, and watershed management. This funding has spurred numerous watershed finance innovations, such as the Ohio EPA's use of CWSRF to support both point and non-point source projects by offering communities low interest rate loans for wastewater treatment plant improvements if the communities also sponsor projects that protect or restore water resources. That said, I also agree that more needs to be done to ensure that adequate resources are available to support effective watershed management.

With regard to your specific recommendations, my responses follow.

- *Recommendation #1: Sponsor a roundtable involving states, localities, financial institutions, businesses, non-profits, and others to explore the full range of possible financing options.*

I believe that such an event would be beneficial if it is well-focused, creates clear and realistic action items that participating entities can pursue, and provides effective mechanisms for disseminating the results to watershed organizations. I believe the focus should be on three themes: diversifying funding options, utilizing private sources of funding, and building watershed organizations business strategies. EPA will explore the availability of funds to sponsor such an event.

- *Recommendation #2: Expand training for watershed groups and others in the use of innovative financing and funding tools and of local resources and networks to increase financing and funding options. Use the existing training capacity of the Association of State and Interstate Water Pollution Control Administrators (ASIWPCA) and others to conduct such training.*

EPA agrees that finance training is a key ingredient to fostering innovative watershed finance. The Agency's State Revolving Loan Fund programs provide continuous training to the States on creative uses of this funding source, and EPA has conducted finance training for all of the 28 National Estuary Programs. Additional watershed finance training is needed, however, and EPA is taking steps to meet this need. OWOW's Sustainable Finance Team is developing an on-line watershed finance training module to help watershed organizations learn about the basic steps involved in watershed finance planning, diversifying their funding sources, and obtaining private funding. The Sustainable Finance Team will also conduct workshops in Maryland, Pennsylvania, Virginia, and West Virginia on innovative approaches to funding non-point source projects.

Still, given that thousands of watershed organizations exist and that many of them are struggling to fund local watershed projects, EPA agrees that even more finance training would be beneficial. To maximize its impact, such training should be in the form of "train-the-trainer" style workshops that enable participants (e.g., extension agents and other trainers) to learn about innovative watershed funding tools and tailor this information to fit their particular audiences.

- *Recommendation #3: Develop additional case studies to provide watershed groups with finance lessons learned. Solicit the EFCs and other university watershed and finance centers to contribute case study materials.*

EPA's Environmental Finance and State Revolving Loan Fund Programs have developed numerous case studies that provide watershed organizations with innovative watershed finance

tools. In addition, OWOW's Sustainable Watershed Finance Team is developing additional innovative watershed finance case studies. We welcome your assistance in developing these case studies and identifying additional universities and finance centers that are interested in contributing to this effort.

- *Recommendation #4: Encourage or require recipients of EPA watershed grants to complete watershed finance training, such as EPA's Watershed Academy finance module.*

I believe this idea has merit. To help ensure that our grantees continue to succeed in the protection and restoration of watersheds, it is essential that they develop long-term financial strategies. Requiring finance training could be one way to facilitate their long-term financial strategies.

As we move into the next level of innovative watershed finance, please know that EPA remains committed to providing innovative finance tools to watershed organizations. Our commitment to watershed groups helps alleviate their financial challenges and enable them to better protect their watershed. We look forward to collaborating with EFAB on a range of approaches that will ensure even greater progress in the coming years.

Thank you again for your letter. I welcome any additional thoughts about my responses to your recommendations or EPA's role in fostering sustainable watershed financing. If you have any questions, please contact me or have your staff call Diane C. Regas, Director, Office of Wetlands, Oceans and Watersheds at (202)566-1146.

Sincerely,

Original signed by Benjamin H. Grumbles

Benjamin H. Grumbles
Assistant Administrator