

Date of Hearing: April 14, 2026

ASSEMBLY COMMITTEE ON ENVIRONMENTAL SAFETY AND TOXIC MATERIALS

Damon Connolly, Chair

AB 2777 (Committee on Environmental Safety and Toxic Materials) – As Amended March 26, 2026

SUBJECT: State Water Pollution Control Revolving Fund program: loans: outdoor eating areas: water reuse

SUMMARY: Authorizes the State Water Resources Control Board (State Water Board), when administering loans under the Clean Water State Revolving Fund (CWSRF), to assess a fee instead of interest (also known as fee in lieu of interest) for financial assistance services rendered under the CWSRF. Makes a technical change to recently enacted legislation dealing with recycled water. Specifically, **this bill:**

- 1) States the intent of the Legislature to provide the State Water Board with the authority to offer larger below-market rate loans that will help reinforce the long-term solvency of the fund and support affordable recycled water, wastewater, and water quality infrastructure in California.
- 2) States the intent of the Legislature that when the State Water Board adopts amendments to the Clean Water State Revolving Fund (CWSRF) policy to implement this law, the State Water Board will collaborate with stakeholders and take steps to ensure projects receiving higher interest rates incur other benefits not offered to projects receiving the lowest offered rate.
- 3) Authorizes the State Water Board, when administering loans under the CWSRF to assess a fee instead of interest for financial assistance services rendered under the CWSRF.
- 4) Requires the loans issued by the State Water Board under the CWSRF to be made below market interest rates.
- 5) Defines "incidental runoff" as unintended amounts (volume) of runoff, such as unintended, minimal overspray from sprinklers that escapes the area of intended use. Water leaving an intended use area is not considered incidental if it is part of the facility or system design, if it is due to excessive application, if it is due to intentional overflow or application, or if it is due to negligence.
- 6) Makes other technical and conforming changes.

EXISTING LAW:

- 1) Declares the intent of the Legislature, that because the federal Clean Water Act (CWA) (33 U.S.C. Sec. 1251 et seq.) provides for establishment of a perpetual water pollution control revolving loan fund, which will be partially capitalized by federal contributions, it is in the interest of people of the state, in order to ensure full participation by the state under the federal CWA, to enact laws to authorize the state to establish and implement a state/federal water pollution control revolving fund in accordance with federal provisions, requirements, and limitations. (Water Code (WC) § 13475.)

- 2) Creates the Clean Water State Revolving Fund in the State Treasury and designates the State Water Board as the state agency responsible for administering the CWSRF. (WC § 13477)
- 3) Establishes requirements for what funds could be deposited into the CWSRF and authorizes the State Water Board to assess an annual charge for financial assistance services rendered not to exceed one percent of the financial assistance balance. (WC § 13477.5)
- 4) Establishes criteria for the uses of moneys in the CWSRF including that the loans are made at or below market interest rates. (WC § 13480)
- 5) Requires the State Water Board to establish uniform statewide recycling criteria for each varying type of use of recycled water where the use involves the protection of public health. (WC § 13521)
- 6) Prohibits a person or public agency, including a state agency, city, county, city and county, district, or any other political subdivision of the state, from using potable water for nonpotable uses, including cemeteries, golf courses, parks, highway landscaped areas, and industrial and irrigation uses if suitable recycled water is available. (WC § 13551)
- 7) Defines "incidental runoff" as unintended amounts (volume) of runoff, such as unintended, minimal overspray from sprinklers that escapes the area of intended use. Water leaving an intended use area is not considered incidental if it is part of the facility or system design, if it is due to excessive application, if it is due to intentional overflow or application, or if it is due to negligence. (California Code of Regulations Title 23, Division 3, Chapter 3.5, Article 3, § 995)

FISCAL EFFECT: Unknown.

COMMENTS:

Need for the bill: This bill is designed to make technical, yet substantive changes to water quality law. Specifically, this bill will provide the State Water Board flexibility when administering the CWSRF at no additional cost to water agencies, with the goal of stabilizing and potentially increasing the resources available within the CWSRF. Additionally, AB 2777 makes a technical clarification to recently enacted legislation dealing with water recycling.

Clean Water State Revolving Fund (CWSRF): The federal CWA established the CWSRF program to finance the protection and improvement of water quality. Many of the projects funded by the CWSRF program address wastewater discharge violations or enforcement orders issued by the Regional Water Quality Control Boards.

California's CWSRF program operates pursuant to an operating agreement between the State Water Board and the United States Environmental Protection Agency (U.S. EPA) Region 9. The CWSRF functions as an environmental infrastructure bank capitalized by federal and state funds – providing a sustainable source of funds for water quality protection and improvement. The CWSRF's capital and its earnings are used to provide financial assistance to a wide variety of water quality projects. States can target specific water quality problems, offer a variety of financing options, and customize terms to meet their water quality needs. Financing options include loans, refinancing debt, purchasing, or guaranteeing local debt, and purchasing bond

insurance. Interest rates must be below the market rate. The repayment period is generally the lesser of 30 years or the expected useful life of the financed asset. Since 2009, federal CWSRF appropriations and California law have also authorized grants, negative interest rates, and principal forgiveness (PF) on a limited basis.

California's CWSRF has grown since financing its first project in 1989 and has executed more than \$14.7 billion in financial assistance agreements with over 500 unique recipients. The program has funded a broad range of projects. The CWSRF can finance publicly owned treatment facilities, nonpoint source projects, and estuary projects. The most common types of application received are for wastewater treatment plants and sewer systems. Funding recipients are government entities, tribes, or non-profit organizations responsible for these projects. The interest rate is half of the most recent General Obligation Bond rate. The most common construction financing term is 30 years. The CWSRF has significant financial assets and is capable of financing projects from less than \$1 million to more than \$100 million.

When the CWSRF loans out funds, the recipient pays back both principal and interest. Currently the principal is deposited in the CWSRF and a portion of the interest is also deposited in the CWSRF.

This bill: Replaces the interest that is attached to a loan from the CWSRF, with a fee (also known as a fee in lieu of interest). The fee will be set at an amount no greater than what the interest would have been. However, this change will provide the State Water Board with flexibility in administering the CWSRF and the possibility that more funds could be deposited in the CWSRF than allowed under current law.

Recent enacted legislation dealing with recycled water: SB 31 (McNerney, Chapter 736, Statutes of 2025) clarified that the use of recycled water is authorized in various applications and under specified circumstances. This bill provided that water discharged from a decorative body of water during a storm event is not an unauthorized discharge if recycled water was used to restore levels due to evaporation. Additionally, the bill authorized incidental amounts of spray, mist or runoff to enter outdoor eating areas of parks and open spaces when irrigated with disinfected tertiary treated recycled water that complies with existing regulations governing the use of recycled water. However, during implementation of SB 31, questions have arisen regarding the definition of incidental runoff.

This bill: In order to assist with the implementation of SB 31, AB 2777 defines "incidental runoff" as unintended amounts (volume) of runoff, such as unintended, minimal overspray from sprinklers that escapes the area of intended use. Water leaving an intended use area is not considered incidental if it is part of the facility or system design, if it is due to excessive application, if it is due to intentional overflow or application, or if it is due to negligence. This definition currently exists in the California Code of Regulations (California Code of Regulations Title 23, Division 3, Chapter 3.5, Article 3, § 995)

Arguments in support: According to the California Association of Sanitation Agencies and WasteReuse California, along with a number of other water agencies,

"This bill would provide additional flexibility for the State Water Resources Control Board to modernize the Clean Water State Revolving Fund (CWSRF) loan program.

The CWSRF is a flagship state infrastructure program that provides low interest loans and principal forgiveness grants (for disadvantaged communities) to public agencies for water quality and recycled water projects. In partnership with the Federal SRF program, the loan program has served as a low-cost alternative to commercial bonds since its inception in the 1980s, protecting California ratepayers by keeping critical infrastructure and water supply reliability project costs as low as possible.

AB 2777 would provide the Water Board with more flexibility to stabilize the loan capacity over time by adjusting interest rates for large borrowers to account for the long-term solvency of the fund while maintaining appealing, below market-rate loan options for water infrastructure projects.

Additionally, AB 2777 would define in code, the term "incidental runoff" that was included in SB 31 (2025, McNerney). A definition was inadvertently omitted from SB 31. The language included in AB 2777 is the exact language that was vetted through a stakeholder process at the Department of Water Resources in 2024/25 and is included in Title 23 of the California Code of Regulations. By including this definition in AB 2777, a costly proceeding does not need to be initiated at the State Water Resources Control Board. Because the definition was robustly discussed in an open and public form very recently, we are confident the language as received due consideration."

Arguments in opposition: None on file.

Related legislation:

SB 31 (McNerney, Chapter 736, Statutes of 2025). Clarifies that the use of recycled water is authorized in various applications and under specified circumstances.

REGISTERED SUPPORT / OPPOSITION:

Support

California Association of Sanitation Agencies
California Municipal Utilities Association
Central Contra Costa Sanitary District
City of Roseville
Clean Water SoCal
Dublin San Ramon Services District
Elsinore Valley Municipal Water District
Inland Empire Utilities Agency
Las Virgenes Municipal Water District
Los Angeles County Sanitation Districts
Orange County Sanitation District
Sacramento Area Sewer District
WaterUse California
West Basin Municipal Water District
Western Municipal Water District

Opposition

None on file.

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