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Santa Margarita Water District

September 18, 2024

The Honorable Maria Hernandez
Presiding Judge of the Superior Court of California
700 Civic Center Drive West
Santa Ana, CA 92701

SUBJECT: Response to Orange County Grand Jury Report, “Emerging Opportunities in South County Water/Wastewater Systems”

Dear Judge Hernandez:

Per your request, and in accordance with *Penal Code* 933.05(a) and (b), please find Santa Margarita Water District’s (SMWD) response to the subject report as approved by its Board of Directors.

If you have any questions, please contact Robert Grantham, General Manager, via email at robertg@smwd.com

Sincerely,

Sandra F. Jacobs

SAUNDRA F. JACOBS
President, Santa Margarita Water District

Enclosure – Response to Findings/Recommendations

CC: Orange County Grand Jury
Board of Directors, Santa Margarita Water District
Robert Grantham, General Manager, SMWD
Don Bunts, Deputy General Manager, SMWD

Santa Margarita Water District
Responses to Findings and Recommendations
“Emerging Opportunities in South County Water/Wastewater Systems”

On June 21, 2024, the Grand Jury released a report entitled “Emerging Opportunities in South County Water/Wastewater Systems.” This report directed responses to the Findings and Recommendations from the Santa Margarita Water District.

SUMMARY RESPONSE STATEMENT:

The Santa Margarita Water District (SMWD) Board of Directors and staff are very proud of what we have accomplished on behalf of the residences and businesses within the City of San Juan Capistrano (City). As the City leadership recognized, the City did not maintain the system to achieve public health and safety level of service goals — replacing 100-year-old infrastructure; addressing critical fire flow deficiencies; and producing local ground water in order to mitigate great impacts to customers.

Our responses below address the following:

1. When establishing rates, SMWD and all municipal water and wastewater agencies are subject to the State of California Constitution and Proposition 218 requirements.
2. SMWD conducted extensive due diligence and implemented a comprehensive public outreach process prior to the annexation.
3. Any regional process to evaluate consolidations in South Orange County should include all affected agencies.
4. As Local Agency Formation Commission (LAFCO) has indicated in their response to your Report, they do not have jurisdiction over joint powers authorities. However, the SMWD Board of Directors is pleased with the progress the region has made thus far in resolving regional issues at South Orange County Water Authority (SOCWA).

Summation: Below is our general response to your reference of inadequate transparency and due diligence and highlights the extensive pre-annexation activities undertaken by SMWD.

Response: We believe there are many mischaracterizations included in the report. SMWD spent over \$200,000 on engineering consultants as part of its due diligence. The District also relied on good faith that the City of San Juan Capistrano (City) adequately disclosed system deficiencies. Unlike the acquisition of a privately held utility through eminent domain, this was a public agency with engineering staff with working knowledge of the system. With respect to transparency, the District spent over \$50,000 on public outreach prior to the annexation as well as participated in roughly 50 community events and meetings over a two year period.

Finally, SMWD was aware of the lack of adequate fire protection within the City's system. Consequently, SMWD made immediate investments in excess of \$15 million dollars. This was a significant driver of the need for rate increases. Under California law cost recovery must be apportioned based on benefit.

SMWD responded to the rate increase concerns by sending out required notices to new Improvement District (ID) 9 ratepayers and met with those severely impacted. The proposed rate increases were publicized by local media, leading to protests from some affected ratepayers. At SMWD's July 12, 2023, public hearing on proposed rates, SMWD staff highlighted the City's deferred maintenance of infrastructure, and the lack of rate increases since July 2018. Specifically, the City's water system severely lacking fire flow capacity, which was identified as part of SMWD's due diligence effort prior to the annexation. The City's existing rate structure did not account for the difference in fire flow needs between different customers. For example, a single-family home requires 24,000 gallons of water stored per dwelling in case of a fire. A commercial property can require between 720,000 gallons and 1.8 million gallons, depending on the type of property. Protesting ratepayers claimed the proposed rate hikes were unjust. Our legal counsel disagrees with the protesting ratepayers.

FINDINGS AND RESPONSES:

Finding F1 - San Juan Capistrano's deferred maintenance of the water/wastewater utility resulted in the need to transition the facility to a larger water provider to allow more efficient management and maintenance of the infrastructure.

Response: SMWD agrees with this finding.

Finding F2 - The SMWD proposed rate increase severely impacted San Juan Capistrano's non-residential customers and led to protests of unfairness and negative attention from the local media.

Response: SMWD strongly disagrees with this finding, and we consider the phrase "led to protest" misleading, considering SMWD only received 26 protest letters out of approximately 70,000 accounts. Additionally, Finding F2 fails to consider the legal requirements imposed on municipal water agencies when establishing rates by Article XIII D of the California Constitution. The California Constitution requires agencies to recover costs proportionate to the benefit received and limits the ability to adjust rates in order to mitigate impacts to a specific customer class. Nevertheless, within the limits of the law, the District will strive to attenuate rate increases experienced by customers within the annexed entity to the degree legal.

Finding F3 - SOCWA's member agencies have widely diverse populations, requirements, and revenues. This has led to conflicts over governance, facility operation, and control, affecting the evolving potential for wastewater reuse.

Response: SMWD agrees with this finding.

Finding F4 - There is currently no unified strategy for the future of water/wastewater provision in South Orange County.

Response: SMWD generally agrees with this finding. However, a process is currently underway to reduce the membership at SOCWA, which could help to resolve some of the historic regional challenges.

RECOMMENDATIONS AND RESPONSES:

Recommendation R1 – The OCGJ recommends that by January 1, 2025, LAFCO studies a policy of conducting a post-consolidation agency review to be held within 24 months of agency reorganizations to determine their overall impact on the public. (F1, F2)

Response: SMWD agrees with this finding.

Recommendation R2 - The OCGJ recommends that by January 1, 2025, LAFCO form a task force comprising representatives of affected water agencies to study the transformation of SOCWA and prepare a report on the future of water/wastewater in South Orange County.

Response: SMWD is not listed under this recommendation but should be listed as a participant in any future process. We believe this to merely be a typographical oversight.