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SUBJECT: MWDOC's Comments on OCWD Municipal Service Review (MSR 23-06) and Sphere of Influence (SOI 23-06) Update, Public Review Draft

Dear Ms. Emery:

The Municipal Water District of Orange County (MWDOC) appreciates the opportunity to provide comments on the Municipal Service Review (MSR 23-06) and Sphere of Influence (SOI 23-06) Update for the Orange County Water District (OCWD), including a Feasibility Analysis of the Potential Consolidation of OCWD and MWDOC, Public Review Draft (Report)¹ dated November 15, 2024. After carefully reviewing the Report, particularly regarding the feasibility study of potential consolidation between MWDOC and OCWD, we have identified several aspects of the analysis that warrant your Commission's attention, analysis, and consideration.

EXECUTIVE SUMMARY

After a thorough analysis of the MSR and SOI Public Review Draft, MWDOC has identified significant concerns that call into question the feasibility and benefits of the proposed consolidation. Our detailed review reveals fundamental flaws in the financial analysis, serious governance concerns, and a lack of demonstrable water management benefits for Orange County. The projected cost savings appear to be significantly overstated, while transition costs and operational risks are understated or omitted entirely. Furthermore, the study fails to adequately consider less disruptive alternatives that could achieve many of the stated objectives through enhanced collaboration between the existing agencies.

This response outlines five critical themes that warrant careful consideration: (1) Flawed financial analysis, overstated benefits, and underestimated transition costs; (2) Significant governance and representation concerns that could diminish local control; (3) Absence of clear water management benefits for Orange County; (4) Potential unintended consequences that could harm ratepayers; and (5) Disproportionate impact on MWDOC and the non-basin agencies (South County cities and agencies, and the cities of Brea and La Habra).

¹ Public Review Draft, Municipal Service Review (MSR 22-06) and Sphere of Influence Review (SOI 23-06) for the Orange County Water District (<https://oclafco.org/wp-content/uploads/2024/11/OCWD-Public-Review-Draft-MSR.pdf>)

MWDOC firmly believes this Report relies on flawed data, superficial assumptions, and insufficient depth of research to support such a significant reorganization of Orange County's water management structure.

By design, **MWDOC and OCWD have different governing acts because each agency was established and authorized to serve separate and distinct functions within the water community.** As the Report highlights, consolidating the two agencies would be challenging, time-consuming, and costly. Further, the most recent MSR of each agency, MWDOC (MSR 20-09)² and OCWD (MSR 23-06),³ identified no deficiencies or significant operational issues. Determination 3 of each MSR stated that each agency is adequately prepared to provide its member agencies with public services within its authorization. Thus, this consolidation feasibility study appears to be a solution in search of a problem.

OVERARCHING OBSERVATION & CLARIFICATION OF REPORT INACCURACIES

The Report **does not** provide compelling evidence that consolidation offers additional benefits to the county other than opportunities for further collaboration, which the Report notes are “qualitative and subjective.” In addition, the comparative financial analysis included in the Report is overly simplistic and contains erroneous assumptions that appear to overstate the estimated cost savings from consolidation. The scope of the study is also very narrow. It lacks a “deep dive” into the full range of issues and consequences of potential consolidation that OCWD appeared to request in its October 4, 2022, application to LAFCO.⁴

Often, the study relies on claims and conclusions that are unsubstantiated by evidence and examples or based on erroneous data and assumptions. For instance, the Report incorrectly asserts that OCWD is the largest purchaser of imported water when, in fact, several South Orange County districts each have exceeded the amount purchased by OCWD over the past three years.⁵ Moreover, OCWD has not purchased any water in the last two years⁶ and has publicly stated that the agency has no plan to purchase imported water from MWDOC in the foreseeable future.

The study contains several critical methodological flaws that suggest support for a predetermined outcome rather than an objective analysis. It is heavily reliant upon the pro-consolidation 2022 Grand Jury report,⁷ while giving minimal, if any, weight to similar Grand Jury analyses done in 1994 (before the incorporation of the cities of Laguna Woods, Rancho Santa Margarita, and Aliso Viejo) and 2013.⁸ These reports concluded that MWDOC and OCWD have vastly different water management roles and responsibilities and should remain separate.

Claims about improved coordination and representation are unsupported by concrete evidence or specific examples in which lack of coordination has resulted in demonstrable adverse outcomes. Instead, the analysis relies heavily on anecdotal conclusions rather than quantitative data to support assertions about

² **Page 45.** Final Municipal Service Review (MSR 20-09) and Sphere of Influence Review (SOI 20-10) for the Municipal Water District of Orange County (https://oclafco.org/wp-content/uploads/2021/10/MWDOC_Final-MSR-20-09.pdf)

³ **Page 48.** Public Review Draft, Municipal Service Review (MSR 22-06) and Sphere of Influence Review (SOI 23-06) for the Orange County Water District (<https://oclafco.org/wp-content/uploads/2024/11/OCWD-Public-Review-Draft-MSR.pdf>)

⁴ **Page 11.** Orange County Local Agency Formation Commission: Active Applications (<https://oclafco.org/how/active-applications/>)

⁵ **Page 21.** Public Review Draft, Municipal Service Review (MSR 22-06) and Sphere of Influence Review (SOI 23-06) for the Orange County Water District (<https://oclafco.org/wp-content/uploads/2024/11/OCWD-Public-Review-Draft-MSR.pdf>)

⁶ Calendar years 2023 and 2024.

⁷ “Orange County Water Sustainability: Who Cares?” Orange County Grand Jury 2012-2013 (<https://www.ocgrandjury.org/sites/jury/files/2023-07/OCGJOC-Water061913.pdf>)

⁸ “Water in Orange County Needs One Voice.” Orange County Grand Jury 2021-2022 (https://www.ocgrandjury.org/sites/jury/files/2023-06/2022-06-22_Water_in_Orange_County_Needs_One_Voice.pdf)

the potential benefits of consolidation. The Report lacks critical elements necessary for informed decision-making, such as a detailed implementation timeline or transition plan, sufficient analysis of service disruption risks during the transition, a complete analysis of governance and representation impacts, consideration of improved water resource benefits, adequate assessment of long-term liabilities, and stress testing of financial projections.

Finally, the Report fails to adequately explore less disruptive alternatives to a potential consolidation. Many of the cited benefits - including unified advocacy and operational efficiencies - could be achieved through improved collaboration and coordination while maintaining essential checks and balances in the current two-agency structure.

To be both thorough and concise, we have organized our comments into five key themes.

THEME 1: FLAWED FINANCIAL ANALYSIS AND OVERSTATED BENEFITS

The financial analysis contains several significant oversimplifications and questionable assumptions that raise questions regarding the projected savings of \$3.98 to \$6.39 million annually. The study bases projections on just three years of historical data. It fails to adequately reflect long-term trends or future needs while simultaneously overstating potential cost savings through unrealistic assumptions about operational efficiencies and staff reductions.

The Report significantly overestimates potential cost savings from these suggested staff reductions.⁹ It is erroneous to simply assume positions with similar titles can be eliminated without accounting for specialized duties and expertise required for groundwater versus imported water management. For example, the Director of Engineering for MWDOC and OCWD have functions and responsibilities that are dramatically different from each other. Eliminating either position would result in a potential loss of specialized expertise critical to operations, cause operational impacts of these reductions on service delivery, and add integration challenges of merging different operational systems and procedures. Simply eliminating positions with the same title does not reflect the current workload for those positions. Work would still need to be done, and staff resources would be required because the Successor Agency would have broader responsibilities and an increased scope and business systems to maintain. As such, and without a detailed workload analysis, the number of positions the Report assumes could be eliminated under a consolidation appears to be overstated.

The administrative expense reductions are inflated through unrealistic assumptions about operational efficiencies and proportionate reductions in administrative costs based upon the overstated staff reductions. For example, building and maintenance expenses, which the analysis shows are reduced with consolidation, ignore the fact that all building facilities would still be utilized and would continue to need maintenance. The Report also includes reductions in membership and sponsorship costs, legal and professional service fees, training, and other administrative costs that are proportionately based on the overstated reductions in staff; this is not a proper analysis of determining cost savings.

⁹ Page 117, Table 14. Public Review Draft, Municipal Service Review (MSR 22-06) and Sphere of Influence Review (SOI 23-06) for the Orange County Water District (<https://oclafco.org/wp-content/uploads/2024/11/OCWD-Public-Review-Draft-MSR.pdf>)

The Report analysis assumes that the Successor Agency will also achieve cost savings by reducing board seats from 17 to 10 members.¹⁰ The assumption of a 10-member Board is arbitrary and is not supported in the Report by analysis or recommendations regarding a proposed governance structure or considerations relating to balanced Board representation. In fact, under current statute, for the consolidated agency to be a Metropolitan Water District of Southern California (Metropolitan) member agency, it would need to be formed under MWDOC's principal act, the Municipal Water District Act of 1911, versus OCWD's groundwater management act. The Municipal Water District Act only allows for 5, 7, or 11 members, not 10 members, as assumed in the Report.

Another significant error in the Report appears to be the estimated \$2.41 million savings in annual retirement costs shown in Table 16.¹¹ These savings are based upon converting all OCWD's 226 employees from their existing 401(k) defined contribution program to MWDOC's existing CalPERS program and is the only retirement scenario analyzed in the Report that demonstrated significant net savings. However, the inclusion of the \$2.41 million annual savings as a benefit of consolidation is specious and should be removed from the Report. Specifically, as previously noted, this scenario calls for OCWD's employees to convert to CalPERS while MWDOC's employees remain in CalPERS. The study fails to disclose that the vast majority of these **savings could be achieved today** by OCWD independently converting its employees to CalPERS **without consolidation**. Although there may be some minor savings from the disputed staff reductions through consolidation, this would be an inconsequentially small portion of the \$2.41 million annual savings, making it inappropriate to include this amount in the Report as a benefit of consolidation.

Transition costs, which are a financial impact of consolidation and not a benefit, are acknowledged but unquantified, particularly potential CalPERS termination payment of \$10.4 million to \$26 million (if OCWD's retirement plan option was selected), legal and consulting costs for contract modifications, technology and systems integration expenses, and staff training and reorganization costs. These expenditures would also diminish the overall projected savings listed in the Report.

Lastly, the Report fails to analyze potential impacts on MWDOC's existing revenue structure, member agency relationships, and revenue-generating capabilities; instead, the Report simply combines current revenues without examining how consolidation might affect them. This requires further examination of the recent rate increase trends of both agencies.

The actual cost savings would be far less than projected in the Report and insufficient to justify such a significant reorganization, particularly given the lack of workload analysis to support estimated staff reductions, the significantly overstated retirement plan savings and the unquantified transition costs.

THEME 2: GOVERNANCE AND REPRESENTATION CONCERNS

The Report's treatment of governance challenges reveals critical oversights and a lack of analysis that presents serious legal and practical concerns that cannot be overlooked. For example, current statutes do not allow the Successor Agency to be formed under the OCWD Act and be a Metropolitan member agency. If the Successor Agency was formed under the Municipal Water District Act, it could be a Metropolitan member agency but would need to have OCWD's authorities incorporated, requiring legislation.

¹⁰ Page 118. Public Review Draft, Municipal Service Review (MSR 22-06) and Sphere of Influence Review (SOI 23-06) for the Orange County Water District (<https://oclafco.org/wp-content/uploads/2024/11/OCWD-Public-Review-Draft-MSR.pdf>)

¹¹ Page 125, Table 16. Public Review Draft, Municipal Service Review (MSR 22-06) and Sphere of Influence Review (SOI 23-06) for the Orange County Water District (<https://oclafco.org/wp-content/uploads/2024/11/OCWD-Public-Review-Draft-MSR.pdf>)

Any new Successor Agency would need to have equal populous divisions, whether formed under the Municipal Water District Act or otherwise. The Voting Rights Act of 1965 and related legal principles require that voting districts, including divisions within a Municipal Water District, comply with the principle of equal population to ensure fair representation. OCWD was formed as a groundwater management agency in 1933, and its Board is an artifact hybrid of elected and appointed Board members that do not represent equal populous divisions. For example, OCWD's Fullerton division represents 139,250 people, while its Anaheim division represents 340,512 people. To ensure fair and equitable representation throughout the County, the Successor Agency would need to implement balanced Board divisions. The Report ignores this issue and how it would be resolved.

The Report also does not address how the Successor Agency would vote on various matters, particularly those matters relating to groundwater basin issues, those pertaining to imported water and issues, and items relating to setting the consolidated agency's water rates and charges. **A bifurcated voting system creates an unwieldy and potentially unworkable governance model** where certain Board members would be limited to voting on specific matters. Moreover, disparate voting rights, where some Board members would be disallowed from voting on certain matters, is **completely contrary to the intent of a "unified" countywide Successor Agency**. Finally, the analysis does not address how the Successor Agency would ensure balanced representation among basin and non-basin agencies (i.e., South County cities and agencies, Brea, and La Habra) while protecting their unique needs and interests.

On legislative and policy matters, coordination can currently occur without consolidation. MWDOC and OCWD presently have regularly scheduled joint planning meetings and numerous opportunities exist to meet with, host, and provide briefing materials to legislators and members of Congress. In the joint planning meetings, the agencies have ample opportunities to have "...collaborative, deliberative and action-oriented..." dialogue as recommended in the Report and to jointly formulate positions and legislative requests.

Finally, the Report incorrectly implies that there is "competition" for state and federal funding among MWDOC and OCWD. No examples were given of such competition, nor were there any instances where MWDOC or OCWD may have displaced each other for funding. Moreover, coordination in seeking state and federal funding can be achieved without consolidation and such coordination among MWDOC, OCWD, and their collective member agencies has occurred successfully in the past.

THEME 3: NO CLEAR WATER MANAGEMENT BENEFITS

The study does not demonstrate any meaningful improvements to water resource management in Orange County. In response to this Report, OCWD's Board has adopted a formal position to preserve the "...Groundwater Producers sole access to the Orange County Groundwater Basin..." under a consolidation with MWDOC.¹² As a result, south Orange County, along with the Cities of Brea and La Habra, would realize no emergency supply reliability, drought mitigation or other water resource management benefits from the Orange County groundwater basin. In fact, when consolidation was analyzed in 2006, **OCWD itself concluded that water management would not be improved with consolidation** because the Successor Agency envisioned by OCWD would not allow access to the groundwater basin for south Orange County.

¹² Adopted by the OCWD Board at their December 18 Board Meeting in discussion of their LAFCO comment letter and principles.

Absent access to the groundwater basin or any beneficial utilization thereof, there is no discernible water resource benefit to south Orange County agencies or the cities of La Habra and Brea of being incorporated into a single Successor Agency with potentially diminished Board representation and a reduced focus on the imported water supplies. The Report fails to address these issues and does not identify higher levels of water supply reliability, drought protection, or other water resource or management benefits for the County as a result of consolidation.

THEME 4: UNINTENDED DETRIMENTAL CONSEQUENCES

Several potential negative consequences require further analysis or clarification. The Cortese Knox Hertzberg Act mandates that existing debt and expenditures remain with current constituents in any consolidation, and OCWD has adopted a position that it would not spread its existing debt to the non-basin portions of the county.¹³ Still, the study does not acknowledge or address this issue or how other future costs of a consolidated agency would be distributed to agencies that receive no direct benefit from the groundwater basin (South County cities and agencies, Brea, and La Habra).

The Report also does not address how the Successor Agency's overall operating expenses would be allocated on a county-wide basis or the potential impacts on rates and charges. Similarly, the Report does not address the potential implications of OPEB-related liabilities, other outstanding legal obligations, and their associated future costs, nor does it evaluate the impact of these costs on the existing customers of OCWD and MWDOC in the event of consolidation.

There are also potential detrimental consequences to the County's representation at Metropolitan that were neither analyzed nor disclosed in the Report. Specifically, a successor countywide water agency consolidating OCWD and MWDOC would need to incorporate the territory of Fullerton, Santa Ana, and Anaheim, per the expanded SOI. In doing so, under the current Metropolitan Act, the new consolidated agency could lose seats on the Metropolitan Board. This is because the Metropolitan Act provides one director for each member agency and one additional director for each 5% of the Assessed Valuation (AV) in the Metropolitan service area.

Specifically, in 2024, MWDOC has 16.76% of the AV and has four Metropolitan directors. Fullerton (0.68% of AV), Santa Ana (0.88% of AV), and Anaheim (1.55% of AV) each have one Metropolitan director. Under consolidation, the total AV of the consolidated Successor Agency would be 19.87% of Metropolitan's AV. This would result in only four directors for the Successor Agency with **Orange County risking the loss of three seats on the Metropolitan Board** and the three cities likely to lose both their director representation and sovereignty at Metropolitan.

THEME 5: DISPROPORTIONATE IMPACT ON MWDOC AND NON-BASIN AGENCIES

The analysis in the Report advances a course that would appear to require MWDOC to bear a disproportionate share of the transitional impacts of consolidation. MWDOC would shoulder most of the transition risks and costs while OCWD maintains its revenue base and gains expanded capabilities. The consolidation threatens MWDOC's established and effective Metropolitan Water District representation without clear benefits to offset this loss. The Report fails to justify dismantling MWDOC's successful

¹³ Adopted by the OCWD Board at their December 18 Board Meeting in discussion of their LAFCO comment letter and principles.

operational model and established member agency relationships. MWDOC would take on additional operational complexities and responsibilities without apparent corresponding efficiencies or financial benefits.

As previously noted, without access to the groundwater basin, there is no discernable benefit to South Orange County and the cities of Brea and La Habra by being incorporated into a larger Successor Agency with more divergent interests. Non-basin agencies would experience a dilution in representation on the Successor Agency's board and as previously noted, could have reduced Board representation at Metropolitan. Representation at Metropolitan is particularly important to South County cities and agencies, which receive the vast majority their water supplies through Metropolitan's imported water system.

CONCLUSION

While MWDOC supports exploring opportunities for improved efficiency in water management, this feasibility study does not provide evidence that consolidation would benefit Orange County water suppliers or their customers. A Successor Agency with a bifurcated voting system creates an inefficient governance model without balanced representation among basin and non-basin agencies and the potential for reduced representation for Orange County on the Metropolitan Board.

Importantly, the Report fails to consider consolidation alternatives adequately. Many of the cited benefits - including unified regional, state, and federal advocacy, coordinated grant applications, and operational efficiencies - could be achieved through improved collaboration between the agencies while maintaining the current structure's essential checks and balances.

We recommend that OCWD and MWDOC focus on opportunities to improve service efficiencies and coordination activities for the benefit of all retail water agencies in Orange County. We believe that such an approach will provide far more significant benefits without the risks, governance issues, and consolidation costs. Some examples of these opportunities, including activities that are currently being undertaken, are as follows:

- Increase Coordination and Collaboration on Metropolitan Water District Issues:
 - Coordinated positions on key Metropolitan issues.
 - Joint advocacy for Orange County's interests.
 - Shared strategic planning for imported water management.
 - Inclusive of MWDOC, OCWD, and the Metropolitan Directors representing OCWD's service area (Fullerton, Santa Ana, and Anaheim).
- Enhanced Coordination on Pursuing State and Federal Funding:
 - Joint application development for major funding opportunities.
 - Shared resources for grant writing, administration, and advocacy.
 - Coordinated joint regional project planning and grant funding coordination with MWDOC's and OCWD's member agencies.
- Joint Legislative Advocacy:
 - Combined legislative advocacy efforts and resources where appropriate.
 - Coordinated response to all material regulatory proposals or changes.
 - Joint development of countywide water policy principles and priorities.
- Identify and Pursue Expanded Partnership Opportunities:
 - Joint public education and outreach programs.

- Shared emergency response planning.
- Combined water resources and water use efficiency programs.
- Strengthened Cooperative Opportunities:
 - Shared staffing, technical, and other consultant resources, where appropriate.
 - Coordinated long-term water supply planning on a collaborative countywide basis.

The most recent Municipal Service Reviews (MSR) of each agency, MWDOC (20-09)¹⁴ and OCWD (MSR 23-06),¹⁵ identified no deficiencies or significant operational issues. Determination 3 of each MSR stated that each agency is adequately prepared to provide its member agencies with public services within its authorization. **The consolidation feasibility study appears to be a solution in search of a problem. As such, the MWDOC Board does not see merit or value resulting from consolidation.**

MWDOC remains committed to working constructively with OCWD and all regional partners to ensure reliable water supplies for Orange County and is open to working with OCWD on the collaborative approaches outlined above to further enhance our services. We appreciate your consideration of these comments as you prepare the Final Report and welcome the opportunity to discuss them further.

Sincerely,



Harvey F. De La Torre
General Manager
Municipal Water District of Orange County

cc: LAFCO Commission
MWDOC Board of Directors
OCWD Board of Directors

¹⁴ **Page 45.** Final Municipal Service Review (MSR 20-09) and Sphere of Influence Review (SOI 20-10) for the Municipal Water District of Orange County (https://oclafco.org/wp-content/uploads/2021/10/MWDOC_Final-MSR-20-09.pdf)

¹⁵ **Page 48.** Public Review Draft, Municipal Service Review (MSR 22-06) and Sphere of Influence Review (SOI 23-06) for the Orange County Water District (<https://oclafco.org/wp-content/uploads/2024/11/OCWD-Public-Review-Draft-MSR.pdf>)