


## MEMORANDUM

**TO:** Board of Directors  
Orange County Water District

**FROM:** Joel D. Kuperberg, General Counsel 

**DATE:** December 3, 2014

**FILE NO.:** 022499-0078

**RE:** Issues Relating to District's Legal Authority to Purchase, Store and Sell  
Desalinated Water

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This memorandum responds to the five questions posed on November 21, 2014 by the OCWD Board President, as a follow-up to the November 19, 2014 Board discussion of the upcoming Board of Directors workshop on certain issues relating to the possible purchase by OCWD of desalinated water from the proposed Poseidon desalination plant in Huntington Beach. Based upon our review of the Orange County Water District Act ("OCWD Act") and other applicable laws, the following are our conclusions to the five questions posed by President Dewane:

1. The District has the legal authority to increase the Replenishment Assessment in order to generate the revenue needed to purchase desalinated water from the Poseidon Huntington Beach desalination facility.
2. Subject to certain conditions and findings by the Board of Directors, the District has the legal authority to sell and directly distribute desalinated water to retail agencies within the District's boundaries.
3. It is questionable whether the District has the legal authority to sell desalinated water to agencies outside of OCWD's boundaries (*i.e.*, south Orange County); and, depending upon the facts, the District may have the legal authority to sell desalinated water to MWDOC for resale to agencies outside of the OCWD boundaries.
4. The District has the legal authority to cause desalinated water purchased by certain third parties to be stored within the Orange County Groundwater Basin for subsequent extraction by the party purchasing the desalinated water.
5. The District has the legal authority to purchase desalinated water and percolate the desalinated water into the Orange County Groundwater Basin.

OCWD, like all special districts, and in contrast to cities and counties, is a district of limited powers. As such, the District possesses only those powers expressly enumerated by law, and those implied powers necessary to the exercise of the powers expressly granted by law, *Crawford v. Imperial Irrigation District*, 200 Cal. 318, 334 (1927); *Carlton-Santee Corp. v. Padre Dam Municipal Water District*, 120 Cal.App.3d 14, 23-24 (1981). The only implied powers a district of limited powers possesses are those “essential to the limited, declared powers provided by its enabling act,” *Water Quality Assn. v. County of Santa Barbara*, 44 Cal.App.4<sup>th</sup> 732, 746 (1996); *Turlock Irrigation District v. Hetrick*, 71 Cal.App.4<sup>th</sup> 948, 952-953 (1999). Consistent with these general legal principles, section 2(13) of the OCWD Act provides in pertinent part that the District has the power “to do all acts necessary for the full exercise of the foregoing [i.e., expressly enumerated] powers.” Consequently, OCWD’s power to take action is generally limited to the authority provided by the OCWD Act, or other statutes granting legal authority either to OCWD specifically, or to local governmental agencies generally.

1. The District has the legal authority to increase the Replenishment Assessment in order to generate the revenue needed to purchase desalinated water from the Poseidon Huntington Beach desalination facility.

Section 23 of the OCWD Act provides that the revenues raised by the imposition of the Replenishment Assessment “shall be used to acquire water and to pay the costs of initiating, carrying on, and completing any of the powers, projects and purposes for which this district is organized.” Accordingly, section 23 authorizes the District to use Replenishment Assessment revenues to purchase water.

Section 2(6) provides that, “for the purpose of managing the groundwater basin and managing, replenishing, regulating and protecting the groundwater supplies within the district,” the District has the power to “Appropriate and acquire water and water rights” (subsection (d)), “Purchase and import water into the district,” (subsection (e)), and “Buy and sell water at such rates as shall be determined by the board of directors” (subsection (g)). The OCWD Act does not either enumerate the sources of water that the District may purchase or restrict the District from purchasing certain sources or types of water. Therefore, the District has the legal authority under sections 2(6) and 23 of the OCWD Act to use Replenishment Assessment revenues to purchase desalinated water from the proposed Poseidon project.

2. Subject to certain conditions and findings by the Board of Directors, the District has the legal authority to sell and directly distribute desalinated water to retail agencies within the District’s boundaries.

Pursuant to section 2(6)(g) of the OCWD Act, the District has the legal authority to “. . . sell water at such rates as shall be determined by the board of directors,” so long as the District conducts such water sales “for the purpose of managing the groundwater basin and

managing, replenishing, regulating and protecting the groundwater supplies within the district.” The OCWD Act does not restrict the source or “type” of water that the District may sell. Accordingly, the District may sell and directly distribute desalinated water to agencies within the District’s boundaries so long as the District finds that the sale of the desalinated water will facilitate management of the groundwater basin or the regulation or protection of groundwater supplies within OCWD.

In addition to selling water, OCWD has the authority both to “Provide for the conjunctive use of groundwater and surface water resources within the district area,” and to “Distribute water to persons in exchange for ceasing or reducing groundwater extractions,” OCWD Act sections 2(6)(a), 2(6)(i). Distributing water for conjunctive use purposes, or to reduce groundwater extractions, does not require the explicit finding that must be made in order to “sell water” pursuant to subsection (g) of that statute.

While the OCWD Act would allow the District to sell desalinated water to retail agencies within the boundaries of OCWD, such sales may expose the District to liability under other laws. The sale of desalinated water by OCWD to retail water agencies within the District’s boundaries would constitute a service analogous to wholesale delivery of water. However, the territory within OCWD’s boundaries is also within the wholesale water boundaries of MWDOC, and the provision of desalinated water deliveries by OCWD within MWDOC’s service area for treated imported water service would constitute a “duplication of facilities” under Public Utility Code section 1501, *et seq.*

Public Utility Code section 1505.5 provides that a water agency that provides or extends water service to territory being lawfully served by another agency that has designed and constructed facilities to provide the “same type of service” can be held liable to pay damages equal to the fair market value of the facilities being stranded by the original water agency when the new agency extends its service. Given that desalinated water is indistinguishable from other sources of potable water, it is assumed that the provision of desalinated water service to retail agencies would be “the same type of service” that MWDOC provides when selling imported water to those same retail agencies. Accordingly, unless OCWD reaches an agreement with MWDOC to permit OCWD to sell desalinated water to retail agencies that are within both the OCWD boundaries and the MWDOC service area, OCWD may have exposure for damages under the duplication of service provisions of Public Utility Code section 1501, *et seq.*

3. It is questionable whether the District has the legal authority to sell desalinated water to agencies outside of OCWD's boundaries (i.e., south Orange County); and, depending upon the facts, the District may have the legal authority to sell desalinated water to MWDOC for resale to agencies outside of the OCWD boundaries.

It is questionable whether OCWD has the legal authority to sell water – whether desalinated or otherwise – outside its boundaries. First, the District generally has only limited authority to act outside its boundaries. The OCWD Act expressly authorizes the District to act outside its boundaries in only six instances:

- Section 2(4) authorizes the District to acquire land within or outside its boundaries.
- Section 2(5) authorizes OCWD to construct, acquire, operate and maintain facilities within or outside the District to protect the underground basin or the quality of the District's groundwater supplies.
- Section 2(6)(b) specifies that the District may store water within or outside the District.
- Section 2(6)(d) authorizes OCWD to appropriate and acquire water and water rights within and outside its boundaries.
- Section 2(7) authorizes the District to provide for the protection and enhancement of the environment within and outside the District, in connection with its water activities.
- Section 2(10) provides that the District may exercise the power of eminent domain for right-of-way purposes outside the District boundaries but within the Santa Ana River watershed.

With the exception of these six activities that are specifically authorized outside of the District's boundaries, all of the powers granted by the OCWD Act implicitly must be exercised within the jurisdictional boundaries of the District. Because the OCWD Act does not authorize the District to sell water outside its boundaries, a significant question arises whether OCWD has the authority to do so.

In addition, it is questionable whether the sale of water by OCWD outside its boundaries – even if authorized by the OCWD Act – would satisfy the groundwater management conditions required by the Act. As noted above, while OCWD has the authority under section

2(6)(g) to sell water, that power may only be exercised “for the purpose of managing the groundwater basin and managing, replenishing, regulating and protecting the groundwater supplies within the district.” Assuming that the OCWD Act otherwise allows the District to sell water outside its boundaries, section 2(6)(g) requires that OCWD show that the extraterritorial sale of water would somehow serve the purpose of managing the District’s groundwater basin or managing, regulating or protecting the District’s groundwater supplies.

Further, legislation other than the OCWD Act appears to restrict the District’s power to sell water outside its boundaries. Under Government Code section 56133, an agency may not provide a new or extended service outside its jurisdictional boundaries unless it first obtains written approval from the Local Agency Formation Commission (“LAFCO”). That statute seemingly allows LAFCO to authorize a new or extended extraterritorial service provision only under two circumstances: Pursuant to section 56133(b), LAFCO may authorize new or extended extraterritorial service to lands within the service provider’s sphere of influence, in anticipation of a later annexation of that territory to the service provider. And, under subdivision (c) of that statute, LAFCO may authorize new or extended service to territories outside a service provider’s sphere of influence to respond to “an existing or impending threat to the public health or safety of the residents of the affected territory.” It does not appear that OCWD can meet the conditions in either subdivision (b) or (c) for LAFCO approval of extraterritorial service.

Government Code section 56133(e) sets forth three circumstances under which the new or extended provision of extraterritorial service is not subject to LAFCO approval. First, the statute does not apply to contracts involving two or more public agencies where the public service to be provided “is an alternative to, or substitute for, public services already being provided by an existing public service provider and where the level of service to be provided is consistent with the level of service contemplated by the existing service provider.” This exception appears to cover situations where one service provider voluntarily relinquishes the entirety of its service provision to a new provider. In the instant case, however, OCWD would not be supplanting the wholesale water service being provided by MWDOC to south Orange County. Second, section 56133 does not apply to contracts “for the transfer of non-potable or non-treated water”; in the instant case, however, the desalinated water is treated potable water. Finally, the statute does not apply to agreements providing “surplus water” to agricultural lands and facilities, or for projects that serve conservation purposes or directly support agricultural industries. In the instant case, it is doubtful that OCWD could find the desalinated water to be “surplus,” and it will not be served (in any appreciable amount) for agricultural or conservation purposes. Consequently, it does not appear that OCWD’s proposed sale of desalinated water outside its boundaries either is exempt from, or would qualify for, the LAFCO approval required by Government Code section 56133.

Finally, assuming it could satisfactorily address the extraterritorial sale of desalinated water under the OCWD Act and for the purposes set forth in section 2(6), and obtain approval

for extraterritorial services from LAFCO pursuant to Government Code section 56133, the provision of that service within MWDOC's service area would implicate the "duplication of facilities" provisions of Public Utility Code section 1501, and expose the District to condemnation-like damages under section 1505.5, in the absence of an agreement with or consent from MWDOC. However, if OCWD were to enter into an arrangement to sell desalinated water to south Orange County agencies by selling the water to MWDOC at a point of sale within OCWD's boundaries, and MWDOC then re-sold the water to the south Orange County agencies, the arrangement would avoid most of the legal impediments described above to OCWD directly selling desalinated water to those agencies. The sale of desalinated water through MWDOC would avoid any issue of the OCWD Act limiting most District actions to within the OCWD boundaries, would obviate the need for LAFCO approval and would resolve any concerns regarding OCWD exposure to damages from MWDOC for "duplication of facilities." However, the sale of desalinated water to south Orange County agencies through MWDOC would not resolve the requirement under section 2(6)(g) that the sale of water by OCWD serve the purpose of "managing the groundwater basin and managing, replenishing, regulating and protecting the groundwater supplies within the district. . ."<sup>1</sup>

4. The District has the legal authority to cause desalinated water purchased by certain third parties to be stored within the Orange County Groundwater Basin for subsequent extraction by the party purchasing the desalinated water.

The OCWD Act specifically authorizes the District to enter into agreements with third parties for the third party storage of water within the Orange County Groundwater Basin. Section 2(6)(c) generally authorizes the District to "regulate and control the storage of water and the use of groundwater basin storage space in the groundwater basin. . .," and section 2.1 specifically authorizes OCWD to enter into groundwater storage agreements. Section 2.1(b) provides that groundwater storage by third parties is a secondary use of the Orange County Groundwater Basin, with the use of the basin for the purpose of managing and replenishing the District's groundwater supplies having the highest priority. Section 2.1(c) provides that OCWD may enter into groundwater storage contracts with public and private entities that are located either wholly or partially within OCWD; however, "where the primary benefits accrue to persons or property within the district," OCWD may contract to allow other parties – with the OCWD

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<sup>1</sup> It should be noted that OCWD could also structure the sale of desalinated water by means of water sales to one or more of its producers (e.g., IRWD), for resale by those producers to south Orange County agencies. Such an arrangement would address the OCWD Act restriction on extraterritorial activities and the need for LAFCO approval, but would not resolve either the concern regarding exposure to damages to MWDOC for duplication of facilities, or the requirement that the sale of the water be for the purpose of managing the groundwater basin or managing, replenishing, regulating or protecting the groundwater resources within OCWD.

Act specifically identifying MWD and DWR – to store water within the Orange County Groundwater Basin.

Section 2.1 of the OCWD Act does not contain any restrictions or limitations on the District’s ability to contract for third party storage of water within the groundwater basin, other than requiring that the basin be used for replenishing and managing the District’s groundwater supplies as a first priority (§ 2.1(b)), and the requirement that the District must both consider and protect the quality of the groundwater and reasonable water supply needs of the District when considering groundwater storage agreements and impose such limitations on the quality of water to be stored as is necessary to protect the quality of the groundwater basin (§ 2.1(e)). Section 2.1(d) authorizes the District to waive the imposition of Replenishment Assessments and Basin Equity Assessments on stored water, and does not limit or require any specific terms to be included in a groundwater storage agreement, other than the above-referenced acknowledgment of the water supply needs of the District and the management and replenishment of the basin.

Based on the foregoing, OCWD has the authority to enter into groundwater storage agreements to store desalinated water, but is limited into entering into such contracts with entities other than the District’s producers unless the District can find that the “primary benefits” of the storage arrangement will accrue to persons or property within OCWD.

5. The District has the legal authority to purchase desalinated water and percolate the desalinated water into the Orange County Groundwater Basin.

As noted above, the District has the authority under sections 2(6)(d), (e) and (g) of the OCWD Act to purchase water for the purpose of managing the groundwater basin and replenishing and protecting the groundwater supplies within OCWD. In addition, OCWD Act section 2(6)(b) expressly provides that OCWD has the authority to “Store water in underground basins or reservoirs within or outside the district,” and section 2(6)(j) authorizes OCWD, among other actions to improve and protect the groundwater supplies, to inject water into the basin. As noted above, the OCWD Act does not distinguish between sources and types of water that the District may buy, such that the District has the authority to purchase desalinated water, in the same way that it may purchase imported water, for replenishment purposes. Accordingly, the District has the authority to purchase desalinated water for the purpose of percolating it into the groundwater basin for replenishment purposes.

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I look forward to discussing these issues with the Board of Directors, and addressing any questions that Boardmembers may have.