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May 18, 2023

San Diego County Local Agency Formation Commission
2550 Fifth Avenue, Suite 725
San Diego, CA 92103

To: Keene Simonds, Executive Officer
Jim Desmond, Chair
Joel Anderson, Commissioner
Barry Willis, Commissioner

Re: Proposed Fallbrook PUD and Rainbow MWD Reorganizations: Wholesale Water Services

Honorable Chair Desmond and Commissioners,

Helix Water District appreciates the opportunity to provide comments on the Proposed "Rainbow Municipal Water District and Fallbrook Public Utility District Reorganizations: Wholesale Water Services | Concurrent Annexations to Eastern Municipal Water District and Detachments from San Diego County Water Authority with Related Actions (RO20-05 & RO20-04)." We also appreciate the effort from LAFCO staff to develop the final report and work done to provide a comprehensive analysis of this complex and significant item that will potentially impact every San Diego County resident.

As you are aware, this item is complex and spans topics and issues that are intrinsically interrelated and go well beyond those considered in this report. The final decision by this commission impacts more than the service areas of Fallbrook PUD and Rainbow MWD, it impacts the entire San Diego region and the water planning efforts made over many decades that ensure sufficient water supply and reliability. It may well be the most significant item, with the broadest impact to every County resident, brought before this commission to date.

Helix has several concerns regarding staff's recommendation to approve the detachment applications with exit fees. Our concerns include:

Focus on short-term gains for the few versus long-term impacts to many.

- The costs that Fallbrook PUD and Rainbow MWD are seeking to avoid are short-term in nature and benefit a relatively small number of County residents versus the remaining 23 San Diego County Water Authority member agencies who will be permanently negatively impacted.

Negative impacts to many San Diego County economically disadvantaged communities.

- The estimated and comparatively few 4,350 economically disadvantaged members of the Fallbrook and Rainbow communities are substantially less than the approximately 112,000 disadvantaged community population of Helix Water District, alone.

Board of Directors

Kathleen Coates Hedberg, President
Daniel H. McMillan, Vice President
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Significance of this action.

- The Helix board recently approved an annual rate increase for its average residential customer of 3.8% or approximately \$40 per year. The recommended action imposes an additional payment of \$11.40 per year, or a 29% increase to these same customers. This is significant, by any measure.

Proposed exit fee methodology.

- The applicants have benefited from hundreds of millions of capital infrastructure investment dollars made by SDCWA that are not being recuperated in the current exit fee calculation methodology. In light of this approach, the application of a discount to the exit fee to account for avoided costs of future infrastructure is inappropriate. Additionally, the duration of the proposed exit fee period should be reconsidered to better align with relevant cost factors.

Focus on short-term gains for the few versus long-term impacts to many

Helix, like the other water agencies in the County, understands the issues facing Fallbrook PUD and Rainbow MWD. We all face many pressures impacting costs and sales, including specific state regulations that limit the amount of water that each agency can sell. Helix itself has deep historic roots in agriculture. Agriculture drove the initial development of our agency 110 years ago. However, over time, it became apparent that agriculture in our service area was not sustainable due to the foreseeable limitations and costs associated with supplying water from regions so far away from our own.

As one of 24 member agencies of the San Diego County Water Authority, Helix has been supportive of programs like SDCWA's Permanent Special Agricultural Water Rate. Our support of this program, which makes water more expensive for Helix customers, has benefited agricultural users. Despite that, Helix Water District has supported this program with the sole purpose of acknowledging the importance of having agriculture within our region. However, we also understand that agriculture will come under increasing cost pressures in the San Diego region due to the continued lack of local water resources that is further strained from a hotter and drier climate. These cost pressures will exist regardless of short-term gains made by moving to a different water wholesaler.

For Fallbrook PUD and Rainbow MWD this is ultimately a relatively convenient decision that provides near-term relief from the larger structural and complex issues facing their ability to operate. These issues cannot be addressed by simply shifting costs to other agencies within the region, including Helix. LAFCO staff acknowledges in the report that both Fallbrook PUD and Rainbow MWD are already seeing a transition that includes reduced agriculture and increased housing units developed in their respective areas. This is a natural transition that supports improved operational benefits to both agencies through an increased customer base to pay for ongoing operational costs.

In the end, this same issue of increasing water costs will arise in the short term for both Fallbrook PUD District and Rainbow MWD, even if they detach and begin receiving service from Eastern MWD. As Eastern MWD and its supplier, the Metropolitan Water District, face the same environmental, reliability and infrastructure challenges that the SDCWA has already faced and, in many ways, addressed, their cost of supplying water to Fallbrook PUD and Rainbow MWD will increase. This is the reality of water supply in Southern California.

Negative impacts to many San Diego County disadvantaged communities

The report identifies disadvantaged communities within the service areas of both Fallbrook PUD and Rainbow MWD that would benefit from reduced costs as proposed by this action to change wholesalers. While this is positive for these disadvantaged communities, the report fails to consider the negative and permanent impact to the many disadvantaged communities outside of Fallbrook PUD and Rainbow MWD.

Based on the data provided in the report, we have estimated that the disadvantaged population in the Rainbow and Fallbrook communities that would potentially see short-term lower water costs as a result of the move to a different wholesaler is approximately 4,350 residents. Helix alone serves an estimated disadvantaged population of 112,000 residents that will see higher water bills from the shift in costs from Fallbrook PUD and Rainbow MWD moving to a new wholesaler. This number does not include the disadvantaged communities that fall within the other water agencies throughout the County, including the city of San Diego, that will also see higher costs. Use of this data point to justify the benefit to Fallbrook PUD and Rainbow MWD is overstated and unfortunately diminishes the impact to a significantly larger population of disadvantaged communities within the region.

Significance of this action

The LAFCO staff recommendation is also based on an additional evaluation of “other material issues”. This includes an analysis to determine the level of “significance” of the proposed action to the other San Diego County Water Authority ratepayers. Staff uses two analyses to make its determination that this proposed action is less than significant to other SDCWA ratepayers, including Helix.

In its first piece of analysis, LAFCO staff compares the financial impact to the SDCWA from a one-year loss of Fallbrook PUD and Rainbow MWD’s gross water sales revenue versus the inflation rate for San Diego County. In the report, staff identifies that it could use an individual year or an average of several years for this comparison. However, staff uses a single base year for the comparison, choosing calendar year 2022, which leads to the conclusion that the 4.4% loss of gross sales revenue is less than the 6.8% rate of inflation, and therefore is considered less than significant.

However, Helix Water District contends that using one single year of inflation data, particularly the single highest year of inflation for the region and the country in decades, skews the comparison and ultimately the basis for the recommendation. Calendar year 2022 inflation is a historical high point, one that the Federal Reserve continues to address in an aggressive campaign to lower inflation. LAFCO staff acknowledges in its footnote on page 31 of its report that the “Inflation rates for San Diego-Carlsbad region over the preceding ten- and five-year periods have been at 3.6% and 4.6%.” Helix recommends using these averages for a comparison, as the longer, although still relatively short, comparative time frames provide a more meaningful comparison. When using this data, the financial impact to the San Diego County Water Authority cannot be “considered reasonably less than significant.”

The second measurement that LAFCO staff used to determine the significance of the financial impact of detachment is to compare the average SDCWA rate increase since 2019 of 3.8%-3.9% to the estimated 2.5% increase to rates on the remaining member agencies, less any exit fees. Helix has difficulty understanding the value of this comparison and the comparative timeframe that was chosen for this conclusion.

SDCWA sets rates to operate the wholesale system that all 24 of its member agencies must use. The average SDCWA rate will vary over time from many factors, including the use of reserves, capital requirements and changing costs required to operate its system. Additionally, the cost impacts from the Fallbrook PUD and Rainbow MWD detachments on SDCWA are additive to the SDCWA rate and not in lieu of the SDCWA rate. If using staff's methodology, the additional rate impact caused by Fallbrook PUD and Rainbow MWD should be **added to the average SDCWA rate** rather than compared to the SDCWA average rate resulting in a determination of a significant financial impact.

Lastly, the staff report and SDCWA financial analysis indicate Helix will have to cover an additional \$749,504 to \$888,840 in costs associated with Fallbrook PUD and Rainbow MWD moving to a new wholesaler. Table 3, page 29 of the report shows an annual ratepayer impact of \$11.44 for Helix customers. This is significant for our service area, which is comprised of over 40% of disadvantaged community residents. The Helix Water District Board of Directors, on April 26, 2023, passed a water rate notice that authorized an annual increase of 3.8%, or \$40.68 for fiscal year 2023-24 for our average residential customer. An additional \$11.44 represents 29% of this amount. This is a significant impact to our customers, including the 112,000 disadvantaged population we serve, and should not be minimized or dismissed.

Proposed exit fee methodology

LAFCO staff recommends the creation of an exit fee to be paid by Fallbrook PUD and Rainbow MWD. Additionally, staff recommends offsetting this exit fee by applying a credit for the value of the avoided costs for a planned Emergency Supply Project pumping facility that would have benefitted these areas. However, this pump station has not been built, nor has the cost of the funds necessary to build the pump station been included in SDCWA rates. Additionally, the proposed exit fee calculation methodology does not account for the debt owed by the applicants to SDCWA for all of the capital project costs it has incurred which have benefitted the applicants over the past 70 years. Therefore to credit avoided capital costs, regardless of direct impacts, is inconsistent with this approach and should not be included as a credit to this fee.

However, given that staff recommends an exit fee credit, Helix questions the calculation of the value of the exit fee credit included in this report. The debt for the ESP would have been financed over several decades. However, under this proposed approach, Fallbrook PUD and Rainbow MWD's annual share of debt for Quantification Settlement Agreement water would only be recouped for the duration of the exit fee period. If LAFCO staff insist that a credit is appropriate, Helix contends that a more consistent approach would be that the credit for the ESP project only include the debt that would be payable during the duration of the exit fee period. If Fallbrook PUD and Rainbow MWD are not going to pay for the long-term QSA debt beyond the exit fee period, they should not get credit for the avoided long-term debt for the ESP North County Pump Station beyond the exit fee period.

Lastly, Dr. Hanemann advised that a reasonable combined exit fee for Fallbrook PUD and Rainbow MWD would be \$13 million per year for 3 to 10 years. LAFCO staff recommends a duration of five years, citing "three relatable considerations" including the completion of Urban Water Management Plans and municipal service reviews every five years and the use of five-year rolling averages for predicting future cost allocations. However, these timeframes are wholly unrelated to the determination of the exit fee duration. The exit fee duration should be based only on financial analysis, not comparison to unrelated reporting cycles. Helix feels that a five-year duration for the exit fee puts the financial burden of QSA

recovery on the larger SDCWA community far too quickly and that the duration should be on the higher end of Dr. Hanemann's recommended window.

Conclusion

Helix appreciates the significance and magnitude of the decision that has been brought forward to this Commission. We appreciate staff effort in attempting to simplify a complex issue into manageable considerations to assist the commission in rendering a decision.

We believe that the quote from Metropolitan Water District Chair Adán Ortega in the staff report sums up the overarching and complex issues associated with this proposal, "If permitted by LAFCO in San Diego County...efforts toward climate adaptation through investments on long-term water supply planning could become trapped in the immediate issues of affordability that could otherwise be addressed in the long-term. This would occur as communities chase after the lesser rates among adjacent Metropolitan Member Agencies in a potential race to the bottom compromising past investment."

In light of the complexity and issues not evaluated as part of the staff report and considerations and conclusions that we feel are in error, Helix Water District would appreciate your consideration in favor of option 4 Disapprove without Prejudice. This option does not pass on significant financial impacts to Helix and other agencies in San Diego for the benefit of a near-term gain for a few and continues to honor the investments and collaboration of the whole San Diego region in developing our long-term water supply.

Sincerely,



Brian M. Olney
General Manager
Helix Water District