ITEM NO. 8.2

THE NEWHALL LAND AND FARMING COMPANY
(A CALIFORNIA LIMITED PARTNERSHIP),
a California limited partnership

June 6, 2023

Via Email (ajacobs@scvwa.org)

April Jacobs
Board Secretary
Santa Clarita Valley Water Agency
27234 Bouquet Canyon Road
Santa Clarita, CA 91350-2173

Re: June 6, 2023 Santa Clarita Valley Water Agency Board of Directors Meeting Objection to Recommended Approval of a Resolution Establishing the Valencia Service Area Retail Capacity Fee

In the spirit of collaboration and good faith, The Newhall Land and Farming Company (A California Limited Partnership), a California limited partnership ("**NLF**") proposed a reasonable compromise that could have resolved this Valencia Service Area retail capacity fee ("**RCF**") dispute in a sensible and fair manner. NLF invited Agency staff to meet and/or discuss our proposal multiple times over the past two weeks, but the Agency did not respond to our proposal, nor would it agree to meet or discuss our proposal other than to ultimately report the RCF as drafted was going to the Agency's Board of Directors for consideration for approval on June 6, 2023. NLF is left with no option but to object to the RCF.

Therefore, this letter is submitted on behalf of NLF. NLF objects to the Santa Clarita Valley Water Agency (the "**Agency**") Board of Directors' proposed approval of the Resolution of the Board of Directors of the Santa Clarita Valley Water Agency Establishing the Rates of Retail Capacity Fees for the Valencia Service Area (the "**RCF Resolution**"). Based on our review of the RCF Resolution and its supporting materials, including the March 6, 2023 Valencia Service Area Retail Water Capacity Fee Study conducted by Bartle Wells Associates (the "**Capacity Fee Study**"), the RCF unlawfully exceeds the reasonable estimated cost of services in violation of Government Code §§ 66013 and Proposition 26 (Cal. Const., art. XIII C, Section 1).

Background

NLF or its subsidiary, The Newhall Land and Farming Company, LLC, constructed a majority of the water system infrastructure now in operation within the Valencia Service Area back when the Valencia Service Area was the Valencia Water Company (the Valencia Water Company was owned by NLF). As you know, in or around December 2012, the Castaic Lake Water Agency purchased from NLF, through an eminent domain settlement agreement, all shares of the Valencia Water Company, which included all infrastructure and assets of the Valencia Water Company, for a purchase price of $73.8 million. Thereafter, the Agency was formed on January 1, 2018, by the merger of Castaic Lake Water Agency and Newhall County Water

District pursuant to the Santa Clarita Valley Water Agency Act, Stats. 2017 ch. 833 ("**SB 634**"). SB 634 also provided for the dissolution of the Valencia Water Company and its inclusion in the Agency shortly after the inception date (the Valencia Water Company became the Agency's Valencia Service Area/Valencia Water Division).

In or around 2021, the Agency commissioned a Retail Water Rate Cost Analysis and Rate Design Study ("**Water Rate Study**") which created a proposed water rate plan for the period spanning FY 2021-22 through FY 2025-26. The Water Rate Study establishes a fixed legacy debt charge to be included on the bills of the Santa Clarita Water Division and Valencia Water Division to comply with terms of SB 634 and ensure that debt service for infrastructure necessary to provide water to the retail purveyors prior to merger will be paid by the customers in those respective service areas. (p. 1.) In other words, the Agency is recovering the cost of the roughly $73.8 million purchase price for the water system infrastructure through its water rates. Pages 33-36 of this study show the calculation of these legacy debt charges, with $6.50 being added to each Equivalent Meter Unit each year for FY 22-26 for customers in the Valencia Water Division.

Summary of Law

Government Code § 66013 states, "Notwithstanding any other provision of law, when a local agency imposes fees for water connections or sewer connections, or imposes capacity charges, those fees or charges ***shall not exceed the estimated reasonable cost of providing the service for which the fee or charge is imposed,*** unless a question regarding the amount of the fee or charge imposed in excess of the estimated reasonable cost of providing the services or materials is submitted to, and approved by, a popular vote of two-thirds of those electors voting on the issue." (Section 66013(a), emphasis added.) In order to impose a fee, the Agency must establish that the RCF bears a fair or reasonable relationship to the costs incurred by the Agency in constructing the facilities attributable to the fee. (*Rincon Del Diablo Municipal Water District v. San Diego County Water Authority* (2004) 121 Cal.App.4th 813, 823.)

Proposition 26 (2010) states that non-taxes, including certain charges imposed for specific government benefits, privileges, services or products provided directly to the payor, cannot exceed "the reasonable ***costs to the local government*** of conferring the benefit or granting the privilege." (Cal. Constitution Article XIII C, Section 1, emphasis added.) "The local government bears the burden of proving by a preponderance of the evidence that a levy, charge, or other exaction is not a tax, that the amount is no more than necessary to cover the reasonable costs of the governmental activity, and that the manner in which those costs are allocated to a payor bear a fair or reasonable relationship to the payors burdens on, or benefits received from, the governmental activity." (Cal. Const., art XIII C, § 1, subd. (e).) Under Proposition 26, SCVWA bears the burden of proving by a preponderance of the evidence that the amount of the RCF is no more than necessary to cover the reasonable costs of the governmental activity, **which it fails to do because the Agency does not establish, identify or support that it incurred any capital costs for constructing the facilities or infrastructure relating to the water system.**

RCF Fails to Comply with Statutory and Constitutional Law

The Capacity Fee Study utilizes a "buy-in" methodology to calculate the RCF, and reasons that the buy-in approach is more commonly used by agencies with water systems that require minimal facility capacity improvements, recognizing that, "the existing Valencia Service Area requires minimal future facility capital improvements." (*Id.*, p. 8.) The purpose of the buy-in approach is for the Agency to recover the capital costs it paid for facilities constructed in advance of development. In the Capacity Fee Study, the RCF is calculated based solely on the ***value***[1] of existing facilities and assets (but not the actual ***costs*** to the Agency of the existing facilities and assets), in current dollars, divided by the capacity of the water system, less outstanding debt. (*Id.*) The Agency's valuation is flawed because it fails to quantify or exclude any contributed capital or in-tract facilities (non-backbone infrastructure)[2], in violation of statutory law and standard industry practices. This failure to exclude contributed capital in the RCF valuation, representing facilities built and donated to the Agency by NLF or its subsidiary at no cost to the Agency, results in NLF effectively paying twice for the same constructed and donated water system infrastructure.

The Capacity Fee Study does not mention that the Valencia Service Division's water infrastructure was constructed by NLF and purchased via the eminent domain settlement. The Capacity Fee Study entirely ignores developer contributions and implies that SCVWA paid the costs to construct the entire Valencia Service Division water system itself, which is not true. The Capacity Fee Study suggests the RCF will recover "the costs of infrastructure, assets, and water supply that benefit new development" (p. 3) – yet, the study fails to mention that SCVWA did not construct or incur capital costs relating to the majority of the infrastructure, assets, or water supply that benefit new development. The study fails to fully explain that, to the extent SCVWA's predecessor paid a cost to purchase the infrastructure, assets, and water supply that benefit new development through an eminent domain settlement agreement, the Agency is recovering that cost through the legacy debt component of the Valencia Service Division's water rates.

The letter provided by the Ratepayer Advocate Robert D. Niehaus, Inc. (RDN), which evaluates the Retail Capacity Fee analysis performed by Bartle Wells Associates ("**BWA**"), misrepresents the funding method for existing facilities, stating: "[The BWA buy-in] approach, which is one of the primary methods recommended by the American Water Works Association ("**AWWA**"), assumes that existing facilities, ***funded by current ratepayers***, have extra capacity to accommodate new development without needing additional expansion. As a result, new development should compensate current ratepayers for the unused capacity they have invested in." This is patently false – current ratepayers did not fund the existing facilities, NLF did. Current ratepayers did not pay a connection or capacity fee, and have never "bought-in" to the

[1] SCVWA relies on the replacement value of existing facilities as the basis for the RCF cost recovery, while at the same time admitting that "the existing Valencia Service Area does not require significant capacity-related capital improvements to accommodate new development." (Capacity Fee Study, p. 1.) The law does not allow for the imposition of a fee or the recovery of revenues based on replacement costs of facilities the agency did not construct.
[2] We confirmed with the Agency that no facilities were funded by grants.

water system; they have only ever paid water rates, which pay for the water service as well as the operation and maintenance of the water system that NLF built.

SCVWA's draft RCF Resolution and supporting materials make repeated, unsubstantiated determinations that, "[T]he [RCFs] do not exceed the estimated reasonable cost of the services and facilities for which a capacity charge will be imposed" but there is zero discussion anywhere in the record that explains, (1) How or why the amount of the RCFs do not exceed the costs of service given the Agency did not construct the infrastructure, or what the estimated reasonable costs of the services and facilities to SCVWA actually were, (2) What the RCFs are proposed to pay for/pay off, or (3) What incurred Agency burden needs to be offset. State law requires public agencies prove a reasonable relationship between the proposed fee and the cost burden incurred by the Agency. Here, SCVWA has not done so.

Despite the SCVWA's contention that the RCF is "based on methods endorsed by the AWWA and presented in the Water Rate AWWA Manual M1," the Capacity Fee Study repeatedly ignores the M1 Manual guidance. The M1 Manual, which is considered instructive in helping policymakers and rate analysts evaluate and set rates such as the RCF, repeatedly and specifically contemplates that developer-contributed capital should not be eligible for inclusion within a capacity fee calculation. (M1 Manual, p. 268 – 272 ["[With respect to] the buy-in methodology, projects funded in part from grants, ***developer contributions***, and so forth, may not be eligible for inclusion within the [capacity fee] calculation."]) Yet, the Capacity Fee Study fails to exclude developer contributions from the system valuation or the RCF calculation in stark contrast to this guidance.

Furthermore, in discussing the reasonable relationship required between the fee charged and the cost associated with providing capacity to the customer, the M1 Manual instructs that the charges, "[M]ust bear a reasonable relationship to the cost burden imposed. Implementation of the planning criteria and ***the actual costs of construction and the planned costs of construction*** will typically establish compliance with the reasonable relationship requirement." Here, SCVWA has not demonstrated that it suffered an actual cost burden, has not identified any actual or planned construction costs, and has not demonstrated a reasonable relationship between the RCF and the cost burden imposed. On top of that, the water agency acknowledges that, "[T]he existing Valencia Service Area does not require significant capacity related capital improvements to accommodate new development" (p. 1), so there are no significant planned capital projects on the horizon that support or explain the collection of this revenue. Moreover, the Agency already has in place separate Regional/Distribution Facility Capacity Fees, which it collects at the time new development occurs to recover for growth-related costs, which NLF has been paying without objection.

Conclusion

In short, NLF constructed a water system, then sold it to the Agency for a price certain roughly a decade ago. Now, the Agency is proposing to charge NLF roughly $25 million in RCFs to "buy-in" to the construction of that very same water system, minus the purchase price (which is being recovered through water rates), under the guise that the system now enjoys a

higher valuation. NLF has no objection to paying the capital costs for the water system infrastructure necessary to service the Valencia Service Area, but it does object to paying for it twice (and/or paying the Agency back for capital costs it never incurred in the first place), which is exactly what the Agency is demanding if it approves the RCF Resolution.

As the Valencia Service Area's largest stakeholder (and consequently, the entity that will be paying nearly the entirety of the proposed RCFs) we demand the Agency Board of Directors reconsider and/or recalculate the proposed capacity fee to account for any contributed capital and in-tract facilities (non-backbone infrastructure). The Agency Board of Directors should not recommend approval of a capacity fee that exceeds the reasonable cost of services in violation of California law.

Sincerely,

THE NEWHALL LAND AND FARMING COMPANY (A CALIFORNIA LIMITED PARTNERSHIP),
a California limited partnership

By: NWHL GP LLC, a Delaware limited liability company, its General Partner

By: _____
Name: Donald L. Kimball
Title: Vice President & Assistant Secretary