

January 4, 1999

**To:** Board of Directors (Legal and Claims Committee--Action)  
**From:** General Counsel \_\_\_\_\_  
**Subject:** Wheeling Litigation (*Metropolitan Water District v. All Persons*) (Conference with Legal Counsel--Existing Litigation; [case pending] to be heard in closed session pursuant to Government Code Section 54956.9(a))

**RECOMMENDATION(S)**

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It is recommended that the Board review the attached options and instruct staff on how to proceed on the issues raised in the litigation entitled *Metropolitan Water District v. All Persons*.

**DETAILED REPORT**

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As the Board will recall, Metropolitan's appeal of the trial court's adverse decision in the wheeling litigation entitled *Metropolitan Water District v. All Persons* is pending. The record on appeal has been filed and a briefing schedule from the appellate court is imminent. Metropolitan's opening brief will be required to be filed 30 days thereafter.

At the invitation of the State Water Contractors (SWC), who are interested in the issues involved, staff has met with representatives of the San Diego County Water Authority (Authority), the Imperial Irrigation District (Imperial) and the SWC to explore the possibility of a mutually agreeable resolution of the issues involved in the litigation. At the most recent meeting, representatives of the Water Authority and Imperial indicated their parameters in any such discussions. These informal meetings have progressed to the point that staff must seek guidance from your Board on whether, and if so how, staff should proceed with the discussions. It is recommended that the Board consider the attached options and direct staff how to proceed with respect to resolution of the issues raised in the wheeling litigation. The attachments to this letter summarize the trial court opinion, outline the issues on appeal, describe the negotiation parameters indicated by the Authority and Imperial and list potential options which the Board may wish to consider.

JR:mg

**Attachment 8-14A**

**Attachment 8-14A**

**WHEELING APPEAL OPTIONS**

**Options**

Proceed with appeal only – Continue with appeal without seeking settlement or legislation. The record will be filed with the appellate court within a few days, and Metropolitan’s brief would be due 30 days thereafter (30-day extensions are commonly granted).

Put appeal on hold and negotiate – MWD could agree with other parties to stay the appeal for some period of time pending settlement negotiations. An appellate settlement justice or a mediator could be utilized.

Proceed with appeal and negotiate concurrently – Pursue appeal on the existing timeline, but informally pursue settlement discussions.

Seek a legislative resolution, with or without continuing appeal – MWD could seek to change the wheeling statute to fix the incremental cost, the postage stamp and protection of other customers issues.

Abandon Appeal – MWD could voluntarily dismiss its appeal, leaving the trial court holding standing on all issues.

## Issues on Appeal

Pro-rata capital and fixed O&M costs v. incremental costs (irrespective of entire system or point to point issues) – The trial court held that the owner of the conveyance system may only charge for the actual incremental costs added by the wheeling party’s use of the system, and may not charge for a pro-rata share of the capital and fixed O & M costs of the conveyance system.

“Postage stamp” v. point-to-point wheeling charges – The trial court held that the owner of the conveyance system can charge only for those portions of the system actually used by the wheeling party (“point to point”), and can not charge a “postage stamp” rate based on the costs of the interconnected system.

Deference given to agency rate determination – Generally, courts defer to agency rate setting determinations, and the wheeling statute specifically incorporates the deferential “substantial evidence” standard. However, the trial court held that whether an agency could charge postage stamp rates or recover pro-rata costs were legal issues on which the court was not required to defer to Metropolitan.

Protection of system customers – The trial court held that the statutory language requiring that the “use of the conveyance facility is to be made without injuring any legal user of water” protects water users in the area of origin, but not other customers of the owner of the conveyance system. This language was a significant underpinning of Metropolitan’s no cost shifting principle; that is, preventing an increase in rates of system customers as a result of a wheeling transaction.

Rate setting in advance or case-by-case – The trial court held that a wheeling rate, at least a postage stamp rate, cannot be set in advance without regard to the particular transaction proposed.

Payment of Attorney’s Fees – Several parties have appealed the issue of who should pay attorney’s fees:

- SDCWA – Requested \$227,675.50
- IID – Requested \$297,895.76
- Indian Tribes – Requested a total of \$51,476.31
- Center for Public Interest Law (CPIL) – Requested \$70,600, plus a 2.5 multiplier (\$176,500 total)
- Trial court decision
  - \* Court denied SDCWA, IID and the Indian Tribes requests because fees are generally not awarded to a litigant who has an economic stake in the litigation.

- \* Court awarded CPIL its actual fees of \$70,600 as a public interest litigant, but did not award a multiplier.
- Appeal
  - \* Metropolitan has appealed the award of actual fees to CPIL.
  - \* SDCWA, IID and Indian Tribes have appealed the denial of their full requests, which would total \$753,547.

## Negotiation Issues

(Based on preliminary staff discussions)

Existing Wheeling Policy – Both SDCWA and IID indicated that they will not agree to a settlement that affirms Metropolitan’s current wheeling policy.

Pro-rata capital and fixed O&M costs – SDCWA and IID have indicated a willingness to discuss wheeling rates which include appropriate capital and fixed O&M charges, based on point-to-point wheeling.

Postage stamp – SDCWA and IID have not indicated a willingness to a settlement that includes postage stamp wheeling rates.

Protection of system customers – SDCWA and IID have not indicated a willingness to discuss cost-shifting and other financial protections for system customers should be part of the rate.

Advance rate setting - SDCWA and IID are willing to explore establishing a rate setting methodology in advance is appropriate, but that actual rates must be set case-by-case, based on the portions of the system used.

Attorney’s Fees – CPIL (and possibly other parties) has specifically stated that recovery of attorney’s fees must be part of any negotiation.

Timeline for negotiation - In previous meetings, SDCWA stated that any negotiations should be completed by mid-January 1999.

**SUMMARY OF WHEELING CASE TRIAL COURT DECISION**  
**(MWD v. All Persons Interested)**

Judge Kay issued a written decision in *Metropolitan Water District v. All Persons Interested* in which he declined to validate the wheeling rates established by Metropolitan. Below is a summary of the main points in that decision. Metropolitan believes that Judge Kay's holding on these issues is incorrect and has appealed.

**Standard of Review**

- ◇ The issue of whether Metropolitan can charge postage stamp wheeling rates and include system-wide costs is a legal issue, subject to de novo review by the court. Therefore, the court need not give any deference to Metropolitan's determination of the proper wheeling rate.
- ◇ Since the postage stamp approach is not allowed by the wheeling statute, the court did not need to review the manner in which Metropolitan calculated the rate.

**Intent of Wheeling Statute**

- ◇ In reviewing a wheeling change the court must interpret the statute in a manner that effectuates the legislative purpose of encouraging water transfers.
- ◇ The legislative purpose of promoting efficient water use is intended to encourage transfer of water used unnecessarily in the areas of origin to areas of need; protecting wheeling system infrastructure by setting rates to recover system-wide costs or prevent cost-shifting is not within that intent.

**Postage Stamp Rate**

- ◇ Metropolitan may charge only for the portions of the system actually used in the wheeling transaction at issue (point-to-point).
- ◇ Metropolitan is not entitled to include costs not actually related to conveyance, such as its SWP costs or conservation incentives even though they are fixed costs.
- ◇ Wheeling changes are intended to apply only where there is unused capacity; therefore the rate can not include costs necessitated by facilities required to provide guaranteed capacity.

**Allowance of only Incremental Costs**

- ◇ Statute's allowance of recovery of charges "incurred" by the wheeling system owner means that the owner can only recover "incremental costs brought about by a particular wheeling transaction." Therefore, an agency can recover only "additional" or "increased" capital and O&M costs caused by the specific transfer, and not a pro-rata share of those costs.

**Protection of Other Customers**

- ◇ Language protecting other "legal users of water" from injury caused by use of the conveyance system is intended to protect water rights holders in the area of origin, not Metropolitan's other member agencies from potential economic harm.

Interruption

- ◇ Metropolitan's interruptible rate is invalid because it is subject to interruption "for any reason"; the statute allows interruption only for "emergency".

Advance rate setting

- ◇ Since the availability of unused capacity and the portions of the system to be used in a wheeling transaction can not be known until a transaction is proposed, a wheeling rate can not be set in advance, but must be set on a case-by-case basis.