

A Case Study For Calif. Cities In Water Utility Takeovers

By **James Oleshansky, Steven Silva and Brad Kuhn** (June 28, 2024)

After more than a year of sustained high levels of precipitation, the National Oceanic and Atmospheric Administration is projecting a shift from El Niño to its climate counterpart, La Niña. La Niña is expected to develop this summer, and typically lasts nine to 12 months.

After the 2023 rain year — California's 10th wettest since recordkeeping began 128 years ago — La Niña signals a big shift for the state toward a drier climate. California's three driest years on record, 2020 through 2022, were La Niña years.

In the face of this kind of water scarcity, some city and county governments in California have turned to using the power of eminent domain to acquire investor-owned utilities, or IOUs, through condemnation, under the theory of improving water service and costs for their communities.

This process of a government acquiring an IOU is called municipalization. Municipalization of IOUs through eminent domain, however, is more difficult than traditional condemnation — because IOUs have the right to contest the government's findings authorizing the use of their eminent domain powers.

California law requires a governing body to adopt a resolution of necessity, or RON, before it can condemn private property. The RON outlines the findings that must be made before a public entity may exercise its eminent domain powers. The general findings required include:

- The public interest and necessity require the project.
- The project is planned or located in the manner that will be most compatible with the greatest public good and the least private injury.
- The property sought to be acquired is necessary for the project.

Further, when the property to be condemned is already appropriated to public use — such as when an IOU owns property used for utility purposes — then California law requires that the governing body must also find that "the use for which the property is sought to be taken is a more necessary public use than the use to which the property is appropriated."

Generally, the adoption of a RON carries with it a conclusive presumption of truth concerning the required findings. Thus, a property owner cannot challenge the finding that the property is necessary for the project, or that the public interest requires the project.

But when a public entity seeks to condemn water facilities already being put to a public use,



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there is a rebuttable presumption of truth concerning the RON's findings. This difference is extremely important.

A RON carrying a conclusive presumption of truth is extremely difficult to invalidate, as it can only be attacked based on the administrative record and matters concerning the validity of the resolution itself. A RON carrying a rebuttable presumption of truth, however, grants an IOU the right to a trial on the merits of the government's decision to condemn the utility company's property.

In other words, when a RON is adopted, the governing body is engaging in a quasi-legislative action that does not require factual findings to be stated in support of its decision to exercise its eminent domain powers. In effect, the legislative process allows the governing body to pass the RON quickly. But it does not prepare the governing body to defend its findings before the court.

In a takeover eminent domain action, an IOU is permitted to introduce extrinsic evidence to challenge whether the public entity's right to take conflicts with the findings in the RON. Disproving one of the RON's findings — by a preponderance of the evidence — will invalidate the RON and defeat the condemnation action.

In essence, the IOU must prove its operation of the water system is more beneficial to the public than municipalization would be. While the IOU carries the burden of proof, litigation will require both parties to introduce evidence to defend their respective claims.

The city of Claremont's attempted takeover of Golden State Water Co. illustrates the impact of the rebuttable presumption on an eminent domain action.

In 2012, the city commissioned an appraisal and feasibility study regarding the acquisition of the Claremont water system. Two years later, voters approved Measure W — a \$135 million revenue bond measure to finance the acquisition of the Claremont water system from Golden State through eminent domain. Shortly thereafter, the city adopted a RON.

City of Claremont v. Golden State Water was subsequently heard by the Los Angeles County Superior Court. Neither the RON nor the city's complaint listed reasons supporting the taking.

The city's first amended complaint provided many reasons why condemnation was in the public interest. Included in the stated reasons were lowering water bills and improving service quality. During the course of a 21-day bench trial in 2016, Golden State presented sufficient evidence to successfully rebut the presumption that the required findings had been established.

Experts testifying on behalf of Golden State concluded that although acquisition may be feasible, bond financing would actually cause an immediate increase in water rates. Their economic analysis disproved the city's stated goal of lowering water bills. Despite evidence of the ratepayers' support for municipalization, the presiding judge held that 30 or more years of increased rates to service the debt was not in the public interest.

Furthermore, Golden State demonstrated that it was more qualified to operate the Claremont water system, through statistics regarding the size of its specialized workforce, its track record of maintaining safe water standards and its network of customer support resources. The city offered no evidence to show that Golden State's ability to deliver water to its customers was deficient in any way.

In his statement of final decision, the judge characterized the city's overarching argument that local control was inherently superior as "dubious." Golden State's expert testimony, economic analysis and water safety record persuaded the judge that it was the premier operator of the Claremont water system.

The city failed to introduce sufficient evidence to support its findings and justify the public's need for, use of or benefit from municipalization. Ultimately, the judge concluded that Golden State had met its burden to rebut the findings in the RON, and dismissed the complaint.

The ability of IOUs to challenge the merits of a proposed acquisition, whether of certain utility facilities, or of the operation of the utility company itself, was affirmed by the California Court of Appeals, Third District, in September 2023, in *South San Joaquin Irrigation District v. Pacific Gas and Electric Co.*

In clarifying the standard of proof to be applied at the trial, the appeals court confirmed that electric, gas or water utilities can defend themselves from municipal takeover by disproving one of the RON's findings by a preponderance of the evidence. This ruling provides guidance and support for many IOUs currently fighting against municipalization efforts.

Condemning property owned by IOUs creates complex legal and practical challenges for governing bodies. The rebuttable presumption of truth alters the landscape of condemnation actions, by empowering IOUs to contest the factual underpinnings of a governing body's decision, and requiring evidentiary substantiation from the condemning entity.

The battle between the city of Claremont and Golden State Water serves as a powerful reminder to government agencies of the importance of comprehensive factual findings that will withstand judicial review. Failure to do so risks protracted and costly litigation.

As California's water systems continue to face challenges of scarcity and access, government agencies must navigate California's eminent domain laws with prudence and diligence to best protect the public interest.

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Disclosure: Brad Kuhn and Nossaman filed amicus briefs on behalf of Southern California Edison and the California Water Association in South San Joaquin Irrigation District v. Pacific Gas and Electric.

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