GEAA Greater Edwards Aquifer Alliance

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West Texas Springs Alliance
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PO Box 15618
San Antonio, Texas 78212
(210) 320-6294
PO Box 15618
San Antonio, Texas 78212
(210) 320-6294
www.AquiferAlliance.org

October 16, 2017

Mayor Ron Nirenberg
City Hall, 4th Floor
100 Military Plaza
San Antonio, TX 78205

Dear Mayor Nirenberg,

Subject: New insights/concerns regarding Vista Ridge WTPA

Recently Mr. Eric Allmon, an environmental attorney, carried out a preliminary review of the Vista Ridge WTPA and its various amendments. I am attaching to this letter a summary of Mr. Allmon's analysis. While Mr. Allmon was clear that his review was neither exhaustive nor definitive, he nonetheless raises a number of disturbing questions about the solidity of the original WTPA's protections of SAWS, SAWS' ratepayers and the City of San Antonio and the potential, further erosion of these due to subsequent contract amendments.

A sample of his findings includes:

- Contrary to the Vista Ridge WTPA, the wholesale water rates are subject to Public Utility Commission of Texas oversight and the rates can be challenged by the Project Company in the future.
- The Central Texas Regional Water Supply Corporation, as it is controlled by a private, for-profit company, may not have the eminent domain authority to acquire easements for the project.
- The WTPA lists groundwater leases that cannot be relied on for Vista Ridge water.
- The amendments to the Vista Ridge WTPA have put ratepayers and the City of San Antonio at risk.

Mr. Allmon's conclusion is that the San Antonio City Council would be well-served to obtain qualified, independent counsel in order to carry out its own definitive review of the WTPA and the potential risks that it poses to SAWS ratepayers and the City itself. You can contact Eric Allmon with any questions you might have at 512-469-6000 / eallmon@lf-lawfirm.com .

We wished to bring this information to your attention, both in your role as Mayor and head of City Council and as a member ex officio of the SAWS Board of Trustees.

Thank you for your consideration,

Annalisa Peace
Director
GEAA

Jim Smyle
Member
GEAA Board

I. The Vista Ridge Contract deserves greater scrutiny

1. Contrary to the Vista Ridge Contract, the wholesale water rates are subject to agency oversight and the rates can be challenged by the Project Company in the future.

The Contract states that the Project Company, which is the wholesale water supplier for the Vista Ridge Project, is not and will not be subject to the jurisdiction over utility rates of the TCEQ or the Public Utility Commission of Texas ("PUCT").[1] However, the Texas Supreme Court has ruled that wholesale water suppliers, as well as water purchasers, may seek review of water rates.[2] The Texas Supreme Court has also held that the Commission's authority is not limited to when the water supplier is appropriating state water, but can also review private water. The PUCT rules explicitly anticipate the review of rates established by a private contract.[3]

This means that the initial Vista Ridge Contract misrepresented the nature of PUCT's authority to review rates established in the contract, and that by seeking to establish rates not subject to the TCEQ or PUCT, the Contract could be deemed invalid and unenforceable. This also means that the risk of the Vista Ridge Project does not lie entirely with the Project Company as SAWS insists, but also on the SAWS ratepayers. If future circumstances change so that providing water is not economically feasible for the Project Company, the private, for-profit company could petition the PUCT and the PUCT could impose higher rates for Vista Ridge water, even over SAWS' objections. One example would be if pumping is cut back in order to comply with local aquifer protection standards and less water is available to the Project Company to sell, the Project Company could petition for a review and increase of the $1,606 per acre-foot rate established under the Contract.

2. The Water Supply Corporation is controlled by a private, for-profit Project Company, and may not have eminent domain authority to acquire the remaining easements needed for the project.

The Contract assumes in several places that the Project Company has control over the WSC. This undermines any pretense that the WSC is acting independently from the private, for-profit Project Company and may put the WSC at risk of losing its non-profit status and its authority to obtain pipeline easements.

The private, for-profit interest and control of the Project Company is also the subject of at least two objections to the WSC's eminent domain authority. Landowners who have been sued by the Central Texas Regional Water Supply Corporation ("CTRWSC") for pipeline right-of-way have filed objections to the Special Commissioner's Award that granted possession of their easement to the CTRWSC.[4] In each objection, attorneys for the landowner argue, among other things, that the WSC is exercising eminent domain for a private benefit, not a public one. The objections also claim that the WSC does not have eminent domain authority because it does not have a certificated service area and has violated constitutional due process requirements. Should defendant landowners prevail, the Project Company will be left without an

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[1] Vista Ridge Water Transmission and Purchase Agreement (hereinafter "Contract"), Section 2.2(L), p. 42.

[2] In *Texas Water Commission v. Brushy Creek Municipal Utility District* the City of Round Rock was supplying water to the Brushy Creek MUD on a wholesale basis and under a 20-year contract. 917 S.W.2d 19 (Tex. 1996). Four years into the contract, Round Rock filed a petition with the Texas Water Commission (since abolished and replaced with Texas Natural Resource Conservation Commission, now known as the Texas Commission on Environmental Quality) requesting the agency establish just and reasonable rates in place of the rates established in the original contract. The TWC assumed jurisdiction and after a hearing, issued an order adjusting the rates, although not in Round Rock's favor. Both the MUD and Round Rock sued for judicial review – the MUD arguing lack of jurisdiction and Round Rock arguing the court should have reopened the record to look at newly available evidence. The Texas Supreme Court determined that Section 12.013(a) allows water purchasers as well as wholesale water suppliers to seek Commissioner review of water rates. *Id.* at 23.

[3] 16 TAC § 24.131.

[4] *CTRWSC v. Southmayd*, No. 17-0121-CV (Guadalupe County 2nd 25th District Court); *CTRWSC v. Wenzel*, No. 2017CVB0070 (Comal County Court at Law No. 2).

entity that can condemn easements, heightening the risk that the easements cannot be acquired pursuant to the Contract's October 2017 deadline.

3. The Contract lists groundwater leases that cannot be relied on for Vista Ridge water.

SAWS has repeatedly said that over 3,400 groundwater leases support the Vista Ridge project. In reality, only 758 are listed in the Vista Ridge production permit from the Post Oak Savannah Groundwater Conservation District ("POSGCD"). And only 1,312 were listed in the "Financial Close" documents as supporting the Project (the permit plus additional rights in case of future cutbacks). Not only is 3,400 leases a gross misrepresentation of the number of leases allocated to Vista Ridge, this number has been incorrectly used to demonstrate the overwhelming support in the source community. However, despite individuals from Milam and Burleson counties asking for a thorough vetting of all groundwater leases associated with the project, neither POSGCD nor the Project Company, nor any member of the project team has confirmed that each of these leases are valid.

In documents that surfaced as a part of a lawsuit filed by Metropolitan Water against Blue Water Systems in December 2016 in Travis County District Court,[5] it seems Met Water has refused to even allow Blue Water full access to Vista Ridge lease files. In addition, Blue Water accuses Met Water of not following directives to maintain Vista Ridge Leases by pooling those leases so they are held by production. Blue Water accuses Met Water of allowing leases specifically dedicated to Vista Ridge project to expire, then creating a new entity, Met Water Vista Ridge ("MWVR"), outside the Project and all contractual agreements, to be the lessee of these expired leases. Several of the leases now held by MWVR are located in or near the Vista Ridge well field. At least two of those leases appear to be for properties upon which Vista Ridge pumping wells are currently planned. Even though these properties are integral to the Vista Ridge Project, no member of the project team has verified them.

Furthermore, at least one landowner whose lease is listed among the 758 groundwater leases that support the Vista Ridge production permit, contests the validity of a lease they say was renewed against their will. On top of that, this same lease is simultaneously being used to support the Vista Ridge permit and has also been pooled with a production unit for the Manor 130 pipeline. Pooling was the only means that Met Water had to renew the lease against the landowners' wishes; however, it is highly suspect whether under POSGCD rules, the correlative 2 acre-feet of groundwater rights associated with an acre of land can be assigned to support two projects at once.

II. The amendments to the Vista Ridge contract put ratepayers and the City of San Antonio at risk.

Since the contract was originally signed in November 2014, it has been amended three times: in June 2016, November 2016, and April 2017. San Antonio's City Council played no role in the review of these proposed changes and thus they lacked the independent review and public scrutiny they deserved. Of major concern is that amendments to the Contract open up ratepayers to the risks that justified the public-private partnership in the first place. Also of concern, is that the amendments weaken the terms of the contract to make them more favorable to the Project Company, requiring San Antonio ratepayers to assume improper, if not unlawful, additional costs.

[5] Blue Water Systems, LP v. Metropolitan Water Co. L.P., No. D-1-GN-16-005866 (Travis County 353rd Civil District Court).

1. The change of control from Abengoa to Garney meant Garney assumed a $120 million liability for a "missing loan", which SAWS ratepayers are now responsible for paying back.

The November 2016 amendment made clear that Garney Construction was taking control of the project from Abengoa and bought an 80% equity stake in the Project Company. The "Bridge Loan" borrowed on July 20, 2015 by then Project Company Abengoa Vista Ridge was apparently included in the liabilities assumed by Garney as a part of this amendment to the Contract. It was never explained how this money was spent or why it was rolled into the cost of the project for SAWS ratepayers.[6,7,8] Not only has the missing $120 million been hidden from ratepayers, it has also never been explained whether this is in fact legal, given the Texas Constitution's prohibition on gratuitous gifts of public money for private purpose.

2. The deadline by which to "acquire" easements has become easier for the Project Company to meet, meaning SAWS has made a large financial investment before the right of way has actually been acquired.

The April 2017 amendments altered the definition of "acquire" to mean that easements are "acquired" when eminent domain proceedings have been initiated. This latest amendment comes after several prior amendments that consistently pushed back the date by which easements must be acquired. The original deadline required the Project Company to be in possession of substantially all the easements by "Financial Close." Then, it was amended to June 10, 2017, and the latest amendment pushed the deadline all the way back to October 13, 2017.

The latest amendment also alters the acceptable encumbrances for the property. Where previously an exception to title was allowed only if it was in a title insurance policy, now, a title commitment will suffice to demonstrate lack of encumbrances. This means SAWS representatives have also been given expanded power to grant variances from easements requirements in the contract. Previously, granting a variance from a required easement deadline for a given parcel would have required a contract amendment, but now a simple "contract memoranda" without an amendment will suffice.[9]

3. Other amendments weaken the protections for San Antonio and ratepayers in favor of the Project Company.

Water quality parameters required for incoming water have been weakened with regard to pH and chlorine levels.[10] The requirement for water treatment facilities at Terminus Site have been removed.[11] It is unclear if this will increase costs of operation for SAWS.

Language has also been added to grant the Project Company the discretion to move the location of the well sites relied upon to provide water.[12]

Insurance requirements of the Project Company have been weakened, so that instead of requiring the Project Company to hold $20 million in professional liability insurance for 10 years, the Contract now only requires $10 million.[13] General liability insurance is now only required for only 10 years after the Contract date of

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[6] Express-News Editorial Board, *Reduce Abengoa's role in Vista Ridge,* San Antonio Express-News, March 17, 2016, *available at:* http://www.mysanantonio.com/opinion/editorials/article/Get-Abengoa-out-of-Vista-Ridge-6908041.php
[7] Brendan Gibbons, *Repaying loan may affect SAWS' pipeline deal*, San Antonio Express-News, April 22, 2016, *available at:* http://www.expressnews.com/news/local/article/Abengoa-bridge-loan-part-of-Vista-Ridge-7304756.php
[8] Brendan Gibbons, *Bankruptcy sheds more light on Abengoa's Vista Ridge dealings,* San Antonio Express-News, Sept. 2, 2016, *available at:* http://www.expressnews.com/news/local/article/Bankruptcy-sheds-more-light-on-Abengoa-s-Vista-9201165.php
[9] Contract at 26.6 (A), (D)(3), p. 190.
[10] Contract, *Appendix 8, Performance Guarantee Requirements* at Table 8-1, p. A8-2; at Table 8-2, p. A8-5.
[11] Contract, *Appendix 1, Description of the Project* at 2.2, p A1-22.
[12] *Id*. at 2.1, p. A1-6.
[13] Contract, *Appendix 7, Insurance Requirements* at 7.1.2, p. A7-3.

November 4, 2014 whereas previously it was required for 10 years after completed operations, which would likely have been for several more decades.[14] This seems like a very significant reduction in cost of insurance and likely increases SAWS' exposure if something goes wrong.

Insurance coverage is simply no longer required for liability for claims related to pollution.[15] The latest amendment also weakens requirements for title insurance for acquired property and easements.

The latest amendments also increase the electricity load requirements at the well heads (from 1,119 KW to 1,345 KW), at each of the pump stations from the original contract (HSPS from 6,869 KW to 7,700 KW; IPS #1 from 5,377 KW to 5,425 KW; IPS #2 from 6,869 KW to 8,210 KW), and at the delivery point (from 39 KW to 75 KW).[16] The guaranteed maximum electricity use and guaranteed maximum electricity demand have also been increased. This effectively increases water delivery costs across the board to SAWS ratepayers.

III. The lawsuit between Blue Water and Met Water may have been improperly dismissed in order to declare financial close, and has now been reinitiated.

In 2006, Blue Water Systems ("BW") and Metropolitan Water Co. ("MW") entered into the "Groundwater Resources Marketing Agreement" for the Vista Ridge Project. In 2008, MW conveyed lease rights to BW with the "Partial Assignment of Groundwater Leases." Given investor concerns with past instances of fraud and theft of Mr. Carlson, MW and BW negotiated a structure of a deal which resulted in a trust to hold lease rights and make payments to the parties. One type of payment was as "reservation fees" that MW and BW would receive while the pipeline was being constructed. In May 2015, MW sued BW over reservation fees related to another pipeline they collaborated on, the Manor 130 pipeline. And then in December 2015, MW sued BW claiming, among other things, that certain Assignment of Met Water Lease Rights and all Existing Agreements should be terminated or rescinded. In May 2016, MW and BW parties, attempting to reach a global settlement to both 2015 suits, signed the "Post-Closing Agreement" that required, among other things, for MW to sign a non-disturbance agreement. Then on November 2, 2016, the Vista Ridge project team declared financial close, and on the same day MW notified BW it would not sign a non-disturbance agreement. On November 10, BW sent MW a notice of default of the Post Closing Agreement, and on December 2, 2016 filed another lawsuit targeting the same issues raised before financial close. Since MW refuses to sign the non-disturbance agreement, the Project Company has withheld payments of about $3 million to the two companies ($1.5 million each).

This pending litigation raises two questions. One, did Met Water and Blue Water feign settlement of their dispute in order to improperly secure a declaration of "financial close"? Two, is there any risk that the underlying leases lack the degree of security and reliability required by the contract?

IV. Conclusions

The above legal issues have been identified based on a fairly limited review of the lengthy, complex contract and the amendments approved by SAWS since the contract approval by the council. Further, detailed

[14] *Id*. at 7.1.3, pp. A7-3–4. The original contract required general liability insurance policy to "have a ten years completed operations coverage tail" whereas the current contract requires general liability policy be "renewed for a period of not less than ten years after the Contract date."
[15] *Id.* at 7.1.7, p. A7-4–5. The current contract removes the requirement to have insurance coverage for first party property damage for pollution claims.
[16] Contract, *Appendix 9, Guaranteed Maximum Electricity Utilization and Demand* at Tables 1, 2, 3, 4 & 5, pp. A9-3–4.

review by qualified counsel, independent from SAWS may well reveal other important issues that would further put the City of San Antonio and SAWS ratepayers at risk.

The Ordinance that the San Antonio City Council passed, which gave significant discretion to SAWS to control the project, envisioned that control of the project would revert to Council in the case that the price of water increased. Because several of the concerns outlined above have the potential to increase costs or risk to ratepayers, it can be argued that Council has the right and obligation to review the contract.

SAWS still has the right to terminate the Contract.[17] The Contract states that a "Project Company Remedial Breach" includes an incorrect representation or warranty that results in any material provision of the contract being unenforceable against Vista Ridge.[18] Since a rate review by the PUCT could mean that SAWS cannot enforce the price of water established by the Contract, this is a misrepresentation that justifies termination of the contract.

This and other options should be considered with support from qualified, independent counsel.

[17] Contract at 20.4, p. 167.
[18] Contract at 20.1(B)(5)(d), p.165.