

The Consultant, the Desert Aquifer and the Future of San Diego's Water

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Photo by Sam Hodgson

At its June meeting, the San Diego County Water Authority voted to renew its contract with law firm Brownstein Hyatt Farber Schreck.

Out in the blistering Mojave Desert, there's an underground lake.

The lake, or aquifer, lies, cool and quenching, beneath the agricultural encampment of Cadiz. It stretches north under the Trilobite and Clipper Mountain wilderness areas and out into the desolate Mojave National Preserve.

The owners of the land above this underground water supply, Cadiz Inc., have long hoped to drill large wells into the aquifer, suck out some of the water and pipe it to Southern California, where it could be steamed into a latte in a Malibu café or blasted through a car wash in downtown San Diego.

The project has the potential to make the company and its shareholders serious money, if they can make it happen.

Two hundred miles from Cadiz, in the San Diego suburb of Kearny Mesa, sits one public agency that has the power to bring this desert

water west. The San Diego County Water Authority is charged with securing freshwater supplies for San Diego in the coming decades. It sets policy, makes deals and can generally tighten or loosen the spigot on the county's water supply.

One of the Water Authority's advisers is attorney Christine Frahm. A former chair of the authority's board, Frahm has been heavily involved in local water policy for years, and currently works for the agency as an attorney and consultant.

While she's been advising the Water Authority, and at least one other local public agency, Frahm's firm has built a significant financial relationship with Cadiz Inc. Another shareholder at the firm where she works, Brownstein Hyatt Farber Schreck, Scott S. Slater, was named Cadiz's CEO in February, and the firm recently signed a contract that promises it hundreds of thousands of shares in Cadiz as its project gets closer to completion.

Frahm's exact role at the Water Authority is unclear. Officials at the agency won't say whether she's advising the board on policy matters that could make the success of Cadiz more likely.



But documents obtained by Voice of San Diego

(<http://voiceofsandiego.org>) show Frahm currently works as a consultant for the Water Authority, and has advised another local agency on the future supply of imported water to San Diego County. As such, she's involved, at least indirectly, in shaping policies that could have a direct impact on the financial success of the Cadiz project and, in turn, the value of Brownstein's shares in the company.

Brownstein's multimillion-dollar contract (<http://voiceofsandiego.org/wp-content/uploads/2013/07/BHFS-Agreement.pdf>) with the Water Authority was re-approved last month. As the agency begins months of crucial discussions over the future of San Diego's water supply, it will be receiving advice from a consultant with a significant financial interest in one of the projects that could supply the county with water.

"I could see how this could easily become a conflict," said Mark Robak, a board member of the Otay Water District, a member agency of the Water Authority. "Could Scott Slater and his company really be

impartial when they're advising the agencies? It's a really fine line."

Frahm declined to comment for this story.

Water Authority officials said they're aware of Brownstein's financial stake in Cadiz.

Water Authority attorney Daniel Hentschke said the agency has followed the correct procedures to ensure that Frahm avoids any conflicts of interest as she advises water policy-makers and staff. He said the agency is not facing any policy decisions that might directly impact Cadiz, and said Frahm must recuse herself if she's asked to opine on anything that might financially benefit her.

Pipe Dreams

Viewed from the air, Cadiz, in remote eastern San Bernardino County, is little more than a few green rectangles in a vast ocean of brownish yellow sand and rocks.

Cadiz began as an agricultural project. In the early 1980s, Los Angeles-based Cadiz Inc. purchased 11,000 acres in the Cadiz Valley.

Cadiz drilled wells and hit water. Lots of water. In 1986, the company started planting crops, beginning with grapes and adding a citrus orchard and vegetables until it became, according to Slater, "the largest agricultural operation in San Bernardino County."

Over the years, the company bought more and more land in the Cadiz Valley. And, as hydrologists mapped out the vast aquifer, Cadiz's mission evolved from farming to mining and transporting water.

By 2008, the company had set its sights on building a pipeline from its aquifer to the Colorado River Aqueduct, Southern California's main channel for fresh water from the east. In September 2008, the company entered into a 99-year lease agreement with the Arizona and California Railroad Company to bury a pipeline adjacent to railroad tracks, between its wells and the aqueduct.

Cadiz's plans weren't popular among environmental groups, several of whom sued the company. But as the years progressed, Cadiz built some powerful allies in the water politics world, most notably the Santa Margarita Water District in Orange County, which approved Cadiz's Environmental Impact Report (<http://www.scpr.org/blogs/environment/2012/07/31/9243/santa-margarita-water-district-approves-cadiz-plan/>) in 2012, giving the company's plans a significant boost.

Over the years, Cadiz's financial fate has been intertwined with its political fate.

Stocks and Surges

On May 9, Cadiz Inc. filed a quarterly financial report

(<http://voiceofsandiego.org/wp-content/uploads/2013/07/SEC-Filing-re-Brownstein.pdf>) with the U.S. Securities and Exchange Commission. The document outlines the company's progress with its water-pumping project, and re-ups its relationship with Brownstein Hyatt Farber Schreck.

In addition to a \$25,000 a month fee, the new contract awarded Brownstein 100,000 shares in Cadiz, and promised another 100,000 shares as the company hit each of three milestones.

Brownstein gets another 100,000 shares once all legal challenges to the Cadiz project's environmental impact report have been dismissed. It gets 100,000 more once Cadiz has signed binding agreements for the purchase of 51 percent of the water it has to sell each year. Finally, Brownstein gets 100,000 shares once construction begins on the major facilities for the project.

For Brownstein, there's a lot of money to be made as Cadiz hits those milestones.

As of July 2, Cadiz's stock was trading at \$5.01 a share. But historically the company's share value has been tied directly to its successes in moving its water project forward.

After the company announced its first plans for storing and transporting water in the late '90s, its shares soared, reaching a peak value of \$337.50 in May 1998 (<http://finance.yahoo.com/echarts?s=CDZI+Interactive#symbol=cdzi;range=19920410,20130510;compare=;indicator=volume;charttype=area;crosshair>) and remaining above \$200 a share for most of the next four years as Cadiz moved closer to a deal.

Key to Cadiz's plans was a partnership with the Metropolitan Water District of Southern California, the major water delivery agency in Southern California.

Under pressure from Sen. Dianne Feinstein, who called the project "a terrible mistake (<http://articles.latimes.com/2002/aug/22/business/fi-cadiz22>)," the Metropolitan Water District backed out of the deal in 2002.

Cadiz's stock collapsed, falling into a funk that remains today.

But recently things have been looking up for the project. Its relatively new partnership with the Santa Margarita Water District, combined with support from San Bernardino County, marks a resurgence for the company's plans.

And, if history is any guide, Cadiz just needs to look like it's going to make its project happen in order to attract investors.

If Cadiz were to see a stock surge similar to the late 1990s, Brownstein's current ownership of 100,000 shares would be worth almost \$34 million. If the company were to concurrently hit all its milestones, Brownstein's ownership will increase to 400,000 shares.

Multiply that 400,000 by Cadiz's highest historic share value of \$337.50 and you get a remarkably round, and remarkably large number: exactly \$135 million.

Water from the North, Water from the East



(<http://voiceofsandiego.org/wp-content/uploads/2013/07/WaterMap1.jpg>)

San Diego County gets its imported water from two sources: From the north, it receives water via the California State Water Project, a system of canals that pumps water down from the Sacramento-San Joaquin Delta. From the east, the county imports water from the Colorado River, via the Colorado River Aqueduct.

For years, California water officials have been sketching out a plan to essentially rebuild the State Water Project.

Known as the Bay Delta Conservation Plan, the project aims to balance a host of conservation issues with the expansion and renewal of the aging infrastructure that currently channels water south.

The massive, multibillion-dollar project is reaching a critical juncture.

Over the next few months, water agencies across the state will be analyzing the project and voting on whether to support it.

One of the big players in that conversation is the Metropolitan Water District, of which the San Diego County Water Authority is a key member.

Steve Erie, a professor of political science at the University of California, San Diego and author of a book on local water politics, said the support of the Metropolitan Water District is crucial for the success of the Bay Delta Conservation Plan. If such a big, powerful agency opposes the project, or seeks to limit its scope, it may be dead on arrival, Erie said.

“Historically, any Northern California water project bringing water to Southern California has required a united front on the part of Southern California’s water agencies,” Erie said.

As the second-largest voting bloc on the Metropolitan Water District’s board, the San Diego County Water Authority has considerable sway on the fate of the Bay Delta Conservation Plan. The Water Authority has 17.57 percent of the board’s vote, second only to Los Angeles in terms of influencing policy.

Water Authority officials said the agency still favors the Bay Delta plan, but recent actions by the agency have indicated that it’s considering another option.

Earlier this year, the Water Authority expressed support for studying a different plan to fix the Bay Delta, known as the “portfolio option,” which calls for a much smaller version of the fix to the water supply from the north.

That confused Tim Brick, who recently retired as chair of the Metropolitan Water District.

“I’m puzzled by San Diego’s recent reluctance to move ahead with the Bay Delta Conservation Plan,” Brick told The Planning Report (<http://www.planningreport.com/2013/06/05/tim-brick-retired-chair-mwd-opines-mets-priorities-options>), a trade publication for urban planning groups, on June 5. “I’m puzzled by why they’ve now stepped back and are in what I guess they would describe as a more diversified approach, but it’s also a much smaller and less adequate approach in terms of ensuring reliability for Southern California.”

A smaller approach to the Bay Delta plan would mean that less water would flow to San Diego from the north. The San Diego County Water Authority would therefore have to focus its attention on other sources of water. One such source would be the Cadiz Project.

Lawyer? Consultant? Adviser?

As the Water Authority prepares to discuss the Bay Delta plan and, ultimately, vote on whether to support it, it will be receiving advice from Frahm.

Just what sort of advice isn’t quite clear.

Brownstein's contract with the Water Authority is vague about Frahm's role. It states that Brownstein will provide legal services for the agency, but it also includes a clause stating that Frahm herself works for the authority as a "consultant." Water Authority officials wouldn't comment on what, exactly, she consults on.

"She advises us on many different things," said Dennis Cushman, assistant general manager at the agency.

Hentschke, general counsel for the Water Authority, said the title "consultant" is a term of art. He pointed to the agency's conflict of interest code to help explain what Frahm actually does.

The code, in summary, defines a consultant as someone who is involved in making a "governmental decision" whether to adopt rules or enter into or renew contracts.

Because the Water Authority isn't currently making any decisions regarding Cadiz, Frahm doesn't need to recuse herself from anything, Hentschke said. If, in the future, the Water Authority was to enter into a contract with Cadiz to buy water, for example, then Frahm would have to re-evaluate her role, he said.

"There may be a point where decisions impact Cadiz," Hentschke said. "I don't think we've reached that."

Lara Day, Brownstein's director of communications, emailed a brief statement regarding Frahm's work at the County Water Authority. It says:

Brownstein Hyatt Farber Schreck complies with the State Bar of California's Rules of Professional Conduct (<http://rules.calbar.ca.gov/Rules/RulesofProfessionalConduct.aspx>) governing conflicts of interest (<http://voiceofsandiego.org/wp-content/uploads/2013/07/Final-Conflict-of-Interest-Code-Appendix-no-redline.pdf>), as it does in each state it practices. The firm implements measures to ensure that it discloses potential conflicts of interest and seeks waivers of conflicts when necessary.

In addition to the Water Authority, Frahm also advises the Otay Water District. Board meeting records from that agency show that Frahm advised policymakers there directly on the Bay Delta plan. In the district's September 2012 board meeting, Frahm spoke as if a smaller Bay Delta plan was all but inevitable. The minutes for Frahm's presentation (<http://voiceofsandiego.org/wp-content/uploads/2013/07/Otay-WD-Frahm-opinion.pdf>) read:

"It is felt that in the end, all will agree that the Bay-Delta issues must be addressed, however, the solution will likely be a smaller more modest project."

Comments like those concern water policy watchdogs like Erie.

Erie said he's troubled that the partner of a firm with such a significant financial interest in a water company is playing a role in advising water policy-makers.

"By not fixing the Bay Delta and therefore limiting deliveries from the north, you increase the value of deliveries from the east such as Cadiz," Erie said. "[Frahm's] advice on the Bay Delta therefore directly impacts Cadiz, as it increases the likelihood the project will happen."

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