



# **HOW TO LOSE \$14 MILLION WITHOUT REALLY TRYING**

FEBRUARY 16, 2017

# WATCHDOG?



WAKE UP!

# GOALS

- EXPLAIN WHAT WENT WRONG IN CLAREMONT
- IDENTIFY COMMON CHALLENGES
- EXPLORE CONSTRUCTIVE RESPONSES

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- 40 YEARS OF EXPERIENCE IN LAW AND ACCOUNTING
- 30 YEARS AS A DEPUTY DISTRICT ATTORNEY
- SPECIALIZING IN MAJOR FRAUDS

# DISCLAIMERS

- I AM SPEAKING ONLY FOR MYSELF
- I AM NOT GIVING YOU LEGAL ADVICE
- I DO NOT PRACTICE CIVIL LAW

# CLAREMONT

- 35,000 RESIDENTS
- 11,000 CONNECTIONS
- SERVED BY GOLDEN STATE WATER SINCE 1927
- “THE CITY OF TREES AND PhD’s”





# MULTIDIMENSIONAL ISSUE

- FINANCIAL
- LEGAL
- POLITICAL
- OPERATIONAL



# MULTIDIMENSIONAL ISSUE

- FINANCIAL
- LEGAL
- POLITICAL
- OPERATIONAL
- **PSYCHOLOGICAL**





# PSYCHOLOGICAL FACTORS

- RATIONALITY
- COMMON GOOD
- HUMILITY
- HONESTY
- INDEPENDENT THINKING
- QUESTION AUTHORITY



# PSYCHOLOGICAL FACTORS

- IRRATIONALITY
- SELF-INTEREST
- ARROGANCE
- PRIDE
- CONFORMITY
- DEFERENCE TO AUTHORITY



“OUR WATER BILLS  
ARE TOO HIGH!”

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- NON-FALSIFIABLE STATEMENT
- WE WANT IT TO BE TRUE
- CALL TO ACTION

# “OUR WATER BILLS ARE TOO HIGH”

- IT'S SOMEBODY ELSE'S FAULT
- WE ARE VICTIMS
- WATER IS A NECESSITY
- MONOPOLY CONTROL

“THE GOVERNMENT MUST STOP THIS  
EVIL AND GREEDY CORPORATION  
FROM EXPLOITING ITS MONOPOLISTIC  
CONTROL OF OUR WATER SUPPLY!”



“THE GOVERNMENT MUST STOP THIS EVIL AND GREEDY CORPORATION FROM EXPLOITING ITS MONOPOLISTIC CONTROL OF OUR WATER SUPPLY!”

- INACTION IS NOT AN OPTION
- THERE MUST BE A SOLUTION TO THIS PROBLEM
- PASSION = RESULTS

# CPUC RATE-SETTING

- FORMAL
- RULES-BASED
- EVIDENCE-BASED
- TECHNICAL
- NON-POLITICAL



# TAKING OVER THE SYSTEM

- MOST CITIES HAVE MUNICIPAL WATER
- THE CITY NEXT DOOR HAS LOWER RATES
- WHY PAY FOR PROFITS TO SHAREHOLDERS?
- WHY PAY FOR INCOME TAXES?
- WE NEED TO SET OUR OWN RATES
- LOCAL CONTROL IS BETTER FOR CONSERVATION, PLANNING, RESPONSIVENESS

**“For every complex problem there is an answer  
that is clear, simple, and wrong.”**

**H. L. Mencken**

- GARDENA (1993): LIABILITY INSURANCE, \$26M
- HERCULES (2003): ELECTRIC POWER, \$9M
- MONTICELLO, MN (2009): BROADBAND, \$26M

# SELLING THE DREAM

- GRASS ROOTS ACTIVISM
- APPRAISAL
- FEASIBILITY STUDY
- TOWN HALL MEETING
- ELECTION

# GRASS ROOTS

- CLAREMONT OUTRAGE
- CLAREMONT FLOW
- LOCAL NEWSPAPERS
- ENDORSEMENTS



# APPRAISAL

- LEGALLY REQUIRED
- NO STANDARDS
- NO EXPERIENCE
- NON-BINDING

# APPRAISAL

- RARE TO HAVE CONTESTED VALUATION
- JURY DECIDES THE VALUE
- CAN PICK ANY NUMBER THEY WANT
- USUALLY SPLIT THE DIFFERENCE
- FAVORS THE PROPERTY OWNER

# APPRAISAL

- BIG BEAR LAKE (1986): WATER, \$10.4M vs \$22M
- FELTON (2008): WATER, \$5.3M vs \$13.4M
- MONTARA (2003): WATER, \$5M vs \$11M
- CLAREMONT: \$55M vs \$200M APPRAISAL
- PREDICTED MINIMUM VALUATION OF \$127M

# FEASIBILITY STUDY

- ASSUMPTIONS ARE EVERYTHING
- APPLES AND ORANGES
- NO SUCH THING AS A SMALL ERROR
- NO ONE IS ACCOUNTABLE

# FEASIBILITY STUDY

- CITY REFUSED TO PUBLICLY DISCLOSE STUDY
- “STUDY” WAS JUST A BIG SPREADSHEET
- ASSUMPTIONS WERE FALSE
- \$100M+ ERRORS
- AT TRIAL: “WE NEVER CLAIMED WE WOULD LOWER RATES”

# TOWN HALL MEETING

- INFORMATIONAL MEETING
- COUNCIL IS KEEPING AN OPEN MIND
- “TRANSPARENCY” AND “DUE DILIGENCE”
- EXPERT OPINIONS



# TOWN HALL MEETING

- 100% OF ATTENDEES WANT LOWER WATER RATES
- 99% OF ATTENDEES ARE UNINFORMED ABOUT HOW WATER RATES ARE ACTUALLY DETERMINED
- INCOMPLETE AND BIASED PRESENTATION OF PROS AND CONS
- EMOTION OVER FACTS
- “WE NEED TO DO THIS FOR OUR CHILDREN AND GRANDCHILDREN”

# ELECTION

- FUTURE BOND FINANCING AUTHORIZATION
- NOT REALLY APPROVING THE TAKEOVER
- CITY GETS TO DEFINE THE MEASURE
- “CORPORATE OWNERS ARE INTERFERING IN OUR POLITICS”

# ELECTION

- “No California city has ever successfully taken over its water utility in a contested eminent domain trial, and it will probably take years of litigation and millions of dollars just to find out if we have the legal right to do so. We could lose in court and have nothing to show for it but a massive hole in our budget.”
- MEASURE W PASSED WITH 71% OF THE VOTE

# WHAT HAPPENED NEXT

- CITY COUNCIL PASSED “RESOLUTION OF NECESSITY” (TWICE!)
- COURT TRIAL ON ISSUE OF “NECESSITY”
- JUDGE DECIDED AGAINST CLAREMONT
- \$14M LOSS - \$6.2M OF CLAREMONT’S LEGAL FEES, \$7.7M TO REIMBURSE GOLDEN STATE WATER COMPANY FOR ITS COSTS

# WHY CLAREMONT LOST

- CASE OF FIRST IMPRESSION
- BB&K APPARENTLY NOT EVEN AWARE OF GSW'S RIGHT TO CHALLENGE NECESSITY
- SERIOUSLY FLAWED FEASIBILITY STUDY
- BLOCKBUSTER "LEAD CONTAMINATION" EVIDENCE
- MISUNDERSTOOD LEGAL PRESUMPTION

# POST-TRIAL REACTION

- THE JUDGE MADE A MISTAKE AND/OR WAS BIASED
- UNREALISTIC EXPECTATIONS FOR APPEAL, WHICH WILL COST US AT LEAST ANOTHER \$1M
- CITY WILL ISSUE \$10M BOND TO PAY DEBT
- COUNCIL MEMBERS WILL ALMOST CERTAINLY BE RE-ELECTED
- 10% MERIT BONUS FOR CITY MANAGER

# CONFLICT OF INTEREST

- CITY ATTORNEY FROM BB&K
- TAKEOVER POLICY ADVISORS FROM BB&K
- LITIGATION TEAM FROM BB&K
- THE SAME LAWYERS WHO WERE ENGAGED TO PROVIDE ADVICE TO THE COUNCIL ON THE PROS AND CONS OF FILING AN EMINENT DOMAIN CASE WERE ALSO ENGAGED TO LITIGATE THE CASE - AND TO BILL THE CITY MILLIONS OF DOLLARS FOR THEIR WORK
- THEIR WORK - AND THE REASONABLENESS OF THEIR BILLINGS - WAS OVERSEEN BY A CITY ATTORNEY WHO IS A PARTNER IN THE SAME FIRM

# FAILURE TO ADVISE

- WATER COMPANY'S RIGHT TO CHALLENGE
- RISK OF LOSING CHALLENGE
- COST OF LITIGATION
- LIABILITY FOR WATER COMPANY'S COSTS
- RISK OF UNAFFORDABLE VALUATION
- RISK OF FAILURE TO TAKE OVER FOR OTHER REASONS
- RISK OF FAILURE TO SUCCESSFULLY OPERATE THE WATER SYSTEM



# HEADS IN THE SAND

- 100% FAILURE RATE
- MISSTATEMENTS IN TOWN HALL PRESENTATION
- NO CONSIDERATION OF WORST-CASE SCENARIOS
- NO ESTIMATE OR BUDGET FOR LITIGATION COSTS
- NO UNDERSTANDING OF MAJOR ERRORS IN THE FEASIBILITY STUDY
- NO UNDERSTANDING OR CONCERN FOR RISKS OF ANY KIND

# THE BOTTOM LINE

**THE ONLY THING WORSE THAN LOSING \$14 MILLION IS  
HAVING TO ADMIT THAT YOU MADE A MISTAKE**

# REALITY CHECK

- PEOPLE OFTEN BASE DECISIONS ON EMOTION INSTEAD OF REASON
- PEOPLE PUT TOO MUCH TRUST IN EXPERTS
- PEOPLE TEND TO BE OPTIMISTIC ABOUT THINGS THAT THEY WANT TO COME TRUE
- PEOPLE TYPICALLY LACK THE WILL AND THE DESIRE TO SERIOUSLY ENGAGE COMPLEX PROBLEMS
- MOST PEOPLE WILL NOT ACCEPT FAILURE UNTIL IT BECOMES IMPOSSIBLE TO RATIONALIZE IT AWAY
- PEOPLE WILL GIVE UP A LOT IN ORDER TO SAVE FACE

# WHAT CAN WE DO?

- USE CLAREMONT AS AN EXAMPLE
- MAKE A RECORD
- FOCUS ON THE NEAR-TERM ISSUES
- FOCUS ON PROCESS, NOT POLITICS
- HOLD LAWYERS AND POLITICIANS ACCOUNTABLE
- UNDERSTAND OUR COMMON HUMAN LIMITATIONS

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