



# Santa Clara Valley Water District

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**File No.:** 22-0116

**Agenda Date:** 2/16/2022

**Item No.:** 4.3.

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## **COMMITTEE AGENDA MEMORANDUM Board Audit Committee**

### **SUBJECT:**

Receive an Update on the Status of the Pacheco Reservoir Expansion Fact-Finding Investigation.

### **RECOMMENDATION:**

- A. Receive an update on the status of the Pacheco Reservoir Expansion fact-finding investigation; and
- B. Approve direction to staff to provide results of the fact-finding to the full Board of Directors.

### **SUMMARY:**

The Board Audit Committee (BAC) was established by the Santa Clara Valley Water District Board of Directors (Board) to identify potential areas for audit and audit priorities, and to review, update, plan, and coordinate execution of Board audits.

At its February 17, 2021 meeting, based on direction from the full Board, the BAC approved an update to the BAC Work Plan to include an audit of the Pacheco Reservoir Expansion Project, specifically to understand the timeline associated with cost increases during the exploratory phase of the effort. At its March 17, 2021 meeting, the BAC expressed a preference that the review be conducted by legal firm instead of an audit firm. At the May 26, 2021 meeting, Legal counsel clarified that the effort being conducted is a “fact-finding investigation” not to be confused with an “audit.”

A list of issues to be addressed in the fact-finding was developed based upon District Counsel Office interviews with members of Valley Water’s Water Storage Exploratory Committee, since that was the body that originally brought concerns to the attention of the Board. The District Counsel’s Office ultimately retained attorney Cepideh Roufougar from San Francisco’s Jackson Lewis, P.C. to conduct the fact-finding.

Ms. Roufougar is an experienced investigator in a wide variety of matters for public entities. Ms. Roufougar’s role was not to perform any technical evaluation of project cost escalations or to evaluate whether the escalators were or were not supported by sound engineering principles. The fact-finding, instead, focused on when certain cost information was known and by whom. The fact-finding included interviews with elected officials, interviews with current and former Valley Water

employees, and the review of records related to the Pacheco Reservoir Expansion Project.

The fact-finding has now been concluded. An Executive Summary outlining Ms. Roufougar's efforts and her conclusions is attached hereto as Attachment-1. As noted in the Executive Summary, Ms. Roufougar made the following overarching determination:

The investigator did not find sufficient evidence to conclude that staff withheld information about the cost escalations for the Pacheco Project for a nefarious reason. Instead, the investigator finds that the project was proceeding on simultaneous tracks, with costing estimates needing to be prepared for funding opportunities prior to completion of the geotechnical analysis. As a result, a more complete picture of the costs of the project was not known until late summer or early fall in 2020. At that time, final calculations were performed and it was determined that the cost of the project would be approximately 2.2 billion, increasing to \$2.5B after considering inflation. Upon learning that the feasibility study submitted to Reclamation had been rejected, District staff took steps to share the costs of the project based on completed geotechnical analysis, and alternative options, with the Water Storage Committee (in December of 2020), and then with the full Board (in January of 2021). (Attachment 1, p. 5.)

Staff will be prepared to address any questions regarding the Executive Summary and the underlying fact-finding.

Formal direction is requested from the BAC regarding how and when to report on the results of the fact-finding to the full Board of Directors.

**ATTACHMENTS:**

Attachment 1: Executive Summary Pacheco Expansion Project

**UNCLASSIFIED MANAGER:**

Brian Hopper, 408-630-2765

*Via Email*

February 9, 2022

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**Re:** Executive Summary of Investigation into Pacheco Reservoir Expansion Cost Escalation

Dear Mr. Hopper:

This letter provides a summary of the investigation conducted into the escalation of construction costs related to the Pacheco Reservoir Expansion Project ("Pacheco Project"). Included is a summary of the information obtained during the investigation, the methodology of the investigation, and my conclusions and findings related to when information was known about cost escalations associated with the project.

## **I. Summary of Information Obtained**

The Pacheco Project is a joint project that involves the Santa Clara Valley Water District ("District"), the San Benito Water District, and the Pacheco Pass Water District. The project serves two purposes: (1) to expand water storage capacity in the District; and (2) to meet the needs of remedying issues with the San Luis low point.

In 2017, the District submitted an application for funding from the State of California in support of the Pacheco Project. In support of this application, District staff determined the anticipated cost of the Pacheco Project to be approximately \$969 million. Although this calculation was done in 2017, it was calculated using 2015 dollars under the term of the application for funds.

This amount did not include the costs of consultant contracts, which were unknown at the time of the application. The District was awarded a grant equal to one-half of the projected cost, or approximately \$485 million (“Prop 1 funds”).

At the time that the District applied for the Prop 1 funds, the District had not performed any significant geo-technical inspection of the proposed site of the Pacheco Project. Instead, the feasibility of the Pacheco Project, including the anticipated costs of the project, was determined based on a conceptual design and based on satellite images and GIS information. To obtain access to the site to perform the necessarily geo-technical inspections and study, the District had to resort to the court to obtain access to the proposed site.

After receiving the Prop 1 funds, and in July of 2018, the District created a temporary division known as the Pacheco Project Division. The purpose of this division was to help to take the Pacheco Project from a grant application phase to “full blown capital improvement project.” This included shepherding the project through the planning, design and construction phases. At this time, District staff escalated the project costs to account from when staff applied for the Prop 1 funds. This brought the anticipated cost of the project to \$1.025 billion.

In November of 2018, the District entered into consultant contracts related to the Pacheco Project. These consultant contracts totaled approximately \$120 million. Once these consultant contracts, along with approximately \$25 million in District labor costs that had not been included in the grant application were factored into the project budget, the Pacheco Project was estimated to cost approximately \$1.182 billion. With estimated future inflation, the cost of the Pacheco Project was revised to \$1.345 billion. This cost was included in the District’s Capital Improvement Plan budget in January of 2019.

In June of 2019, the District began performing the geotechnical analysis at the proposed project site. This analysis included taking soil samples and to use a laser survey to get a 3-D landscape of the current site. There were some starts and stops of the geo-technical work, in part due to issues with obtaining site access. Based on what was being discovered during the geotechnical analysis, it was discovered that some of the assumptions in the conceptual design were significantly underestimated. The analysis also revealed challenges that were not obvious in the conceptual design.

While the geotechnical analysis was underway, the District had an opportunity to pursue federal funding to pay for a portion of the Pacheco Project. Specifically, the District applied to receive funding through the Water Infrastructure Improvements for the Nation Act (“WIIN”). In February of 2020, the District prepared and submitted a feasibility study to the Bureau of Reclamation (“Reclamation”). This study included a new preliminary cost estimate of approximately \$1.8 billion (and up to \$2.167 on the high end of contingencies). This cost estimate was created



from scratch and considered the site-specific information that was obtained during the ongoing geotechnical analysis.

In the spring of 2020, District staff were attempting to determine what number should be included in the Capital Improvement Plan budget for the Pacheco Project. According to a witness, staff were debating if they should escalate the costs of the Pacheco Project to be approximately \$2 billion. The District was endeavoring to keep water rates low and adjusting the cost of the Pacheco Project would impact those rates. The decision was made to keep the current costs listed in the budget until the geotechnical analysis was complete and final numbers could be determined.

In June of 2020, the geotechnical analysis for the Pacheco Project was completed. The District began to look at design alternatives to the one which had been proposed in the feasibility study submitted to Reclamation. Several possible alternatives were identified. Because the District was still awaiting a final decision from Reclamation on its application for WIIN funding, staff was sensitive to publishing any information about potential design alternatives while waiting for a decision from Reclamation. Staff was concerned that it would jeopardize efforts to obtain federal funding if staff was to publicly present an alternative that was different from the one described in the feasibility report.

In October of 2020, staff needed to prepare figures for the Capital Improvement Budget. Using the preliminary design figures, staff prepared an update that included approximately \$145 million in “soft costs” such as consultant fees and District costs, plus approximately 5% for construction management costs. The updated costs of the Pacheco Project increased to \$2.2 billion, and up to \$2.5 billion after considering inflation. These figures were then shared with the Water Storage Committee in December of 2020 and with the full Board in January of 2021. This updated cost information was shared after District staff learned that the District would not be receiving WIIN funds through Reclamation.

## **II. Methodology of the Investigation**

The District retained Jackson Lewis P.C. to conduct an investigation into the cost escalations associated with the Pacheco Project. As the investigator, I did not perform a technical evaluation of the cost escalations or evaluate whether the escalations were or were not supported by sound engineering principles. Instead, the focus of the investigation was to determine when certain cost information was known and by whom.

I interviewed District staff assigned to the Pacheco Project. I also reviewed various documents related to the Pacheco Project, including the preliminary cost estimate, various powerpoint presentations, staff reports, and other documents.

In reaching the conclusions summarized below, I did not set out to prove or disprove any sequence of events, but rather to gather information in a neutral fashion and then reach reasoned conclusions. In reaching the conclusions described below, and weighing the evidence that was gathered, a preponderance of the evidence standard was applied. Therefore, an incident was found to have occurred if the preponderance of the evidence obtained during the investigation supported a conclusion that it was more likely than not that the event occurred. In reaching conclusions, I considered information from witnesses that would be considered hearsay in a legal proceeding and gave appropriate weight to such information. Credibility determinations were also made where appropriate.

### III. Summary of Investigation Findings

Based on the information obtained during the investigation, the investigator finds that District staff knew of the potential for cost escalations from the initial application for Prop 1 funds. The original feasibility study was based on a conceptual design, using satellite and GIS information. No geotechnical analysis had been done at the time, and instead, District access to the proposed site was limited by property owners who did not want to grant access. Thus, from the beginning, it was expected that there would be cost increases to the Pacheco Project.

In the summer of 2019, the District began to perform the necessary geotechnical analysis at the proposed site of the Pacheco Project. Based on this analysis, it was determined that the original conceptual design would need to be modified significantly. These design modifications resulted in increases to the construction costs of the Pacheco Project. The first preliminary cost estimate based on the geotechnical analysis was prepared in February of 2020 and in connection with an application for WIIN funds through Reclamation. This preliminary cost estimate provided for an increase in project costs from \$1.3 billion to \$1.8 billion (and up to \$2.167 billion on the high end of contingencies).

The geotechnical analysis was completed in the summer of 2020. After the analysis was completed, it was estimated that the Pacheco Project would cost approximately \$2.2 billion (and up to \$2.5 billion after considering inflation). This estimate was completed in October of 2020 and included in the District's Capital Improvement Plan budget.

Those employees who worked in the Pacheco Project Division were aware of the potential cost increases to the Pacheco Project. A determination was made to not share the preliminary estimate that was submitted to Reclamation for the following reasons:

1. The geotechnical analysis was on-going and had not been completed yet. This information would impact water rates, and so a decision was made to wait on escalating project costs in the District's budget until final costs could be determined.



2. The information provided to Reclamation was a preliminary draft. Staff expressed concern with publishing draft information, as well as information that could negatively impact the pending request for WIIN funding. Staff was sensitive to publishing information and/or taking any steps that could cause Reclamation to believe that staff was exploring project alternatives that differed from the proposal contained in the feasibility study submitted in support of the requested WIIN funding.

On September 9, 2020, during a budget working group meeting, the information from the preliminary cost estimate provided to Reclamation was shared with the District's CEO and elected officials. This information was shared as staff presented information on efforts being made to obtain federal funding for various projects. The Pacheco Project was listed as one of the items for which funding was being sought. During the meeting, staff attempted to explain that the number listed belonged to Reclamation.

The investigator did not find sufficient evidence to conclude that staff withheld information about the cost escalations for the Pacheco Project for a nefarious reason. Instead, the investigator finds that the project was proceeding on simultaneous tracks, with costing estimates needing to be prepared for funding opportunities prior to completion of the geotechnical analysis. As a result, a more complete picture of the costs of the project was not known until late summer or early fall in 2020. At that time, final calculations were performed and it was determined that the cost of the project would be approximately \$2.2 billion, increasing to \$2.5 billion after considering inflation. Upon learning that the feasibility study submitted to Reclamation had been rejected, District staff took steps to share the costs of the project based on completed geotechnical analysis, and alternative options, with the Water Storage Committee (in December of 2020), and then with the full Board (in January of 2021).

Thank you for the opportunity to assist the District in this matter. Please let me know if there are any questions or concerns.

Very truly yours,



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