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## State Water Resources Control Board

December 14, 2015

### VIA ELECTRONIC MAIL

TO: ENCLOSED SERVICE LIST OF PARTICIPANTS

### **PROCEDURAL RULING: MOTION BY PROSECUTION TEAM TO COMPEL PRODUCTION OF DOCUMENTS IN RESPONSE TO SUBPOENA DUCES TECUM**

#### **Background**

On October 30, 2015, the Division of Water Rights Prosecution Team (Prosecution Team) served a subpoena duces tecum on Scott Fahey and Sugar Pine Spring Water, LP (Fahey). The subpoena describes nine categories of documents to be produced related to the diversion and delivery of water by Fahey during the period from May 1, 2014 to at least November 13, 2015.<sup>1</sup> Three of these categories are at issue, specifically:

7. ALL DOCUMENTS and COMMUNICATIONS RELATING TO water sales from the DIVERSIONS covered by Permit 20784 and/or Permit 21289 during the period May 1, 2014 through September 30, 2015; such DOCUMENTS and COMMUNICATIONS shall include invoices, and shall be unredacted, such that the purchase price per unit (e.g. price per gallon), the total purchase price, the purchaser, and the total number of units sold are included and identifiable.
8. ALL DOCUMENTS and COMMUNICATIONS RELATING TO SCOTT FAHEY's personal State and Federal income tax returns or other filings for tax years 2014 and 2015, including any quarterly submittals.
9. ALL DOCUMENTS and COMMUNICATIONS RELATING TO SUGAR PINE SPRING WATER, LP's personal State and Federal income tax returns or other filings for tax years 2014 and 2015, including any quarterly submittals.

On November 18, 2015, Fahey responded by raising certain general objections and by producing certain documents. With respect to categories eight and nine, Fahey refused to disclose any documents, citing the privilege against disclosure of tax returns. With respect to category seven, Fahey indicated that the Prosecution Team already possessed copies of invoices specifying the total number of units sold but with the purchaser, purchase price per unit, and total purchase price redacted. Fahey refused to disclose the redacted information, asserting that it constituted proprietary information and trade secrets. Through counsel, Fahey also admitted that:

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<sup>1</sup> The subpoena specifies that "[u]nless otherwise indicated, the time period covered by this subpoena is from May 1, 2014 to up to five days before [Fahey's] full compliance with this subpoena."

The total Invoice and Contract Sales for Sugar Pine for the period from May to October 2014 was \$119,300.00. The total Invoice and Contract Sales for Sugar Pine for the period from April to October 2015 was \$136,346.36. The total Invoice and Contract Sales for the requested period of 2014 and 2015 was \$255,646.36.

On November 25, 2015, the Prosecution Team filed a motion to compel production of the information requested in categories seven through nine of the subpoena duces tecum, arguing that these documents are relevant to the standard for fixing the amount of civil liability under Water Code section 1055.3 and further arguing that Fahey's tax returns are necessary to rebut a possible inability to pay defense. The Prosecution Team also provided copies of redacted invoices apparently submitted by Fahey. On December 8, 2015, Fahey timely filed its opposition to the motion to compel. With respect to the unredacted invoices, Fahey argued that the motion should be denied because it improperly seeks Fahey's proprietary information and trade secrets. With respect to the tax returns, Fahey contended that the motion violates the tax return privilege and that disclosure of Fahey's tax returns to respond to an inability to pay defense would be premature and unwarranted.

## Legal Analysis

The State Water Board conducts adjudicative proceedings in accordance with the provisions and rules of evidence set forth in section 11513 of the Government Code. (Cal. Code Regs., tit. 23, § 648.5.1.) Pursuant to the Government Code, the Board shall admit evidence "if it is the sort of evidence on which responsible persons are accustomed to rely in the conduct of serious affairs." (Gov. Code, § 11513, subd. (c).) The Administrative Procedure Act authorizes the presiding officer in an adjudicative proceeding to issue an order that is appropriate to protect the parties or witnesses from unreasonable or oppressive demands pursuant to a subpoena or subpoena duces tecum, including violations of the right to privacy. (Gov. Code, § 11450.30, subd. (b); see also Cal. Code Regs., tit. 23, § 649.6.) The scope of discovery shall be limited if the burden, expense, or intrusiveness of that discovery clearly outweighs the likelihood of discovering admissible evidence. (Cf. Cal. Civ. Code Proc., § 2017.020.)<sup>2</sup> A method of discovery shall be restricted if the discovery sought is unreasonably cumulative or duplicative, or is obtainable from some other source that is more convenient, less burdensome, or less expensive. (Cf. *id.*, § 2019.030, subd. (a)(2).) Rules of privilege are effective in Board hearings to the extent that statute otherwise requires the State Water Board to recognize them in a hearing. (Gov. Code, § 11513, subd. (c).)

### 1. Unredacted invoices

#### a. Relevancy of the requested documents

If administrative civil liability is warranted pursuant to sections 1052 and 1055 of the Water Code, then the Hearing Officer will be asked to set the amount of administrative civil liability pursuant to section 1055.3 of the Water Code. Water Code section 1055.3 provides that:

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<sup>2</sup> The State Water Board is not required by statute or regulation to apply the Civil Discovery Act when determining the scope of discovery in adjudicative proceedings before the Board. However, the Hearing Officers have broad power to issue an order that is appropriate to protect the parties or witnesses from unreasonable or oppressive demands pursuant to a subpoena duces tecum. (Gov. Code, § 11450.30.) For the purposes of this ruling, the Hearing Officers find that sections 2017.020 and 2019.030 of the Code of Civil Procedure are persuasive as to the appropriate standard to determine the scope of discovery.

In determining the amount of civil liability, the board shall take into consideration all relevant circumstances, including, but not limited to, the extent of harm caused by the violation, the nature and persistence of the violation, the length of time over which the violation occurs, and the corrective action, if any, taken by the violator.

Any net profits derived from the alleged unlawful diversion would be relevant to “the nature and persistence of the violation.” Indeed, any income derived from the alleged unlawful diversion, whether gross or net, would speak “to the nature and persistence of the violation.” Therefore, the purchase price per unit and total price charged to purchasers are relevant to this proceeding to the extent that they reveal any income derived from the alleged unlawful diversions at issue in this proceeding.

However, the Prosecution Team has not argued that the identities of particular purchasers of water are relevant to this proceeding. The relevancy of this information is not readily apparent. We therefore find that the purchase price per unit and total price, but not the purchasers’ identities, are relevant.

**b. Burden, expense, or intrusiveness of production vs. likelihood of discovering admissible evidence**

The Prosecution Team argues that the proposed discovery is likely to lead to evidence admissible to show an economic benefit from the alleged unlawful diversions pursuant to section 1055.3 of the Water Code. Fahey’s price per unit of water sold and the total price charged to a purchaser would be admissible for this purpose.

However, the proposed method of discovery is highly intrusive. Fahey’s business depends on selling water to haulers for the highest price he can negotiate. Disclosing Fahey’s pricing structure could interfere with his ability to secure favorable prices with existing and new customers. Although the proposed discovery is likely to produce admissible evidence, we are not convinced that imposing this intrusion on Fahey is warranted for the reasons discussed below.

**c. Cumulativeness, duplication, and adequacy of other methods of discovery**

Fahey has already provided his “total Invoice and Contract Sales for the requested period of 2014 and 2015” in response to the Prosecution Team’s subpoena duces tecum. Fahey has also provided redacted invoices that detail the unit sold. These figures should be the sum of all total purchases prices contained in the unredacted invoices. The request for the unredacted invoices is therefore duplicative except to the extent that this information is needed to verify Fahey’s representations in response to the subpoena.

Should the Prosecution Team wish to question the accuracy, completeness, or other attributes of the information disclosed, it will have the opportunity to cross examine Fahey at the hearing. Cross examination is not limited to scope of the opposing party’s case in chief. (Gov. Code, § 11513, subd. (b); see generally Cal. Code Regs., tit. 23, § 648, subd. (b).) Should the Prosecution Team believe that it needs to cross examine additional witnesses to assess the accuracy or completeness of information provided by Fahey, the Prosecution Team is able to subpoena those witnesses to compel their attendance at the hearing. (See Cal. Code Regs., tit. 23, § 649.6.) Therefore, we find that the discovery sought is obtainable from other sources more convenient, less burdensome, or less expensive.

#### **d. Privilege objections**

Because we decline to compel production of the unredacted invoices, we do not reach Fahey's objection that the motion to compel should be denied pursuant to title 5 of part 1 of division 4 (commencing with section 3426) of the Civil Code.

### **2. Tax returns**

#### **a. Relevancy of the requested documents**

Tax returns generally contain a description of the taxpayer's income and liabilities. (See, e.g., 26 U.S.C. §§ 61-66, 1201-02, 1211-12; Rev. & Tax. Code, §§ 17071-78, 18151.) To the extent that Fahey's tax returns contain information on Fahey's income from the sale of water specifically at issue in this proceeding, they are relevant to fixing the amount of civil liability under Water Code section 1055.3 should the Prosecution Team carry its burden of proving that Fahey unlawfully diverted water. The tax returns are also likely to contain information describing Fahey's assets and liabilities, which could be relevant to evaluating Fahey's ability to pay should Fahey raise an inability to pay defense.

#### **b. Burden, expense, or intrusiveness of discovery vs. likelihood of discovering admissible evidence**

The Prosecution Team argues that the proposed discovery is likely to lead to evidence admissible to show an economic benefit from the alleged unlawful diversions. However, it is doubtful that disclosure of Fahey's tax returns will lead to the discovery of evidence admissible for the purposes of determining the appropriate amount of civil liability, if any, under section 1055.3 of the Water Code. Fahey's returns may not differentiate income from any sales of water under the alleged unlawful diversions from Fahey's other tax information. If so, then the tax returns could only provide a general description of Fahey's assets and liabilities. Unless Fahey's ability to pay is in controversy, it is not clear why such a general description would be relevant to determining the appropriate amount of civil liability, if any, under section 1055.3 of the Water Code.

The Prosecution Team also argues that the proposed discovery is likely to lead to the discovery of evidence admissible to rebut an ability to pay defense that could be introduced in Fahey's case-in-chief or rebuttal. However, at this time, Fahey has raised no such defense. Fahey has until December 16 to file exhibits and submit his case-in-chief. It is currently unclear whether Fahey's ability to pay will even be made an issue in this proceeding. Unless made an issue in the Prosecution Team or Fahey's case in chief,<sup>3</sup> it is not clear why Fahey's ability to pay would be relevant on rebuttal. (See Cal. Code Regs., tit. 23, § 648.4, subds. (b), (c); see also *id.*, § subds. (a), (e).)

The proposed discovery is highly intrusive. Fahey has a privacy interest in controlling the disclosure or non-disclosure of his financial affairs. Under certain circumstances, Fahey's tax returns may be privileged. (See Rev. & Tax. Code, § 19542; former Rev. & Tax. Code, § 19282, repealed by Stats. 1993, ch. 31, § 22, p. 152 and readopted without substantial revision

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<sup>3</sup> Modesto Irrigation District, Turlock Irrigation District, and the City and County of San Francisco indicated that they would participate in the hearing by cross-examination or rebuttal only.

by Stats. 1993, ch. 31, § 26, p. 275; see also *Webb v. Standard Oil Co.* (1957) 49 Cal.2d 509, 513; *Scnhabel v. Superior Court* (1993) 5 Cal.4th 704, 721.)

For the foregoing reasons, we find that, at this time, the burden, expense, or intrusiveness of the disclosure of Fahey's tax returns outweighs the likelihood of discovering admissible evidence.

**c. Cumulativeness, duplication, and adequacy of other methods of discovery**

As was discussed in section 1.c., above, Fahey has already disclosed information to the Prosecution Team concerning his total income from water sales during the periods that the Prosecution Team alleges diversion to be unlawful. Even assuming that Fahey's tax returns contain this information, it would be duplicative of information already disclosed to the Prosecution Team.

Should the Prosecution Team wish to question the accuracy, completeness, or other attributes of the information disclosed, it will have the opportunity to cross examine Fahey at the hearing. Therefore, the discovery sought is obtainable from other sources more convenient, less burdensome, or less expensive.

**d. Privilege objections**

Because we decline to compel production of Fahey's tax returns, we do not reach Fahey's objection that the motion to compel should be denied pursuant to the tax return privilege.

**Conclusion**

For the foregoing reasons, the motion to compel is denied. This ruling is made without prejudice to Fahey and without prejudice to any other party filing a subsequent motion based on information not previously offered.

Sincerely,



Frances Spivy-Weber, Vice-Chair



Dorene D'Adamo, Board Member

Enclosure: Service List

**SERVICE LIST OF PARTICIPANTS**  
**G. Scott Fahey and Sugar Pine Spring Water, LP**  
**Administrative Civil Liability Complaint and Cease and Desist Order**  
**(November 13, 2015; Revised 11/30/15)**

Parties	
THE FOLLOWING <b><u>MUST BE SERVED</u></b> WITH WRITTEN TESTIMONY, EXHIBITS AND OTHER DOCUMENTS. (All have AGREED TO ACCEPT electronic service, pursuant to the rules specified in the hearing notice.)	
<p><b>DIVISION OF WATER RIGHTS</b>                      SWRCB Office of Enforcement                      Prosecution Team                      Kenneth P. Petruzzelli                      1001 I Street, 16th Floor                      Sacramento, CA 95814  <a href="mailto:kenneth.petruzzelli@waterboards.ca.gov">kenneth.petruzzelli@waterboards.ca.gov</a></p> <p>Andrew Tauriainen, Attorney III                      1001 I Street, 16th Floor                      Sacramento, CA 95814  <a href="mailto:Andrew.Tauriainen@waterboards.ca.gov">Andrew.Tauriainen@waterboards.ca.gov</a></p> <p>(revised: 11/30/15)</p>	<p><b>G.SCOTT FAHEY AND SUGAR PINE SPRING WATER , LP</b>                      Abbott &amp; Kindermann, LLP                      Diane G. Kindermann                      Glen C. Hansen                      2100 21<sup>ST</sup> Street                      Sacramento, CA 95818  <a href="mailto:dkindermann@aklandlaw.com">dkindermann@aklandlaw.com</a>  <a href="mailto:ghansen@aklandlaw.com">ghansen@aklandlaw.com</a></p> <p>Bart Barringer                      Law Offices of Mayol &amp; Barringer                      P.O. Box 3049                      Modesto, CA 95353  <a href="mailto:bbarringer@mblaw.com">bbarringer@mblaw.com</a></p> <p>(revised 11/30/15)</p>
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