



July 10, 2012

*District Mission:
Dedicated to Satisfying
our Community's
Water Needs*

The Honorable Thomas J. Borris
Presiding Judge
Orange County Superior Court
700 Civic Center Drive West
Santa Ana, CA 92701

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Subject: Response to the 2011-2012 Orange County Grand Jury Report, "Let There Be Light" Dragging Special Districts from the Shadows

Honorable Judge Borris:

The following represents Mesa Consolidated Water District's (Mesa Water) response to the Orange County Grand Jury Findings and Recommendations. All responses are from Mesa Water's perspective.

GRAND JURY FINDINGS:

F-1 Most Orange County special districts, with or without the assistance of the Local Agency Formation Commission (LAFCO) have been incapable or unwilling to consolidate, absorb, or eliminate these outmoded and/or redundant agencies. LAFCO typically addresses larger issues such as merging of cities and elimination of "islands" within the county. The special districts themselves have not worked seriously toward their consolidation or demise. In this regard, the enterprise special districts and the non-enterprise special districts require independent evaluation and handling.

F-1 Response: Mesa Water disagrees with this finding. Mesa Water's Board believes that the power to reorganize (i.e., consolidate, absorb, eliminate, etc.) special districts should always rest with the local citizens who established them and depend on their services. Furthermore, LAFCO has reported that, for the past 20 years, it has given extensive attention to Orange County special districts to proactively and collaboratively consolidate, dissolve and/or merge special districts, with nine such reorganizations since 1995. Lastly, Mesa Water welcomes independent evaluation of its services, and has undergone LAFCO's Municipal Service Reviews ("MSRs") which take place every five years and have found no significant issues with the District (more information at www.oclafco.org).

F-2 Special districts have made very little progress in complying with the recommendations made by various governmental agencies. To ensure recommendations are followed, more coordination and cooperation is needed from the city and county agencies.

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F-2 Response: Mesa Water disagrees with this finding as it is unclear what recommendations this finding references. Mesa Water has complied with various governmental agencies' recommendations -- including recommendations from the Orange County Grand Jury -- that benefit its customers, such as increasing transparency and public information, to provide accountable, efficient and effective core local services. Mesa Water has a long record of coordinating, cooperating, and proactively working together with other public agencies in the area, including regular communications to explore potential economies of scale and further operational efficiencies with the City of Costa Mesa, Costa Mesa Sanitary District, Orange County Water District, Municipal Water District of Orange County, and LAFCO, as well as other regional water districts, municipalities, and governmental agencies.

F-5 The sixteen enterprise districts typically started as local agricultural irrigation providers and sanitation providers for local communities. These special districts have transitioned into providers of potable water and sewage disposal for the cities that blossomed around them after 1950. These districts grew until their boundaries met a neighboring special district that was also growing. Some of these local smaller providers have already been absorbed by larger districts under one management.

F-5 Response: Mesa Water agrees with this finding which shows that special districts provide a focused service to specific communities and those special districts have been consolidated when and where deemed appropriate. Indeed, Mesa Water was formed in 1960 with the consolidation of four small water districts that previously served the area. Today, Mesa Water is an effective district that provides safe and reliable water service to over 110,000 residents, which makes it in the top 1.5 percent of water agencies nationally as discussed in a recent publication on infrastructure funding by the American Water Works Association. Indeed, Mesa Water is a right-sized agency that operates efficiently and effectively as measured by independent analysis and rigorous internal analysis. In over 50 years of operation, Mesa Water has had no reported incidences of water-borne illnesses attributed to its water, and the District has never shut off its water. Furthermore, Mesa Water is among the most economical and efficient water agencies in Orange County according to a recent report -- posted on www.MesaWater.org -- by Raftelis Financial Consultants, which compared per capita annual expenditures among ten Orange County water districts. The report found that per capita expenditures ranged from \$230 to \$635, and Mesa Water's annual expenditure was the lowest at \$230 per capita.

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F-6 The sixteen enterprise special districts of Orange County founded between 1919 and 1964 have grown with the urbanization of the county. Thirteen of these special districts rely upon taxes collected by the county while three rely on fees and other sources for their revenue. This suggests that all of these enterprise special districts could wean themselves from tax subsidies and rely on fees for their revenue. Severance from the tax subsidies would enable financial transparency and let the customers see the true cost of the services provided.

F-6 Response: Mesa Water agrees with this finding as the District is committed to financial transparency and operates without having to rely on property taxes. Because Mesa Water is funded solely by ratepayer fees for water use, the District can better communicate the true cost of its services to customers.

F-7 The unrestricted reserves of the special districts are available to the governing boards to spend as they please. Local citizens are not openly informed of this wealth when agencies ask for fee increases, special assessments, or bond measures. Most of the special districts do not appear to have specific criteria for amassing these reserves nor do they have published long-range plans for their constructive use.

F-7 Response: Mesa Water disagrees with this finding. The District's governing board has established a six-pronged strategic plan, posted on its website at www.MesaWater.org, with financial responsibility as one of its goals. Furthermore, Mesa Water's Board has a written policy of supporting practices that maintain the District's current AAA credit rating from two of the three credit rating agencies. The AAA rating saves money for ratepayers in that it allows the District to finance its capital improvements at the lowest available interest rate. Maintaining a AAA rating involves specific criteria for "days cash on hand" and reserves funding levels. While Mesa Water's reserves are legally classified as "unrestricted", the Board has categorized them as "designated funds" for the sole purpose of economically and effectively maintaining, operating, and repairing the District's already efficient water system. Mesa Water's budget and comprehensive annual financial report for the most recent three consecutive years is posted on its website www.MesaWater.org for local citizens to view. Currently, Mesa Water is working toward publishing a long-range (five-to-ten year) financial plan which, when complete, will also be accessible information for local citizens.

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F-8 The twenty-seven special districts in Orange County have amassed unrestricted reserves of over \$866,000,000. That is enough money to fund all of these special districts for more than year without taxes, fees, interest, or other sources of revenue. The boards of directors have the sole discretion to spend these unrestricted reserves.

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F-8 Response: Mesa Water disagrees with this finding. Barring a catastrophe or emergency situation, it would be irresponsible for a special district to fund its operations by spending its reserves, whether or not they are unrestricted. Just as it is prudent for individuals to save for many years in advance to fund a child's college education, or for retirement, and for homeowner associations to save reserve funds for property upkeep, the Mesa Water Board believes that it is sound financial management to set aside reserves for funding future infrastructure replacement, refurbishment and improvements so that customer rates can remain stable and not be severely impacted with sizeable, sudden increases or special assessments to pay for large capital expenditures in the future. Using sophisticated financial planning models, the Mesa Water Board regularly evaluates its future infrastructure funding needs. These best practices have been emphasized for more than a decade by respected national organizations including the American Water Works Association, which recently released another study indicating the looming need for adequately funding infrastructure replacement through a combination of savings and strategic borrowing. Mesa Water has been ahead of the curve on this issue and is recognized as a leader in prudent financial planning. Please also refer to the response to F-7 regarding the Mesa Water Board's reserves funding policy and purpose.

F-10 The enterprise special districts could save millions of dollars in administration costs by consolidation into regional special districts. Five or six such enterprise special districts within Orange County could save at least \$500,000 per year for each special district absorbed.

F-10 Response: Mesa Water disagrees with this finding on the basis that it is unclear what criteria, if any, the Grand Jury used in selecting "five or six" enterprise special districts or in arriving at the "\$500,000" figure. Furthermore, a one-size-fits-all, top-down approach of consolidating into regional special districts may not allow Mesa Water to deliver the needed local service. Deliberate study and planning at the local level, such as LAFCO's MSRs, are necessary to identify efficiencies and ensure consumers receive effective services. As mentioned in our response to F-5 above, Mesa Water is already in the top 1.5percent of agencies nationwide in terms of

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size. As has been amply demonstrated for many decades, larger government does not translate to more efficient government. Further consolidations of large agencies like Mesa Water with other agencies with other large agencies are unlikely to produce the results imagined. Mesa Water and other independent special water districts in Orange County provide valuable services to consumers; these districts do an excellent job of providing safe, reliable, affordable water. Mesa Water encourages the Orange County Grand Jury to further weigh its concerns against the benefits that independent special districts provide. Furthermore, please also refer to Mesa Water's responses to F-1 and F-2 above, which apply to this finding as well.

F-15 Only one of the special districts, The South Coast Water District, has had recent performance audits. The lack of performance audits for the remaining special districts leaves the potential for inefficiencies, poor practices, outmoded operations, etc. hidden from the governing boards and the communities they serve. The lack of published performance audits has contributed to the public's ignorance of these districts.

F-15 Response: Mesa Water disagrees with this finding. Mesa Water has undergone LAFCO's Municipal Service Reviews ("MSRs") which take place every five years and have found no significant issues with the District (more information at www.oclafco.org). Additionally, Mesa Water has undertaken, published, and reported on several audits in the areas of finance and operations which show that the District is performing well with effective, efficient and up-to-date practices. The District annually undergoes a financial audit by a credible third-party accounting firm. Furthermore, for the past 17 consecutive years, *Mesa Water has received a Certificate of Achievement for Excellence in Financial Reporting* from the Government Finance Officers Association.

With regard to Mesa Water's operational efficiency, please refer to the response to F-5 above. Also, a 2011 study by the American Water Works Association of the District's water system found that Mesa Water has one of the lowest water loss rates in North America...which means that the District's water system is "water tight." Furthermore, the District has accomplished recent achievements in the areas of a) administration; b) communications; c) conservation; and, d) customer service as outlined below:

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- a) **With respect to the District's administration, Mesa Water is a *California Special Districts Association District of Distinction* (since 2007 when this accreditation was inaugurated), accredited by the *Special District Leadership Foundation*. This accreditation recognizes agencies that provide essential public services in a fiscally responsible manner.**
- b) **In the area of communications, Mesa Water has won three awards in the past year for the District's public information and outreach activities—a *PROTOS* from the *Public Relations Society of America, Orange County Chapter* for outstanding achievement in community relations; a first place *Excellence in Communications Award* from the *California Association of Public Information Officers*; and, the *Exceptional Public Outreach Award* from the *California Special Districts Association*.**

From the standpoint of conservation, Mesa Water has one of the highest rates of customer water use efficiency (a.k.a. water conservation) among Orange County water agencies, and the District has already achieved its "20 percent by the year 2020" reduction in per capita water use mandated by the Water Use Efficiency Senate Bill, SBx7-7, also known as the Water Conservation Act of 2009.

- c) **For customer service, according to a recent poll, over 90 percent of Mesa Water customers are satisfied with the District's water quality and customer service. Mesa Water annually performs over 30,000 water quality tests to ensure its tap water is clean and safe, and the District's water meets and surpasses all State and Federal water quality standards.**

Finally, and significantly, Mesa Water will soon achieve its Board's long-standing vision of having a 100 percent local and reliable water supply when the District's improved Colored Water Treatment Facility returns to service, *inevitably saving ratepayers' money and reducing the District's carbon footprint with less energy use and reduced greenhouse gas emissions.*

GRAND JURY RECOMMENDATIONS:

- R-1 All special districts (except the Vector Control District and the County Cemetery District) should be eliminated from the county tax rolls and should rely solely on fees or the services of surrounding governments. (See F2, F3, F4, F5, & F6.)

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R-1 Response: The recommendation will not be implemented because it is not warranted (please refer to Mesa Water's responses to F-2, F-5, and F-6 above). Mesa Water already does not receive property tax revenue and has not since the 1970s.

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R-4 Water and sewer districts should be consolidated into no more than six regional districts. Consideration should be given to including the city water agencies in the consolidation. LAFCO should meet with the water and sewer districts before October 31, 2012 to develop plans and schedules for consolidation. (See F5, F6 & F9.)

R-4 Response: The recommendation will not be implemented because it is not reasonable. It is unclear what, if any, criteria were used in reaching this recommendation. While "six" may sound like a nice round number, it is not the number of special districts that is paramount but the ability of each district -- like Mesa Water -- to deliver core local services effectively and responsibly. Mesa Water is sensitive and responsive to the community it serves (please refer to Mesa Water's responses to F-5 and F-6 above). Furthermore, LAFCO has stated its disagreement with this recommendation in that it has made no analysis, as required by the government code, of such a proposal. However, if LAFCO arranges the recommended meeting with regional water and sewer/sanitation districts, Mesa Water would participate. As it should, LAFCO does continue to meet regularly with water and sewer districts -- including Mesa Water -- as well as with cities, in order to assess the quality of services and recommend improvements where appropriate, using thoughtful criteria and applying it case-by-case.

R-5 Water and sewer districts should be removed from the tax rolls and operate solely on fees and other revenues for their services. Consideration should be given to forming non-profit agencies with ownership shared by the constituents. These districts should meet with county officials before October 31, 2012 to prepare plans and schedules to remove themselves from the county tax rolls. (See F2, F5, & F6.)

R-5 Response: The recommendation will not be implemented because it is not warranted (please refer to Mesa Water's responses to F-2, F-5, and -F6 above).

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R-6 Special districts should adopt "board of director's practices" for all their reserves, restricted and unrestricted. All reserves should be classified in their 2013-2014 budgets according to GASB Standard No. 54. LAFCO should work with the special districts to prepare standard criteria for accumulating reserves according to the new classifications by December 15, 2012. These standards should be used in preparing the 2013-2014 budgets. (See F7 & F9.)

R-6 Response: The recommendation will not be implemented because it is not warranted. Mesa Water already has a "board of director's practices" for the District's reserves (please refer to Mesa Water's responses to F-7 above). Regarding the Government Accounting Standards Board (GASB), as an enterprise district, Mesa Water is not required to operate according to GASB Standard No. 54, and the District meets GASB standards appropriate to enterprise districts.

R-7 Excessive unrestricted reserves should be used to reduce existing debts. Future revenues should be reduced to avoid the accumulation of unallocated revenue that does not meet the adopted new standards. (See F7 & F8.)

R-7 Response: The recommendation will not be implemented because it is not warranted. It is unclear what "excessive unrestricted reserves" is considered to be, and it is unclear what the adopted new standards will be. It is important to note that there are myriad variables that the Mesa Water Board considers in budgeting and long-term planning. Furthermore, Mesa Water's Board is successfully executing its fiduciary responsibilities to the District's constituents (please refer to Mesa Water's responses to F-7 and F-8 above).

R-8 Each special district should have an independent performance audit at least every three years. The executive summary of the performance audit should be distributed to all the taxpayers of each special district. Each of the special districts that has not had a performance audit within the last five years should contract with an independent outside consultant to conduct such an audit during 2012. These audits should be repeated at least every three years. (See F15.)

R-8 Response: The recommendation will not be implemented because it is not warranted (please refer to Mesa Water's response to F-15 above). Mesa Water annually undergoes a financial audit by a credible third-party accounting firm, and the District offers a multitude of performance reports posted on its website at www.MesaWater.org, including its budget and comprehensive annual financial report for the most recent three consecutive years. Additionally, Mesa Water's MSR by LAFCO, which takes place

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every five years, has found no significant issues with the District (Mesa Water's most recent MSR is posted online at www.oclafco.org).

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R-9 Each special district should contribute 1percent of its unrestricted reserve fund to LAFCO to help finance preparing and directing the consolidation, absorption, or elimination, and the setting of standards for reserves for the special districts. These funds should be included in LAFCO's future programs and budgets until the consolidation, absorption or elimination of each special district is achieved. With these additional funds, LAFCO should begin meeting with each special district before the 2014 fiscal year is budgeted for consolidation, absorption and/or elimination of these districts. (See F1, F2, F3, F4, F5, & F6.)

R-9 Response: The recommendation will not be implemented because it is not reasonable (please refer to Mesa Water's responses to F-1, F-2, F-5, and F-6 above). The arbitrary nature of this 1percent recommendation is similar to the recommendation of six regional water agencies for Orange County. It is unclear as to what, if any, criteria were used in quantifying how much revenue LAFCO needs, not to mention the implications in using this funding source. Furthermore, a process currently exists for funding LAFCO, which includes a combination of assessments upon local agencies, including special districts like Mesa Water, based on their revenues and application fees for specific LAFCO efforts. The Mesa Water Board believes it is inappropriate and dangerous to arbitrarily shift funds safeguarded for affordable rates, emergency preparation, infrastructure maintenance, and long-range capital improvements. Shifting money from special districts' reserves will not reduce the need for prudent reserves funding. Rather, as evidenced by past funding shifts from the state, this will: a) increase cost pressures on ratepayers and taxpayers to fund core services; b) increase fiscal uncertainties; and, c) place pressure on some local agencies in Orange County to increase reserve funding.

Respectfully,



Fred R. Bockmiller, Jr., P.E.
President, Board of Directors

c: Roy B Baker III, Forman, Orange County Grand Jury
Mesa Water Board of Directors