



# Yorba Linda Water District

*Reliable and Trusted Service  
for More Than 100 Years*

July 26, 2012

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

Dear Judge Borris:

Thank you for the opportunity to review and comment on the Orange County Grand Jury's report, "Let There Be Light – Dragging Special Districts from the Shadows". The comments provided address the findings and recommendations requiring a response from the Yorba Linda Water District (YLWD).

Regards,

Phil Hawkins, President  
YLWD Board of Directors

CC: Orange County Grand Jury

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## YORBA LINDA WATER DISTRICT FINDINGS

**F1.** *“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 those outmoded and/or redundant agencies. LAFCO typically addresses larger issues such as the merging of cities and the 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.”*

**Response:** *Disagrees with Finding*

The ability or willingness of an overburdened city to provide yet another service does not make it an improvement over the focused, expert capabilities a special district provides. Overwhelmed and understaffed, the City of Yorba Linda, in 2011, requested that YLWD assume responsibility for their sewer system in a cooperative move aimed at improving service quality for the community. In its own words, the Grand Jury states that special districts were created *“to provide services that neither the county nor the local cities were able or willing to provide.”* The 2011 sewer transfer transition supports this statement as still appropriate. The Grand Jury’s use of the past tense in the statement, however, explains its one-size-fits-all, top-down approach to reforming special districts. If nothing else, YLWD’s experience supports the fact that deliberate study and planning at the local level is necessary to ensure viability and identify efficiencies. Ultimately, the power to reorganize local services should always rest with the local citizens who established them and depend on them.

**F2.** *“Special Districts have made very little progress in complying with the recommendations made by various government agencies. To ensure recommendations are followed, more coordination and cooperation is needed from the city and county agencies.”*

**Response:** *Disagrees with Finding*

To the best of YLWD’s knowledge, it has never received recommendations from city or county agencies. In the event that such a recommendation is received, it will be given due consideration. While YLWD supports coordination and cooperation amongst local agencies, it retains its independent jurisdiction and cannot and should not be mandated to follow the recommendations of external agencies.

**F5.** *“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 small providers have already been absorbed by the larger districts under one management.”*

**Response:** *Agrees with Finding*

**F6.** *“The sixteen enterprise 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.”*

**Response:** *Disagrees with Finding*

Financial transparency is independent of the true cost of service. The Grand Jury's focus on financial transparency would not be furthered by an increase in fees or a reduction in property tax revenue. Currently, every property tax dollar received is budgeted and factored into the premier level of service that is offered by YLWD.

Though the true cost of service of governmental agencies provided to the general public is a valid issue, it tends to be “hidden” more in cities and counties than in special districts. Recent concerns with local cities have highlighted the fact that fees paid for specialized services, including those of water and sewer, often are supplementing other aspects of the city. Special districts focus on specialized services and while property taxes may be used to lower fees associated with those services, property taxes are NOT diverted to other government programs as revenues could be by a city or county.

YLWD agrees that severance from property taxes would allow customers to see the true cost of the services provided. However, YLWD does not agree that severance from property taxes would be in the best interest of the public. The loss of property tax revenue requires raising rates to compensate for the revenue losses in order to maintain operations. The three special districts referred to did not voluntarily wean themselves from taxes collected by the county, but rather never had access to them. It would be irresponsible of a public agency not to utilize every possible source of revenue so as to maintain the lowest practical fees for their customers.

**F7.** *“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.”*

**Response:** *Disagrees with Finding*

YLWD finds the majority of this finding to be blatantly false. While YLWD does agree that unrestricted reserves are able to be spent at the discretion of the Board, governing boards are just that – elected by the public to make policy decisions; such as in the case of reserves.

At YLWD, a Financial Reserves Policy is adopted annually to give guidance over reserves and target balances. For each reserve, the policy defines the reserve, identifies target levels and establishes requirements for its use. Long-range plans are

detailed in the annual budget, which is available to the public for comment prior to its adoption and at all times on the District's website. Reserves are reviewed by the Board and available to the public on a monthly basis.

**F8.** *"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."*

**Response:** *Disagrees with Finding*

To date, YLWD's reserves have not exceeded the guidelines set forth in the Financial Reserves Policy. The District's current concern is one of being below a prudent reserve level rather than that of amassing excessive unrestricted reserves.

The Grand Jury is making the assumption that "unrestricted reserves" are actually undesignated reserves - available for any purpose at any time. The Grand Jury is not considering that governmental agencies are unable to legally call reserves that are designated for particular purposes, such as capital improvements or emergency funds, "restricted reserves". "Restricted reserves" are only monies that an external source has legally restricted. An example of this is an improvement district or community services district voting to issue a bond to fund infrastructure while pledging to pay off the bond from proceeds on their property tax rolls.

As of June 30, 2012, YLWD has 4 unrestricted, yet designated reserves - Emergency Reserve, Capital Replacement Reserve, Maintenance Reserve and Employee Liabilities Reserve. YLWD has only one legally restricted reserve - US Bank 2008 COP Reserve, which is required as a part of our bond agreement. The only "undesignated" reserve YLWD has is an Operating Reserve, which contains one to two months of annual operating expenses, as recommended by the Government Finance Officers Association.

**F9.** *"The Orange County Auditor-Controller allocated nearly \$35,000,000 to four enterprise special districts (Costa Mesa Sanitary District, South Coast Water District, Trabuco Canyon Water District, and Yorba Linda Water District) that did not show this revenue in their budgets provided to the Grand Jury. What happened to that money is not clearly recorded. Budgeting without the allocated taxes indicates that, along with the three other enterprise special districts that do not rely on tax revenue, these enterprise special districts could function without tax revenues."*

**Response:** *Disagrees with Finding*

The Grand Jury never approached YLWD to obtain budgets. The budget referred to in the comment is not identified by year. The District has posted all budgets from FY 09/10 to the current on its website. In all of those budgets, the District has clearly recorded property tax revenue as a Non-Operating Revenue. Without those tax revenues, the District would require an immediate increase in the water rate to meet debt service coverage requirements and budget prudently.

**F10.** *“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 beyond.”*

**Response:** *Disagrees with Finding*

It is unclear how the Grand Jury chose “five or six” enterprise districts or arrived at the figure of “at least \$500,000,” however, YLWD sees such a consolidating effort as an inevitable disaster. YLWD services the communities of Yorba Linda and a small portion of Placentia. This allows customers to elect their board from their community and attend the meetings which are held locally. To construct massive consolidated conglomerates would only serve to further distance customers from their special districts as well as prove a monumental task with regards to managing services across such large areas.

**F14.** *“The true cost of water and sanitary sewers in the enterprise special districts is hidden when both taxes and fees fund these districts. Only when the monthly service bills to the customers include all the costs for these services without the tax subsidy will the public understand the true cost of these services and achieve financial transparency.”*

**Response:** *Disagrees with Finding*

Please refer to the response to F6 above as it applies to this finding as well.

**F15.** *“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.”*

**Response:** *Disagrees with Finding*

YLWD participated in an American Water Works Association (AWWA) run, anonymous self-evaluation by employees 2 years ago. The employees knew best the areas for further improvement in their respective departments and since the evaluation YLWD has been working toward addressing and improving upon these areas. It is also important to note that had the Grand Jury discussed the referenced performance audit with The South Coast Water District, it would have found that it was a raging disaster. The auditor had no experience working with special districts and even went so far as to recommend a decrease in service quality because the potentially catastrophic risk imposed on the community was considered more cost effective than regular maintenance.



**R1:** *“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.”*

**Response:** *The recommendation will not be implemented because it is not reasonable.*

The legal definition of a tax is a charge levied against a transaction for revenue to be spent in an unrelated activity. An example of this is the referenced County property tax which is not being used to pay for costs incurred by the County as a result of the property but, in the case of YLWD, to subsidize water and sewer. The legal definition of a fee is a charge levied to support the actual governmental cost of an activity. This means that should this recommendation be adhered to, the cities of Yorba Linda and Placentia would have to either absorb YLWD so that the increased charge to the community could be called a fee, raise taxes in any number of ways to subsidize the loss of revenue to YLWD as a result of the County cuts, or remove themselves from the equation all together leaving YLWD with no choice but to raise their fees to make up for said cuts.

It is also important to highlight the fact that, as stated in the response to F6, this recommendation does not propose to cut the tax roll of the County, but instead removes YLWD's access to the tax revenue stream. This would result in a greater cost to the community who would see those taxes levied against them by the County remain the same while the taxes and fees of their city and/or YLWD increase.

**R4.** *“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.”*

**Response:** *The recommendation will not be implemented because it is not reasonable.*

According to the 2010 census, the population of Orange County is 3,010,232 people. Given the Grand Jury's recommendation that all of the county's water and sewer be provided by six districts, that means that each new district would provide both services to over 500,000 customers. YLWD currently provides water and sewer to just under 25,000 customers and regularly experiences the difficulties involved in attempting to balance the often competing needs and concerns of its customers. Simply by making a district more than 20 times larger than YLWD, it will become virtually impossible to maintain this level of customer service. It is for this reason that YLWD does not intend to meet at any time in the foreseeable future over matters of such broad scale consolidation.

**R5.** *“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.”*

**Response:** *The recommendation will not be implemented because it is not reasonable.*

Please see responses to F6 and R1.

**R6.** *“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.”*

**Response:** *Disagrees with Finding*

GASB 54 was written solely for agencies recording governmental activities. YLWD, as well as the vast majority of all the special districts in Orange County, operates as a type of proprietary fund, and is exempt from the standards written in GASB 54. YLWD annually adopts a Financial Reserves Policy, which defines, identifies target levels, requirements for the use, and requires periodic review requirements for each reserve. With each special district being so unique and facing unique circumstances, creating standard criteria for accumulating reserves would be difficult at best, and would absolutely fall outside of the purpose of LAFCO.

**R7.** *“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.”*

**Response:** *Agrees with Finding*

It is difficult to determine what the Grand Jury defines as “excessive unrestricted reserves”. Regardless of the definition, however, YLWD believes that their reserves would not fall into this category. YLWD annually adopts a Financial Reserves Policy by resolution, which sets target levels for reserves to ensure that the District never reaches “excessive unrestricted reserves”.

**R8.** *“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.”*

**Response:** *The recommendation will not be implemented because it is not reasonable.*

Please see response to F15.

**R9.** *“Each special district should contribute 1% 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 special districts. These funds should be included in LAFCO’s future programs and budgets until the consolidation, absorption or eliminating 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.”*

**Response:** *The recommendation will not be implemented because it is not reasonable.*

If all special districts followed the Grand Jury’s recommendation, the immediate impact would be that every special district customer would have their rates increased or a significant level of service decrease to counter the revenue lost by a new “unfunded mandate”. Fortunately the Grand Jury is not able to create this mandate, just to recommend it. YLWD believes our 1% would result in zero consolidations, absorptions or eliminations. The City of Yorba Linda has no interest in taking on the responsibility of the local area’s water and sewer pipelines, as is evidenced by the City’s transfer of their sewer system to YLWD in July 2011. No special district shares a boundary with YLWD, and while Golden State Water Company does, the Grand Jury would be hard pressed to find any customer of YLWD who is requesting to have a for-profit company provide their water.