

## Grand Jury Report

### RESPONSE FORM

**Report Title: Ukiah Valley Sanitation District – Change and Transparency Needed**

**Report Date: June 19, 2019**

---

**Response Submitted By:**

Ukiah Valley Sanitation District  
Theresa McNerlin, Chair  
151 Laws Avenue  
Ukiah, California 95482

Responses MUST be submitted, pursuant to *Penal Code* § 933, no later than September 17, 2019

**We reviewed the report and submit our responses to the FINDINGS portion of the report as follows:**

- We agree with the findings numbered:
- We disagree wholly or partially with the findings numbered: F1, F2, F3, F4, F5, F6, F7, F10, F11, F12, F13, F14. Attached, as required, is a statement specifying portions of the findings that are disputed with an explanation of the reasons therefor. (See **Attachment**, “FINDINGS” section.)

**We reviewed the report and submit our responses to the RECOMMENDATIONS portion of the report as follows:**

- Recommendations numbered: R1 and R4 have been implemented. Attached as required is a summary describing the implemented actions. (See **Attachment**, “RECOMMENDATIONS” section.)
- Recommendations numbered: R2 and R3 will not be implemented because they are not warranted or are not reasonable. Attached, as required, is an explanation of why the Recommendation(s) are not warranted and/or not reasonable. (See **Attachment**, “RECOMMENDATIONS” section.)

We have completed the above responses, and have attached, as required, the following number of pages to this response form:

Number of Pages attached: 159  
Exhibits: 11

We understand that responses to Grand Jury Reports are public records. They will be posted on the Grand Jury website: [www.mendocino county.org/government/grand-](http://www.mendocino county.org/government/grand-)

jury. The clerk of the responding agency is required to maintain a copy of the response. The response will all be posted on the District's website: [www.uvsd.org](http://www.uvsd.org).

We understand that we must submit this signed response form and attachment as follows:

First Step: E-mail in pdf format to:

Grand Jury Foreperson at: [grandjury@mendocinocounty.org](mailto:grandjury@mendocinocounty.org)

The Presiding Judge: [grandjury@mendocino.courts.ca.gov](mailto:grandjury@mendocino.courts.ca.gov)

Second Step: Mail all originals to:

Mendocino County Grand jury

P.O. Box 939

Ukiah, CA 95482

Theresa McNerlin  
Chair, Ukiah Valley Sanitation District

Date: September 16, 2019



**UKIAH VALLEY SANITATION DISTRICT BOARD OF DIRECTORS' RESPONSE TO  
2018-2019 GRAND JURY REPORT**

**UKIAH VALLEY SANITATION DISTRICT – CHANGE AND TRANSPARENCY NEEDED**

The Ukiah Valley Sanitation District Board of Directors welcomes this opportunity to respond to the Grand Jury report titled Ukiah Valley Sanitation District – Change and Transparency Needed.

**Pursuant to the request of the Grand Jury, The Board of Directors responds as follows.**

**INTRODUCTION**

In October of 2018, the Ukiah Valley Sanitation District (“District”) entered into a final agreement to settle its lawsuit with the City of Ukiah (“City”). The settlement resolved two issues of concern, not only to the District, but to the 2013 Grand Jury as well. In its April 3, 2013 report, the Grand Jury suggested, “the UVSD should seek legal counsel regarding capture of lost revenues and options to disassociate from the [Participation Agreement],” which was then in place with the City. (Exhibit 1, p.1.)

The lawsuit resulted in the District recovering millions of dollars from the City, implementing the 2013 Grand Jury’s recommendation (R3) that “[t]he UVSD use legal counsel to recapture lost revenues from the City of Ukiah.” (Exhibit 1, p. 6.) The final settlement agreement in the lawsuit also addressed the 2013 Grand Jury’s opinion that “[t]he [Participation Agreement] that binds the two entities has been biased towards the City from the start, and is not a fair or workable document.” (Exhibit 1, p. 3.) The 2013 Grand Jury observed that “[t]he City ha[d] no motivation or reason to change the [agreement]” and therefore recommended (R4) that “[t]he UVSD seek legal counsel regarding options to disassociate from the Participation Agreement.” (Exhibit 1, pp. 3, 6.) With that mind, as part of the final settlement agreement, the District insisted on a new and fair Operating Agreement (Exhibit 2), which replaced and superseded the old Participation Agreement.

The District is now free from the unfair and one-sided Participation Agreement, as it had been amended over the years, and is looking forward to working with the City to make cost efficient changes. The Operating Agreement promotes transparency and gives the District the opportunity to operate and serve its ratepayers more efficiently. The new agreement doesn’t mean the District will withdraw from utilizing City services, it simply provides an opportunity to explore and implement cost savings measures not afforded under the old Participation Agreement.

The District has since hired an experienced manager at a substantial savings to District ratepayers. Its financial processes under the Operating Agreement serve to provide monthly, quarterly, and annual reports and extend important oversight over the expenses it is charged by the City, which has already proved valuable.

## **FINDINGS**

**F1:** The lawsuit settlement between the City and District left unresolved issues resulting in current arbitration, and continued duplication of services and costs.

**RESPONSE: The District disagrees wholly with this finding.** The lawsuit settlement did not leave “unresolved issues resulting in current arbitration” or continued duplication of services and costs. The budget dispute, which is the subject “unresolved issue,” did not even exist when the parties settled the lawsuit. Therefore, it was not something left unresolved by the settlement.

In fact, the parties did not engage in the budget process that led to the dispute until after the lawsuit was settled. Further, the parties have yet to engage arbitration over the budget disputes. The District is making every effort to resolve these disagreements without arbitration.

The District is an independent governmental entity that is required to function as such.<sup>1</sup> There are few, if any, functions performed by the District that duplicate services performed by the City aside from those inherent in a joint system.

**F2:** There is only one sewage collection and treatment system, which serves both the City and District.

**RESPONSE: The District disagrees partially with this finding.** There are two sewage collections systems, one owned by the District and the other owned by the City. The District also owns the trunk line into which all sewer mains, both District and City, flow. The trunk line, in turn, transports all wastewater to the treatment plant site, which the City owns. However, the District owns a certain portion of the treatment plant’s capacity. (Exhibit 2, pp. 23-26, § II.E.1. [“DISTRICT Dedicated Capacity”].) The treatment plant treats the wastewater from both systems. While these components are physically connected, they are identifiably distinguishable systems.

**F3:** The City and District being jointly responsible for the single sanitation system has led to significant needless expense.

**RESPONSE: The District disagrees wholly with this finding.** The system is comprised of two interconnected systems. It is not accurate to describe it as a single system, including in relation to governance. (See Response F2.)

The District is an independent governmental entity. While the District disagrees with this finding, the District does agree with a related finding (F3) in the 2013 Grand

---

<sup>1</sup> In the 2009 Grand Jury’s report, the District’s rights and duties as an Independent Special District were outlined, inclusive of the following items: procure services, enter into contracts and agreements, incur debt, employ personnel, adopt resolutions and ordinances, initiate and approve annexations, approve and construct sewer extensions and new connections, establish user rates, fees and charges. (Exhibit 3, p. 7.)

Jury's report: "The unilateral management [of the Combined System] by the City of Ukiah has resulted in fees/fines that the UVSD has been required to pay. City upper management has shown a lack of respect to UVSD by being unresponsive to requests, and expecting UVSD to immediately concur with the City's decisions." (Exhibit 1, p. 6.) The District is responsible to serve and protect the best interests of its ratepayers and must conduct itself accordingly. The Operating Agreement serves to further that end.

It is unclear what the Grand Jury means by needless expense since no supporting facts are specified for the finding. That said, the District's governance and oversight of the Combined CITY/DISTRICT Sewer System ("Combined System") has *saved* it from absorbing significant improper expense charged to it by the City and created millions of dollars in benefits that would have otherwise been lost or unrealized.

In terms of expenses, for example, there are two post-lawsuit charges levied by the City that are illustrative.

1. The first was a charge to the District of \$773,000 imposed by the City for indirect cost allocation months after the District's 2017-2018 financial compilations had been completed and sent to its auditors. The District's contractors questioned the charge, ultimately resulting in an \$182,000 savings to the District for that one item.
2. The second was a \$706,145 charge by the City for capital improvements. On being informed the charge with potentially improper, the District's attorneys and contractors investigated and determined it was an expense that should be paid by the City, not District. The City later agreed.

With these two items alone, the District's oversight and governance served to save the District nearly \$900,000.

Regarding benefits realized as a result of District oversight, issues surrounding the District's right to treatment space (capacity) in the plant are revealing. One subject in the lawsuit involved the District's claim that substantial errors existed in the City's calculations and allocation of ESSUs<sup>2</sup> as between the District and City. ESSUs serve to measure the amount of the treatment plant's capacity that has been consumed by both the District and City and also measures the remaining treatment space available to the District and City, respectively.

The District investigated and conducted discovery on the subject during the lawsuit. The Settlement Agreement, which contained a standard release of claims, specifically excepted certain issues from the settlement. The dispute concerning the ESSUs was one exception. (Exhibit 2, p. 24, § E.1 ¶ 2.)

Over the last several decades, the City produced various reports detailing the number of ESSUs consumed by the District and City, respectively, based on calculations done by the City. Since 1996, the City published this information in an annual "ESSU

---

<sup>2</sup> ESSU stands for equivalent sewer service units. In addition to capacity, ESSUs *formerly* served as the basis for allocating operating and capital costs between the District and City.

Statistics Report.” The report detailed the ratio of ESSUs used by the District and City as of March 31 each year, which, in turn, set the percentage of total expenses each party was required to pay under the Participation Agreement for the next fiscal year<sup>3</sup>.

In its 2018 report, the City represented that the District had consumed 5,808.49 ESSUs and the City had consumed 6,414.15 ESSUs, leaving remaining ESSUs of 541.03 for the District and 221.87 for the City. (Exhibit 4.)

After multiple efforts to meet and confer, on November 7, 2018, the District’s counsel submitted a letter to the City, with supporting documents sourced from City records, in an effort to finally resolve the dispute regarding ESSU calculations and consumption. (Exhibit 5.) It largely contained information and analysis derived from the District’s lawsuit efforts, including an analysis detailing how the City’s calculations did not coincide with building permits issued in the City and District. The City subsequently conceded multiple errors on its part and accepted the District’s position.

The true numbers, detailed in a written agreement entitled “Agreement Resolving Dispute Under Section II.E.1 of the Operating Agreement Between the City of Ukiah and the Ukiah Valley Sanitation District,” show that the District, in fact, has 1,162.54 (as opposed to 541.03) remaining ESSUs available, an increase of 621.51 beyond that calculated and reported by the City. (Exhibit 6, p.2.)

In other words, if left unchecked, according to the City, the District’s remaining plant capacity would have been 541.03 ESSUs. Due to its efforts, the District was able to show it had the right to an *additional* 621.51 in unused ESSUs (1,162.54 – 541.03). These ESSUs, as noted above, are part of the District’s “Dedicated Capacity,” a valuable asset it owns. Each unused ESSU is presently valued at \$12,240, representing the fee that must be paid to the District for each ESSU consumed by a new connection, under District Ordinance 35. (Exhibit 7.)

The District’s expenditures and diligence during the lawsuit and beyond resulted in an increase of **\$7,607,282.40** (12,240 x 621.51) in potential future connection fee revenue and the District’s Dedicated Capacity. These are future revenues the District would have been lost absent its efforts.

**F4:** Due to limited staffing and high turnover, the District has not demonstrated the capability to responsibly manage its business and financial affairs. Failure to provide audited financial reports for five years (2014-2018) further demonstrates this lack of capability.

**RESPONSE:** **The District disagrees partially with this finding.** While turnover in District management has occurred due to a variety of reasons, ranging from illness to the termination by the board of a service contract, the District entered into an

---

<sup>3</sup> Contrary to the Grand Jury’s report, under the Operating Agreement, that ratio is no longer used to allocate expenses. (Exhibit 2, p. 11, §II.D.) ESSUs are used to set treatment plant capacity rights. (Exhibit 2, p. 23-26, §II.E.)

arrangement with the Willow Water District to provide management services going forward in 2019. Willow County Water District is a special district that occupies the same office building as the Ukiah Valley Sanitation District. The ability to hire qualified full-time management, especially from outside the area, is not an uncommon problem across many industries in Mendocino County.

The District Board has exercised and continues to exercise oversight of business affairs and financial transactions. Financial account materials, including details, are provided at Board meetings, along with financial statements from the City and the County of Mendocino. Further, the Board has two members with 10 years and 6 years, respectively, of continuous Board service. Additionally, during the District-City lawsuit, the District's financial condition was highly scrutinized by legal and financial experts for the period in question.

A significant issue underlying the District's inability to prepare audited financial statements in prior years resulted from the failure or inability of the City, who was contractually responsible for maintaining all financial information for the joint sewer system, to provide adequate records for this purpose. These complications were acknowledged dating to the 2013 Grand Jury's report.

Specifically, the 2013 report stated, "the City does not maintain records of the specific costs involved; it is impossible to determine the accuracy of the City's allocation of costs to the [District]. The [District] has found reason to question the City's records and charges." (Exhibit 1, p. 3.) The 2013 Grand Jury went on to recommend that the "UVSD complete the creation of its own accounting system." (Exhibit 1, p. 6.) The Operating Agreement is designed to do just that and, further, to ensure proper financial reporting occurs between both parties. (Exhibit 2, pp. 21-23, § II.D.4.)

In 2018, the District engaged an external accounting firm (Clifton, Larson, Allen) to prepare monthly financial statements and to update the District's budgeted expenses to actual each month. This same firm prepared the financial statements for audit purposes for the years 2014-2018. (Van Lant & Fankhanel—the same firm who audits the City's financial statements). The District retained both firms for the same purposes for the Fiscal Year Ending June 30, 2019.

The District's 2014-2018 financial statements and audits have been prepared and issued. It should be noted that *no material adjustments* were made to the District's financial statements as a result of the audits for 2014-2018. It is continuing to have monthly financial statement information prepared by an external accountant for the Board and Management to review and act upon as required in their respective roles.

The District's FYE 2019 Financial Statements will be prepared by the same two firms that prepared and audited the 2014-2018 financial statements respectively. The continued use of the same two firms will provide a high degree of continuity to the District's financial reporting, enhancing its ability to meet the needs of its customers.

**F5:** In the absence of staffing continuity with technical and financial expertise, the District has used expensive attorneys and consultants to conduct day-to-day business and negotiations with the City.

**RESPONSE: The District disagrees wholly with this finding.** The District's Manager is well versed in sewer and wastewater affairs. The District maintains a contract engineer, who consults on an as-needed basis at minimal cost. The District does not have a dedicated finance department. It uses well-qualified contractors to prepare its financial statements, work with auditors, and review City financial statements, as required by law and the Operating Agreement. The District's legal counsel has been present with staff or other representatives at meetings with the City to address legal issues. The City Attorney also attends those meetings for the same purpose when needed. These services have saved the District hundreds of thousands of dollars since October 2018, as described above, demonstrating not only the need for, but also the utility of, these services. Expenses for legal services are decreasing, as illustrated in the District's latest budget, and will reduce further as outstanding issues, such as the budget dispute, which has long-standing implications, resolve.

**F6:** The District claims the funds paid to them by the City are for damages. This is misleading. Of the \$16,415,296 paid, \$11,431,986 were from existing District reserves held by the City on the District's behalf.

**RESPONSE: The District disagrees wholly with this finding.** To characterize the District's recovery from the City as damages is not misleading, it is accurate. The District's claims against the City for damages embraced improper charges levied against it by the City and the City's wrongful retention of District funds. It is no secret that the damages' claims *all* sought the return of funds that rightfully belonged to the District. There were no claims for payment of *City* money. Indeed, there was nothing to recover or that could be recovered from the City other than sums rightfully belonging to the District, as governmental entities are insulated from many liabilities that might otherwise attach to individuals or other entities as a result of their wrongful conduct.

Damages are broadly defined by law to include any money claimed by, or ordered to be paid to, a party to a lawsuit. (Black's Law Dictionary, 7<sup>th</sup> Ed.) Stated differently, damages are "the amount of money which a plaintiff (the person suing) may be awarded in a lawsuit."(dictionary.law.com.) There are many types of damages: losses due to contractual breach, losses resulting from a violation of a duty (e.g. tort), and money or property claimed by one party to be wrongfully withheld by another party. Damages are, in their most basic form, meant to restore the claimant to their rightful position.

In 2012, the District discovered it had millions of dollars on hand with the City. The funds were held by the City. The District felt it necessary to protect its own reserves since the City had wrongfully charged the District for expenses, drawing payment from funds on hand with the City. The District did not wish to have its reserves held by the same entity that had wrongfully charged it over time. The District requested that the City turn over the reserves. The District also sought to informally resolve the issues and requested the City enter into what is known as a tolling agreement, which would have allowed the parties to work through their disputes without the formality of litigation. The City refused.



In September 2013 the District was forced to file a Government Claim with the City. A Government Claim is a prerequisite to filing a lawsuit against a governmental entity. Only after that claim was filed, on October 3, 2013, the City paid the District \$2.8 million dollars, representing a portion of the funds the City had withheld from the District and that the District had previously demanded. The claim was otherwise denied, which forced the District to file its complaint against the City in the Superior Court. (*Ukiah Valley Sanitation District v. City of Ukiah, et al.* Sonoma County Superior Court Case No. SCV 256737.) Absent that action, the District would have forever lost its right to pursue the overcharges or the balance of improperly withheld funds.

In 2015, through the litigation process, the District again demanded the return of funds wrongfully withheld by the City. The City again refused to do so, and the District filed a motion with the Court in the lawsuit to force the City to turn the funds over to the District. (Exhibit 8.) The City relented, and the District and City entered into a *written agreement* to resolve that motion. The agreement's terms required that the City pay over to the District \$1.5 million of the withheld funds, and the District preserved its rights to seek the balance of funds as the litigation unfolded. (Exhibit 9.)

Then, in 2017, the parties agreed to mediate the balance of issues in lawsuit before the Honorable Ronald Sabraw, Judge (ret.). Aside from the lawsuit issues, there was nothing to mediate. In short, the mediation concerned nothing but the claims made by the parties in the lawsuit. In mediation, the City attempted to negotiate a final payment of the withheld funds that was less than the remaining \$4.5 million then on hand. The District, of course, rejected the offer and made it clear that it would not negotiate these sums nor would it continue to mediate the balance of issues until full payment of withheld funds was made. Ultimately, the City capitulated. In the mediation on May 11, 2017, Judge Sabraw generated a *written mediation agreement* on this issue requiring that the City pay over to the District the remaining \$4,544,482 then being withheld. (Exhibit 10.)

In October 2018, the parties entered into another *written agreement*, which served to resolve the balance of issues in the litigation, excepting a few specified items (e.g. ESSU issues addressed above in response to F3 above). In that agreement, the City agreed to pay the District an additional \$7.5 million, which was expressly "in addition to" the sums referenced above. More specifically, the agreement obligated the City to pay the District approximately \$5 million in cash through installment payments and to transfer approximately \$2.5 million, representing the District's portion of unspent bond proceeds, to a trustee for prepayment of the District's share bond debt (as a matter of contract and law, these funds cannot be paid directly to the District, but must pass through the trustee). (Exhibit 11.)

The implication that the City's payments were somehow not all part of the District's legal action ignores fact and defies logic. If all the District had to do was ask for the funds as the City contended, there would have been no need to file claims, motions, engage in expensive mediation over them, or generate written agreements as part of lawsuit proceedings. The fact of the matter is that the District continuously requested the City turn over the withheld funds and the City refused. This is one of the many reasons the lawsuit was filed.

Also, it is categorically false to characterize the unspent bond proceeds as funds the City openly held for the District's benefit. In fact, the District's claim for unspent bond proceeds was initially rejected by the City. When confronted with evidence that the proceeds existed, the City subsequently denied the claim, producing financial reports and information to support its position. The District, through its legal team, dug deeper and countered the City with additional support. The City reviewed the material and responded by producing additional internal reports, which it relied on to again claim that unspent bond proceeds did not exist. The District persevered, and provided yet additional information it obtained in the lawsuit's discovery proceedings to demonstrate that the City was off base. Finally, the City relented and agreed.

In short, it is pure artifice to characterize the unspent bond proceeds as something the City openly held for the District's benefit. It took substantial effort during the lawsuit to uncover the funds and prove that the District's position was correct.

**F7:** To avoid further legal expense, the City agreed to pay the District \$4,984,310 over five years. This amount is substantially less than the legal costs of the lawsuit to the District. The difference will be paid by the District's ratepayers.

**RESPONSE:** **The District disagrees wholly with this finding.** The City paid the District all funds described above because it was liable for the same and faced substantial risk for repayment of even greater sums if the lawsuit proceeded to trial. It is illogical to suggest the City paid the District millions of dollars without having actual liability for the payments simply to avoid litigation costs. The settlement occurred on the eve of trial, after the vast majority of litigation expenses had already been incurred.

As explained above, the District's legal costs resulted in recovery of funds far in excess of those expenditures and fostered a new, balanced, Operating Agreement. Beyond that, its legal expenditures resulted in a benefit of approximately \$7,607,282.40 in additional Dedicated Capacity at the treatment plant, as noted above. The District and its ratepayers received a substantial benefit, and there is nothing related to the lawsuit for its ratepayers to pay.

**F8:** The City's settlement and legal expenses will be borne by the City's ratepayers.

**RESPONSE:** Pursuant to the Grand Jury Report, the District was not required to respond to this finding.

**F9:** The City no longer holds any of the District's reserves.

**RESPONSE:** Pursuant to the Grand Jury Report, the District was not required to respond to this finding.

**F10:** The District's claim that it can save over \$1.5 million per year by assuming responsibility for the billing, maintenance and sewage treatment for its ratepayers is not supported by any documentation.

**RESPONSE: The District disagrees wholly with this finding.** The District has no immediate plans to take over the maintenance of any portion of the Combined System. There is only one Wastewater Treatment Plant at which all sewage treatment will take place for the foreseeable future. The District received an estimate to assume its own billing and collection functions, but will only proceed if there is cost savings and benefits to the District's ratepayers.

**F11:** Future changes allowed in the settlement could trigger redundant expenses to be borne by all ratepayers. These include detachment of the overlap areas by the City and the District's assumption of their billing, maintenance, and sewage treatment.

**RESPONSE: The District disagrees wholly with this finding.** It is unclear how detachment would result in redundant costs. The District understands that detachment could result in the City assuming sewer service responsibility for the overlap area, which represents that portion of the District's sewer-service territory presently within the City limits. It is assumed that, if detachment occurred, the City assume system expenses associated with and effected by this area. However, while detachment isn't likely to trigger redundant costs, it may trigger a myriad of other issues.

Regarding services listed in the Operating Agreement, the District is permitted to assume those functions as detailed there. (Exhibit 2, pp. 6-8.) If the District assumes any of these functions, it doesn't follow that the by-product of the action would be redundant costs. The costs exist whether the District or City provide the service. The District is not likely to assume a service function unless it is more economically efficient to do so.

The District currently has a service agreement with Willow County Water District. Willow currently undertakes billing and collections for a majority of District ratepayers for water service in Willow and Millview's water districts. The District received an estimate to take over billing and collection, but will only proceed if there is cost savings and benefits to the District's ratepayers.

**F12:** The MOU/JPA proposed by the City is intended to provide a cost-effective solution to the ongoing disputes between the City and the District by operating as a single system with the same rate structure applying to all customers.

**RESPONSE: The District disagrees wholly with this finding.** Initially, to the best of the District's knowledge, the City did not offer any "Joint Powers Agreement" ("JPA"). A review of the City's agendas and minutes does not reveal that the subject was ever discussed or approved by the City Council. Rather, the document was presented to the District by a sole City representative. That said, more substantively:

- Despite its title, the City’s proposed JPA is not a joint powers agreement at all. It contemplates no joint conduct. Under the proposal, one party—the City Council—solely makes all decisions for the Combined System. The District board would exist, ostensibly, only to approve audits, yet even that function would be nothing but ministerial since the City would, under the proposal, control all books, records, reporting, and other financial affairs. The salient feature of a joint powers agreement is *joint* governance—hence the title—comprised of representatives from two or more
- agencies sitting on one combined board to collectively make decisions for the subject of the agreement.
- The City’s JPA “proposal” envisions the City Council exclusively making all decisions, including expenditures and assuming further debt for the Combined System. Since District ratepayers are largely unable to cast election votes for Council members, District ratepayers would have no voice in electing representatives, yet would be compelled to pay whatever expenses the City placed on the Combined System. The City’s proposal fails to acknowledge, and seeks to sidestep, a fundamental aspect of democratic government.
- The District agrees with the 2009 Grand Jury’s recommendation (R15) that, “the District, apart from its contractual relationship with the City under existing Agreements, retain its identity, and continue exercising power and discretion as an *independent special district*.” (Exhibit 3, p.10.)
- The proposed JPA would eliminate the City’s obligation make its final payments to the District under the Settlement Agreement, which amounts to millions of dollars that belong to District ratepayers as a consequence of years of improper charges levied by the City. Consequently, the District’s ratepayers would, under the proposal, end up subsidizing the City (and its ratepayers).
- The City’s proposed JPA would equalize the parties’ ability to use the treatment plant capacity for future connections. However, of the roughly \$75,000,000 in indebtedness assumed through the 2006 Wastewater Bonds, approximately 26% was attributable to the Capacity Project (i.e. the portion of the project that grew plan capacity). (Exhibit 2, p. 17.) Since repayment of the bonds first began, the District has been charged with 65% of the Capacity Project repayment costs since it has more physical room from growth (more potential connections). In other words, District ratepayers have been charged substantially more for debt service than City ratepayers over the last decade—plus in order to secure the right to use capacity. The City’s proposal would eradicate that right without compensating District ratepayers for the substantial extra costs they paid for it.
- Similarly, as explained in response F3, a portion of the lawsuit dealt with improprieties in ESSU calculations, which *previously* was utilized to establish the ratio of system expenses annually attributable to each party. ESSUs are, however, still used to divide the remaining treatment plant capacity between the District and City. As noted above, through its efforts, the District was able to demonstrate it had a significant number of available ESSUs beyond that

claimed by the City, resulting in an increase of \$7,607,282.40 in future revenue for the District's Dedicated Capacity, representing future revenues (connection fees) available to the District. The City's proposal would eliminate this benefit without compensation.

- The "joint powers" proposal is silent on these points. District ratepayers shouldered the burden of higher costs for the plant capacity for years. The City's "proposal" would put itself on equal footing with the District without compensation or consideration of these facts—a result that would be patently unfair to its ratepayers.

**F13:** The District has violated the intent of the Brown Act which has reduced transparency for District ratepayers.

**RESPONSE: The District disagrees wholly with this finding.** The District complies with the letter and intent of the law known as the Brown Act. There have not been any lawsuits alleging that the District has done so.

**F14:** The \$23 million combined legal costs and lost opportunities to refinance the bond will be borne by the City and District ratepayers.

**RESPONSE: The District disagrees wholly with this finding.** The assertion that \$14 million dollars of potential bond interest savings was lost because the District did not have audits completed for Fiscal Years 2014-2018 is incorrect. In fact, bond attorneys and municipal advisors working for the District and City made it clear that, while the audits would be useful, they were not necessary to refinance the bond debt. The reason refinance has not occurred to date is due to a number of issues, including, but not limited to: Utility Billing; Allocation of Debt Services Shares going forward; Potential Reorganization (the City detaching part of the District's territory and customers); Operating Budgets; Prepayment of Debt by either party; Bond structuring (one bond or two bond offerings for the District and City, respectively); and, the determination of the status of certain customers to ascertain if they are the District's or the City's. The audits are now complete, yet these issues are outstanding. The Operating Agreement requires that both parties "*shall make a good faith effort to complete the Refinancing to obtain the most favorable debt service obtainable and to accommodate the District's elections... in accordance with this Agreement.*" (Exhibit 2, p. 17, ¶ c. Bond Debt Refinancing.)

The estimated savings of \$14 million dollars in interest payments is based on a maturity date of March 31, 2036. To that end, much, if not all, the potential interest savings is still available if these issues can be resolved and the bonds refinanced in the current rate climate. The present Bond is structured so it can be refinanced on two specific dates each calendar year. Further, the District and the City have agreed to use funds on hand from the original bond proceeds to pay down part of the existing principal remaining on the bonds. The principal will be reduced by approximately \$4.8

million on September 1, 2019. The reduction in principal will itself reduce the annual interest expense over the life of the bonds, whether they are refinanced or not.

The District's legal fees have already been paid and the District's audit for 2018 shows the District maintains a Net Position of \$9.5 million, \$6.9 million of which is unrestricted. Payment of the City's legal fees or the City's remaining payment obligations will not be costs shared by District ratepayers. Therefore, with the legal fees already paid and given the fact the potential interest savings are unrealized, the District's ratepayers should not realize any increase in their monthly sewer bills because of these two items.

## **RECOMMENDATIONS**

**R1:** The City and District work together to find a way to manage the overall sewer system as a single entity equitably and efficiently for all ratepayers,

**RESPONSE: The recommendation was implemented before publication of the 2019 Grand Jury report.** What is recommended was implemented prior to the Grand Jury's June 19, 2019 report. The Operating Agreement, if followed, would serve to equitably and efficiently manage the Combined System. Operating the Combined System by a *single entity* is feasible, but would require at least the City and perhaps the District to cede managerial and operational control of the system, and to some extent ownership of it, to an agency vested with the power and authority over the whole of the system.

**R2:** The District enter into negotiations with the City regarding the proposed MOU/JPA,

**RESPONSE: The recommendation will not be implemented because it is not warranted or reasonable.** See Response F12, above.

**R3.** The District provide specific details to ratepayers for its claims that it can save over \$1.5 million per year by assuming billing, maintenance and sewage treatment responsibilities with a detailed feasibility and cost analysis.

**RESPONSE: The recommendation will not be implemented because it is not warranted or reasonable.** The District is looking into taking over the billing and collections for their ratepayers. The District has received an estimate to take over the billing and collection, but will only proceed if there is cost savings and benefits to the Districts ratepayers. The decision to proceed will be discussed by the Board during open sessions, as well as possibly at committee meetings. The final decision will be done at a public meeting, with all documents relating to bids, costs etc., being available to the public.

The District has received an estimate to do so and will continue to look for ways to eliminate expenses. The District has no immediate plans to take over the

maintenance of the system and the sewage treatment will continue to be handled by the City's wastewater treatment plant.

**R4.** The District Board must act in accordance with the Brown Act which promotes transparency and public participation.

**RESPONSE: No action required.** The recommendation simply recites a legal obligation, which the District has been complying.