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Michael D. Ott

Special Counsel

Michael G. Colantuono

**AGENDA
SPECIAL DISTRICTS ADVISORY COMMITTEE
FRIDAY, December 19, 2014, 9:30 A.M.**

**Note: Location at
County Operations Center
5560 Overland Ave, Room 171
San Diego, CA 92123**

<u>Agenda Item:</u>	<u>Recommended Action:</u>
1. Welcome and Roll Call	
2. Approval of Minutes of Meeting held March 21, 2014	Approve
3. Consultant's Recommended Agenda Revisions	Receive
4. Public Comment Opportunity for persons to speak to the Committee on any subject within the Committee's jurisdiction, but not an item on today's agenda. Each speaker's presentation may not exceed 3 minutes.	
5. Review Draft Fallbrook PUD/Rainbow MWD Reorganization Report*	Discussion/ Comment
6. Selection of Chair and Vice Chair for 2015	Information
7. Consider Action to Nominate Two Persons to Fill Vacancies for 2015.	Approve
8. Adjournment to the January 16, 2015 Meeting Date if necessary.	Adjourn

*See Staff Report

DRAFT
LOCAL AGENCY FORMATION COMMISSION
SPECIAL DISTRICTS ADVISORY COMMITTEE
MARCH 21, 2014 MEETING

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There being a quorum present, the meeting was convened at 9:30 a.m., by Chairman Tom Pocklington (Bonita-Sunnyside FPD). Attending were: **Committee Members** – Gary Arant (Valley Center MWD)(left at 10:30 a.m.), Brian Brady (Rainbow MWD) (left at 10:30 a.m.), Tom Bumgardner (Valley Center Parks & Recreation District), Judy Hanson (Leucadia WWD), Jon Lorenz (Lakeside FPD), John Pastore (Rancho Santa Fe CSD), Augie Scalzitti (Padre Dam MWD) (arrived at 9:35 a.m.), Terry Thomas (South Bay ID) and Kimberly Thorner (Olivenhain MWD). Absent were: **Committee Members:** Jim Archer (Alpine FPD), Gary Croucher (Otay Water District), Bill Haynor (Whispering Palms CSD), Margarette Morgan (Vista FPD), Janine Sarti (Palomar Health), Dennis Shepard (North County Cemetery District), Others Attending: Harry Ehrlich, LAFCO Consultant; Robert Barry, LAFCO Governmental Analyst and Paul Bushee (Leucadia WWD).

Item 2

Approval of Minutes of December 20, 2013

ON MOTION of Brian Brady, seconded by Judy Hanson, and approved unanimously by the Committee members present. The Committee dispensed with reading the December 20, 2013 minutes and approved said minutes.

Item 3

Consultant's Recommended Agenda Revisions

Harry Ehrlich indicated there are no revisions to the Agenda Items presented at today's meeting but wanted to introduce the following district representatives in attendance: David Barnum, Rich Hannasch, and Ricardo Soto from Ramona MWD; and Jim Kirkpatrick, Lakeside FPD.

Item 4

Public Comment

There were no members of the public requesting to speak.

Item 5

Review Draft Ramona Municipal Services Review Report

Harry Ehrlich provided a PowerPoint presentation and draft report regarding the Ramona Municipal Water District as part of LAFCO's Five-Year Sphere of Influence and Municipal Service Review Program. He indicated that this presentation will highlight

and review some of the details and concerns from the report. Mr. Ehrlich requested input from the Committee and informed them that their recommendations related to the report will be presented to the Commission.

Mr. Ehrlich informed the Committee that the following issues were addressed at the LAFCO Commission meeting held on June 3, 2013: 1) Governance/ Communication/ Community Transparency; Development of the San Vicente Water Reclamation Facility; Compliance with Propositions 26 and 218 in establishing fees and charges for services; Emergency evacuation routes and response plans; Sewer connection and capacity fees; and the District's consideration of alternative service methods and capabilities.

Mr. Ehrlich informed the committee members that since last year's meeting, LAFCO staff has met with interested parties and conducted additional review of associated issues. After discussion from the committee members; district representatives and public members present, the Committee made the following recommendations to the Commission:

ON MOTION of Judy Hanson, seconded by Terry Thomas, John Pastore requesting to abstain, and the remaining members present were in favor to make the following recommendations to the Commission:

- 1) Seek a coordinated sewer service delivery method and governance structure within the Ramona MWD area and not consider the formation of a separate service agency overlapping the MWD; and
- 2) To approve the sphere review, MSR, and associated determinations presented in the staff report; and
- 3) To focus upon providing sewer and recycled water service in the Montecito Ranch development within the existing Ramona MWD sewer system structure; and
- 4) For the Ramona MWD Board of Directors to take action to address the situation of a long-term absence of one of the members of the Board of Directors.

Item 6
Committee Member / Consultant Announcements

Committee members made announcements and discussed current projects within their districts.

There being no further business to come before the Special Districts Advisory Committee, it was noted that the next meeting is tentatively planned for April 18, 2014, if a meeting is to be held. The meeting was adjourned at 11:05 a.m.

Ruth Arellano
Administrative Assistant



Chairman

Andrew Vanderlaan
Public Member

December 19, 2014

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Vice Chairman

Vacant

TO: Special Districts Advisory Committee

Members

Bill Horn
County Board of
Supervisors

FROM: Executive Officer
Local Governmental Consultant

Dianne Jacob
County Board of
Supervisors

SUBJECT: "Fallbrook Public Utility District and Rainbow Municipal Water District Reorganization" – Involving District Dissolution, Annexation, and Latent Powers Expansion for Sewer Service (Ref. Nos.: RO/SA(a)(b)14-04; MSR/SR13-66).

Bud Pocklington
South Bay
Irrigation District

EXECUTIVE SUMMARY

Lori Zapf
Councilmember
City of San Diego

Initiation of Reorganization Proposal

Jim Janney
Mayor
City of Imperial Beach

This item has been referred to the Special Districts Advisory Committee for review and comment regarding a reorganization of the Fallbrook Public Utility District (PUD) and Rainbow Municipal Water District (MWD). The reorganization was initiated by the Fallbrook PUD and involves the dissolution of the Rainbow MWD, annexation of the Rainbow MWD territory to the Fallbrook PUD, and expansion of the PUD's latent powers for sewer service restricted to the territory formerly within the Rainbow MWD. Due to the complexity of the reorganization, the Committee should provide LAFCO staff approximately 30 minutes for a staff presentation and ten minutes each for the Fallbrook PUD and Rainbow MWD to provide brief presentations.

Sam Abed
Mayor
City of Escondido

Alternate Members

Greg Cox
County Board of
Supervisors

As the proponent, the Fallbrook PUD requests that the Commission approve the reorganization, because the PUD believes that the proposal will simplify service provision and result in cost-savings, projected to be about \$2.5 million per year. The Fallbrook PUD indicates in its application to LAFCO that combining the two districts will result in:

Sherri Lightner
Councilmember
City of San Diego

Jo MacKenzie
Vista Irrigation District

Lorraine Wood
Councilmember
City of Carlsbad

- Capturing economies of scale and reducing administrative overhead;
- Sharing equipment and reducing vehicle fleet including heavy/specialty equipment;
- Improving emergency response;
- Enhancing coverage for service zones and pressure zones at district boundaries;
- Integrating and consolidating both districts' management and staff;
- Improving water resource management via use of recycled water;

Harry Mathis
Public Member

Executive Officer

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- Improving the ability of the combined district to fully utilize local water supplies; and
- Strengthening financial capacity.

The Fallbrook PUD estimates that over a three-year period, a reduction in staff of up to 20 full-time equivalents could be accomplished while maintaining the existing level of service. The estimated cost savings of \$2.5 million and projected staff reduction figures were developed by the staffs of the Fallbrook PUD and Rainbow MWD (Rainbow MWD's General Manager, Dave Seymour, with the assistance of Rainbow Finance Manager, Gene Buckley). Both Mr. Seymour and Mr. Buckley have since retired from the Rainbow MWD. Additional cost-savings, estimated to be approximately \$300,000 annually, were also projected from the following areas of increased operational efficiency: reduced property and liability insurance; reduced vehicle fleet including heavy/specialty equipment; reduced information technology costs; reduced banking service fees and greater investment performance; expanded internal training opportunities; reduced legal costs; reduced director costs; reduced audit costs; reduction in general office expenses; optimization of service areas and pressure zones at district boundaries; and reduction in more costly outsourcing.

Reorganization Proposal Opposed by Rainbow MWD

The Rainbow MWD disputes the justification for reorganization and is actively working with ratepayers to oppose Fallbrook PUD's proposal. Approximately 396 letters of opposition and 23 letters of support were sent to LAFCO staff by a comment due date of August 1, 2014. The letters are available on the San Diego LAFCO's website and can be viewed or downloaded from the following link: [http://www.sdlafco.org/document/Fallbrook%20Website%20Docs/Comments%20received%20by%20August%201,%202014/Comments by August1.pdf](http://www.sdlafco.org/document/Fallbrook%20Website%20Docs/Comments%20received%20by%20August%201,%202014/Comments%20by%20August1.pdf).

In addition to directly urging ratepayers to oppose the reorganization, the Rainbow MWD has also placed statements on its website requesting that ratepayers communicate their objections to LAFCO's Executive Officer. The Rainbow MWD has expressed the following objections: Fallbrook PUD's application violated notice and hearing requirements and the PUD should have received consent from the Rainbow MWD before proceeding; Fallbrook PUD's proposed reorganization will neither lower or raise rates and there is no obvious financial benefit to the reorganization; Fallbrook PUD is trying to capitalize on Rainbow's growth; Fallbrook PUD will terminate Rainbow MWD's debt ordinance (No. 95-1) thereby depriving Rainbow ratepayers of a right to vote on additional public debt; Fallbrook PUD needs Rainbow's \$100 million in assets to leverage more borrowing; Fallbrook PUD's claim of savings from a terminated JPA and equipment sharing is either irrelevant or impractical; Fallbrook PUD's representations regarding savings have not addressed the loss of efficiency or impact on service to ratepayers; Fallbrook PUD will marginalize Rainbow's agricultural community; Fallbrook PUD's governance structure will impair the ability of a protected class to elect candidates of its choice or to influence the outcome of election in violation of the California Voting Rights Act; Fallbrook PUD has misrepresented Rainbow MWD's position on governance; Fallbrook PUD's proposal does not take into consideration Rainbow MWD staff objections; Fallbrook PUD failed to respect the JPA contractual process; and Fallbrook PUD improperly initiated the LAFCO application, and violated the Ralph M. Brown Act.

The Rainbow MWD has filed with LAFCO a Resolution of Objection covering the above issue areas pursuant to Government Code Section 56668.3(4). The Fallbrook PUD has accordingly filed a response refuting Rainbow MWD's objections. Both of these documents are posted on LAFCO's website and summarized in this staff report. The Rainbow MWD and Fallbrook PUD have also made filings with the

Fair Political Practices Commission regarding expenditures for political purposes in excess of \$1,000. According to the most recent reports filed with the FPPC, the Rainbow MWD has spent \$65,746 (through October 2014) to oppose the reorganization and the Fallbrook PUD has spent \$8,415 (through October 2014) to support the reorganization. Below is a brief profile of each agency, a summary of the proposed reorganization, and a discussion of major issue areas requiring advisory committee review and discussion.

Attached to this report are four supporting documents prepared by LAFCO staff, the Fallbrook PUD and Rainbow MWD: (1) Preliminary LAFCO staff report and North County JPA Consolidation study; (2) Fallbrook PUD JPA Cost Savings Memo, May 12, 2014; (3) Rainbow MWD memorandum claiming misrepresentation of facts by Fallbrook PUD, November 6, 2014; and (4) Fallbrook PUD memorandum responding to misrepresentation claims, November 12, 2014.

AGENCY BACKGROUND

Fallbrook PUD

The Fallbrook PUD currently provides water and wastewater services within the unincorporated North County communities of Fallbrook and De Luz. Wastewater service is restricted to territory of the former Fallbrook Sanitary District within a 4,200-acre area of downtown Fallbrook. Today, the District provides imported water and sewer service to 35,000 residents living on about 28,000 acres (43.75 square miles). Almost half of the water is used for agricultural uses. The District also produces about one and one-half million gallons of recycled water daily that is used to irrigate nurseries, playing fields, landscaped freeway medians and common areas. The Fallbrook PUD sphere of influence was originally adopted in 1985 and is generally coterminous with district boundaries. Since adoption, the sphere was amended five times; the last sphere amendment was approved 24 years ago in 1990 and resulted in the addition of 12,000 acres corresponding with the De Luz Heights MWD Reorganization; the De Luz Heights MWD was dissolved and its service area annexed to the Fallbrook PUD. A municipal service review was conducted of the PUD in 2007 and no service issues were identified.

Rainbow MWD

The Rainbow MWD is located in northern San Diego County coterminous with the San Diego/Riverside County border. The Rainbow MWD provides water and wastewater collection services within approximately 80 square miles of a predominately rural and agricultural area. Today, the District provides potable water and wastewater collection services within portions of the unincorporated North County communities of Bonsall, Fallbrook, Pala, and Rainbow. Sewer service is provided to about 14% of developed parcels; the majority of existing residences utilize septic systems. A municipal service review was adopted in 2014 and no major service issues were identified. However, it was noted that the District has undergone periods of instability in terms of governance and administration. In 1984, Rainbow MWD's original sphere was adopted. Since that time, eight amendments have been approved, thus making the sphere generally coterminous with the District's existing boundary. Currently, there are two islands in the District's boundary. One is a small, square-shaped area in the District's northeastern region that represents a non-contiguous portion of the neighboring Pauma MWD. The second is the western, non-contiguous portion of the San Luis Rey MWD. On April 7, 2014, LAFCO updated Rainbow MWD's sphere and approved the following amendments: (1) Inclusion in the sphere of a non-contiguous portion of the San Luis Rey MWD, the Warner Property, the segment of Pala Road adjacent

to the Warner Property, as well as three areas located north of San Luis Rey MWD and south of Rainbow MWD, and (2) Resolution of the I-15 Special Study Area.

PROPOSED REORGANIZATION

The proposed reorganization involves dissolution of the Rainbow Municipal MWD, annexation of the territory within the Rainbow MWD to the Fallbrook PUD, and expansion of Fallbrook PUD latent sewer powers authority to cover the territory within the district dissolution area (Rainbow MWD). The reorganization was first initiated by the Board of Directors of the Fallbrook PUD on March 10, 2014 and then re-initiated on April 28, 2014 after holding a public hearing pursuant to Government Code Section 56824.12(c)(1). The proposal was re-initiated on April 28th, based on comments received by the Rainbow MWD stating that a hearing should have been held by the PUD on March 10, 2014. The Fallbrook PUD questioned the validity of this hearing requirement because most district initiation proceedings are not subject to such hearing requirements. However, to be responsive to the Rainbow MWD, the Fallbrook PUD decided to re-initiate the reorganization on April 28th subject to a noticed public hearing.

Reorganization Justification

The Fallbrook PUD cites compelling reasons as the basis for moving forward with the reorganization, even without the support of Rainbow MWD. The PUD believes that a reorganization is necessary to continue the cost-savings that resulted when operations and administration were functionally consolidated in 2013, through the establishment of the North County Joint Powers Authority (JPA). Fallbrook PUD states that a cost-effective means of providing service was achieved for ratepayers, pursuant to the terms of the JPA's Employee Leasing Agreement. The following cost benefits resulted from the JPA, according to the Fallbrook PUD: economies of scale were captured; administrative overhead was reduced; equipment was shared; vehicle fleet including heavy/specialty equipment was reduced; emergency response was improved; coverage for service and pressure zones at district boundaries was enhanced; district management and staff were integrated and consolidated; water resource management was improved through use of recycled water; ability to fully utilize local water supplies was improved; and financial capability was strengthened. Primarily through attrition, the combined staffing levels between the two districts were reduced via the JPA (from a high of 124 in 2011) to approximately 114 at year-end 2013. According to a report prepared by both districts, the 2013 net combined savings was slightly over \$1 million, significantly exceeding original expectations. The operational success of the 2013 partnership between the Fallbrook PUD and the Rainbow MWD established the basis for Fallbrook PUD to consider moving forward independently with a formal application to LAFCO.

In addition, the Fallbrook PUD states that a reorganization is necessary because Rainbow MWD took destabilizing actions that are believed to have jeopardized current and future economic and efficiency-based benefits to ratepayers within both Rainbow MWD and Fallbrook MWD. In particular, the Fallbrook PUD states that the Rainbow MWD board took two provocative actions: (1) rehired a general manager and other senior management positions, plus considered a proposal to double board member compensation, and (2) initiated the dissolution of the North County JPA, effective April 5, 2014. The Rainbow MWD subsequently decided not to double board member compensation. The Fallbrook PUD claims that these actions would eliminate the savings gained in 2013, as well as cause major disruptions within employee work groups.

Objections Raised by Rainbow MWD

As with most jurisdictional proposals, there is often disagreement between a proponent's and opponent's claims as to the benefits and disadvantages of reorganization. The Fallbrook PUD / Rainbow MWD Reorganization is no exception. On July 23, 2014, the Rainbow MWD filed with LAFCO a Resolution of Objection to the proposed reorganization. Under state statute, LAFCO must give great weight to such a resolution that is based on service and financial concerns (Government Code Section 56668.3(b)). Per Government Code Section 56857(d), the Commission's consideration can only be based on financial or service related concerns as defined in this statute. These statutes contain rather narrow definitions for these two terms. In the context of Government Code Section 56857(d) (1), financial concerns mean that the proposed uses within the territory proposed to be annexed do not have the capacity to provide sufficient taxes, fees, and charges, including connection fees, if any, to pay for the full cost of providing services, including capital costs. Cost allocation shall be based on general accepted accounting principles and shall be subject to all constitutional and statutory limitations on the amount of the tax, fee, or charge. Government Code Section 56857(d)(2) defines service concerns as a district's inability to provide services that are the subject of the application without imposing level of service reductions on existing or planned future uses in the district's current service area. Service concerns do not include a situation when a district has the ability to provide the services or the services will be available prior to the time that services will be required.

The advisory committee is requested to provide comments to assist the Commission in determining whether the issues raised by the Rainbow MWD have merit and satisfactorily meet the financial or service criteria specified in Government Code Sections 56668.3 (b) and 56857(d). Below is a discussion of the areas of objection and issues identified by the Rainbow MWD and ratepayers, and LAFCO staff. These issues cover the following: (1) Notice and hearing requirements; (2) Affected Agency Initiation Provisions; (3) Relevancy of water rate comparison; (4) Capitalizing on Rainbow MWD's Assets and Growth; (5) Status of Rainbow MWD's Ordinance No. 95-1; (6) Debt of Rainbow MWD and Fallbrook PUD; (7) Relevancy of JPA Cost Savings; (8) Validity of reorganization cost savings; (9) Effect on Agriculture; (10) Governance and California Voting Rights Act; (11) Rainbow MWD's Position on JPA and Governance; (12) Election Provisions; (13) Payment of Election Costs; (14) Rainbow MWD staff objections; (15) Respecting the JPA contractual process; and (16) Proposition 218 notification. Specific questions posed to the advisory committee are located the end of the staff report.

REORGANIZATION ISSUES

Notice and Hearing Requirements

The Rainbow MWD contends that the Fallbrook PUD's March 10, 2014 Resolution of Application to LAFCO (Resolution No. 4813) violated various notice and hearing requirements. In response to this contention, the Fallbrook PUD decided to re-initiate the reorganization after publishing a notice for a public hearing per Government Code § 56824.12. On April 28, 2014, the PUD passed Resolution No. 4815, which amended Resolution No. 4813. The amended resolution (No. 4815) was submitted to LAFCO together with an Application for Reorganization on April 29, 2014. The Rainbow MWD filed with LAFCO a Resolution of Objection, pursuant to the Cortese-Knox-Hertzberg Local Government Reorganization Act of 2000, with specific reference to Sections 56668.3(a)(4) and 56668.3(b) of the California Government Code.

Response: The Fallbrook PUD formally responded to Rainbow's allegation by holding a public hearing on April 28, 2014. The notification issue raised by Rainbow MWD appears to have been resolved by the Fallbrook PUD and is no longer an issue. However, the rapid manner in which the proposal was initiated by the Fallbrook PUD has resulted in a highly contentious relationship between the two districts.

Affected Agency Initiation Provisions

Rainbow MWD objects to the Fallbrook PUD Resolution and Application because it contends that the proposal was made to LAFCO without the consent or approval of Rainbow. Members of the Rainbow board of directors and staff appeared at Fallbrook PUD's April 28, 2014 public hearing and verbalized this objection directly to the PUD. Rainbow MWD states that it should be allowed to continue operating as a special district and that hostile takeovers of neighboring districts are bad public policy, foster distrust, deflate public confidence, and should be discouraged.

The Rainbow MWD additionally states that the Fallbrook PUD Board of Directors and General Manager acted hastily and unlawfully in filing its application with LAFCO by not providing proper notice of the March 10, 2014 hearing. Rainbow MWD believes that Fallbrook PUD violated the Ralph M. Brown Act (Government Code Section 54950 et seq.) by discussing, deliberating, or taking action related to the March 10th resolution and application for reorganization outside of a noticed public meeting. The Rainbow MWD also believes the PUD deprived the public of information and the opportunity to witness, discuss or question these discussions, deliberations, or actions, in violation of the Brown Act. The Rainbow MWD claims that the Fallbrook PUD's General Manager, who also served as Rainbow's General Manager from April 2013 - March 2014, failed to properly report to the Rainbow Board of Directors and took action to plan a hostile takeover of Rainbow.

Response: The submittal of the reorganization to LAFCO without the consent from the Rainbow MWD is a recurring theme of opposition from the Rainbow MWD. This has resulted in a highly negative relationship between the two districts and a number of Rainbow ratepayers. The Rainbow MWD believes that the reorganization should not have been initiated by the Fallbrook PUD in this manner, and the proposal should accordingly be disapproved by LAFCO. Pursuant to Government Code Section 56375, LAFCO may review and approve with or without amendment, wholly, partially, or conditionally, or disapprove most proposals for changes of organization. The only exceptions are consolidation proposals (initiated by a majority of the subject districts) and municipal island annexations (if initiated by a subject city). District consolidation and island annexation proposals must be approved by LAFCO. The Fallbrook PUD / Rainbow MWD reorganization proposal was submitted by the Fallbrook PUD and is neither a consolidation nor a municipal island annexation proposal; therefore, LAFCO has complete discretionary authority to disapprove, approve, or modify the reorganization.

While there is no question as to the legality of Fallbrook PUD's authority to initiate the dissolution of the Rainbow MWD per Government Code Section 56654, the Rainbow MWD is philosophically against the reorganization because it was initiated without the consent of Rainbow. However, Government Code Section 56654 permits an affected local agency to initiate by resolution, an application for a jurisdictional change affecting another local agency. Consent from a subject agency (district) is not required per this statute. This law has been codified for over fifty years and has been used for decades by the approximate 3,500 special districts and 500 cities in California. Regardless of the legality of the initiation, the San Diego LAFCO does have authority to disapprove the proposed reorganization, in addition to its authority to approve, modify the proposal (wholly, partially, or conditionally).

The subject of whether the Fallbrook PUD appropriately initiated the proposed reorganization was previously addressed in this staff report (refer to above discussion). With respect to alleged Brown Act violations, the Fallbrook PUD, by letter to the Rainbow MWD Board of Directors on April 23, 2014, formally responded to Rainbow's allegations. Per Government Code Section 54950 et seq., Fallbrook PUD denied any violation of the Brown Act, and in turn identified several (alleged) Brown Act violations made by Rainbow MWD. The Fallbrook PUD also specifically denied the allegation regarding violation of fiduciary responsibility of its general manager. Both claims have no bearing on the Fallbrook PUD's Resolution of Application, especially since no factual evidence has been presented to LAFCO regarding alleged Brown Act violations, aside from the allegation itself. The former president (George McManigle) of the Rainbow MWD claims that LAFCO's acceptance of the Fallbrook PUD's application makes LAFCO an "accomplice in an illegal effort." Again, this remark lacks basis and is not supported by evidence.

Regarding the Rainbow MWD's claim that the Fallbrook PUD General Manager did not keep the Rainbow MWD updated about pre-application meetings with LAFCO staff, adopted LAFCO guidelines encourage applicants to confer with LAFCO staff by scheduling pre-application meetings (LAFCO Procedures Guide, 2013 Special Edition, page 5). In summary, the rapid manner in which the dissolution proposal was initiated resulted in a public relations issue with individual Rainbow board members and ratepayers; however, the reorganization application was properly initiated and pre-application meetings are encouraged. Whether the Fallbrook PUD General Manager should have kept the Rainbow MWD board updated about pre-application meetings is a personnel matter that should be dealt with between Rainbow and the Fallbrook PUD General Manager.

Relevancy of Water Rate Comparison

Rainbow MWD objects to the Fallbrook PUD's reorganization proposal, because the MWD states that water rates will not automatically increase or decrease for either Rainbow or Fallbrook PUD ratepayers. The Rainbow MWD also contends that based upon keeping the finances of the two agencies separate into the future (divisional accounting), there will be no obvious financial benefit associated with the proposed reorganization.

A number of ratepayers, on the other hand, have contended that the proposed reorganization will result in rate increases. For ratepayers, an important measure of a district's financial performance is the price paid for utility service. Ratepayers within Rainbow MWD have made a large issue about water rates and claim that Fallbrook PUD's reorganization application will result in higher rates. Claims have also been made that water rates are higher in the Fallbrook PUD than in the Rainbow MWD. To determine the validity of these claims, the Fallbrook PUD commissioned a rate comparison study (Michael Bell Consulting Management Consulting – MBMC). According to this report, the following findings were made:

- Fixed charge domestic rates are lower in the Fallbrook PUD than in the Rainbow MWD. Fallbrook PUD's domestic customer water bills were estimated to be about 10-15% lower than those for Rainbow MWD customers during the time the two districts were cooperatively exploring consolidation. In 2014, the MBMC report concluded that the ¾ inch meter class within the Rainbow MWD was 13.1% higher than in Fallbrook (\$219 annual savings). The 1 inch meter class within Fallbrook PUD was 18.6% lower than in Rainbow (\$352 annual savings).

- Agricultural rates appear to be lower in the Fallbrook PUD than in the Rainbow MWD. Fallbrook PUD's fixed charges (agricultural class) were estimated to be about 20% less than in the Rainbow MWD in 2013 at the time the two districts were exploring consolidation. In 2014, the MBMC report concluded that Fallbrook PUD's water rates are about 20.50% less than the agricultural rates in the Rainbow MWD. Based on the comparison for all consumption levels, the Fallbrook PUD customer with a 2" meter has a monthly savings of 20% -- a range of savings for all meters sizes is 10.5% to 20.5%. The Rainbow MWD disputes these figures, however, the Rainbow MWD's statements and claims cannot be validated by either Rainbow MWD's budget records or by San Diego County Water Authority documents. The Rainbow MWD has also claimed that the MBMC report used the wrong Special Agricultural Water Rate from respective rate schedules of both districts, and that MBMC improperly included capital improvement charges in its calculations. Again, these claims do not appear to be valid. The MBMC report, plus responses from the Rainbow MWD and Fallbrook PUD are available on LAFCO's website.

The Rainbow MWD has questioned the relevancy of water rate analysis commissioned by the Fallbrook PUD in the context of the proposed reorganization. The Rainbow MWD states that a comparison of water rates between the two districts is irrelevant because divisional accounting will keep ratemaking separated for a "Rainbow" and a "Fallbrook" division. The Fallbrook PUD has responded that it conducted a water rate comparison because ratepayers within the Rainbow MWD made opposition a cornerstone out of the water rates issue. The PUD also states that divisional accounting does not restrict the passing of shared savings onto both groups of ratepayers; thus, applying the Fallbrook PUD's rate-setting policies to Rainbow agricultural users would be beneficial to Rainbow customers.

Response: In reviewing this rate issue, LAFCO will have several factors to consider. Under state statute, if a change of organization includes a district annexation, LAFCO must consider whether the proposed annexation will be in the interests of landowners and future inhabitants (Government Code Section 56668.3(b)). The Commission must also give great weight to Resolutions of Objection based on financial or service related concerns. The Commission's consideration per this statute can only be based on financial or service related concerns as defined in Government Code Section 56857(d). In the context of Government Code Section 56857(d) (1), financial concerns means that the proposed uses within the territory proposed to be annexed do not have the capacity to provide sufficient taxes, fees, and charges, including connection fees, if any, to pay for the full cost of providing services, including capital costs. Cost allocation shall be based on general accepted accounting principles and shall be subject to all constitutional and statutory limitations on the amount of the tax, fee, or charge. Government Code Section 56857(d)(2) defines service concerns as whether a district has the inability to provide services that are the subject of the application without imposing level of service reductions on existing or planned future uses in the district's current service area. Service concerns do not include a situation when a district has the ability to provide the services or the services will be available prior to the time that services will be required. According to a review of the proposed uses within the territory proposed to be annexed, sufficient taxes, fees and charges, including connection fees appear to exist to pay for the full cost of providing services. Fallbrook PUD has also postulated that cost-savings resulting from reorganization are in the interests of landowners and future inhabitants.

Capitalization on Rainbow MWD's Assets and Growth

Rainbow MWD states that it rests on a strong financial footing and stands to gain further strength from anticipated growth of residential, educational and commercial developments. In contrast, Rainbow MWD contends that the Fallbrook PUD is nearly built out, and is trying to capitalize on Rainbow's growth. Rainbow MWD's assertion that Fallbrook PUD could use Rainbow's \$100 million in assets in order to leverage more borrowing for Fallbrook PUD's future construction needs has been disputed by the Fallbrook PUD. Based upon divisional accounting requirements and generally accepted rate-making principles, the PUD states that it will not be able to use Rainbow MWD's assets to benefit Fallbrook PUD projects; nor can Fallbrook PUD's assets be used to benefit Rainbow MWD's projects.

Response: According to a review of the proposed uses within the territory proposed to be annexed, sufficient taxes, fees and charges, including connection fees to pay for the full cost of providing services appear to exist, or will be generated. The Fallbrook PUD's Engineering Department estimates that at build-out of the territory currently within the District will involve an additional 1,000 meter installations. No evidence has been presented indicating that the Fallbrook PUD has insufficient capacity to provide sufficient taxes, fees, and charges, including connection fees, if any, to pay for the full cost of providing services, including capital costs. In addition, evidence has not been provided demonstrating Fallbrook PUD's inability to provide services, or that it will need to impose service level reductions on existing or planned future uses in the district's current service area.

Status of Rainbow MWD's Ordinance No. 95-1

Rainbow MWD contends that Rainbow's Ordinance No. 95-1 keeps Rainbow's debt low and manageable and allows the public to participate in the public indebtedness decision-making process. Ordinance 95-1 was adopted by the Rainbow MWD board of directors in 1995 after more than 15% of Rainbow's voters signed petitions to support a public debt initiative. According to the Rainbow MWD, this ordinance serves an important purpose of protecting Rainbow and its ratepayers against incurring excessive public debt by securing the right of ratepayers to vote upon proposed additional public debt. Per this ordinance, whenever Rainbow carries cumulative debt in excess of one million dollars, it cannot incur additional public debt unless additional public debt is first placed on the ballot. Rainbow MWD states that dissolution of the MWD and annexation of Rainbow territory to Fallbrook PUD would terminate Ordinance No. 95-1, thereby depriving Rainbow ratepayers of their right to vote upon proposed additional public debt in the reorganized district. It is also claimed that termination of Ordinance No. 95-1 would subject the Rainbow ratepayers to increased public indebtedness and could increase rates for Rainbow ratepayers.

Response: The Fallbrook PUD's proposal does not state that Rainbow MWD's Ordinance 95-1 is to be terminated. However, LAFCO staff believes that, if approved, the proposed reorganization should include a term and condition providing assurances to Rainbow ratepayers that Ordinance 95-1 will be retained. Therefore, if the Commission approves the proposed reorganization, consideration should be given to modifying the terms and conditions by adding a provision requiring the transfer of responsibility for the debt provision obligation per Ordinance 95-1 to the successor district (Fallbrook PUD). This would be considered an existing obligation. Government Code Section 56886(c) authorizes LAFCO to impose conditions related to the imposition, exemption, transfer, division, or apportionment of obligations of dissolved districts.

Rainbow MWD & Fallbrook PUD's Debt

Rainbow MWD claims that it is a low-debt, budget-conscious district that has reduced costs and prevented rate hikes, while Fallbrook PUD has shown a history of ineffective long-term financial planning. The Rainbow MWD states that the PUD has amassed significant debt, and needs Rainbow's \$100 million in assets in order to leverage more borrowing for Fallbrook PUD's future construction. Rainbow MWD believes that reorganization of the two agencies into one would permit the successor board to create policies and make decisions which could negatively impact Rainbow's revenue and increase public indebtedness, to the detriment of ratepayers.

Response: Rainbow MWD claims that the MWD is a low-debt budget conscious district, while Fallbrook PUD has amassed significant debt appears to be based on speculation and not fact. A review of each district's financial statements reveals that both Rainbow MWD and Fallbrook PUD have comparable financing characteristics and debt levels. The Fallbrook PUD's current total debt outstanding is \$20.6 million. When the PUD's Wastewater Treatment Facilities project is completed at year-end in 2015, Fallbrook PUD's estimated total debt outstanding will be approximately \$37 million. In comparison, when a pending CALTRANS agreement is finalized with the Rainbow MWD, total outstanding Rainbow debt will possibly rise to over \$31 million in 2014-15. Below is a breakdown of the Fallbrook PUD's and Rainbow MWD's debt:

- Fallbrook PUD has a \$7.2 million Qualified Energy Conservation Bond for a 1.0 MW solar facility (balance is \$5.57M) with an effective interest rate of 1.72% (70% federal subsidy). The bond is essentially self-funded, paid for by a California Solar Initiative rebate and savings offset from not having to pay SDG&E for power. This is Wastewater Department debt.
- Fallbrook PUD has a \$6.2 million SRF (State Revolving Fund) loan for the Red Mountain Reservoir UV Treatment Facility (balance is \$5.3M). Interest rate is 2.57%.
- Fallbrook has a \$28.3 million SRF* loan for an in-progress major Wastewater Treatment Plant Rehabilitation. As May 31, 2014, Fallbrook PUD has drawn down \$9.8 million in funds. The interest rate is 2.2%.
- Rainbow MWD has two outstanding SRF* loans totaling \$18.2 million. Both loans have an interest rate of 2.09%.
- Rainbow MWD has an action pending on a \$12 to \$14 million reimbursement agreement to CALTRANS for sewer realignment in the Highway 76 East Segment Project. Rainbow MWD's May 27, 2014 CIP forecast shows a projected 10 year repayment schedule at an unspecified interest rate.
- Rainbow MWD's current total debt outstanding is \$18.2 million. When the pending CALTRANS agreement is finalized, RMWD's total outstanding debt could rise to over \$31 million by year-end 2014.

With respect to using another district's operating assets as collateral for loans, this practice would be unlikely to occur as both districts borrow most of their construction funds from the State of California. The state requires a pledge of revenues, not assets, to secure loans. Assets do not have value in this type of borrowing process. In addition operating assets (pipes, pumps, reservoirs, trucks and buildings)

are considered long-term liabilities because they depreciate, wear out or become obsolete and need to be replaced. Therefore, they represent future costs, not collateral. Lastly, divisional accounting procedures included as a term and condition, plus accounting rules would prevent cross-subsidies between both districts.

Relevancy of JPA Cost Savings

Rainbow MWD states that any cost savings previously experienced from the terminated Joint Powers and Employee Leasing Agreements are now irrelevant because the two agencies are again operating independently. Rainbow MWD believes that Fallbrook PUD should not be exaggerating the cost-savings benefits from the JPA, since the JPA was disbanded over a year ago. Furthermore, Rainbow believes that to force the agencies to merge again would result in more costs and inconveniences.

Response: Rainbow MWD's assertions about cost savings from the terminated JPA being irrelevant will be reviewed by LAFCO staff for relevance. In general, efforts that save public funds are to be encouraged. Achieving cost savings through jurisdictional reorganizations or through functional consolidations, such as joint powers agreements enables agencies to improve their ability to provide services without the need to raise taxes, fees and charges, including connection fees to pay for the full cost of providing services.

Validity of Reorganization Cost Savings

Rainbow MWD claims that the Fallbrook PUD overstates reorganization cost savings and did not reveal how an estimated \$2.5 million in cost savings was calculated. The Rainbow MWD also claims that the consolidation study was performed without input from Rainbow senior staff or department heads resulting in speculative projections regarding staffing. Fallbrook PUD's application additionally identifies \$300,000 of savings from sharing of heavy equipment, such as backhoes and sewer maintenance trucks; however, Rainbow MWD believes that sharing this equipment is not practical. Additionally, Rainbow MWD claims that Fallbrook PUD's representations regarding savings have not addressed the loss of efficiency or impact on service to ratepayers, contractors, or developers resulting from the reduction in district employees, and/or the relocation of employees to/from Fallbrook PUD from Rainbow MWD. Lastly, Rainbow MWD claims that most of the savings from staff reductions identified in the reorganization application were achieved before creation of the Joint Powers Authority. Rainbow MWD states that it has reduced its labor force by 15% over the past four years.

Response: The consolidation study referenced by the Rainbow MWD was co-authored by Fallbrook PUD and Rainbow MWD, therefore, the claim that the study was performed without input of Rainbow senior staff is not supported by evidence. Rainbow MWD's General Manager, Dave Seymour, and Rainbow MWD's Finance Manager, Gene Buckley, helped prepare the study in consultation with Fallbrook PUD management staff. The 2013 operating results of the two districts working under the umbrella of the North County Joint Powers Authority resulted in about \$1 million in collaborative savings, which appear to confirm assumptions contained in the consolidation study. In terms of heavy equipment statements made by the Rainbow MWD, there was not a proposal for the two districts to share a single sewer maintenance truck (Vactor) or a single backhoe. The proposal was to eliminate one of the three Vactor trucks (the oldest) and one of the backhoes (the oldest). The majority of the \$300,000 annual projected savings is estimated to be in reduced administrative and general expenses such as duplicate insurance premiums, audit costs, training costs, association membership fees, etc.

In response to the substance of this Rainbow objection, the nearly \$1 million in net collaborative savings in 2013 took into account additional commuting time caused by the relocation of services to FPUD's offices for employees, vendors, and customers. In response to Rainbow MWD's comments about staff reductions implemented prior to the JPA, the MWD is currently under-staffed in key areas, as the engineering department is staffed with just one engineer, one administrative assistant, and one inspector. This staffing level is probably inadequate to manage the forecasted three-year construction budget of over \$40 million. Increases in the use of consultants, temporary staffing, and overtime will likely be necessary to provide district engineering and other services. Other areas of staffing concern are Finance and Accounting (one individual with no backup) and Customer Service (long-term use of field personnel to compensate for inadequate customer representative staffing levels).

Effect on Agriculture

The Rainbow MWD claims that dissolution of Rainbow MWD would marginalize Rainbow's agricultural community and threaten the existence of important local farms. Rainbow MWD claims that if the Fallbrook PUD's application is approved, the successor board would have the authority and the ability to set policies and priorities, and rates regarding or affecting the agricultural community. Rainbow MWD also disagrees with the Fallbrook PUD's determination that the proposed reorganization is exempt from environmental review. Rainbow MWD accordingly demands that LAFCO evaluate and identify the potential environmental impacts that could result from the proposed reorganization, and take affirmative action to avoid or mitigate those impacts.

Response: In response to Rainbow MWD's statements, a review of Fallbrook PUD water sales statistics show that over 50% of PUD water sales are to groves and nurseries; farmers within the PUD pay 15% to 20% less for water, compared to Rainbow farmers. Fallbrook PUD claims that it sells water to farmers with no markup in price in contrast to Rainbow MWD. If the Fallbrook PUD rate-setting policies were hypothetically applied to agricultural rates within Rainbow, it could potentially benefit Rainbow farmers/agriculture. Therefore, the potential impact on agriculture would be either unchanged or positive.

In terms of CEQA review, the Fallbrook PUD exempted the reorganization from CEQA review, because the geographical area in which previously existing powers are exercised will remain the same. No physical changes to the environment, including agriculture resources, will result from the reorganization. Any future decisions that Fallbrook PUD may take regarding policies and priorities would be subject to CEQA review. The Rainbow MWD had an opportunity to challenge Fallbrook PUD's environmental determination after the exemption was cited on April 28, 2014, but decided not to pursue a challenge. LAFCO would be acting as a responsible agency pursuant to CEQA and not the lead agency for the reorganization.

Governance and California Voting Rights Act

A major objection raised by the Rainbow MWD pertains to governance. Currently, members of the Rainbow MWD are elected by division pursuant to Water Code Section 71250. The proposed reorganization calls for the successor board to be elected by both an "at-large" and "division" (territorial unit) governance structure per the Public Utility District Act (Public Utilities Code Section 15973.1). Rainbow claims that "at-large" voting allows bloc voting that effectively renders the votes of racial and ethnic minorities meaningless. Rainbow MWD states that this election method subjects the reorganized district to risks of lawsuit under the California Voter's Rights Act (Elections Code §§ 14025 et seq.).

Rainbow MWD also questions whether the successor agency for the reorganization should instead be a municipal water district.

Response: While the governance and voting rights issue does not meet the criteria specified in Government Code section 56668.3 (b) related to financial or service-related concerns, it is an important subject area for LAFCO to consider. As addressed in other sections of this report, the Fallbrook PUD has proposed a governance structure consisting of a combination of board members elected at-large and by territorial unit (division). LAFCO does not have authority to structure a governing board of a reorganized PUD in a manner that conflicts with State Law (e.g., a PUD board composed of members elected exclusively by territorial unit - division). Fallbrook PUD's Resolution of Application includes a term and condition requiring that the Board of Directors of the reorganized Fallbrook PUD be elected by territorial unit (4 members) and at large (3 members).

The Rainbow MWD originally theorized that if LAFCO approves the reorganization, LAFCO may exercise considerable authority and may designate a new PUD governing board that consists of members elected exclusively by division (territorial unit). The Rainbow MWD's conclusion regarding governance diverges from provisions contained in both the Public Utility District Act (Public Utilities Code Section 15973.1) and the Cortese-Knox-Hertzberg Local Government Reorganization Act of 2000 (Government Code Section 56886(k)). According to the PUD Act, a new board may be established consisting of all members elected at-large, or as proposed by the Fallbrook PUD, consisting of a combination of members elected by territorial unit and at-large (e.g., four members selected by territorial unit and three members selected at-large). Therefore, the Fallbrook PUD's proposal specifying that the reorganized district consist of four board members elected by territorial unit (division) and three elected at-large conforms to requirements in State Law. According to a survey of 48 Public Utility Districts in California, all PUDs in the state indicate that board members are elected exclusively by an at-large method and none indicated that board members are elected exclusively by territorial unit (division).

The Rainbow MWD further states that a challenge under the California Voting Rights Act (CVRA) would likely ensue due to the governance structure proposed by the Fallbrook PUD. However, successful CVRA litigation typically requires a showing that racially polarized voting has occurred in a district's governing board elections. In the case of the proposed reorganization, there is no voting history under the combined governance structure and no claim of racially polarized voting. Furthermore, the few cases that have been litigated on voting rights challenges have not challenged a combined (territorial unit and at-large) voting structure as proposed by the Fallbrook PUD. Accordingly, to the extent no claim of racially polarized voting could be proven under the present voting systems, a viable claim under the California Voting Rights Act would probably be unlikely. Having a board consisting of a combination of at-large members and directors elected by division may also produce certain governance benefits such as maximizing representation of the entire region, plus providing the dual opportunity for smaller voting districts to be represented via territorial units.

The Rainbow MWD also questions whether LAFCO could designate a municipal water district (e.g., Rainbow MWD) as the successor agency for the reorganization, instead of the Fallbrook PUD. While LAFCO has considerable authority to modify proposals, selection of a different principal act other than the PUD Act, would not fall within the permitted areas for proposal modifications. A more appropriate vehicle to accomplish this objective would have been for the Rainbow MWD to initiate a conflicting proposal with LAFCO within a 60-day time period from April 28, 2014. Such a conflicting proposal was not initiated by Rainbow MWD. Therefore, LAFCO must base its decision on the proposal, as submitted

by the Fallbrook PUD and the principal act under which the Fallbrook PUD was formed (Public Utility District Act).

Rainbow MWD's Position on JPA and Governance

The Rainbow MWD objects to the Fallbrook PUD's reorganization proposal because it believes the Fallbrook PUD misrepresented Rainbow's position regarding operation of the former North County JPA and the proposed successor agency under the Public Utility District Act. The Rainbow MWD states that the PUD never took the position that elections by divisions were not legally permitted under the Public Utility District Act, and would have instead supported operation under the Municipal Water District Law with Rainbow as the successor agency. Organization under the Municipal Water District Law requires a district to be divided into five divisions in such manner as to equalize, as nearly as practicable, the population in the respective divisions (Water Code Section 71160).

Response: The issues raised by the Rainbow MWD regarding Fallbrook PUD's alleged misrepresentation of the governance structure of the reorganized district do not appear to be supported by the record and minutes from both of the districts.

Election Provisions

If LAFCO approves the proposed reorganization of the Fallbrook PUD and Rainbow MWD, then voters and landowners would have an opportunity to submit written protests pursuant to Government Code Sections 57077.3. If 25% or more of the number of landowners within the Rainbow MWD who also own at least 25% of the assessed value of land, or if 25% of the voters within the MWD submit written protest at a protest hearing, then the reorganization would be subject to an election within the boundaries of the Rainbow MWD. However, if a majority protest was present (50% or more of the voters residing within the Rainbow MWD), then proceedings would be terminated pursuant to Government Code Section 57078.

In addition, Government Code Section 56877 specifies that LAFCO has the option of imposing a condition requiring that when an election is required due to protest, that it be held within both the annexation area and the territory of the district to which annexation is proposed, if certain voter and assessed value thresholds are satisfied. For example, if the assessed value of land within the annexation territory (Rainbow MWD) equals one-half or more of the assessed value of land within the territory of the district to which annexation is proposed (Fallbrook PUD), or the number of registered voters residing within the annexation territory (Rainbow MWD) equals one-half or more of the number of voters residing within the district to which annexation is proposed (Fallbrook PUD), then LAFCO may condition its approval on an election to be called with both the annexation territory and the local agency annexing the territory.

Response: If the proposed reorganization is approved by LAFCO and an election is ordered, LAFCO would have the option to condition its approval on voter confirmation within both the Rainbow MWD and Fallbrook PUD. Given the assessed value characteristics of the proposed reorganization, an argument could be made that LAFCO should determine that an election should be held both within the Rainbow MWD and Fallbrook PUD. This special provision in Government Code Section 56877 is applicable only when an election is already required per the protest provisions contained in Government Code Section 57077.3; it does not permit LAFCO to order an election absent protest. We have confirmed that the proposed reorganization satisfies both the assessed value and registered voter

minimum requirements of Government Code Section 56877. According to the County Assessor, the assessed value of land within the Rainbow MWD is \$1,636,165,143.00, compared to \$1,364,964,053.00 within the Fallbrook PUD (as of July 29, 2014). The number of registered voters in Rainbow MWD is 12,418 and 14,759 within the Fallbrook PUD (as of April 4, 2014). Therefore, LAFCO will have the option of ordering an election, if one is required per Government Code Section 57077.3 in both the Rainbow MWD and Fallbrook PUD. LAFCO will need to determine whether the votes should be tallied separately within Rainbow MWD and Fallbrook PUD or cumulatively within both districts. If LAFCO determines that the Section 56877 condition should be imposed, then a modification to the proposed terms and conditions submitted by the Fallbrook PUD would be necessary.

Payment of Election Costs

If the proposed reorganization is approved and an election is held, LAFCO may require that the Fallbrook PUD be responsible for paying all election costs, whether the ballot measure succeeds or fails. Unless LAFCO makes this payment condition a part of the reorganization, State Law would require that the costs associated with the dissolution component of the reorganization be the responsibility of the dissolved district per Government Code Section 57150(c) -- if the ballot measure is successful. If unsuccessful, the costs would be underwritten by the County of San Diego. Estimated election costs range from \$3,320 to \$335,000 depending on when an election is held and the territory/agencies LAFCO includes in the election per Government Code Section 56877.

Response: As previously discussed, LAFCO has the ability to modify proposals that are submitted to the Commission. As submitted, the Fallbrook PUD application does not contain a term and condition covering payment of election costs. If the reorganization is approved by LAFCO, a term and condition could be added to LAFCO's approval requiring that the applicant (Fallbrook PUD) pay all costs associated with reviewing protest petitions and conducting an election. This matter could be addressed by LAFCO as a modification to the terms and conditions submitted by the Fallbrook PUD.

Rainbow MWD Staff Objections

Rainbow MWD objects to the proposed reorganization on behalf of its staff, who oppose the proposed reorganization because the MWD believes that the two agencies have incompatible employee benefit structures, which would disadvantage the Rainbow employees and cause additional expense. Further, the Rainbow MWD believes the Fallbrook PUD has medical retirement benefit intricately woven into the Vacation Holiday, and Sick leave plans (VHS) plan; while Rainbow's medical retirement benefit stands apart from the Paid Time Off (PTO) program. In addition, Rainbow MWD claims that combining the two employee groups under the same CalPERS retirement contract creates additional expenses for the Rainbow ratepayers. Rainbow MWD also states that current employer retirement contribution for its employees is 14.66% of payroll, while Fallbrook PUD's employer contribution is 28.39%. A reorganization of the two agencies into one would force the Rainbow employees to operate under one contract, which Rainbow believes will create a lower cost for Fallbrook PUD ratepayers but a higher cost for Rainbow ratepayers.

Response: A review of the benefits for the two employee groups reveals that employee benefits are similar between the two districts. Modifications necessary to develop a common MOU would involve a meet-and-confer process. Informal meetings between shared Fallbrook PUD/Rainbow management and the two district employee associations had begun in late 2013. The issue raised by the Rainbow MWD regarding the employer retirement contributions also appears debatable. As of July 1, 2014 the

contributions were very similar: Rainbow MWD 15.7% and Fallbrook PUD: 16.6%. The nine-tenths of one percent (0.9%) difference in rates represents a survivor benefit provision in the Fallbrook PUD contract that is absent in the Rainbow contract. Post reorganization, when combined as a single workforce, the net impact of this enhanced retirement benefit would be in the range of \$30,000 per year.

Rainbow MWD also states that the two agencies' employee benefit structures would inconvenience the Rainbow employees and may, in the long run, increase costs for Rainbow ratepayers. According to Rainbow, a reorganization of the two agencies into one would force the Rainbow and PUD employees to operate under one contract, which would likely create a lower cost for PUD ratepayers but a higher cost for Rainbow ratepayers. Again, in reviewing the benefit structures of Fallbrook PUD and Rainbow MWD, both organizations appear to have similar employee MOUs and CalPERS retirement contracts. As Rainbow MWD employees transition to the Fallbrook PUD retirement contract, their benefits could be enhanced compared to the current Rainbow MWD contract (e.g. additional survivor benefit provisions). Fallbrook PUD's employer contribution was scheduled to drop to about 16% as of July 1, 2014. Divisional accounting will also prevent cross subsidies between customer groups.

Respecting the JPA Contractual Process

The Rainbow MWD states that the Fallbrook PUD failed to respect the contractual processes laid out in the Joint Powers Agreement. In March 2014, after a year of attempting to work with Fallbrook PUD, Rainbow MWD decided that it was not in the best interest of its ratepayers to consolidate with Fallbrook PUD, and began the formal termination process pursuant to the terms of the joint powers agreement. Instead of respecting Rainbow's decision to withdraw from the joint powers authority, the Rainbow MWD states that the Fallbrook PUD took the equivalent of a hostile action and filed an application with LAFCO to dissolve the MWD. The Rainbow MWD believes the PUD's actions show a disregard for the consensus-building process previously agreed to by the agencies, and resulted in a trust issue.

Response: Rainbow MWD was within its rights to provide notice and no longer be a party to the North County JPA. As with Rainbow MWD, the Fallbrook PUD was also within its rights under the Cortese-Knox-Hertzberg Act to submit an application for reorganization. Whether it was strategically advisable for the Fallbrook PUD to submit an application at the time it decided to do so was questionable given the strong opposition from the Rainbow MWD, ratepayers, and employees. However, The Fallbrook PUD did not violate any LAFCO statutes in initiating the reorganization application. This initiation issue was previously addressed in the report.

Proposition 218 Notification

A complaint had been received by LAFCO staff claiming that the Fallbrook PUD board violated the intent of Proposition 218 regarding a pending rate increase. The complaint alleged that a recent PUD notice stated that 89% of the increase in water rates would be due to the increase in the cost the PUD must pay to our wholesalers for water. The concerns expressed by the complainant were referred to the Fallbrook PUD for a response. The Fallbrook PUD states that the Proposition 218 public notice to PUD customers, by law, establishes the upper limit of new water rates that the PUD Board may consider during the annual budget process. Fallbrook PUD staff incorporates the San Diego CWA's projected highest rate scenario into the District's financial model and the Proposition 218 notice. Typically, Board-adopted rates are less than those contained in the notice.

Response: Fallbrook PUD's General Manager and Administrative Services Manager met with the complainant twice during the budget process to discuss, in detail, the rate setting process. They also corresponded with the complainant three times from July 24, 2013 to August 5, 2013. During the 2014 budget process, the Fallbrook PUD Board directed district staff to begin setting water rates on a calendar year rather than a fiscal year basis, consistent with rate changes from the CWA. This change was also considered comparable with respect to Rainbow MWD, which already sets rates on a calendar year basis.

ADVISORY COMMITTEE DISCUSSION / RECOMMENDATION

Most, but not all Jurisdictional proposals are submitted to LAFCO with the concurrence of subject agencies. In the case of the reorganization of the Fallbrook PUD and Rainbow MWD, concurrence was not obtained. The Fallbrook PUD cites compelling reasons to move forward without the support and consent of the Rainbow MWD. Fallbrook PUD believes that cost savings and efficiencies will result from reorganization of the two districts, thus, justifying the initiation of the reorganization application. On the other hand, Rainbow MWD disputes Fallbrook PUD's claims and wants to be left alone. The Rainbow MWD cites local control and the will of the people as the basis for retaining the status quo. The MWD filed a Resolution of Objection with LAFCO and requests that LAFCO disapprove the reorganization. To assist LAFCO staff and the Commission in making an informed decision on whether to approve, disapprove, or modify the proposed reorganization, the Special Districts Advisory Committee is requested to review the information provided in this report and provide advice on three important subject areas: (1) Financial and Service Feasibility; (2) Proposed Governance Structure; and (3) Treatment of Rainbow MWD's Objections.

1. Rainbow MWD and Fallbrook PUD's Financials and Service Plans: The advisory committee should review the service summary and financial discussion covered in this staff report and attachments and provide comments on any of the following:

- a. Has the Fallbrook PUD demonstrated that the proposed reorganization is financially feasible?
- b. Have financial or service issues been identified requiring further review and analysis?

2. Governance: The governance structure of the proposed reorganized district represents one of the most fundamental areas of the Rainbow MWD's objection to the Fallbrook PUD's reorganization proposal. The advisory committee should comment on the following:

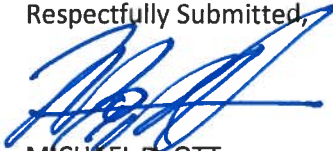
- a. If the reorganization is approved by LAFCO, would it be appropriate to establish a governing board for the successor district (Fallbrook PUD) consisting of a four board members elected by territorial unit (division) and three members elected at-large?

3. Rainbow MWD's Objection: The advisory committee should review Rainbow MWD's objections and provide comments on the following:

- a. Which of the Rainbow MWD's objections have merit?
- b. If the majority of Rainbow's objections have merit, should LAFCO deny the proposed reorganization?

- c. If Rainbow MWD's objections do not have merit, should the reorganization still be denied given the strong objections of the Rainbow MWD, ratepayers, and Rainbow employees? Note that if LAFCO denies the proposed reorganization, the process terminates and an election will not be scheduled.
- d. If Rainbow MWD's objections lack sufficient merit, should LAFCO approve the reorganization allowing Rainbow residents to have an opportunity to mount a protest and seek an election on the question of whether the reorganization should be affirmed or rejected? Note that if LAFCO approves the proposed reorganization, the process continues with protest and election provisions.
- e. If LAFCO approves the reorganization and sufficient protest is submitted, should LAFCO:
1. Require that an election occur **both** within the Rainbow MWD and the Fallbrook PUD?
 2. Require that the votes be counted **separately** within Rainbow MWD and Fallbrook PUD or within the **combined** territory of both districts?
- f. If LAFCO approves the reorganization and an election is ordered, should the Fallbrook PUD be required to pay for all protest and election-related costs (estimated to be \$3,200 to \$335,000 for an election)?

Respectfully Submitted,



MICHAEL D. OTT
Executive Officer



HARRY EHRLICH
Local Governmental Consultant

MDO:ra

Exhibit

Vicinity map

List of Attachments (Available from Links listed below):

- (1) Preliminary LAFCO staff report and North County JPA Consolidation study
- (2) Fallbrook PUD JPA Cost Savings Memo, 5/12/14
- (3) Rainbow MWD memorandum claiming misrepresentation of facts by Fallbrook PUD, 11/6/14
- (4) Fallbrook PUD memorandum responding to misrepresentation claims, 11/12/14

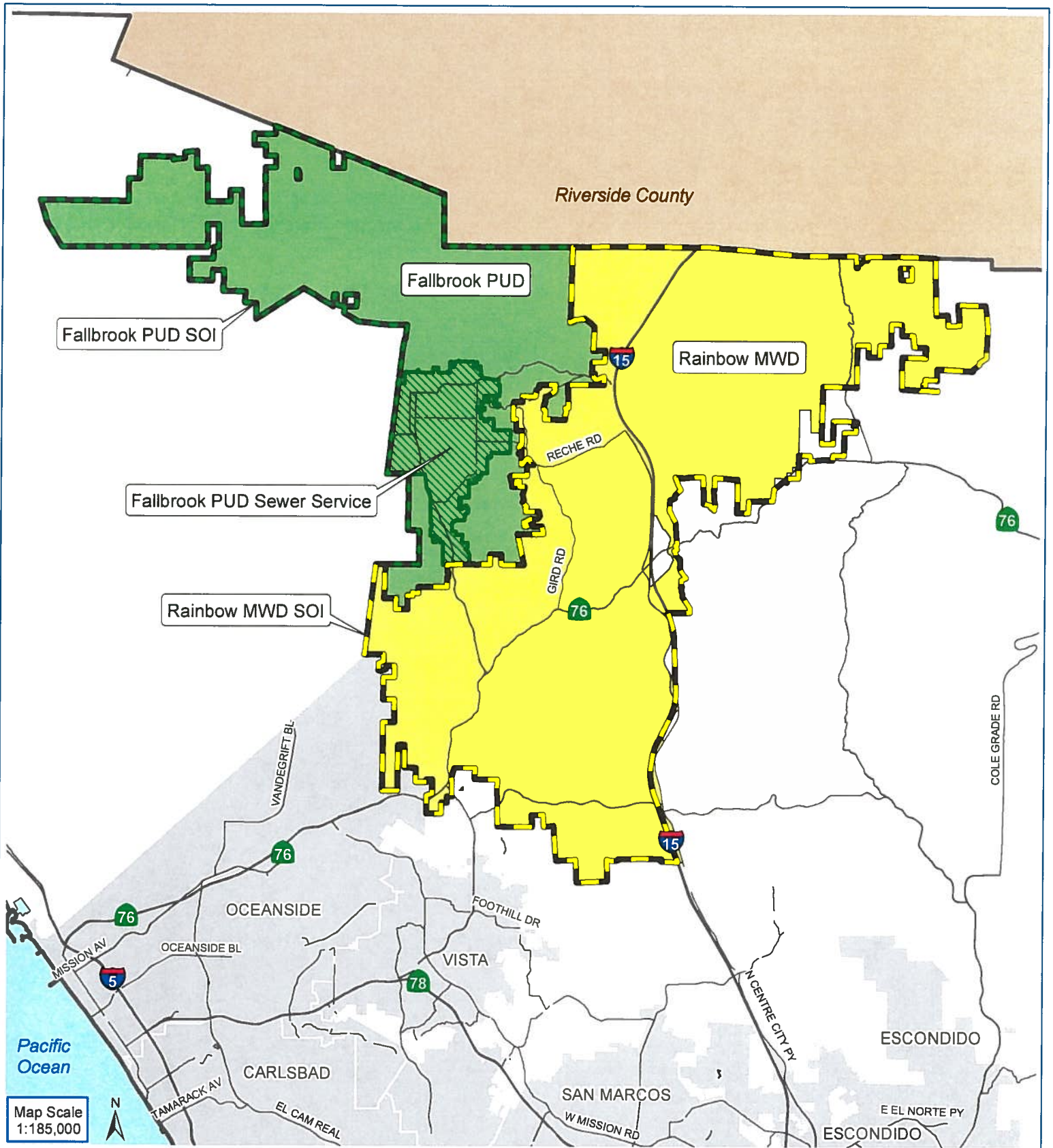
Links to Attachments:

<http://www.sdlafco.org/Agendas/AdvisoryCommittee/2014December/LAFCOPreStaffReport.pdf>

<http://www.sdlafco.org/Agendas/AdvisoryCommittee/2014December/FPUDCostSavingsMemo05-12-14.pdf>

<http://www.sdlafco.org/Agendas/AdvisoryCommittee/2014December/FPUDResponseRMWDLetter11-12-14.pdf>

<http://www.sdlafco.org/Agendas/AdvisoryCommittee/2014December/RainbowMWDLetter11-06-14.pdf>



RO14-04
 SA14-04(a) Fallbrook PUD
 SA14-04(b) Rainbow MWD
 MSR/SR13-66

Proposed "Fallbrook PUD & Rainbow MWD Reorganization" - Involving district dissolution, annexation, and latent powers expansion for sewer service

- Fallbrook PUD
 - Fallbrook PUD SOI
 - Fallbrook PUD Sewer Service
 - Rainbow MWD
 - Rainbow MWD SOI
- SOI = Sphere of Influence

Chairman

Andrew Vanderlaan
Public Member

December 19, 2014

Vice Chairman

Vacant

TO: Special Districts Advisory Committee

Members

Bill Horn
County Board of
Supervisors

FROM: Harry Ehrlich; LAFCO Special Districts Consultant

Dianne Jacob
County Board of
Supervisors

RE: Selection of Committee Officers for the Special Districts
Advisory Committee for 2015

Bud Pocklington
South Bay
Irrigation District

Dear Advisory Committee Members:

Lori Zapf
Councilmember
City of San Diego

The Special Districts Advisory Committee Rules (Rules) provide for selection of the Committee Officer positions of Chair and Vice-Chair at the December meeting, if held, or as soon as possible thereafter. In prior years, the Committee has selected Officers after a member election but now those elections are held every other year. Therefore it is recommended to select the Officers annually at your December meeting.

Jim Janney
Mayor
City of Imperial Beach

Your current Officers are Chairman Tom Pocklington and Vice-Chair Kimberly Thorner. At the December 2014 meeting, nominations will be accepted from the Committee for the Officer positions and all members are qualified to be nominated.

Sam Abed
Mayor
City of Escondido

If you have any questions, please feel free to contact me to have them addressed. LAFCO staff anticipates 2015 to be a busier year for the SDAC so we look forward to serving the role of the SDAC and Commission.

Alternate Members

Greg Cox
County Board of
Supervisors

Sherri Lightner
Councilmember
City of San Diego

Jo MacKenzie
Vista Irrigation District

Sincerely,

Lorraine Wood
Councilmember
City of Carlsbad



Harry Mathis
Public Member

HARRY EHRLICH, SDA
Local Government Consultant

Executive Officer

Michael D. Ott

HE:ra

Special Counsel

Michael G. Colantuono