

Staff Report

May 14, 2014

Agenda Item No. 7.b.

Sativa County Water District Municipal Service Review (MSR) and Sphere of Influence (SOI) Update

Agenda Item 7.b. is consideration and approval of the Sativa County Water District (Sativa or District) Municipal Service Review (MSR) and Sphere of Influence (SOI) update.

Background

Since 1971, LAFCOs have been required to develop and adopt a Sphere of Influence for each city and special district. Government Code Section 56076 defines an SOI as “a plan for the probable physical boundaries and service area of a local agency, as determined by the commission.”

Developing SOIs is central to the Commission’s purpose. As stated in Government Code Section 56425:

“In order to carry out its purposes and responsibilities for planning and shaping the logical and orderly development and coordination of local governmental agencies so as to advantageously provide for the present and future needs of the county and its communities, the Commission shall develop and adopt a Sphere of Influence for each local governmental agency within the county and enact policies designed to promote the logical and orderly development of areas within the Sphere.”

Section 56425(g) further requires that the Commission update Spheres of Influence “every five years, as necessary.”

Timeline

12/30/1938	Sativa County Water District incorporated with the State of California
11/2005	LAFCO issues Draft MSR (“Round One” Cycle of MSRs)

Draft MSR:

“The District does not provide water conservation services.”

“The District noted that water mains need to be upgraded, relocating services from the rear of properties and alley ways in order to prevent structures being built over service lines.”

“The District has limited reserves and uses a pay-as-you-go approach for improvements, which may be a constraint for implementing infrastructure improvements.”

“The Sativa-Los Angeles County Water District does not have metered accounts.”

“Due to the size of its service area, condition of the infrastructure, and financial resources, it is recommended that LAFCO consider adopting a zero sphere influence for the Sativa-Los Angeles County Water District.” [emphasis added]

12/14/2005 Commission considers staff recommendation, and continues to 2/22/2006 Meeting

Staff Report:

“In the case of the Sativa-Los Angeles County Water District, staff recommends that the Commission adopt a zero sphere of influence for the agency, as suggested in Dudek’s MSR Report [Dudek is the consultant who prepared the Draft MSR], with possible future dissolution of the agency to be considered by the Commission. The District has been highly uncooperative in providing staff with any information and has refused to provide any financial accounting statements other than their budget for 2003-2004.”

2/2006 Consultant issues Addendum to November 2005 MSR

“The District’s sphere of influence should remain coterminous with its service area boundaries. [emphasis added]

2/22/2006 Commission approves MSR

03/09/2011 Commission approves “Round 2” MSR Schedule

04/11/2012 Commission awards contract to Hogle-Ireland, Inc., to prepare Draft MSR for Sativa County Water District.

8/2012 Hogle-Ireland release Draft MSR

8/16/2012 LAFCO provides copy of Draft MSR to Sativa County Water District

- 09/13/2012 Sativa Board of Directors sends letter to LAFCO re “hostile takeover” and referral to its counsel “to turn over the LAFCO MSR matter to California courts”
- 10/10/2012 Commission closed session conference with counsel in light of written threat of litigation
- 10/1/2013 Mark Cummins, CPA, issues Forensic Audit -- Final Report of Findings

With respect to the November 2005 MSR, the records indicate that Sativa Board President Johnny Johnson testified at the December 14, 2005, Commission meeting requesting additional time to provide updated information to LAFCO. The Commission continued the matter, and on January 20, 2006, Sativa provided additional information to Dudek (LAFCO’s consultant who prepared the November 2005 MSR). Dudek summarized the information from Sativa in the February 2006 MSR Addendum.

Staff notes that the reasoning for the change in staff’s recommendation—from a zero sphere of influence at the 12/14/2005 Commission meeting to a coterminous sphere of influence at the 2/26/2006 meeting—is not documented in LAFCO’s records.

Sativa County Water District Draft MSR and SOI Update

On April 11, 2012, the Commission awarded a contract to Hogle-Ireland, Inc. to assist in preparing an MSR for the Sativa County Water District.

The consulting team assembled by Hogle-Ireland included both urban planning professionals as well as a water engineer with more than three decades of experience designing, constructing, and managing public water systems.

Staff of Hogle-Ireland met with representatives of Sativa County Water District in person, and also communicated with Sativa’s staff via e-mail and telephone on several occasions. Representatives of Hogle-Ireland also met with other water district representatives; specifically, these meetings included the Central Basin Municipal Water District, the City of Compton, the Golden State Water Company, and the Park Water Company. LAFCO staff met with representatives of Sativa County Water District, the Central Basin Municipal Water District, and the Park Water Company.

In August of 2012, Hogle-Ireland released its “Sativa L.A. County Water District Administrative Draft Municipal Service Review” (Draft MSR). The Draft MSR recommended “that the Board [Commission] consider dissolving the Sativa Los Angeles County Water District and reducing the District’s sphere of influence to zero; and increasing the Central Basin Municipal Water

District's sphere of influence to include all of the Sativa Los Angeles County Water District's former sphere of influence" (Draft MSR, Page 44). This is, essentially, a consultant recommendation that LAFCO consider dissolving the Sativa County Water District and concurrently annexing Sativa's territory into the boundaries of the Central Basin Municipal Water District. Staff notes that this same outcome could more effectively be implemented were the Commission to approve a consolidation of the two districts (Sativa and Central Basin).

In the course of completing the Draft MSR, staff of Hogle-Ireland utilized the entire budget in its contract with LAFCO. Following the issuance of the Draft MSR, Hogle-Ireland was acquired by Moore Iacofano Goltsman (MIG) and the employees at Hogle-Ireland who worked on the Sativa Draft MSR are no longer employed by MIG. For these reasons, the consultants who worked on the original Draft MSR are not available to LAFCO for follow-up consultation.

Hogle-Ireland's recommendation reflected concerns about Sativa's "pay as you go financial approach," the fact that the "[d]istrict does not have the present financial ability to fund major replacements that will be required for an aging system," and the "District's management deficiencies [which] have been adequately documented" (Draft MSR, Page 44).

Sativa County Water District representatives were sent a copy of the Draft MSR on August 16, 2012. Pursuant to the conversations at a meeting shortly thereafter between LAFCO staff and Sativa representatives, staff felt that it was appropriate to provide the District with ample time to address the concerns expressed by the Consultant.

There followed a lengthy exchange of information, and multiple communications (meetings, letters, telephone conversations) between staff and Sativa representatives, coordinated by the District's former legal counsel. Of primary concern was the lack of financial audits going back to Fiscal Year 2005-2006. As a courtesy to the District, staff felt it important to have such documents and to provide the District with sufficient time to engage a qualified consultant to complete the work. The District retained an accountant (Mr. Mark Cummins, CPA) to prepare financial audits for several years. LAFCO specifically requested a forensic audit—which covers additional items not necessarily covered in a financial audit—and the District agreed to a forensic audit and retained Mr. Cummins to prepare it.

Starting in late 2013, and continuing into early 2014, the District provided LAFCO with several financial audits, as well as a forensic audit, prepared by Mr. Cummins, CPA. In early 2014, having now received a significant volume of information, as well as financial audits to bring the District current, staff resumed preparation of a staff report and recommendations to the Commission, as described in more detail herein.

Summary of Recommendations

It is important to note that staff has reached a different conclusion and recommendation than the consolidation of Sativa with Central Basin Municipal Water District recommended by the

consultant in August of 2012. Based on staff's reviews since the Draft MSR in August, 2012, and substantial supplemental information augmenting the 2012 Draft MSR as summarized in this staff report, staff is recommending a change from the current coterminous Sphere of Influence established in 2006. Staff recommends adoption of a Zero Sphere of Influence (Zero SOI) at this time based upon the entire record of this Draft MSR and the previous MSR in 2005.

MSR Determinations:

In order to prepare and to update an SOI for a district, , the Commission is required, pursuant to Government Code Section 56430, to conduct a review of the municipal services in that particular district. In some cases the staff has prepared the municipal service review, and in some cases staff has been assisted by a consultant in completing this review.

LAFCO staff has supplemented the consultant's Draft MSR documentation with significant additional material since August of 2012. Proposed determinations and recommendations in this staff report are those recommended by the staff, and not those of the consultant, which recommended that the District be dissolved and the residents ultimately be served by the Central Basin Municipal Water District.

Staff has prepared the following draft determinations for Commission approval:

1. Growth and population projections for the affected area. The District's service area is primarily built out with an estimated population of 6,320 persons and 1,631 active service connections, and 12 vacant lots. There are no plans for future redevelopment within the service area, and the existing population of 6,320 persons is not anticipated to increase or decrease significantly over the next 20 years.
2. The location and characteristics of any Disadvantaged Unincorporated Communities (DUCs) within or contiguous to the Sphere of Influence. Three small areas, along and within the southwesterly and southerly boundaries of the District, are located within the City of Compton; collectively, these areas represent a very small portion of the territory within Sativa's boundaries. Most of the territory within the boundaries of the Sativa County Water District is within County unincorporated territory. All of this unincorporated territory—more or less bound by Mona Boulevard on the East, Oris Street on the south, Paulsen Avenue on the west, and Wayside Street/130th Street on the north—is a DUC. The area, which is less than one-third of a square mile in size, is almost entirely single-family residential homes, with some multi-family residential (primarily duplex units), and a handful of non-residential uses. Streets tend to be somewhat narrow with a significant amount of on-street parking. The area is bisected in a north-south direction by the Metro Blue Line near Willowbrook Avenue, and the

Alameda Corridor is just outside the district's eastern boundary. The DUC within Sativa continues to the north of Sativa, and is also predominantly residential in nature, with the exception of commercial/retail uses along El Segundo Boulevard.

3. Present and planned capacity of public facilities, adequacy of public services, and infrastructure needs or deficiencies including needs or deficiencies related to sewers, municipal and industrial water, and structural fire protection in any DUCs within or contiguous to the Sphere of Influence. The District is currently able to meet its water demands through a combination of three active ground water wells and purchasing leased water. The District also has an emergency water interconnection with the City of Compton. The District, formed in 1938, has an aging infrastructure that will require costly improvements over time. The District has done a poor job of planning for future infrastructure needs, including the installation of water meters, relocation of water lines to the front of properties, and construction of a replacement water well to increase water supply and pressure.
4. Financial ability of agencies to provide services. The District operates on a "pay as you go" approach, and has failed to conduct any meaningful long-term planning efforts. Funds have not been set aside for improvements to an aging infrastructure, the District's rate structure is inconsistent with the rates charged by surrounding service providers, and the District has yet to develop a strategic plan to continue to provide service in the future.
5. Status of, and opportunities for shared facilities. In 2007 the District installed an emergency connection (a 4" one-way water line) to the Compton Municipal Water Department, to be utilized in the event that the District had an interruption of its water supply. As far as LAFCO staff is aware, the emergency connection has never been utilized. A contract with the City of Compton, dated March 19, 2007, enables Compton to supply water to Sativa in an emergency. There do not appear to be any additional opportunities for shared facilities with other service providers in the vicinity of the District.
6. Accountability for community service needs, including governmental structure and operational efficiencies. In some respects, the District is accountable to the community it serves: members of the Board of Directors live in the community, the District maintains an office that is available to the public during normal business hours, and staff maintains customer complaint logs which document incoming complaints and their resolution. In most other respects, the District does a poor job of conveying information to the public: failure to adopt and follow annual budgets, failure to commission financial audits prepared and made

available to the public in a timely manner, and a website that is woefully lacking in concrete, substantive information that would be useful to the general public.

7. Any other matter related to effective or efficient service delivery, as required by Commission policy. Many of the issues raised herein—lack of water meters, location of water lines, no adopted annual budgets, little or no apparent comprehensive long-term planning—go back several years. Some of these issues have been brought the District's attention by outside parties (LAFCO and others). The District's Board of Directors and employees have been slow to implement necessary changes or have ignored these issues altogether.

SOI Determinations:

In determining a Sphere of Influence, pursuant to Government Code Section 56425, the Commission is required to make specific determinations. Staff has prepared the following draft proposed determinations for Commission approval:

1. The present and planned land uses in the area, including agricultural and open-space lands. The present and planned land uses are predominantly low-density residential uses. There are no agricultural and open space uses within the boundaries of the District.
2. The present and probable need for public facilities and services in the area. Residents within the boundaries of the Sativa County Water District will continue to need water service indefinitely.
3. The present capacity of public facilities and adequacy of public services that the agency provides or is authorized to provide. The District is currently able to meet its water demands through a combination of three active ground water wells and purchasing leased water. The District also has an emergency water interconnection with the City of Compton. The District, formed in 1938, has an aging infrastructure that will require costly improvements over time. The District has done a poor job of planning for future infrastructure needs, including the installation of water meters, relocation of water lines to the front of properties, and construction of a replacement water well to increase water supply and pressure.
4. The existence of any social or economic communities of interest in the area if the Commission determines that they are relevant to the agency. Given the very small size of the area—less than one third of a square mile—there are no social or economic communities of interest that are relevant to the agency.

5. The present and probable need for sewers, municipal and industrial water, or structural fire protection services and facilities of any DUC within the existing Sphere of Influence. Sativa has an existing Coterminous SOI, which means that the boundaries of the District and its SOI are the same. Most of the territory within the boundaries of the District is within County unincorporated territory. All of this unincorporated territory—more or less bound by Mona Boulevard on the East, Oris Street on the south, Paulsen Avenue on the west, and Wayside Street/130th Street on the north—is a Disadvantaged Unincorporated Community, or DUC. Residents within Sativa's boundary will continue to need sewer, water, and structural fire protection indefinitely.

These determinations are addressed in Section 2 of the attached Resolution No. 2012-00 RMD.

Information Reviewed:

In the course of preparing this report, staff conducted a thorough review of information from a wide variety of sources, including, but not limited to:

- Forensic Audit – Final Report of Findings, Conclusion of Formal Field Work on Forensic Audit, Findings as of October 1st, 2013, as well as accompanying District Management Review prepared by Mark Cummins, CPA [consultant to the Sativa County Water District].
- Sativa – Los Angeles County Water District, Independent Auditor's Report, Fiscal Year Ended June 30, 2013, issued December 17, 2013, prepared by Mr. Cummins, CPA.
- Sativa – Los Angeles County Water District, Independent Auditor's Report, Fiscal Year Ended June 30, 2013, issued December 7, 2013, prepared by Mr. Cummins, CPA.
- Sativa – Los Angeles County Water District, Independent Auditor's Report, Fiscal Year Ended June 30, 2012, issued November 06, 2013, prepared by Mr. Cummins, CPA.
- Sativa – Los Angeles County Water District, Independent Auditor's Report, Fiscal Year Ended June 30, 2011, issued November 06, 2013, prepared by Mr. Cummins, CPA.
- Sativa – Los Angeles County Water District, Independent Auditor's Report, Fiscal Year Ended June 30, 2010, issued November 06, 2013, prepared by Mr. Cummins, CPA.
- Sativa – Los Angeles County Water District, Independent Auditor's Report, Fiscal Year Ended June 30, 2009, issued October 1, 2013, prepared by Mr. Cummins, CPA.

- Sativa – Los Angeles County Water District, Independent Auditor's Report, Fiscal Year Ended June 30, 2008, issued January 8, 2013, prepared by Mr. Cummins, CPA.
- Sativa – Los Angeles County Water District, Independent Auditor's Report, Fiscal Year Ended June 30, 2007, issued December 17, 2012, prepared by Mr. Cummins, CPA.
- Sativa – Los Angeles County Water District, Independent Auditor's Report, Fiscal Year Ended June 30, 2006, issued November 20, 2012, prepared by Mr. Cummins, CPA.
- Sativa – Los Angeles County Water District, Independent Auditor's Report, Fiscal Year Ended June 30, 2005, issued November 15, 2012, prepared by Mr. Cummins, CPA.
- Sativa – Los Angeles County Water District, Independent Auditor's Report, Fiscal Years Ended June 30, 2004, 2003, and 2002, issued August 3, 2005, prepared by the Los Angeles County Department of Auditor-Controller.
- Numerous policies adopted by the Sativa County Water District Board of Directors between 2004 and 2013.
- Office of the State Controller Comprehensive Annual Financial Reports (CAFRs) for Fiscal Year 2010-2011.
- Correspondence to LAFCO from Mr. James D. Ciampa of the law firm of Lagerlof, Senecal, Gosney & Kruse (former counsel to the Sativa County Water District).
- Meetings, e-mail communications, and telephone interviews with former District legal counsel (James D. Ciampa), consulting engineer John Mundy (formerly the General Manager of the Las Virgenes Municipal Water District), members of the Sativa County Water District Board of Directors, staff of the Sativa County Water District, representatives of the Central Basin Municipal Water District, and representatives of the Park Municipal Water Company.
- Media reports concerning the Sativa County Water District alternative service providers.
- The November 2005 MSR ("Round 1") adopted by the Commission on February 22, 2006.
- The August 2012 Draft MSR prepared by Hogle-Ireland, Inc.

- Records of interviews that Hogle-Ireland conducted with the Central Basin Municipal Water District (June 19, 2012); the City of Compton Water Division (May 21, 2012); and Sativa County Water District (May 31, 2012).

Staff Analysis

Based upon a review of the Draft MSR prepared by the Consultant and the information on which it was based, and other sources of information including, but not limited to, more recent communication with Sativa County Water District representatives (Board-Members, staff, consulting engineers, as well as former legal counsel and current legal counsel); documentation provided by Sativa representatives; communication with representatives of other public agencies familiar with Sativa's operations; and publicly available information, staff identified a series of concerns in three broad categories: financial oversight concerns, operations and long-term planning concerns, and miscellaneous/transparency concerns. A short summary of the relevant issues, and the District's progress in addressing them, is provided in Exhibit "F," attached to this report.

Financial Oversight Issues. The issues associated with the District's oversight of its finances include the following:

- Audits. Section 30540 of the Water Code requires that county water districts "retain an auditor as an independent contractorto conduct an annual audit of the district's books, records, and financial affairs." In its initial review, LAFCO learned that the District's last independent audit of the District was prepared for Fiscal 2004-2005, meaning that the District had not hired an independent auditor to review its books for seven years. Based upon LAFCO's inquiries, in November of 2012 the District retained a Certified Public Accountant (Mark Cummins) to prepare audits for the "missing" years. In late 2013, Mr. Cummins completed his work, and Sativa's legal counsel provided LAFCO with copies of audits for Fiscal Years 2005-2006 through 2011-2012. In April of 2014, the District provided LAFCO with the financial audit for Fiscal Year 2012-2013.
- Annual Budgets. Based upon a request from Hogle-Ireland, Sativa provided a budget for Fiscal Year 2011-2012, which formed the basis of further inquiries from Hogle-Ireland and LAFCO. In meetings with LAFCO, District representatives conceded that this "budget" was created merely to satisfy LAFCO's inquiry, and in the normal course of operations the District does not adopt annual budgets. The first "catch-up" audit prepared by Mark Cummins (for FY 2005-2006) confirms this by noting that "[f]or the current fiscal year the district did not prepare [a] budget." (Sativa- Los Angeles County Water District, Independent Auditor's Report, Fiscal Year Ended June 30, 2006, Page 10)

Mark Cummins, the CPA who prepared audits for Sativa, noted the following:

“In addition to its primary purpose of allocating funds for District purposes, a budget is also a picture window for the public’s use in examining how their public dollars are being spent. The Sativa Budget is not detailed enough for this purpose.

“The entire Sativa budget was 2 pages. While it did include all of the District revenues and expenses, it offered virtually nothing to the public as far as information about the budget items. Moulton’s budget [the Moulton Niguel Water District, which Cummins used for comparative purposes] was 103 pages.” (District Management Review Letter, October 12t, 2013, Page 1.)

The comments by Mr. Cummins mirror the findings of LAFCO staff, who reviewed available budgets provided by Sativa representatives. The few budgets provided by Sativa representatives provide only a modicum of information compared to what LAFCO has identified in most other public agencies.

More recently, and although District staff has prepared budget reports that are lengthier, staff finds that there is relatively little additional substantive information beyond that provided in earlier budgets.

- Board-Member Compensation (Meetings). Sativa County Water District is a relatively small water district, both in terms of geography (0.28 square miles) and service connections (1,667). For Calendar Year 2011, Board-Members attended 26 Regular Meetings (bi-monthly), 4 Policy Meetings, 4 Safety Meetings, 4 Special Meetings, and 4 Planning Workshops (note that in some instances, board-members may have missed one or more of these meetings). This totals 42 “internal” meetings—nearly one per week over the course of the year—and is in addition to “outside” meetings (trade associations, conferences, seminars, and meetings with other public agencies) and an annual Christmas Bonus (see below). (Note: This was the only year (2011) for which Sativa provided the breakdown of Director compensation).

Pursuant to a resolution adopted in July of 2003, members of the Board of Directors are paid a \$150 stipend per meeting. The District’s Auditor compared the stipends for Sativa’s Board of Directors with a sample of ten similar water districts, and determined the following:

- “Sativa’s Directors attend 3.1 times as many meetings as the two most comparable districts by size in the survey.

- "Sativa's Directors are paid a 50% higher stipend than the directors of the two most comparable districts by size in the survey.
- "Sativa's Directors are paid 12% above the average directors stipend of all districts surveyed, most of which are far larger than Sativa." (Forensic Audit – Final Report of Findings, October 1, 2013, Pages 7).

The District also has a policy restricting members of the Director to reimbursement "with a budget not to exceed \$2,000 per year," and, further, that Directors can be reimbursed for a maximum of six meetings in any one month. Information provided by Sativa's legal counsel suggests that a Director may have exceeded the annual reimbursement limit by \$1,277 in Calendar Year 2011; in that same year, it appears that no director was reimbursed for more than six meetings in any one month. Staff cautions that the lack of detail provided means that it cannot be determined, definitely, whether a Director violated the policy.

On April 8, 2014, the Board of Directors adopted a policy for ad hoc committees (identified as "Safety Committee, Planning Meeting, Policy Workshop, and Ad Hoc Special Meetings") to "waive receipt of a stipend for special meetings held during this time." (Memo from Sativa Los Angeles County Water District to LAFCO, Subject: Board Members Compensation, dated April 9, 2014). Staff notes that this action is very recent and comes after the issue was raised repeatedly by LAFCO and Sativa's auditor.

Despite the issues raised by LAFCO and Mr. Cummins, staff notes that, in the most recent budget (FY 2012-2013), the budgeted for board of directors stipends for board meetings (\$19,500) and meetings/seminars (\$10,500) is unchanged from the previous year (FY 2011-2012).

- Christmas Bonuses to the Board of Directors. According to the records Sativa provided, each Board-Member was provided a \$1,500 Christmas bonus on November 29, 2011. In a meeting at LAFCO on November 19, 2011, Board Chair Johnny Johnson indicated that the District had been providing some Board-Members with the annual Christmas bonus since 1991. For Fiscal Years 2005-2012, Sativa's auditor identified the total Christmas bonuses paid to directors as follows:

Johnny Johnson:	\$9,100
Ruben Hernandez:	\$9,100
Elizabeth Hicks:	\$9,100
Mamie Franklin:	\$9,100
April McCall:	\$7,100
Anita Emery:	\$1,000

Sativa's auditor further reported that "Mrs. Johnson [Sativa's Office Manager] said they [directors] have received such bonuses for the past 20 years." (Forensic Audit – Final Report of Findings, October 1, 2013, Page 5). As best as staff could tell, the origin of the Christmas bonuses for directors and staff goes back to a policy adopted by the Board in 1993 (Resolution 011-930). Since Mr. Cummins only reviewed Fiscal Years 2005—2012, and combined with statements by Mrs. Johnson and other Sativa representatives, staff notes that the actual amount of Christmas bonuses paid to members of the Board of Directors is unknown.

Once staff raised the Christmas bonus issue with Sativa representatives, and upon recommendation of Sativa's former legal counsel, several directors executed promissory notes in early 2013 and established repayment plans to pay back the amount of the Christmas bonuses for the years 2005-2012. Mr. Cummin's forensic audit notes that "Director Johnson and McCall are in compliance with the terms of the promissory notes, while former Director Hernandez and Director Hicks are behind on the payments" in the amount of \$750 and \$250, respectively." (Forensic Audit – Final Report of Findings, October 1, 2013, Pages 5-6).

In a memorandum to LAFCO on April 9, 2014, Sativa noted that "[t]o date, Director Johnson is current on his repayment of funds." The memorandum goes on to state:

"[F]ormer Directors Hernandez, Hicks and McCall are all delinquent in their payments. Legal counsel, Anthony Willoughby, referred this matter to the local District Attorney's office for criminal prosecution. The communication between legal counsel and the District Attorney's office is a confidential communication; however, without waiving any privileges, all individuals who have received illegal bonuses have been so referred. Additionally, at the Board of Directors meeting held on March 25, 2014, the District approved the allowance of legal counsel to pursue the reimbursement within the civil court.

"The Board of Directors has also adopted a policy that no future bonus payments will be made to Directors." (Memo from Sativa Los Angeles County Water District to LAFCO, Subject: Christmas Bonuses to Board of Directors, dated April 9, 2014).

Based upon a review of the records and information supplied to LAFCO, there is no indication Board Member and current District Chairman Luis Landeros received any Christmas bonus payments.

- Employment of Relatives. Mr. Johnny Johnson has served on the District's Board of Directors since 1981; for much of that period, he also served as the District's Board President. In 1986, he married Theresa Johnson, who is the District's Office Manager. Mrs. Johnson's adult daughter from an earlier relationship is also an employee of the District. Staff understands that the District has adopted a policy on

this issue—Policy 3090—which “allows for employment of relatives without requiring an outside search for the best available candidate.” (Forensic Audit – Final Report of Findings, October 1, 2013, Pages 12). District representatives cited a “legal opinion” which allowed the employment of relatives so long as the Director recuses himself or herself from votes involving relatives; despite multiple requests, no such written legal opinion was provided to LAFCO. As noted by the District’s auditor, “there are three family members in influential roles within Sativa, namely the [former] Chairman of the Board [Johnny Johnson], the Office Manager, and the Administrative Manager. This has led to suspicion that this could put Sativa’s assets at risk should there be collusion between or among related parties in relation to Sativa’s finances.” (Forensic Audit – Final Report of Findings, October 1, 2013, Page 2).

In documents prepared for the District, County of Los Angeles representatives noted that the District employed relatives of a Director (Sativa – Los Angeles County Water District, Independent Auditor’s Report, Fiscal Years Ended June 20, 2004, 2003, and 2002, issued August 3, 2005, prepared by the Los Angeles County Department of Auditor-Controller, Page 22). It is important to note that the County Auditor-Controller first raised this issue in writing in 2005.

As noted by the District’s former legal counsel, “[b]ecause Director Johnson has a community property in his wife’s salary, her employment as the District’s Office Manager would constitute such a prohibited conflict of interest if no exception applies and she would not be eligible for employment at the District.” (Letter from Jim Ciampa to Mark Cummins, December 17, 2013, Page 2). Staff was unable to ascertain whether Director Johnson signed checks for his spouse.

Some of the potential conflict issues have been addressed relatively recently. Director Johnson is no longer the Chair of Sativa’s Board of Directors, as Director Landeros succeeded him in late 2013 and continues to serve as the Chair. With respect to Mrs. Johnson, the Office Manager, a memorandum from Sativa to LAFCO states the following:

“On March 25, 2013 [sic, should be 2014], the Board of Directors eliminated the Office Manager position at the District, which was held by Mrs. Johnson. Mrs. Johnson was informed of the elimination of her position and was provided with a two week notice. As such, there are no longer any conflict of interest issues between Director Johnson and Mrs. Johnson.” (Memo from Sativa Los Angeles County Water District to LAFCO, Subject: Conflict of [Interest] Issues, dated April 9, 2014).

Staff notes that the change relative to Mrs. Johnson comes nearly a decade after the County’s Auditor-Controller first raised the issue, and only after the issue was

repeatedly brought to the District's attention by LAFCO, the District's former legal counsel, the District's current legal counsel, and the District's auditor.

- Extraordinary Payments to Staff. The Office Manager was paid a total of \$2,717.90 for preparing an emergency assessment manual and a procedures manual for the District; a substantial portion of this was for copying charges of \$130 each for 21 manuals. As noted by the auditor, "We view these items as being required in the ordinary course of Sativa's business, which could either have been outsourced less expensively or should have been covered under Mrs. Johnson's obligations as Office Manager." (Forensic Audit – Final Report of Findings, October 1, 2013, Page 6).

Staff was formerly compensated with a \$150/day "stipend" for meetings that were more than 50 miles from the District's office (totaling \$6,900 for the years 2005-2012) as well as \$100 "bereavement checks" (totaling \$1,000 for the years 2005-2012) when relatives passed away. In a memorandum to LAFCO addressing staff payments, Sativa noted "At the April 8, 2014 board meeting, the Board of Directors for the Sativa Los Angeles County Water District adopted a policy prohibiting \$150/day stipends for meetings that are located more than 50 miles from the District." (Memo from Sativa Los Angeles County Water District to LAFCO, Subject: Extraordinary Payments to Staff, dated April 9, 2014).

Pursuant to Resolution Number 7-12003, adopted by the Board of Directors on July 1, 2003, the Recording Secretary (Ms. Johnson) was paid \$100 "for the purpose of recording and transcribing the minutes and orders of business for said meeting" for each board of directors meeting. LAFCO staff and the District's auditors separately noted that such duties would, in most public agencies, be a component of staff's responsibilities, and not something for which staff would receive additional compensation.

- Sale of District Automobile to Staff. In 2004, the District advertised the sale of an existing vehicle and solicited bids. The Board of Directors, after a closed session meeting, voted 3-1 with Director Johnson abstaining to sell the vehicle to District employee Ms. Williams for an amount less than three bids received from members of the public through an on-line service. The auditor went on to recommend that the District "adopt an Asset Disposal policy that requires solicitation of a minimum of three outside, arms-length bidders when selling District property with a book value exceeding \$500 in value." (Forensic Audit – Final Report of Findings, October 1, 2013, Pages 9).
- Sole-Source Contract. The District hired a construction company for the construction of a storage garage, and paid out \$130,816 on a contract valued at 191,187.50. As noted by the District's auditor, "Despite the large size of this contract, it was not bid out for tender. As custodians of the District's assets, the Board of Directors have a

high duty of care to ensure that major investments of the District's funds are made on a transparent and arms-length basis." (Forensic Audit – Final Report of Findings, October 1, 2013, Pages 9). The year of the contract is not known to LAFCO it was not stated in the Forensic Audit.

On December 3, 2013, the Board of Directors adopted a policy relative to purchasing, essentially requiring bids for work in excess of \$2,500, and requiring approval by the Board of Directors. (Memo from Sativa Los Angeles County Water District to LAFCO, Subject: Sole Source Contracts, dated April 9, 2014).

- Missing Payroll Deductions. The District's Auditor identified more than \$12,000 in payroll deductions that were not made for stipends paid to District employees for Social Security, Medicare, and State Disability Insurance for "most of the period under review," which would be Fiscal Years 2008-2009 through 2011-2012. Roughly 50% of the payroll deductions are owed by employees, and 50% are owed by the District. (Forensic Audit – Final Report of Findings, October 1, 2013, Page 11). According to information provided recently by Sativa representatives, efforts are underway to pay for the missing payroll deductions, and the amount will be re-paid by the end of 2014.
- Accountability for Cash Receipts. Staff shared the sentiments expressed by the District's auditor, that District "staff with access to assets should not perform record-keeping functions related to those assets." The auditor went on to note that "[t]here has been no change in how the District collects and records its cash payments." (Forensic Audit – Final Report of Findings, October 1, 2013, Page 19). Staff notes that these issues were raised as early as 2005, (Sativa – Los Angeles County Water District, Independent Auditor's Report, Fiscal Years Ended June 20, 2004, 2003, and 2002, issued August 3, 2005, prepared by the Los Angeles County Department of Auditor-Controller, Page 22)

In a recent memorandum to LAFCO staff, Sativa representatives noted that the "District has separated the duties of individuals with access to cash receipts." (Memo from Sativa Los Angeles County Water District to LAFCO, Subject: Accountability for Cash Receipts., dated April 9, 2014).

- Credit Card Expenses and Documentation. The District's auditor identified some missing credit card statements, a lack of independent review of credit card spending, and a high percentage of "items unsupported by invoice [that] ranged from 14% (2005) to 43% (2007)" and goes on to note that "it is impossible to confirm whether or not charges were for business purposes" given the lack of documentation. (Forensic Audit – Final Report of Findings, October 1, 2013, Pages 4).

The lack of documentation is particularly troubling given that the District has an existing policy (Sativa Credit Card Policy, Policy Number 5030.02) which identifies as a “credit card violation” the “[f]ailure to turn in packing slips, receipts or other back up documentation to the SATIVA bookkeeper within 30 days of the purchase.” Said policy goes on to describe how the District’s treasurer must review and approve “periodic statements” and “[t]he bookkeeper must keep statement date and proof of reconciliation, including receipts and packing slips.”

According to information recently provided to LAFCO, the District has implemented measures to address these practices.

- Telephone Expenses. In the Calendar Year 2011 Budget provided by Sativa, LAFCO staff noted a telephone expense of \$14,197.52, which appeared to be a relatively large number for a small water district with 6 employees (the figure, for example, is substantially higher than what LAFCO pays for an office of 7 employees). In subsequent meetings, Sativa representatives indicated that the figure included Internet access as well as cell phones for all Board-Members and several employees. As noted by the District’s Auditor, “all Directors have cell phones with Sprint/Nextel,” all of which have “unlimited minutes plans fully paid for by Sativa, when they are not involved in the daily operation of Sativa’s business.” The auditor also noted “relatively high phone usage by Director Hicks and high data/Internet usage by Director Johnson, [and District employees] Ms. Williams, Mr. Dredd and Mr. Udeh.” (Forensic Audit – Final Report of Findings, October 1, 2013, Pages 9). In the 2012-2013 Budget adopted by the Board of Directors on February 26, 2013), the “Telephone/Communication” account is budget at \$18,272.00, which appears to remain relatively high for a small office.
- Audit Expenses. In the Calendar Year 2011 Budget provided by Sativa, LAFCO staff noted an expense of \$505.96 for a year (“2009-2010 Actual”) in which no audit had been prepared. In subsequent meetings, Sativa representatives indicated that the figure was incorrectly described, and was not an audit expense, but a retirement plan contribution.

Operations and Long-Term Planning Issues. Issues associated with the District’s operations and long-term planning include the following:

- Lack of Water Meters. Sativa County Water District does not have water meters for its customers. Based upon its independent research, staff has concluded that this is relatively uncommon for water districts in developed, urbanized areas—most districts without meters are in rural, remote, and/or agricultural areas that are sparsely populated. The lack of water meters makes it impossible for Sativa to implement a system of “tiered” water rates or implement water conservation measures that are

common in many water districts. This issue was raised in the MSR which LAFCO prepared and the Commission adopted on February 22, 2006. The absence of water meters presents several challenges:

- Impairs the District's ability to secure Federal and State water grants. To its credit, District representative indicate that they have applied for such grants, but further indicate that a consistent reason these grant applications have been rejected is the lack of water meters.
- Renders the District's water conservation efforts ineffective.
- Eliminates any incentive for residents to conserve water.

Again, LAFCO raised this issue in the November 2005 MSR. Based upon the responses provided to LAFCO inquiries—including, for example, cost estimates that ranged from a low of \$200,000 to a high of \$1.2 million—it does not appear that the District is making an effort to install water meters for its customers at any point in the foreseeable future.

Although State law changed in 1992 (AB 2672) to require the installation of water meters for districts with 3,000 or more connections; staff and legal counsel concur with the District's legal counsel that this law does not require the District to install water meters (the District has roughly 1,600 service connections). While not mandated, there is no question that installation of water meters is critical to the long-term operation of the District. It is also clear, from conversations with Sativa representatives, that the District's ability to qualify for many Federal and State grants is significantly impaired by the fact that the District does not have water meters.

Sativa recently applied for a \$1.2 million grant from the California Department of Public Health to install water meters. In November of 2013, the State notified Sativa that it had met the standards for the "pre-application" phase of the program, and Sativa is now engaged in the formal application process. It is unclear whether Sativa will receive this grant funding and, additionally, how long the process will take.

- Location of Pipelines. Sativa County Water District was formed in 1938. The District has installed water mains and connections to its customers over several decades since then. Most of these underground pipes were installed at the rear of properties, rather than in the public rights-of-way (streets) fronting private properties that is customary. In some instances, and as reported by Sativa representatives, property-owners have built homes, garages, and other accessory structures over these water lines, presenting obvious challenges relative to repairs and replacement. The location of water lines could prevent or delay Sativa staff from accessing lines in need of repair or inspection, could inconvenience residents, and, in extreme cases, might necessitate the relocation of water lines. In a meeting with LAFCO staff (February

12, 2013), Satava representatives indicated that they “didn’t know” whether the District had rights-of-way and easements for the District’s water lines on private properties. While District representatives noted recently that “most” of the pipelines are in public rights-of-way, such as streets and alleyways, they concur that the District has not maintained sufficient documentation concerning ownership and easement rights.

In the 2005 MSR, LAFCO staff noted that “[t]he District needs to locate water mains to streets and the front of properties to avoid structures being built over existing service lines.”

In a recent memorandum to LAFCO staff, Satava noted the following:

“The water lines that traverse private property . . . have been investigated and have been determined to belong to the County of Los Angeles. Therefore, no easement documents are required.” (Memo from Satava Los Angeles County Water District to LAFCO, Subject: Location of Water Lines, dated April 9, 2014).

Staff considers this Satava statement to be unclear and unsubstantiated. Satava provided no documentation concerning the ownership or easement interests in said rights-of-way by the County and the District. The same memorandum then goes on to state that the District “plans on relocating the water lines into the public “Right-of-Way,” and that the District “will look for funding through the re-allocation of funds within its fiscal year budget proposal,” and that the District “also plans on applying for state grants and lobbying in Sacramento for funds available to low income communities such as the Satava Water District.” (Memo from Satava Los Angeles County Water District to LAFCO, Subject: Location of Water Lines dated April 9, 2014).

A 2013 Water Master Plan prepared by CivilTec, a consultant to Satava, and recently sent to LAFCO in April of 2014, identified nearly \$4 million in costs associated with relocating water lines from the rear of properties into the public streets (rights-of-way) in front of properties. (Final Draft, Satava Los Angeles County Water District 2013 Water Master Plan, CivilTec Engineering, March 2014, Page ES-3). At this time the District does not have the funding for such an expensive undertaking.

- Emergency Preparedness. In 2007, the District installed an emergency connection (a 4” one-way water line) to the Compton Water Division, to be utilized in the event that Satava’s had an interruption of its water supply. As far as LAFCO staff is aware, the emergency connection has never been utilized. In recent conversations, District representatives noted that there is no “regulating valve” on this connection, which

means that there is no means of measuring the amount of water that would come through this connection.

The District does not have adequate reserves should they be needed in case of an emergency, such as well contamination, tank failure, water line rupture, or natural disaster.

Mark Cummins' audit report identified the issue of emergency preparedness and raised the following questions:

“What is the source of water for the emergency connection to Compton?”

“Has the emergency connection ever been tested?”

“How often are the emergency generators tested, if at all?” (District Management Review Letter, October 1st, 2013, Page 3.)

Staff was unable to locate District responses to these questions in any of the documentation provided.

- Water Rates. As noted on Table 7-1 in the MSR (page 35), Sativa's monthly water rate for a typical single-family home is \$55 per month, the same amount indicated on Sativa's website. This amount is substantially less than the rate charged by surrounding water agencies, which range from roughly \$88-\$90/month (Golden State Water Company and Park Water Company, two investor-owned utilities) to \$130/month (City of Compton Municipal Water Department). Because most of the District's territory qualifies as a Disadvantaged Unincorporated Community (“DUC”), in which the average household income is 80 percent or less than the statewide median household income (\$46,662.40) the issue of water rates is sensitive. However, the combination of rates lower than surrounding water agencies, coupled with the District's failure to undertake and comprehensive long-term planning efforts, is of concern. Over the next few decades, the District will undoubtedly encounter large one-time expenses, as do all water districts with an aging infrastructure. Many of these expenses are known, such as drilling new water wells and the installation of water meters. But there are potentially unforeseeable expense associated with unexpected well failures, emergency repairs to aging water lines, increased cost of purchased water, and increased treatment costs due to a changing regulatory climate. The District is ill-prepared for any of these eventualities, and as difficult as periodic rate increases may be for this community, they could be easier to accommodate than one or more sudden, large rate increase to address large, un-budgeted expense.

Mark Cummins noted the following:

“Of all the management deficiencies previously described in the [LAFCO Draft] MSR, the most harmful and egregious action of the Satava Board as it pertains to the public’s interest is the decision to adopt a ‘Pay as you go’ system for setting customer’s water rates. This system includes only the District’s budgeted operating costs with very limited reserves, and does not include any provision for Asset Management techniques through Replacement and Refurbishment funds (R&R). Such an omission is virtually unheard of in today’s publicly-owned water districts.

“The District’s ‘Pay as you go’ system makes absolutely no adequate provisions for replacing or refurbishing facilities. A good example is the necessity to replace the District’s Well #4. The District closed that well in 2009 because it had traces of manganese and iron that exceeded water quality levels. Because there is no R&R, the District has been unable to replace the well. They have tried for the last three years to get a grant for the project, to no avail. The District applied for a \$950,000 grant to replace the well from Los Angeles County from money the County received in 2009 from the American Recovery and Reinvestment Act, but were denied as their project was not deemed to be a top priority project.

“A ‘Pay as you go’ system is a great public relations tool, as it artificially lowers water rates and keeps customers happy—until things start wearing out.” (District Management Review Letter, October 1st, 2013, Pages 1-2.)

In a recent memorandum to LAFCO staff, Satava noted that “The District has not increased the water rates in approximately 5 years. As part of the FY 2013-2014 budget review, the District is considering a \$5 (9 percent) increase of the current water rates.” (Memo from Satava Los Angeles County Water District to LAFCO, Subject: Raising Funds for Capital Improvements, dated April 9, 2014).

- No Significant Water Conservation Measures. According to information presented to Hogle-Ireland (interview of May 31, 2012), Satava representatives “do not have any conservation programs.” The notes reflect that the District “does not have regulations regarding water usage that they enforce such as . . . filling/re-filling of swimming pools, washing cars, watering landscaping.” The notes do reflect that the District “distribute[s] water conservation related handout and conduct water use surveys twice per year,” an answer consistent with information provided to LAFCO in response to our survey questionnaire. As far back as LAFCO’s 2005 MSR, it was noted that “[t]he District does not provide water conservation services.”
- Long-Term Planning. Based upon conversations with District representatives, it appears that the District has made little or no effort to perform any long-term planning. There is no Capital Improvement Plan, no documented “sinking fund” for

anticipated infrastructure improvements, and no quantifiable reserves nor their equivalent. As noted by the District's auditor, "no reserve funds have been set up in the chart of accounts." (Forensic Audit – Final Report of Findings, October 1, 2013, Page 7). There is no long-term plan for the replacement of critical infrastructure (water tanks, pumps, and water lines) in a district with aging infrastructure. Although the District hired a qualified civil engineering firm (Psomas & Associates) several years ago to examine the condition of the District's water lines, it does not appear to have resulted in any further action to maintain, improve, or replace District infrastructure. (Despite staff's repeated requests, the District failed to provide a copy of the Psomas report).

For nearly two years, District representatives have, on multiple occasions, referred to a "master plan" that was being developed by an outside consultant (CivilTec Engineering). Although LAFCO staff has been in constant communication with District representatives for the last two years, such a document was not finalized nor made available. At a meeting on March 24, 2014, Sativa representatives were only aware of a draft report with comments from the District's consulting engineer from several months earlier.

On April 9, 2014, a copy of the CivilTec report was finally provided to LAFCO. The document, identified as a "Final Draft," identifies multiple deficiencies in Sativa's system, including:

- "No independent fire storage or emergency storage." (Page 5-1);
- Actual capacity of fire flow of "413 gpm [gallons per minute] to 1,164 gpm at 46 hydrant locations" when the "current requirement" is "fire flow of 1,250 gpm at each hydrant location." (Page 8-41); and
- Actual capacity of "zero" pumping capacity when the "current requirement" is "2,049 gpm" (Page 8-41).

The report estimates improvement costs that total approximately \$10.1 million.

Despite the delays in securing the report, staff views the release of the report as positive. The CivilTec report is the first comprehensive examination of Sativa's system to be prepared in years, if not decades, and it lays out a clear, comprehensive, and thoughtful approach to making system improvements. Having said that, staff remains concerned about Sativa's ability to finance these improvements, not to mention the fact that such improvements will take years, if not decades, to implement.

- Reserves. In several meetings, District representatives constantly referred to the amount of cash on hand (deposited in the District's bank account) and its investments

with the State of California Local Agency Investment Fund ("LAIF") as "reserves." District representatives also noted the "growth" in the State investment fund as an example of sound fiscal stewardship of District assets. The use of the word "reserves" mis-characterizes the nature of these funds, as they are, in essence, on-going funds of the District.

- District-Owned Vehicles. The District is relatively small, both in terms of geography (0.28 square miles) and service connections (1,667). The District owns and maintains three vehicles, two of which are trucks, utilized by field employees, as well as a van, utilized by office staff. As noted by the District's auditor, "[t]here is no system for recording who is using Sativa's vehicles, what they are used for, when, and the mileage covered during each use." The auditor further noted "unexpected high usage patterns in the early years, and very low usage in the last 16 months or so, suggesting the possibility of an ongoing pattern of private usage until the last 16 months. The van goes home overnight and on weekends with the Administration Manager (Ms. Williams), who was unable to adequately explain these unusual variances." (Forensic Audit – Final Report of Findings, October 1, 2013, Pages 8).
- General Manager. Among other requirements, state law requires that county water districts "appoint a general manager." For years, the District operated without a general manager; based upon interviews with Sativa representatives, the last general manager left the employ of the district in 2006. Since then, according to statements he provided, Director Johnny Johnson served in the capacity of acting general manager of the district until relatively recently. This service by Director Johnson is prohibited by state law governing county water districts, which states that "[a] director shall not be the general manager, secretary, treasurer, or auditor."

In mid 2013, and believed to be in response to questions from LAFCO, the District retained John Mundy, the retired general manager of the Las Virgenes Municipal Water District, as a consultant. According to Mr. Mundy, his service to Sativa is "winding down" and is expected to conclude in mid-2014.

In early 2014, the District entered into a contract with Romejan, Inc, a consulting firm, under which Ed Castaneda is serving as Sativa's Interim General Manager. Staff notes that Romejan's contract is short-term in nature and was only recently executed by Sativa.

Miscellaneous/Transparency Issues. Miscellaneous and transparency issues include the following:

- Website: After multiple inquiries from Hogle-Ireland and LAFCO about the lack of a District website, in November of 2012 the District finally created a website.

Although this is a step in the right direction for a public agency, staff notes the following deficiencies in the website:

- There is no map of the District's service territory.
- There is no calendar of Board Meetings for the current calendar year or fiscal year.
- There is no agenda (nor staff reports, draft resolutions, and back-up materials) for past or upcoming Board Meetings (in a letter dated February 4, 2013, the District's former legal counsel stated that "District staff will immediately begin posting agendas and will continue to do so").
- There are no copies of policies adopted by the Board of Directors.
- There are no copies of financial audits.
- There is relatively little information provided in Spanish translation. Although many of the District's residents are Spanish-speaking, only one small section of the website ("2008 Consumer Confidence Report) is available in English and in Spanish.
- As a result of elections in November in 2013, the composition of the Board's membership and the assignment of Board officers changed. As of mid-April of 2014, the website did not accurately reflect the current Board-members or Board officers.

Most, if not all of these features, can be found on the websites for other water districts.

On April 9, 2014, Sativa representatives provided a memorandum from a consultant identifying a proposed website for the District, to be modeled after the website of the Palmdale Water District. The memorandum provides no clear timeline/schedule of when the website changes will be implemented and available to the public. Sativa representatives have reported to LAFCO on multiple occasions about "progress" on its website with various consultants for the last two years without completing or maintaining a current website.

- Computer Systems. According to Sativa representatives, the District has four (4) computers, which are not networked to each other (the District does not have a server). The District's Auditor recommended that the District install a computerized accounting program (Forensic Audit – Final Report of Findings, October 1, 2013, Page 15). The lack of rudimentary computer hardware and software presents multiple challenges relative to documentation, management, and transparency.

- Published Budgets. The budget adopted by the Board of Directors in early 2013 is the first adopted by the District in more than a decade. The budget is not available on the District's website.
- Audits. Although the District has retained a CPA to prepare audits, copies of these audits are not available on the District's website.
- Threatened Litigation. In a letter dated September 13, 2012, following receipt of the Draft MSR and meeting with Hogle-Ireland and LAFCO staff, and described as "Response to Municipal Services Review," the District "Board of Directors" threatened to sue LAFCO, citing a "so called hostile take-over attributed to LAFCO and the MSR process (copy attached as Exhibit "E"). In numerous subsequent communications, this letter was not mentioned by the District, and District representatives indicated that they did not provide a copy to the District's new counsel.

In fairness to the District, it should be noted that the District's approach to LAFCO has moderated significantly since the issuance of the letter in September of 2012. Staff attributes this change to continued communication with LAFCO staff, District legal counsel's advice (both former counsel and current counsel), and changes on the composition and officers of the Board of Directors.

Staff credits the District's board for following through on the hiring of a Certified Public Accountant (Mark Cummins) to prepare a forensic audit, which was completed in October of 2013 (a copy of the forensic audit as Exhibit "D"). In the conclusion to the forensic audit, Mr. Cummins stated the following:

"The findings in this forensic report represent significant deficiencies in internal controls, proper accounting documentation, and appropriate Board policy. Significantly, our audit did not note any fraud or embezzlement in the course of our audit. Taken as a whole, the above areas are serious, but all can be resolved with proper attention and management by the Board." (Forensic Audit, Page 15)

As noted herein, many of the concerns in this report were addressed raised by LAFCO in the previous MSR prepared by staff in 2005 and adopted by the Commission in 2006. Other than some recent activity—the result of repeated inquiries by Hogle-Ireland, LAFCO staff, and the District's auditors over the past several months—it appears that the District has made very little effort to address many of these concerns. Further, other sources, such as the Los Angeles County Auditor-Controller's Office, raised some of these issues as far back as 2004.

California Environmental Quality Act (CEQA)

MSRs are feasibility and planning studies for possible future actions that have not been approved, adopted, or funded. The preparation and adoption of an MSR is statutorily exempt from the provisions of the California Environmental Quality Act (CEQA) pursuant to State CEQA Guidelines Section 15262.

As set forth in State CEQA Guidelines section 15061, approval of the SOI Update is not subject to the California Environmental Quality Act (CEQA) because it can be seen with certainty that there is no possibility that the Sphere of Influence Update will have a significant effect on the environment. Additionally, in that the consultant and staff are recommending that the Commission adopt an SOI for the Satava County Water District that is less than the existing SOI, these recommendations are not a project for purposes of CEQA because they are organizational activities of governments with no direct nor indirect effects on the physical environment, pursuant to Section 15378 of the State CEQA Guidelines.

Public Hearing Notice

Pursuant to the requirements of Government Code Sections 56427, the public hearing notice for the MSR and SOI Update was published on April 4, 2014, in the Daily Commerce. A copy of the public hearing notice was sent—both via e-mail and U.S. mail—on April 7, 2014, to representatives of the Satava County Water District, Central Basin Municipal Water District, City of Compton, Golden State Water Company, Los Angeles County Supervisor Mark Ridley-Thomas, and Park Water Company.

SOI Recommendation:

In terms of the District's current SOI Update determination, staff could recommend any of the following options:

- Consolidation with the Central Basin Municipal Water District (CBMWD). This was the Consultant's recommendation in the Draft MSR in August, 2012. In the event of a consolidation, and as the largest water agency in the region, CBMWD could summon considerable expertise, staffing, and resources. But because CBMWD is a wholesaler, not a retailer, it has no history of providing retail water service to individual customers (with 2-3 limited exceptions). The recent turnover amongst CBMWD's board of directors and staff raises additional concerns, as do other issues involving CBMWD's board, staff, outside consultants, and local elected officials.
- Consolidation with the City of Compton Water Division. The City of Compton operates a municipally-owned utility (MOU) that provides water service to residents and business-owners within the City of Compton. Staff notes that the City of Compton MSR, adopted

by the Commission on November 13, 2013, identified several concerns about on-going fiscal challenges facing the City of Compton; for this reason, staff has concerns about Compton taking on additional challenges within the context of existing budgetary issues. Additionally, a consolidation would result in an outcome whereby Satava customers—who, with limited exceptions, are not residents of the City of Compton—would have recourse on these issues only to a city council for whom they do not vote.

- Transfer of Retail Water Responsibilities to Golden State Water Company or Park Water Company. As investor-owned utilities (IOUs), both Golden State Water Company and Park Water Company are responsive to shareholders. By definition, the management of an IOU has a fiduciary duty to its board and shareholders to maximize profits, a duty which may or may not be compatible with what is best for Satava's existing customers. Additionally, such a transfer would deprive Satava customers of an elected board of directors.
- Adoption of a Zero Sphere of Influence (Zero SOI). The Commission could adopt a Zero SOI, a designation which includes no territory. This was the original recommendation in 2005 when this District was last reviewed. A Zero SOI assumes that the public responsibility and function of the agency should ultimately be re-assigned to another agency or alternate service provider; this could occur through a consolidation, dissolution, or other mechanism. Adoption of a Zero SOI precludes the District from annexing territory. Adoption of a Zero SOI signals, to other agencies and the public, that LAFCO has determined that the District is an under-performing public agency.

This would not be the first time that the Commission has adopted a Zero SOI. In 2005, the Commission adopted a Zero SOI for the Huntington Municipal Water District. The Commission dissolved the Huntington Municipal Water District in 2013.

- Adoption of a Coterminous Sphere of Influence (Coterminous SOI). The District currently has a Coterminous SOI, wherein the boundaries of the District and its SOI are the same. Adoption of a Coterminous SOI represents a public determination by the Commission that the District is able to provide adequate service to its customers over the long-term.

Staff has concerns about most of the above-referenced options. Although State law empowers the Commission to initiate a consolidation of the District with another public agency, staff cautions that such actions are subject to protest by landowners and registered voters; the outcome of protest, especially in such a small geographic area, is unpredictable. Transfer to a private water company would involve removing management of retail water service out of the public realm—a county water district—and placing it in the private realm—in an IOU. Staff considers a Commission reconfirmation of the existing Coterminous SOI to be an endorsement of the

District's management, which is contrary to the recommended determinations and current documentation.

Given the broad range of concerns about the District, as documented herein, and similar concerns found in audits prepared by Mark Cummins and the County of Los Angeles Auditor-Controller, staff is recommending that the Commission adopt a Zero SOI for the Sativa County Water District at this time.

It is staff's hope that the Zero SOI determination and the findings herein, as well as the recommendations from its own auditor and other professional consultants, will encourage the District's board of directors to implement necessary corrective plans and procedures. There is substantive guidance from these sources for the District. Additional sources of specific information and guidance are also available from statewide organizations of similar districts, such as the Association of California Water Agencies (ACWA) and the California Special Districts Association (CSDA). Because some of the issues addressed herein are beyond LAFCO's regulatory jurisdiction, the Executive Officer plans to send a copy of the Draft MSR and this staff report to the Los Angeles County District Attorney and the State Controller's Office.

The attached map and resolution reflect the staff recommendation.

Staff Recommendation:

In consideration of information gathered and evaluated for the service review of the Sativa County Water District, staff recommends that the Commission:

- 1) Open the public hearing and receive testimony on the MSR and SOI Update;
- 2) There being no further testimony, close the public hearing;
- 3) Determine that the MSR is a feasibility and planning study that is statutorily exempt from the California Environmental Quality Act (CEQA) pursuant to State CEQA Guidelines Section 15262; that the SOI Update is not subject to the California Environmental Quality Act (CEQA) because it can be seen with certainty that there is no possibility that the SOI Update will have a significant effect on the environment; and, further, that the MSR and SOI Update are organizational activities of governments with no direct nor indirect effects on the physical environment, pursuant to Section 15378 of the State CEQA Guidelines.
- 4) Adopt the attached Resolution RMD 2014-00, which includes the necessary determinations for an SOI Update pursuant to Government Code Section 56425, as well as the necessary determinations for an MSR pursuant to Government Code

Section 56430, consistent with the determinations identified in the staff report and portions of the Draft MSR and other documentation in the record;

- 5) Adopt a Zero Sphere of Influence for the Sativa County Water District, as identified in the attached map entitled "Sativa County Water District Sphere of Influence;" and
- 6) Direct the Executive Officer to mail copies of the resolution as provided in Government Code Section 56882

Attachments:

- | | |
|------------|---|
| Exhibit A: | Sativa County Water District Sphere of Influence Map |
| Exhibit B: | Hogle-Ireland, Inc. Sativa L.A. County Water District
Administrative Draft MSR August 2012 |
| Exhibit C: | November 2005 MSR (Excerpts)
November 2005 MSR Addendum of February, 2006 |
| Exhibit D: | Forensic Audit of October 1 st , 2013 by Mark Cummins, CPA |
| Exhibit E: | September 13, 2012 Letter from Sativa County Water District
Board of Directors to LAFCO |
| Exhibit F: | Sativa County Water District Progress on LAFCO Issues |