

Revised Letter

039

PROPOSED REPLY

Honorable Robert P. Ahern
Presiding Judge
Santa Clara County Superior Court
191 North First Street
San Jose, CA 95113

Dear Judge Ahern:

Subject: 1993-94 Santa Clara County Grand Jury—Review of the Santa Clara Valley Water District Response Due Under California Penal Code Section 933

The Board of Directors (Board) of the Santa Clara Valley Water District (District) welcomes the opportunity to respond to the Review of the Santa Clara Valley Water District that was included in the Final Report of the 1993-94 Santa Clara County Grand Jury.¹ California Penal Code Section 933 directs the governing body of the public agency to comment on the "findings and recommendations pertaining to matters under the control of the governing body." The Board considered these comments in open session at its meeting of August 23, 1994.

The District and its predecessors have been responsible for water resources management and flood control protection in Santa Clara County for nearly 65 years. Against the backdrop of that long history, the District's initial reaction to the Grand Jury report is one of concern that any outside agency could readily or quickly understand the complexity and breadth of the District's programs, responsibilities, and activities. It is with some perspective then, given the limited length of time that Grand Jurors had to review the District, the many other duties of the Grand Jury, and the possible preconceptions and opinions of the District held by individual Grand Jurors, that the description of the District contained in the report appears hurriedly prepared, somewhat brief and simplistic, and, as a result, somewhat inaccurate. Nevertheless, the District believes that no useful purpose would be served in a long dissertation about the mission and accomplishments of the District. Nor will we engage in a point-by-point refutation of the generalizations contained in the introduction and description of the District, except as may be necessary to clarify our comments on the findings and recommendations.

¹Our General Counsel advises that although the cover letter of June 24, 1993, from Foreman Augustus B. Bruneman references California Penal Code Section 925a as the authority for the Grand Jury's review, that section applies to cities and joint powers agencies only. The District is an independent special district established by the state legislature under Chapter 1405 of the Statutes of 1951 (West's California Water Code Appendix, Chapter 60). As an agency that receives general tax revenues and that levies voter-approved assessments under the Benefit Assessment Act of 1982 (California Government Code Section 54703, et seq.), the Grand Jury has jurisdiction under Penal Code Section 933.5 to examine the District's books and records and to investigate and report on the District's method or system of performing its duties.

FINDING NO. 1: CONSTRUCTION PLANS

The District agrees with the Grand Jury review that within the Board's current authorization, the District has scaled back a feasibility study for a 170,000-square-foot building estimated in 1990 to prospectively cost \$40.5 million to an approximate 85,000-square-foot building, which staff has estimated at a construction cost of \$14 million. The planning parameters used to size the project initially used a time horizon of 2020. The smaller building is based on estimates of District personnel needs in the year 2005. The estimates have been refined from time to time and have been scaled back by 17 percent between the preliminary estimates that were made in 1990 and the time of the Board approval of the first phase architectural contract in September 1993. Consolidation of the District work force by efficient productive functions in a healthful and adequate work environment has been the primary impetus for seeking larger quarters. Losses in productivity, employee morale, and project coordination have had immeasurable adverse impacts on District projects and programs. District personnel performing the planning, design, and operation of these projects and programs have been spread in very close quarters in more than four different locations. This is understandable given that the present headquarters was sized in 1970 for a 15-year growth period. District staff was forthcoming with the Grand Jury in providing the justification for the site evaluation report and headquarters consolidation plans. The staff of the District and its Board are constantly evaluating and reevaluating alternative plans and sites at existing buildings. However, there are tradeoffs in every alternative, and simply choosing an existing site that may have a lower initial dollar cost does not eliminate substantial refurbishing and possible productivity and environmental costs of other less desirable locations. Construction standards of many existing sites do not meet District needs for secure emergency operations and other design criteria. The District, as the Grand Jury report finds, is also mindful of marketing any existing vacant office space in ways that will reduce costs. However, it should be emphasized that the District projects less than a 10 percent vacancy in available office space in all of its facilities in 1997 when the new building is scheduled for occupancy. The District also pursues a policy of selling off unneeded assets where appropriate.

FINDING NO. 2: DEBT REFINANCING

The Grand Jury properly expresses concern over the choice of negotiated versus competitive placing of public agency debt. During its history, the District has issued very little debt, but has used both competitive and noncompetitive methods. However, the Grand Jury makes an assumption that competitive bidding would have "assured both the SCVWD Board and County taxpayers and rate payers that the financing is being conducted on the best possible terms." This is not necessarily so. The District had not marketed a debt offering since 1990, for flood control purposes and since 1986 for water supply. The latest water supply issue was a refinancing of prior debt without any substantive change in the terms and conditions on which that debt was offered to the investment community. Propositions 13 and 4 in California, and substantial amendment of the federal tax laws in 1986 and 1992, merited a complete review of the District's debt structure. In strict compliance with the State of California's guidelines for negotiated and competitive sales, the Board decided to use the services of an underwriting firm to completely restructure the method by which the District would finance long-term debt. To protect the District's and the public's interests, the District selected, by competitive proposals and third party review, a financial advisor to guide the process. The financial advisor's compensation was fixed and structured to make them impartial in the review and recommendation of the negotiated proposals of the underwriters. With the assistance of the competitively selected advisor, Public Financial Management, Incorporated (PFM), the District assembled an underwriting team of Paine Webber; Smith Barney Shearson, Incorporated; Merrill Lynch and Company; and Charles A. Bell Securities, all of whom were selected using a competitive proposal process.

Almost as important as the refinancing and securing new money for flood control projects throughout the county was the rating of District debt by Standard & Poors (S&P) and Moody's Investor Service (Moody's). The District was able to restructure its debt (removing several onerous terms), provide greater flexibility in the use of various debt instruments, and secure an upgrading of its bond rating for both water supply and flood control debt from S&P without affecting its highly regarded AA ratings from Moody's. This was at a time when the State of California was undergoing very close scrutiny and the District's traditional revenues were under severe attack.

Not only did the District reposition itself for the future through restructuring its debt and covenants while strengthening its bond rating, but PFM's independent analysis of both competitive and noncompetitive sales on June 23, 1994, when the District's debt was priced, showed that the District's placement was very competitively priced based on a comparison to a commercially available index rating of all tax exempt debt.

FINDING NO. 3: PERSONNEL

The District had 122 engineering positions in 1994, which was 22 percent of the total authorized positions. This percentage of total District work force has been at the same level since 1984. The District's 1994-95 budget includes \$40 million for salaries and benefits for employees, \$1.9 million for contract employment services, and \$17.6 million for consultants of various types.

The District constantly evaluates the wisdom of utilization of consultants and temporary employees to perform work versus doing that work with internal staff. Generally, the use of consultants, contract services, and temporary employees is based on meeting one or more of the following criteria:

- obtain services in highly specialized areas not available within internal staff and that does not require full-time or long-term attention.
- use professional and/or technical services to provide for fluctuating program levels where it is uneconomical or impractical to retain excess staff during low periods or to recruit for peak work levels.

As part of the continuous review of this issue, the District recently approved the addition of six internal staff positions to the Nonpoint Source Control Division to develop expertise in order to replace consultant services, achieve cost savings, and develop staff support for the other copermittees. (A federally required permit is administered by the District for all northern county cities and the County of Santa Clara.)

GRAND JURY RECOMMENDATIONS TO DISTRICT BOARD AND GENERAL MANAGER²

Recommendation No. 2: That they reevaluate plans for a central administration building, in view of their having currently unused space in the Crest and Blossom Hill Annexes.

The District continues to evaluate the best use of existing District facilities (none of which currently has any unused space) and the availability of alternative sites, consistent with the primary District objective of consolidating its work force in a healthful and productive work environment the size of which is based on conservatively projected staffing needs and related work space requirements.

Recommendation No. 3: That they use competitive bidding in the awarding of contracts, including contracts related to the financing or refinancing of future debt.

The District Board favors competitive bidding for debt issuance unless market volatility or other considerations strongly suggest the advisability of using a negotiated sale in conformity with the State of California guidelines for the issuance of public debt. In situations where a negotiated sale is advisable and appropriate, the District will normally retain an independent financial advisor on a competitive basis.

Recommendation No. 4: That they use current financial reserves to reduce District debt, including the portion owed to the U.S. Bureau of Reclamation (Bureau) that is not in dispute.

The District Board agrees with the Grand Jury recommendation that uncommitted or unallocated reserves should be used to reduce or avoid debt, or to provide rate relief in appropriate cases. However, the District's legal advisors are of the view that there is no debt owing to the Bureau until the parties reach a mutual agreement to create an obligation that will be due before 2007. The District is actively pursuing a negotiated resolution of the Bureau claim. Other District reserves are either restricted funds or earmarked for specific projects or programs.

²Responses to recommendations follow the numbering of the Abstract of the Grand Jury Report forwarded to the District by cover letter dated June 24, 1994. Recommendation No. 1 of the abstract is directed to the Santa Clara County Board of Supervisors and the County Executive. The District Board would not want to presume to tell the County Supervisors how to structure their process for appointing the two directors on the District Board under the direction of state law (Section 7.2 of Chapter 1405 of the Statutes of 1951, as amended, added by Chapter 205 of the Statutes of 1967; West's California Water Code Appendix, Chapter 60, Section 7.2). The process now rotates among supervisors alternately appointing one of the directors, whose four-year terms are staggered (Santa Clara County Code, Section A5-47). However, we would point out that the issue of term limits is one about which reasonable people can disagree. Further, since one appointed director represents the north county area of the territory of the former Santa Clara Valley Water Conservation District, and the other represents the south county area formerly within the South Santa Clara Valley Water Conservation District, only one supervisorial district covers the south county area. The suggestion that an appointee reside in the district of the Supervisor making an appointment will not work unless only the supervisor representing District One were to make the south county appointment. Representation at large is historical, based on the consolidation of the three water conservation districts that operated within the county at various times.

Recommendation No. 5: That they review District use of outside consultants for engineering projects.

The District continually evaluates the relative costs of adding permanent staff versus contracting for consultant services. The Board identified the study of additional permanent and less than full-time employees as a Board task to be undertaken during fiscal year 1994-95.

Recommendation No. 6: That, if they decide to build a new office building, they continue with plans for the down-sized 85,000-square-foot building.

The District Board has authorized the staff to proceed with the design of a building of approximately 85,000 to 90,000 square feet in size. The staff is not pursuing the earlier mentioned 170,000-square-foot building.

We trust that this commentary provides the court with some understanding of the District's position on the issues raised by the 1993-94 Grand Jury Report as it relates to the District. We do intend to offer future grand juries the opportunity to hear in greater detail an explanation of the District's mission, responsibilities, and programs. The District appreciates the Grand Jury's efforts and will continue to be open and receptive to reviews by the community served by the District.

Sincerely,

James J. Lenihan
Chairman/Board of Directors