



## 2005-2006 SANTA CLARA COUNTY CIVIL GRAND JURY REPORT

# SPECIAL SANITARY DISTRICTS

## Summary

The 2005-2006 Santa Clara County Civil Grand Jury (Grand Jury) inspected three special sanitary districts in Santa Clara County (County). The Grand Jury reviewed the operations and financial statements of one dependent and two independent enterprise special sanitary districts, which are all managed by Mark Thomas & Company (MTCO). The three enterprise special sanitary districts discussed in this report are:

- County Sanitary District 2-3 (SD2-3), a dependent district
- Cupertino Sanitary District (CSD), an independent district
- Burbank Sanitary District (BSD), an independent district

## Background

Oversight for dependent enterprise districts is provided by the County Board of Supervisors (BOS) or the city council, depending on whether the district is located in the unincorporated County or within a city. An independent enterprise district has an elected Board of Directors (BOD). The Grand Jury's objective was to review the operational and financial health of the three districts, including the following areas:

- Management
- Infrastructure
- Operations and maintenance
- Capital improvement plans
- Financial controls

The mission of a sanitary district is to provide sewer services to the residents and property owners residing in the district. In some cities, these services are provided by the Public Works Department of the city. In other cities, responsibility for these services is outsourced to a professional company.

A special district is a form of local government, created by a local community to meet a specific need. Inadequate tax bases and competing demands for existing taxes make it difficult for cities and counties to provide all the services their citizens desire. When residents or landowners want new services or higher levels of existing services, they can form a district to pay for and administer them. The County Local Area Formation Commission (LAFCO) exercises limited authority over special districts.

The three special sanitary districts in this report are managed by MTCO, which is a privately owned company with its own Board of Directors. MTCO has provided engineering, surveying, site development, transportation and planning for projects in the County for the last 75 years. Management, operations, and capital improvements for these districts are contracted to MTCO.

SD2-3 serves unincorporated areas in northeastern Santa Clara County. The area is generally defined by Penitencia Creek, Story Road, Carothers Road, and Capitol Avenue, including the County Fairgrounds area. This District was formed by the merger of Districts 2 and 3 in December 1977. The former District 2 was formed in May 1948 and District 3 in May 1953. MTCO has performed the managerial and engineering functions for the District since the merger.

CSD primarily serves the Cities of Cupertino and Saratoga. It also serves some unincorporated portions of Saratoga and the City of Los Altos. The District is generally defined by Homestead Road, Pierce Road, Mt. Eden Road, Lawrence Expressway, Tantau Avenue/Stevens Creek Boulevard, and St. Josephs Drive. The District was formed in 1956 and has been managed by MTCO since its inception.

BSD serves an unincorporated section of Santa Clara County, generally defined by Forest Avenue, Revey Avenue, Parkmoor Avenue, and Buena Vista Avenue. BSD was established in May of 1940 and is surrounded by the City of San Jose. The District was self governed by its Board from its inception until 1989. David Evans and Associates managed the District from 1989-2002. ABR Engineers managed it from 2002 until 2005. Subsequently, MTCO took over District management.

## **Discussion**

The Grand Jury reviewed the management, operations, and finances of the three sanitary districts. A significant amount of background documentation was requested from and supplied by MTCO, including:

- Financial data and reports
- Maintenance schedules and reports
- Budget plans

A summary of the audited financial reports for Fiscal Years 2000-2005 is included in Appendix A.

The operations performed by MTCO for the districts include:

- Operation and maintenance of pump stations and sewer lines
- Response to emergency calls

MTCO must meet environmental requirements, perform preventive maintenance, report spills to the State Water Resources Control Board (SWRCB), and expeditiously repair breakdowns.

Table 1 compares the three special districts based upon a number of different aspects.

District Comparison	Units	County District 2-3 (SD2-3)	Cupertino (CSD)	Burbank (BSD)
District Oversight		County BOS	Independently Elected BOD	Independently Elected BOD
Sewer line	miles	91	271	8
Age of infrastructure	years	40 to 50	35 to 40	50 to 60
Number of property connections		6,960	22,771	1,792
Residential Annual Fee		\$270	\$262	\$313
2004-2005 Revenue	millions	\$1.90	\$6.70	\$0.43
Operating Expense	millions	\$1.60	\$5.70	\$0.33
Capital Plan, next 5 years	millions	\$1.50	\$3.00	unavail
Total reserves	millions	\$8.70	\$15.30	\$1.64
Reserves compared to revenue		4.6X	2.3X	3.8X
Reserves per connection		\$1,250	\$672	\$915
Reserves per mile of sewer line		\$95,604	\$56,457	\$205,000
Estimated system replacement cost	millions	\$42	\$167	\$4.1
Estimated replacement cost per mile	millions	\$0.46	\$0.62	\$0.52
Year of last rate increase		FY 1995	FY 2005	FY 2005
Stoppage/Repairs in CY 2004		112	130	unavail
Stoppage/Repairs in CY2005		114	130	6
Major spills in CY 2004		3	0	unavail
Major spills in CY 2005		2	0	0
Note: FY=Fiscal Year, CY=Calendar Year, unavail=unavailable				

**Table 1: District Comparison.**

## **MTCO**

MTCO has a total of 160 employees, of whom about 16 support the operations of these three districts. The employees supporting the sanitary districts are supervised by a Vice President. MTCO serves under contract to the respective district boards.

MTCO manages the budget, project revenues, operating expenses, capital improvement plans, and maintenance plans to ensure that citizens of the districts receive the services for which they are paying. MTCO appears to follow accepted Government Accounting Standards Board (GASB) financial practices as certified by the independent auditor.

MTCO charges all the districts at 2.7 times the hourly pay rate of their employees. Each employee has to submit a log of hours charged to each district. The markup includes employee salary, personnel overhead such as benefits and taxes, and MTCO's profit of 10%. All other sewer expenses, such as charges by vendors to maintain and improve the sewer systems, supplies, and miscellaneous expenses are paid directly by each district.

When a spill of more than 1,000 gallons occurs, MTCO is responsible for sending a report electronically to the SWRCB within 24 hours. If the spill is less than 1,000 gallons but is a serious health hazard, MTCO is also required by law to inform the SWRCB within 24 hours. MTCO also has to comply with the California Health and Safety Code.

## **DISTRICT OVERSIGHT AND MANAGEMENT**

SD2-3 is a dependent special district. The BOS acts as the District's Board. The BOS must review and approve master plans, annual budgets, and capital improvement plans. MTCO submits monthly expenses, budget, and capital improvement proposals to the County Finance Agency for their review and approval. The County Finance Director then sends an approval letter to BOS for their approval prior to making payments to the creditors. Public hearings for fee increases or capital improvement plans are held to allow property owners to protest or approve rate increases.

Unlike SD2-3, CSD and BSD are independent sewer districts. Each has an elected BOD which reviews District master plans, budgets, and capital improvement plans. The Boards for CSD and BSD each meet twice a month. MTCO submits their invoices to the CSD and BSD Boards, respectively, for review and approval prior to payment. Public hearings for fee increase proposals or capital improvement plans are held to allow the property owners to protest or approve the rate increases.

MTCO spends about two days per week inspecting each district's sewer system and has a schedule to inspect the entire system by using closed-circuit TV. The complete system must be checked every five years.

## **BUDGET AND FINANCE**

The financial management provided by MTCO includes planning, budgeting operating expenses, creating capital improvement plans, and projecting rate increases. The annual financial reports are reviewed by independent auditors. The districts must adhere to GASB Accounting Guideline 34 that establishes requirements for annual financial reporting by government agencies. This guideline was developed in an attempt to make annual reports easier to understand.

The Grand Jury reviewed budgets for these districts for FYs 2000-2005. Key financial data, including year-to-year operating revenue and expenses, capital investments, assets, and reserves, are shown in Appendix A.

The Grand Jury notes that each of these districts holds substantial reserves – in the aggregate and as measured per connection and per mile of sewer line (see Table 1). The amounts vary widely among districts and there are no apparent guidelines to determine whether or not these holdings are appropriate.

Sewer service fees for the districts are collected from property taxes and deposited into a district-specific account set up by the County. Interest earned is credited to each district's account.

SD2-3 has not had a rate increase since FY 1995. BSD had rate increases in FYs 2004 and 2005, and has approved further annual increases through FY 2007. CSD had a rate increase in FY 2005 – its first increase in 10 years.

All three districts participated with San Jose in funding the shared San Jose/Santa Clara Water Pollution Control Plant with a bond. Each district pays its share of the bond principal and interest as part of its operating expense.

## **Conclusions**

County Sanitary District 2-3 is a dependent special district overseen by the Board of Supervisors. The County Controller-Treasurer's Office provides financial oversight. The BOS is responsible for final approval of rate increases, capital improvement planning, and operations.

The elected boards of the independent districts, Cupertino Sanitary District and Burbank Sanitary District, provide management oversight. The boards are responsible for final approval of rate increases, capital improvement planning, and operations.

Mark Thomas & Company, under contract, performs day-to-day operations, management, and engineering functions for all three districts.

PASSED and ADOPTED by the Santa Clara County Civil Grand Jury on this 11<sup>th</sup> day of May, 2006.

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Thomas C. Rindfleisch  
Foreperson

## References

### Documents and Data

1. Comprehensive Annual Financial Report data for FY 2001 through FY 2005 for the three subject districts.
2. Independent Auditor Reports for FY 2003 through FY 2005 for the three subject districts.
3. Burbank Sanitary District, <http://www.burbanksanitary.org/> (last visited May 2, 2006).
4. Mark Thomas and Company, <http://www.markthomas.com/> (last visited on May 2, 2006).
5. Santa Clara County Local Agency Formation Commission, <http://santaclara.lafco.ca.gov/> (last visited May 2, 2006).
6. General Accounting Standards Board <http://www.gasb.org/repmode/oview34.pdf> (last visited on May 5, 2006).

### Interviews

1. September 7, 2005, October 5, 2005, November 5, 2005, January 23, 2006, February 22, 2006, March 24, 2006, and May 5, 2006, Vice President and staff of Mark Thomas & Company.
2. February 17, 2006 and April 24, 2006, County Controller-Treasurer and staff.

## Appendix A Key Financial Data

### COUNTY SANITARY DISTRICT 2-3

<i>Financial Statement</i>	<i>FY 2000-2001</i>	<i>FY 2001-2002</i>	<i>FY 2002-2003</i>	<i>FY 2003-2004</i>	<i>FY 2004-2005</i>
1 Operating Revenue	\$1,888,352	\$1,862,944	\$1,866,803	\$1,870,033	\$1,864,300
2 Total Operating Expenses	\$977,219	\$1,891,340	\$2,308,785	\$2,564,718	\$1,590,593
3 Repairs & Maintenance Expense	\$134,759	\$63,232	\$325,800	\$373,789	\$303,928
4 Capital Investment	-	-	-	-	\$69,838
5 Net Assets, Beginning	\$8,061,407	\$8,309,900	\$8,490,236	\$8,202,394	\$7,537,929
6 Net Assets, Ending	\$8,309,900	\$8,490,236	\$8,202,394	\$7,537,929	\$7,943,842
7 Cash On Hand	\$7,891,083	\$8,839,676	\$8,366,272	\$8,624,685	\$8,667,580

### CUPERTINO SANITARY DISTRICT

<i>Financial Statement</i>	<i>FY 2000-2001</i>	<i>FY 2001-2002</i>	<i>FY 2002-2003</i>	<i>FY 2003-2004</i>	<i>FY 2004-2005</i>
1 Operating Revenue	\$5,830,636	\$6,136,286	\$5,611,222	\$5,787,710	\$6,684,490
2 Total Operating Expenses	\$4,860,060	\$4,430,177	\$6,231,682	\$6,295,420	\$5,686,017
3 Repairs & Maintenance Expense	\$829,322	\$1,057,515	\$1,500,786	\$963,595	\$1,002,972
4 Capital Investment	\$29,392	\$45,000	\$39,908	\$84,223	\$556,211
5 Net Assets, Beginning	\$38,737,040	\$39,868,965	\$40,482,676	\$39,908,752	\$39,967,269
6 Net Assets, Ending	\$39,868,965	\$40,482,676	\$39,908,753	\$39,336,247	\$40,965,742
7 Cash On Hand	\$13,721,457	\$14,202,926	\$14,534,273	\$14,462,487	\$15,289,092

### BURBANK SANITARY DISTRICT

<i>Financial Statement</i>	<i>FY 2000-2001</i>	<i>FY 2001-2002</i>	<i>FY 2002-2003</i>	<i>FY 2003-2004</i>	<i>FY 2004-2005</i>
1 Operating Revenue	\$402,472	\$559,960	\$395,011	\$432,253	\$432,847
2 Total Operating Expenses	\$237,192	\$257,129	\$299,653	\$358,060	\$329,108
3 Repairs & Maintenance Expense	\$16,385	\$12,625	\$19,766	\$22,214	\$5,000
4 Capital Investment	\$63,321	-	-	-	-
5 Net Assets, Beginning	\$1,234,128	\$1,450,522	\$2,593,412	\$2,525,900	\$2,509,480
6 Net Assets, Ending	\$1,450,522	\$1,800,924	\$2,525,900	\$2,509,480	\$2,663,942
7 Cash On Hand	\$1,591,293	\$1,547,051	\$1,485,413	\$1,446,440	\$1,641,554