

#2

May 4, 2009

**BY HAND**

Honorable Joseph Centeno, Chair, and Members of the Board of Supervisors  
County of Santa Barbara  
105 E. Anapamu Street, Suite 407  
Santa Barbara, CA 93101

Steven A. Amerikaner

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RE: Proposed Detachment from Goleta West Sanitary District  
[May 5, 2009 Meeting, Agenda Item 2 (Departmental Agenda)]



Dear Chair Centeno and Members of the Board of Supervisors:

This letter is submitted on behalf of the Goleta West Sanitary District. We respectfully oppose the staff recommendation before you, and ask that the proposed Resolution and Agreement either be rejected or revised in accordance with the following comments.

**Summary of Key Points**

1. The City of Goleta's detachment proposal is an inappropriate use of the LAFCO process to siphon money from a vital utility to the City's general fund. Everyone agrees that Goleta West's record of sewer service and street sweeping is exemplary, and thus the City's proposal is simply a money grab and not an effort to improve a vital public service.
2. This financial scheme threatens an important water quality project – the planned upgrade of the regional wastewater treatment plant. As a financial partner in that regional treatment plant, the County has a strong independent interest in ensuring that the upgrade project is not undermined.
3. This financial scheme will cause a dramatic increase in sewer charges in the Goleta Valley. Many families are already facing severe financial stress and this will increase the burden.
4. This financial scheme creates a threat to ongoing City programs. In the current economy, it is wrong to presume that the voters will quietly accept a dramatic increase in sewer charges. If they reject the increase under Prop 218, the City will find itself saddled with an expensive new utility service and no way to pay for the sewer system's capital needs other than cutting other City services.
5. The wastewater system in the Goleta Valley is a single integrated system. The five partner agencies in that system, including the County, are only as strong as the weakest link. The County has an obligation to act now and condition the tax exchange agreement in a way that avoids a situation where the City, as a new partner in the wastewater system, creates a fiscal, environmental and political nightmare for the entire Goleta Valley.
6. The County, acting on the District's behalf, is under no legal obligation to come to an agreement with the City on the terms of the property tax exchange. Before doing so, the District believes that the proposed Resolution and Agreement must be revised in four significant ways, which are described herein, in order to create an equitable division of funds for all of the District's customers.

## Background

The history of this issue is described in our earlier letter to the Board dated February 23 (copy attached). For the sake of brevity, that information will not be repeated here.

Our February 23 letter requested that the County recuse itself from the property tax exchange negotiations because of the structural conflict of interest caused by the 2001 Revenue Neutrality Agreement. The basis of that request is described in that letter.

In a March 20 letter responding to our request (copy enclosed), County Counsel disagreed with our suggestion. On April 7, Goleta West received written notice that the negotiations between the County and the City were about to commence. On April 9, Goleta West submitted to Mr. Baker a letter outlining its position on the detachment issues. On April 13, 2009, Mr. Baker and other County staff met with Goleta West representatives to discuss the upcoming negotiations, and on April 28 a second meeting was held with County and Goleta West representatives to discuss the outcome of those negotiations. The County did not accept Goleta West's request to be present at the negotiations.

Since Goleta West's April 9 letter explains the District's negotiating position in depth, it will not be repeated here. We respectfully urge the Supervisors to review that letter, a copy of which is attached.

## Outcome of the Negotiations

1. Treatment Plant Upgrade. The staff report includes Recommendation C suggesting that \$20 million be escrowed to pay for the upgrade. Goleta West commends County staff for understanding the need to ensure that the treatment plant upgrade project will not be delayed or scaled back. The negative fiscal, environmental and political impacts that would befall Goleta Valley if the \$20 million are not escrowed were detailed at length in our presentation to your Board on April 7, which was attached to the staff report.

At the same time, Goleta West believes that the staff recommendation must be significantly strengthened:

a. Real Teeth. Staff Recommendation C is merely advisory, not binding. It proposes that the County send a letter to LAFCO with a "recommendation" that a \$20 million escrow fund be established. With due respect, this is not strong enough. The City could reject the escrow fund proposal or LAFCO could ignore it and our mutual constituents in Goleta Valley would suffer the consequences. The County has an opportunity to put some real teeth behind its conviction by clearly stating that its approval of the tax exchange agreement is contingent on the City's agreement to this escrow.

Why should the County take such a strong position? First, this is a vital project which has been mandated by the Regional Board for environmental quality reasons. Ensuring that the project is completed on time is important to avoid Clean Water Act fines and penalties that could result in building moratoriums in Isla Vista and Goleta similar to the one the County faced in Orcutt over the LCSD treatment plant. Securing the funds for the upgrade also ensures ongoing protection of our ocean water. Second, the County is a partner in the treatment plant and has a compelling financial interest in ensuring that the other partners in that plant fulfill their obligations. If the detachment occurs, the City of Goleta will suddenly become a new partner in the plant. The County has a unique opportunity to ensure the City joins the wastewater business as a financially viable partner. Third, the County is considering detaching itself from the remainder of Goleta West, and as a potential successor-in-interest, the County has another compelling financial interest in ensuring that the funds the District prudently collected for the upgrade are available for that purpose.

b. Cost Overruns. Staff Recommendation C speaks to a \$20 million escrow. That amount is understandable, since the current project cost estimate is \$50 million and Goleta West's contractual share is 40.78% (= \$20,390,000). However, the project is currently in the design phase, and construction is not expected to begin for approximately ten months. It is conceivable (perhaps even likely) that the cost will go up by the time construction is completed. Goleta West believes that including a cost overrun contingency is prudent, and 10% more should be placed in escrow.

2. Future Sewer System Capital Needs. The Staff Report is silent on a crucial issue: How will the City pay for its share of future capital expenses of the sewer system it will own? Sewer systems are famously expensive to maintain, repair, expand and upgrade. To cite just one example: Goleta West recently completed construction of a new sewer main in Hollister Avenue to replace an existing main which was too small and in need of rehabilitation and repair. The project cost \$3.2 million, and was paid with property tax reserves.

If detachment occurs, the City will own or control 44 miles of sewer mains currently operated by Goleta West (including about four miles inside EMID). If the City takes the lion's share of the property taxes, and diverts that money into parks, recreation, street repair and other City services, how will the future capital needs of the sewage collection system be met?

There is one simple and unavoidable answer: **The City must raise sewer charges**. This has been established by an independent fiscal impact study recently completed for Goleta West which shows that rates in the City will more than double.

But, there is one very large fly in the ointment: Proposition 218. According to a recent California Supreme Court decision, sewer and water charge increases are subject to Prop 218, which means that the voters can block any increase in City sewer charges by a simple majority protest. It has already occurred in California (e.g., City of Dixon)

In the current economic environment, it is easy to imagine the residents of the Goleta Valley voting to protest a sudden and large sewer charge increase. If that occurs, the City will find itself owning 44 miles of sewer mains and having no money to repair them. Since the Clean Water Act and the Regional Board do not allow spills from sewer systems to remain uncorrected, the City will have no choice other than to divert money from parks, recreation, street repair and other City services.

There is a straightforward way to avoid this risk: The tax exchange agreement should provide that the City must place all future property taxes into a dedicated reserve for operations, repairs, and long-term capital needs of the sewer system, except to the extent those tax revenues are replaced by enhanced sewer service charges. The purpose of this requirement is to ensure that there are adequate funds available for future capital needs and that a failure to raise sewer service charges in the future (whether due to Prop 218 protests or other reasons) does not impair the City's ability to fund those needs.

Again, you may be asking why the County should take such a strong position. To put it simply, the wastewater collection and treatment in the Goleta Valley is part of a single interconnected system. If your Board sends a financing agreement to LAFCO that is built on an unsound foundation, it creates a risk for all five partners in the wastewater business in Goleta Valley. Additionally, as the potential successor-in-interest to the Isla Vista system, the County will be dependent on the sewer system in Goleta to transfer its waste to the treatment plant. So, if Goleta isn't properly maintaining its system because it is under-funded, the County will suffer. What is more, Goleta West believes that such a condition is sound public policy concerning property taxes, and prudent environmental policy as well.

3. The Proposed 78% Re-Allocation is Disproportionate to the Service Transfer.

The Staff Report recommends that 78% of the property taxes currently received by Goleta West be transferred to the City. Goleta West believes that this recommendation is fundamentally flawed because it fails to reflect the actual shift in sewer service responsibilities that will occur under detachment.

The proposed detachment area (including EMID) has:

- 47% of the development potential of Goleta West
- 51% of the land area of Goleta West
- 52% of the total wastewater flow from Goleta West to the regional plant
- 68% of the collection system (about 44 miles)

If the City's proposal to allocate 78% of future property taxes is accepted, Goleta West will be left with **48%** of the wastewater flow and just **22%** of the capital funds needed for the facilities that handle that flow. Goleta West's capital improvement plan cannot be sustained if its share of the property taxes is cut so significantly, and significant rate hikes in Isla Vista will be unavoidable.

Based on principles of revenue neutrality, Goleta West respectfully submits that the appropriate measure of "service responsibility" should be based on two factors: current wastewater flow and future development potential. The logic of this position is explained in Goleta West's April 9 letter (attached).

Goleta West recommends that the County impose a new condition on its approval of a tax exchange agreement. That new condition would require that the City agree to:

- (i) Reduce its proposal for a share of property taxes from 78% to 52%, and
- (ii) Pledge those property tax revenues to future capital needs of the treatment plant and the collection system.

This proposal is based on the simple fact that the detachment – if approved – will not alter the reality that the City, District and County will be inextricably dependent upon one another for the proper operation of the wastewater collection and disposal system. If the City is unable to make its payments for O&M and capital costs of the treatment plant, the other partners in that plant (including the County and Goleta West) will be required to make up the deficit. This duty is not mitigated by the ability of the County or Goleta West to sue the City to force payment. Sewer plant operations cannot be suspended while lawsuits are resolved.

**The City of Goleta's Response: Surrender or No Deal**

County staff has submitted a Supplemental Report dated May 1 concerning the City of Goleta's response to the negotiations.

The City has drawn a line in the sand. It has told the County that it will only agree to the \$20 million escrow if the County surrenders its claim to 70% of the re-allocated taxes under the Revenue Neutrality Agreement.

It is clear that the City and County have not reached a "meeting of the minds" on these important issues, and that inability to agree justifies a simple rejection of the tax exchange agreement by the Board of Supervisors.

### Summary of Recommendations

Based on the foregoing, Goleta West respectfully requests that the proposed Agreement be rejected.

If the Board does not wish to reject the Tax Exchange Agreement, we respectfully ask that the Resolution and Agreement be revised to implement the following:


1. Real Teeth. Add a contingency to approval of the Agreement: the City must agree to escrow the treatment plant money.
2. Cost Overruns. Increase the escrow by 10%.
3. Dedicated Funds for Future Capital Needs. Require that future property taxes be dedicated to pay for future capital needs, until rate increases are implemented.
4. Proportionality. Reduce the City's tax allocation from 78% to 52% of all the taxes generated in the District to reflect the actual transfer of 52% of the service responsibility.<sup>1</sup>

For your convenience, we are attaching a separate sheet with the language changes needed to implement these suggestions.

### Conclusion

Goleta West appreciates the Board's attention to these issues of importance to the Goleta Valley.

Sincerely,



Steven A. Amerikaner

Enc.: Proposed Changes to Board of Supervisors Resolution and Agreement  
February 23, 2009 Letter to Board of Supervisors from Goleta West Sanitary District  
March 20, 2009 Letter from County Counsel  
April 9, 2009 Letter to County negotiation team from Goleta West Sanitary District

cc: (with Proposed Changes only; earlier correspondence excluded)  
John Baker, Assistant CEO/Planning Director  
Goleta West Sanitary District Board of Directors  
Mark Nation, GWSD General Manager  
Robert Braitman, Executive Officer, LAFCO  
Daniel Singer, City Manager, City of Goleta

SB 504699 v1:006888.0070

<sup>1</sup> The calculation appearing on the attached sheet is explained by the fact that 52% of the taxes generated in the entire District is the same as 67% of the taxes generated in the detachment area.

# PROPOSED CHANGES TO BOARD OF SUPERVISORS AGREEMENT AND RESOLUTION

Submitted by Goleta West Sanitary District  
May 4, 2009

(changes shown with ~~strikeouts~~ and underscoring)

## AGREEMENT

### 1. ALLOCATION OF PROPERTY TAX REVENUES

Sixty-seven percent of All future *ad valorem* property taxes currently allocated to District for properties which are detached from the District through the Proceeding shall be reallocated to the City, and that allocation shall be annually adjusted to reflect the actual proportion of wastewater flows from the detachment area.

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## RESOLUTION

### SECTION 3.

The Agreement is hereby approved and authorized to be executed by the Chair, provided the City agrees to Section 4 of this Resolution.

### SECTION 4.

In order to avoid the situation where the reserves of the District are insufficient to fulfill its remaining contractual obligation to the Goleta Sanitary District for treatment plant upgrades and in recognition of the proportionate need for capital improvements outside the City, the Board of Supervisors supports the following allocation of District reserves and use of future property taxes:

- a. Property tax reserves Assets of the District in the amount of ~~\$22,500,000~~ \$20,000,000 shall be transferred to Goleta Sanitary District to be held in escrow, with any interest thereon applied to any increases in the obligation of District and City for treatment plant upgrades, such interest to be applied to future obligations of District and City in proportion to their obligations for any cost increases in the treatment plant upgrades;
- b. Any contractual obligations for treatment plant upgrades beyond the transfer of District Reserve Funds Nos. 4935 (treatment plant) and 4910 (property tax reserves) shall be allocated to City in proportion to the flow of wastewater from properties detached from the District;
- c. Remaining reserve funds which were generated by property tax payments shall be allocated to City in proportion to the assessed value of property detached from the District;
- d. Property taxes re-allocated to the City shall be placed in a dedicated reserve fund for operations (including street sweeping), maintenance, repairs, and long-term capital needs of the sewer system as shown on the District CIP, except to the extent those tax revenues are replaced by revenues generated by sewer service charges.

February 23, 2009

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**HAND DELIVERY**

The Honorable Joseph Centeno, Chair, and Members of the Board of Supervisors  
County of Santa Barbara  
105 E. Anapamu Street  
Santa Barbara, CA 93101

RE: Proposed Detachment from Goleta West Sanitary District; Property Tax Negotiations

Dear Chair Centeno and Members of the Board of Supervisors:

This letter is submitted on behalf of the Goleta West Sanitary District ("Goleta West" or "District").

On February 3, 2009, the Goleta City Council adopted a resolution authorizing its staff to submit an application to LAFCo to detach approximately 4300 parcels of land from Goleta West. The parcels are all located within the City limits. The effect of the detachment would be to shift from Goleta West to the City the responsibility for providing wastewater collection and treatment services to parcels in the detachment area. On February 4, 2009, the City of Goleta submitted its detachment application to the LAFCo Executive Officer.

The purpose of this letter is to respectfully ask the Board of Supervisors to recuse the County from negotiating a property tax exchange agreement on behalf of Goleta West because of a structural conflict of interest and to delegate that role to Goleta West.

**Background**

Goleta West currently provides wastewater collection and treatment services, as well as street sweeping, to the western end of the Goleta Valley, including a portion of the City of Goleta, Isla Vista, the Embarcadero Municipal Improvement District ("EMID"), and properties north of the City boundary. Wastewater is collected and transported by Goleta West's collection system to a treatment plant owned by the Goleta Sanitary District located near the Santa Barbara airport. Goleta West holds a contractual right to use approximately 40% of the treatment plant capacity.

Goleta West's operations are funded by a variety of means. The two major revenue sources are annual sewer fees paid by Goleta West customers (including those outside the District boundaries, like EMID property owners) and property taxes paid by the owners of properties within the District. Goleta West's residential customers pay \$14 per month, and the District collects about \$2.4 million per year in sewer fees. Those revenues are used to fund operations, maintenance and repair. Goleta West also receives about \$1.6 million per year in property taxes. Those revenues are used to fund street sweeping and are also deposited into the District's reserves to pay for capital projects.

By contrast, the neighboring Goleta Sanitary District charges its residential customers \$34 per month and collects about \$100,000 per year in property taxes. Its sewer fees are much higher than Goleta

West's fees because they are used to finance capital projects as well as daily operations and maintenance. Goleta Sanitary District does not provide street sweeping.

Goleta West has prudently managed its finances over the years. In particular, it has saved up property taxes to be used for capital maintenance of collection and treatment systems. At present, the District has about \$30 million in capital and operating reserves. Of that amount, \$20 million has been placed in restricted reserves to fund the District's share of a \$50 million project to upgrade the treatment plant to full secondary standards, a project mandated by the Regional Water Quality Control Board under state and federal clean water laws. The project is currently being designed, and construction is due to begin in 2011. It is likely that the project will be more expensive by the time construction begins. The balance of the reserves has been earmarked for other capital projects, including improvements to the Devereux Creek line intended to prevent sewage spills in a riparian habitat.

Goleta West is committed to both efficient utility service and environmental protection. Its operations are lean and efficient, and it works hard to maintain sufficient reserves to keep its facilities in top-notch operating condition to minimize the likelihood of spills and resultant environmental damage. It views the planned treatment plant upgrade as an important environmental betterment project that will improve the quality of our ocean water and thus confer a broad public benefit. In addition, it must be kept in mind that this upgrade project has been mandated by the Regional Water Quality Control Board. Should it be delayed because of a funding shortfall caused by a diversion of reserves to other purposes, the Regional Board is likely to impose penalties or restrictions on the volume the plant may treat, which in turn, could result in limits on City and County power to approve land use applications. Other, more significant remedies are available to the Board as well.

### **The Detachment Proposal**

The City's proposal would shrink the District boundaries by excluding parcels located within the City, and shifting the sewer service responsibility within the detachment area from the District to the City. (The proposal is silent on the City's intentions concerning street sweeping.) The City is asking that 78% of the property taxes received annually by the District (about \$1.28 million) be shifted from the District to the City as a result of the detachment. It is also proposing that a similar proportional share of the District's reserves (about \$24 million) be transferred from the District to the City. It appears that this 78% share proposal was calculated by comparing (i) the assessed valuation of the parcels proposed for detachment, to (ii) the assessed valuation of all parcels currently in the District's boundaries.<sup>1</sup>

The City's proposal is conspicuously silent with respect to the \$1.28 million in annual property tax revenues it seeks to acquire and equally silent with respect to the \$24 million in reserves. At the City Council meeting of February 3, a number of Council Members and staff indicated their belief that property taxes should be used for "general city services" and not for specific utility services. Based on these comments, and similar statements in the staff report to the City Council, the District believes that the City intends to utilize the annual property tax revenues and reserve funds for general city services, and not to support the provision of sewer services. In essence, this proposal is driven by the City's search for revenue and not by prudent planning of the appropriate agency to provide efficient street-sweeping and wastewater collection and treatment services. Indeed, if good governance were the

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<sup>1</sup> Goleta West has not had an opportunity to independently verify the assessed value calculation. Even if it is correctly computed, Goleta West questions the legality and equity of this method of dividing the property tax revenues and reserves. The District has received property taxes since well before enactment of Prop 13 in 1978 to fund the services it provides. The parcels in the detachment area account for 50% of the wastewater flow collected and treated by the District's facilities. If the City's proposal is accepted, Goleta West would be left with 50% of the wastewater stream but only 22% of the property taxes to support the capital needs of those customers.



motivation, the City would be proposing to take over all sanitary services within the City's boundaries, instead of just the portion currently served by the District.

### **The County's Role in the Detachment Proceedings and the Structural Conflict of Interest**

The County has an important role to play in a proceeding like this one.

Pursuant to the Cortese-Knox-Hertzberg Local Government Reorganization Act of 2000 (Cal. Gov't Code §§ 56000 *et seq.*) (the "Reorganization Act"), the City's detachment application triggers a statutory procedure under which a negotiated property tax reallocation agreement between the District and the City may result. The procedure is set forth in state law (Rev. & Tax Code § 99), which states as follows:

In the event that a jurisdictional change would affect the service area or service responsibility of one or more special districts, the board of supervisors of the county or counties in which the districts are located shall, on behalf of the district or districts, negotiate any exchange of property tax revenues. Prior to entering into negotiations on behalf of a district for the exchange of property tax revenue, the board shall consult with the affected district. The consultation shall include, at a minimum, notification to each member and executive officer of the district board of the pending consultation and provision of adequate opportunity to comment on the negotiations. (Emphasis added.)

Thus, according to this statute, the County serves as an agent for Goleta West in the property tax exchange negotiations.

The problem arises from the fact that, on the facts of this proposal, Santa Barbara County is not the disinterested party in these negotiations the Reorganization Act and Revenue & Taxation Code § 99 envision. Indeed, it has a substantial financial stake in the outcome that arises from the 2001 Revenue Neutrality Agreement ("Agreement") between the City and the County. Section 4.2.1 of that Agreement provides:

4.2.1 After incorporation of the City, the County will continue to have ongoing obligations to provide public services to the City and its residents and that such services are reasonably estimated to amount to \$3,300,000 during the first complete fiscal year following incorporation. In order to insure that the effect of incorporation is neutral as to the County, the parties agree to the following allocations of tax revenues in perpetuity:

- (i) Property tax generated by property located in the City and which would otherwise accrue entirely to the City, commencing on the Effective Date will be shared equally by the parties; . . . .

Section 4.12 of that Agreement provides:

4.12 Change in property tax allocation factors. In the event that the property taxes currently received by Goleta West Sanitary District are reallocated, City and County shall share in the manner set forth in this

paragraph. As an incentive for the future annexation of the neighborhood known as Isla Vista, any increased property tax revenues that may result from a change in the allocation factor ("the revenues") shall be shared, 70% to the County and 30% to the City, so long as the City boundaries do not include Isla Vista. In the event that the City annexes Isla Vista, the City shall be entitled to 70% of the revenues and the County shall be entitled to 30%. County's share of the revenues shall be transferred in its entirety to the County Fire District.

Under these provisions, it is apparent that the County has a financial interest in the property tax transfer negotiations which would incline the County to favor reallocation to the City over the District, since the County has a right to share in any financial benefit secured by the City. It would be unseemly, and would raise substantial legal issues, if your Board were to negotiate with the City on behalf of the District when the County's and City's financial interests are legally aligned – effectively two parties on the same side of the bargaining table would negotiate to the exclusion of the District – the party on the other side of the table. Such a process would be both unfair and unwise.

#### **The County's Duties as a Fiduciary to the District**

As noted above, the Reorganization Act provides that the County serves as an agent of Goleta West in the property tax transfer negotiations. Under California law, this agency relationship results in the creation of a fiduciary relationship between the County and Goleta West (see Frankel, *Fiduciary Law*, 71 Cal. L. Rev. 795, 808-09 (1983)). As a fiduciary, the County owes the same duties of diligence, loyalty and faithful service to Goleta West as if it were serving as a trustee. See e.g., Gov't Code § 27000.3; *Duffy v. Cavalier* (1989) 215 Cal. App. 3d 1517, 1531.

At the same time, under California law the Board of Supervisors owes a duty of "absolute loyalty and undivided allegiance to the best interests of the governmental body or agency of which they are officers." *Klistoff v. Superior Court* (2007), 157 Ca. App. 4th 469, 478. In other words, the Board of Supervisors owes its loyalty to the County and the population it serves.

Thus, the Board of Supervisors finds itself with incompatible duties of loyalty. This situation is described in the Restatement (3rd) of Agency:

When an agent deals with the principal on the agent's own account, the agent's own interests are irreconcilably in tension with the principal's interests because the interest of each is furthered by action — negotiating a higher or a lower price, for example — that is incompatible with the interests of the other. If an agent acts on behalf of the principal in a transaction with the agent, the agent's duty to act loyally in the principal's interest conflicts with the agent's self-interest. Even if the agent's divided loyalty does not result in demonstrable harm to the principal, the agent has breached the agent's duty of undivided loyalty.

(Rest. 3rd Agency § 8.03)

By virtue of its Revenue Neutrality Agreement with the City, the County has financial interests in the property tax transfer negotiations that cannot be reconciled with its fiduciary duties to the District and its tax- and rate-payers under the Reorganization Act.

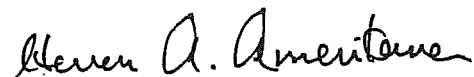
### **Goleta West's Request to the County**

The District respectfully requests that the County recuse itself from representing the District's interests in the negotiations concerning an exchange of property tax revenues related to the City's detachment proposal. We believe this recusal can be accomplished by the Board of Supervisors adopting a resolution delegating to the District Board of Directors the authority to undertake those negotiations. The District is prepared to undertake that representation on its own behalf, to keep your Board fully informed of the progress of negotiations and to consult with your Board – as your Board would be obliged to consult with the District – before agreement is reached with the City under Revenue & Taxation Code § 99.

The District would be pleased to discuss this issue with you or your representatives at any time.

Thank you for your kind consideration of this request.

Sincerely,

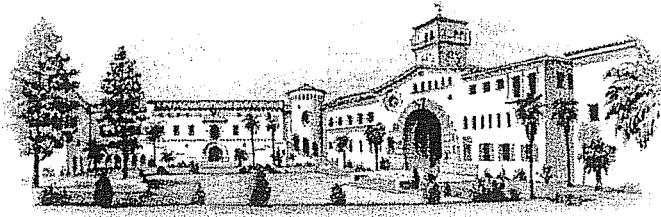


Steven A. Amerikaner  
General Counsel  
Goleta West Sanitary District

cc Michael Brown, County CEO  
Dennis Marshall, County Counsel  
Robert Geis, County Auditor-Controller  
Robert Braitman, LAFCo Executive Officer  
Bill Dillon, LAFCo Counsel  
Dan Singer, Goleta City Manager  
Tim Giles, Goleta City Attorney  
Board of Directors, Goleta West Sanitary District  
Mark Nation, General Manager, Goleta West Sanitary District

# COUNTY OF SANTA BARBARA

**Dennis A. Marshall**  
County Counsel



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## COUNTY COUNSEL

March 20, 2009

Steven A. Amerikaner  
General Counsel  
Goleta West Sanitary District  
21 E. Carrillo Street  
Santa Barbara, CA 93101-2706

RE: Proposed Detachment from Goleta West Sanitary District; Property Tax Negotiations

Dear Mr. Amerikaner:

We have received and carefully reviewed your February 23, 2009 letter to the Board of Supervisors regarding Goleta West Sanitation District's (GWSD) contention that the Board should or must recuse itself from participating in the exchange of property tax revenues mandated by Revenue & Taxation Code § 99. As you know, section 99 is triggered by virtue of the City of Goleta's petition to LAFCO to detach certain parcels located within the City from GWSD's boundaries.

We understand your client's contention is based upon the following two theories:

- (1) The County statutory duty to negotiate on behalf of GWSD creates an agency relationship and a corresponding fiduciary duty between the County and GWSD.
- (2) Because the County receives a portion of the future tax revenue pursuant to the Goleta Revenue and Neutrality Agreement, a conflict of interest exists precluding the County from negotiating on GWSD's behalf; therefore, the County should recuse itself from the negotiations required by section 99 and allow GWSD to negotiate on its own behalf.

In response to the first issue, it's the County's position that it is not an agent of GWSD for purposes of the negotiations required under section 99(b)(5). It appears that GWSD relies on language in section 99 which indicates that the County negotiates "on behalf of" the District. However, there is no indication that the legislature intended to create an agency relationship by the use of that phrase. Further, the words in context recognize the County's exclusive role in the negotiation process. Section 99 requires consulting with the District, but there is no requirement that agreement be reached or that GWSD agree to an exchange of property tax revenue, provided that City and County agree (see 71 Ops. Cal. Atty. Gen. 344 (1988)). In order to establish an

agency relationship, it must be shown that the principle has the authority to control the behavior of the agent. *Flores v. Brown* (1952) 39 Cal.2<sup>nd</sup> 622, 628.

In this case, neither the City nor GWSD has any legal power to control the County's actions in the negotiations held pursuant to section 99. Therefore, an essential element of an agency relationship is not present and the County acts as an agent for neither party. It is fundamental that the law presumes that no agency exists, and it is the burden of the party alleging such to prove the existence of an agency. (*Armatov Baden* (1999) 71 Cal.App.4<sup>th</sup> 885)

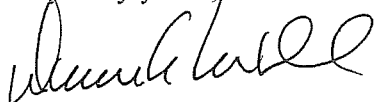
Second, the County concludes that it has no authority to delegate its statutory duty to negotiate the property tax exchange "on behalf of" GWSD. The County acknowledges that its existing revenue neutrality agreement with the City of Goleta would provide the County with a percentage of any GWSD property tax allocated pursuant to section 99 to the City. As you may know, it is not unusual for a county to have a financial stake in the appropriation of tax revenues among local agencies within its jurisdiction. However, neither section 99 nor any case or opinion interpreting this section, requires or authorizes the County to recuse itself from negotiating on the grounds that it would be financially affected by the outcome. Absent such legal authority, the County concludes that delegating negotiating authority to GWSD is contrary to the express language of section 99. We also believe that section 99 specifically guarantees that the City of Goleta has a statutory right to negotiate the property tax exchange agreement with the County and not the District.

To permit a district to negotiate on its own behalf would defeat the very purpose of "negotiations" since the district could simply allow section 99's statutory time frames to expire without any good faith negotiation. There is nothing to indicate the legislature intended that degree of control vest with districts. Delegating negotiating authority to districts is contrary to the express language of section 99 because a failure to reach agreement would allow a district to block the detachment proceedings by adopting an intransigent negotiating position.

The County will comply with the express terms of section 99 and will negotiate with the City of Goleta. Also consistent with section 99, the County will consult with GWSD and allow GWSD an adequate opportunity to comment on the negotiations.

If you have any further questions, please don't hesitate to contact me.

Very truly yours,



Dennis A. Marshall  
County Counsel

April 9, 2009

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**HAND DELIVERY**

Mr. John Baker  
Assistant County Executive Officer  
County of Santa Barbara  
105 E. Anapamu Street  
Santa Barbara, CA 93101

RE: Property Tax Exchange Negotiations Related to Proposed Detachment from Goleta West  
Sanitary District

Dear Mr. Baker:

This letter is submitted on behalf of the Goleta West Sanitary District (Goleta West) with respect to the application submitted to the Santa Barbara Local Agency Formation Commission (LAFCO) by the City of Goleta (City) proposing that certain Goleta West territory be detached from the District. Pursuant to Revenue and Tax Code Section 99, the County soon will be negotiating on behalf of the District a tax exchange agreement with the City. While we disagree with the County Counsel's decision not to recuse the County from this role as stated in his March 20 letter, we remain hopeful that the County will fulfill its fiduciary duty and negotiate this tax exchange at arms-length on behalf of Goleta West.

This letter sets forth Goleta West's positions with respect to the negotiations.

**Need for Additional Information**

The City's application to LAFCO was submitted on February 4, 2009. Goleta West sent a letter to LAFCO on February 11 pointing out significant omissions from the application. LAFCO forwarded Goleta West's letter to the City, but the City has not yet responded to it. A copy of our February 11 letter to LAFCO is enclosed.

The deficiencies Goleta West identified make it very difficult for the County to engage in meaningful negotiations over the terms of a tax exchange agreement. We believe that, at a minimum, the following questions must be answered by Goleta before the negotiations begin:

1. In light of the City's proposal that it receive 78% of Goleta West's current reserves and future property taxes, is the City willing to accept the obligation to pay 78% of all treatment plant costs, including O&M, the pending upgrade, and future capital needs that, absent the detachment, would be obligations of Goleta West? If not, what share of these three categories of cost is the City prepared to accept?
2. Is the City willing to commit to pay the costs of the pending upgrade with funds it receives from Goleta West's property tax reserves reserves by the deadline set by the Regional Board and the Goleta Sanitary District?

3. Will the City agree to a LAFCO term and condition requiring that it assume Goleta West's contractual obligations to the Embarcadero Municipal Improvement District (EMID), including providing wastewater collection system operations, maintenance, repair and rehabilitation, as set forth in the existing agreement between Goleta West and EMID?
4. Will the City agree to a LAFCO term and condition requiring that it enter into one or more extra-territorial service agreements with the owners of parcels north and west of the City boundary which are currently within the boundaries of the District?
5. Will the City agree to a LAFCO term and condition requiring that it pay Goleta West a "wheeling charge" to transport wastewater from the City boundary to the regional wastewater treatment plant to pay a fair share of the O&M and capital costs of the sewer mains and pumping facilities used by that wastewater stream?

### **The City's Proposal to Reallocate Property Taxes**

The City has proposed that the tax exchange agreement provide for reallocation of 78% of the future property taxes from the District to the City. The City's position is based on its claim that the area proposed for detachment includes real property constituting 78% of the assessed value of all property in the District.

Goleta West believes the City's proposal is fundamentally flawed because it fails to reflect the actual shift in sewer service responsibilities that will occur if the detachment is implemented. Indeed, the shift in sewer service responsibilities to the City will be between 43% and 66%, depending on which measure of "service responsibilities" is chosen.

The proposed detachment area includes:

- o 43% of the registered voters of the District as of November 2008.
- o 47% of development potential of the District
- o 51% of the land area of the District
- o 52% of the total wastewater flow of the District for 2008-09.
- o 66% of the collection system (measured in linear feet without considering pipe diameter)

Goleta West respectfully submits that the appropriate measure of "service responsibility" should be based on two factors: current wastewater flow and future development potential, for the following reasons.

Historically, Goleta West has used property tax revenues (and associated interest earnings) for its capital projects and street sweeping. There are two kinds of capital projects: activities related to the regional wastewater treatment plant and activities related to the collection system. Goleta West is one of five participants in the treatment plant, which is owned by Goleta Sanitary District. Its participation is governed by a contract dating back to the 1960s, which requires Goleta West to pay approximately 40% of the costs of the plant. Under that contract, Goleta West has agreed to participate in periodic capital projects for the plant, including construction of the ocean outfall in the early 1990s.

The most costly capital project involving the wastewater treatment plant is the planned upgrade to full secondary treatment levels. The upgrade was mandated by the Regional Water Quality Control Board as a part of a settlement agreement with Goleta Sanitary signed in 2004. Under the settlement agreement, all construction financing must be acquired by December 31, 2010. The settlement agreement also imposes a timeline for construction. The treatment plant is currently being engineered and designed, and is scheduled to be under construction in March 2010. For that schedule to be met, Goleta Sanitary District will want to have firm assurances that all treatment plant participants have the funds on hand to meet their obligations.

The current estimated cost of that project is approximately \$50 mm and the District's 40% share of that expense is approximately \$20 mm. The District has long planned to eschew borrowing and instead finance its obligation from its reserves, which consist of property taxes and associated interest earnings.

Goleta West intends to use future property tax revenues for similar purposes, including annual collection system rehabilitation, replacement and repair work. To cite one example: Goleta West recently completed construction of a new sewer main in Hollister Avenue to replace an existing main substandard in size and in need of rehabilitation and repair. The project cost \$3.2 mm, and was paid for with reserve fund derived from property tax revenues.

Goleta West's financial consultant has estimated that the District's Capital Improvement Plan ("CIP") expenditures between 2011 and 2029 will be \$47.7 mm, including \$31.8 mm for the treatment plant upgrade and other plant capital expenditures during this period.

If the City's proposal to reallocate 78% of future property taxes is accepted by the County on behalf of Goleta West, Goleta West will be left with 48% of the wastewater flow and just 22% of the capital funds needed for the facilities that handle that flow. Goleta West's capital improvement plan cannot be sustained if the District's share of the property tax revenues is reduced to 22%.

To make up the shortfall, the District will be compelled to quadruple annual sewer service charges to District customers.. This conclusion appears in a study of the fiscal impacts of detachment recently prepared for Goleta West by Raffelis Financial Consultants, Inc. Of course, since sewer service is considered a property-related fee under Proposition 218, the ratepayers could block the sewer service charge increase by a simple majority protest.

If that were to occur, the District would be unable to fulfill its contractual obligation concerning the treatment plant upgrade, and would be unable to implement its Capital Improvement Program, which is needed to ensure that the collection system operates in an environmentally-responsible way that complies with state and federal regulations.

There is one additional and important point. At present, the District uses about 55% of its contractual entitlement in the treatment plant. In other words, the District pays for capacity in the plant that it is not currently using, and that it is holding to accommodate future development. The amount of future development potential within the City of Goleta is about equal to the amount of future development potential in Isla Vista, based on a 2006 study of future development patterns completed by Dudek & Associates ("Dudek Study").

If the allocation of property taxes and treatment plant capacity rights fails to consider future development potential, the City or the District could find itself with additional plant capacity that it will never need or, possibly, an allocation of plant capacity that will be inadequate for its future development



needs. Thus, the split of property taxes and plant capacity should take account of the future development potential of the City compared to Isla Vista.

### Proposed Negotiating Positions

Based on the foregoing, we urge the County to assert the following positions on behalf of Goleta West in the upcoming negotiations with the City of Goleta:

1. As a condition of a tax exchange agreement, the City must agree to execute an agreement with Goleta Sanitary District under which it will assume the following portion of Goleta West's existing obligations to Goleta Sanitary with respect to the regional treatment plant:

a. 52% of annual O&M expenses, to be adjusted annually to reflect actual wastewater flows from properties served by the City.

b. A share of the costs of the pending upgrade project, and all future capital expenditures related to the treatment plant, calculated as follows:

(i) Utilized Capacity. This term refers to the portion of the Goleta West contractual capacity of 3.11 mgd that is actually utilized. For 2008-09, Goleta West is utilizing about 55% of this capacity, or 1.7 mgd. This Utilized Capacity should be allocated to the City and Goleta West in accordance with their respective wastewater flows in any given year, and the allocation should be adjusted annually.

(ii) Additional Capacity. This term refers to the portion of the Goleta West contractual capacity of 3.11 mgd that is not actually utilized in a given year, but instead is above and beyond the District's needs in that year. For 2008-09, Goleta West is holding about 45% of its total contractual capacity as Additional Capacity, or 1.4 mgd. This Additional Capacity should be allocated to the City (47%) and Goleta West (53%) in accordance with their future development potential as analyzed in the Dudek Study, and should be adjusted every five years to reflect the most current available information concerning development potential.

2. As a condition of a tax exchange agreement, the City must agree to (i) reduce its proposal for a share of the Goleta West property tax reserves from 78% to 52% (as adjusted in accordance with paragraph 1,b) , (ii) legally pledge those reserves to funding the treatment plant obligation noted in paragraph 1 above and other projects identified in the Goleta West CIP within the City's boundaries, and (iii) adopt Goleta West's CIP as the City's Sewer CIP for the portions of the collection system within the City boundaries and the areas the City will be required to serve under an extra-territorial service agreement (e.g., EMID).

This proposal is based on the simple fact that detachment will not alter the reality that the City and the District will be inextricably dependent upon one another for the proper operation of the wastewater collection and disposal system. If the City is unable to make its payments for O&M and capital costs of the treatment plant, the other partners in that plant (including Goleta West) will be required to make up the deficit. This duty is not mitigated by Goleta West's ability to sue the City to recover any funds expended by Goleta West. Sewer plant operations cannot be suspended while lawsuits are being resolved.

3. The District's reserves of \$30.4 mm should be segregated into funds comprised of connection fees and capital facility fees (and interest earned thereon) ("Capital Fee Reserve"), which Goleta West estimates to be about \$2.5 mm of the total, and funds comprised of property tax revenues (and interest

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earned thereon). Funds in the Capital Fee Reserve cannot lawfully be transferred to purposes other than capital related to the wastewater system (under Gov't Code Sec. 66000), and those funds shall be allocated to the City and Goleta West in accordance with the Goleta West Sewer CIP.

4. The tax exchange agreement should provide that for the 2010-11 tax year, the City will receive 52% of the property taxes currently allocated to Goleta West (adjusted in accordance with paragraph 1,b to take into account Additional Capacity), which equals the estimated quantity of wastewater generated in 2008-09 by users within the City's boundaries. For each year thereafter, the City will receive an allocation of property taxes that equals its share of the capital costs for the treatment plant calculated per paragraph 1,b.

This allocation should be calculated annually to ensure the property tax exchange is revenue neutral in the future on both the City and Goleta West, and to account for the possibility that (i) development will be more intensive in Isla Vista than in the City, thus increasing wastewater flows and associated capital expenses, and (ii) development potential may be increased for properties in one area compared to another, thus requiring a reallocation of Additional Capacity.

5. The tax exchange agreement should provide that the City must place all property taxes received as a result of the tax exchange agreement into a dedicated reserve for operations (including street sweeping), maintenance, repairs, and long-term capital needs of the sewer system as shown on the Goleta West CIP, except to the extent that those revenues are replaced by revenues generated by sewer service charges. The purpose of this requirement is to ensure that there are adequate funds available for future capital needs, and that a failure to raise sewer service charges in the future (whether due to Prop 218 protests or other reasons) does not impair the City's ability to fund those needs. We believe that such a condition is needed for both public policy (as explained above) and CEQA reasons.

#### **Request to Attend Negotiations**

Goleta West respectfully request that the County invite District representatives to attend the property tax exchange negotiations.

Please contact me if you have any questions concerning the foregoing positions. We look forward to consulting with the County and providing input on the terms as they are negotiated.

Sincerely,



Steven A. Amerikaner

Enclosure

cc Board of Directors, Goleta West Sanitary District  
Mark Nation, General Manager, Goleta West Sanitary District  
Michael Ledbetter, Deputy County Counsel