October 21, 2011

Hon. Roger Dickinson
Assembly Member, 9th District
Room 3126, State Capitol
Sacramento, California 95814

Dear Assembly Member Dickinson:

Summary of Findings

You asked the Legislative Analyst's Office to evaluate three questions regarding the (1) efficiency of small special districts, (2) accountability of small special districts, and (3) effectiveness of Local Agency Formation Commissions (LAFCOs).

Our overall findings are as follows:

- We find evidence that in certain cases smaller districts can be less efficient and less accountable than larger districts. However, it is not clear that these associations between district size and efficiency or accountability are true for districts of all types or in all areas of the state. Instead, our analysis suggests that many factors affect the efficiency and accountability of special districts.
- We further find that the LAFCOs are generally well positioned to review the effectiveness and accountability of special districts, though their general approach to undertaking these reviews has some limitations. We also identify some barriers to the implementation of consolidations even when doing so makes analytical sense to the LAFCO.
- Finally, at your request, we offer some options for your consideration that we believe could promote better efficiency and accountability of special districts, as well as improve the LAFCO process.

Project Overview

Scope of Project. You asked us to answer three sets of questions:

- ***Efficiency.*** Are small special districts less efficient or effective than larger districts? Would consolidation of small districts with other special districts improve efficiency and effectiveness of service delivery? Do functional consolidations improve efficiency and effectiveness?
- ***Accountability.*** Are small special districts less accountable to the public than larger districts or general-purpose governments? Are small districts less transparent to their constituents?

- ***LAFCO Process.*** How effectively is the LAFCO process working? Do LAFCOs evaluate the "right" metrics when considering consolidations? What barriers exist to LAFCOs initiating consolidations?

Given the broad nature of your questions and the limited time to carry out the research, we agreed to follow a case study approach and to focus predominantly on water supply and fire districts. In general, we focused our analysis on independent special districts, though some of the consolidations we discuss in this letter included dependent districts. Finally, in evaluating the questions about the merits of special district consolidation, we generally focused on consolidations of special districts and not on other governance changes, such as mergers of special districts with general-purpose governments (cities and counties).

In conducting our analysis, we talked with representatives of statewide organizations, including those representing special districts, water districts, fire districts, and LAFCOs. We met with special district and LAFCO representatives in each of our three case study counties. We also conducted a literature review, consulted with local government experts, and reviewed statewide special district data where available.

Case Studies Used. We selected three counties on which to focus our analysis—Napa, San Bernardino, and San Diego. In part, we selected these counties, particularly San Bernardino and San Diego, because we were informed that they included a number of successful and unsuccessful attempts to consolidate fire and water districts in recent years. We hoped that these consolidation attempts would help illuminate how well the LAFCO process works, what role efficiency and accountability play in determining which districts should be consolidated, and how efficiency and accountability were affected by consolidations. In addition, we chose these three counties in an attempt to capture some different cross sections of the state. While we do not claim that these three counties reflect a representative sample of California counties, they do represent some differences in population size, urbanization, regions, and relative number of special districts. The table below illustrates some of these differences.

Figure 1

Independent Special Districts in Case Study Counties

(2008-09)

County	Independent Special Districts	Population	Independent Districts per 100,000 Population	Independent District Revenues (In Millions)
Napa	12	137,359	8.7	$45
San Bernardino	54	2,054,423	2.6	703
San Diego	69	3,169,490	2.2	3,314
Statewide	2,184	38,134,496	5.7	23,181

Our research consisted of visits to each of the three counties where we met with LAFCO executives and multiple special district representatives. For each county, we reviewed Municipal Service Reviews (MSRs) and other reports prepared by the LAFCO, as well as special district websites and financial information where available.

The Challenge of Defining "Small" Districts. One of the challenges of this research is defining what we mean by a "small" special district as distinct from a medium or large one. This is a challenge for a few reasons:

- First, based on our conversations with state and local representatives, there is no common definition of a small district generally, nor do there appear to be common definitions of small districts even within the different types of services.
- Second, some information we might like to use when comparing district size—such as district population, land area, or service volume (for example, number of emergency responses for fire departments or water volume for water districts)—does not appear to be collected in any single place. The one set of data we have for all districts statewide is revenue and expenditure data collected by the State Controller's Office (SCO).
- Third, there is great variation in the types of services that special districts provide, making comparisons across types of special districts very difficult. For example, the average independent water district in 2008-09 had $10.6 million in total revenues. By comparison, the average independent fire district had $2.7 million and the average cemetery district had $314,000. So, when using a metric like total revenues, a district that might be considered small among water districts could be considered medium or large among fire and cemetery districts.

Given these limitations, we use different metrics for defining small districts throughout this letter, depending on what data were available to us.

Caution About Findings. While most of the findings in this letter reflect information that we found consistently throughout our review, it is important to stress that many of these findings are based on a small sample of counties and special districts. Therefore, we suggest that you consider our findings to be issues meriting further legislative review and would caution you against assuming that our findings extend to all special districts statewide.

EFFECTS OF DISTRICT SIZE AND CONSOLIDATION ON EFFICIENCY

In this section of our letter, we discuss our findings regarding how district size and consolidation affect efficiency. In summary, we find some evidence that larger districts, and consequently consolidation of small districts, can result in improved efficiency in some cases. However, we also find that consolidations have costs that have to be weighed, and the potential of consolidation to generate ongoing efficiencies depends on several factors, including the type of services provided, location, fiscal resources, and the capacity of management. Moreover, we find that many districts, both large and small, are participating in "functional consolidations" to reduce costs and achieve better efficiencies. In such cases, structural consolidation would not necessarily achieve much greater efficiencies.

Defining Efficiency. Fundamentally, efficiency is a measurement of the level of goods or services provided at a certain cost. Measuring efficiency allows one to evaluate in a single metric (1) the quantity (or quality) of a good or service produced and (2) the price for that good or service. One can then compare the efficiencies of different good or service providers, as well as evaluate how the efficiency of a single provider changes over time. For example, one could compare the water rate (dollars per acre-foot) charged by like water agencies to make an assessment of which was providing that service more efficiently.

Because efficiency is a metric that takes into account both costs and quantity, a higher efficiency level can be demonstrated in two ways. First, the savings from improved productivity can be reinvested and used to provide customers a higher level of service without changing the cost charged to the customers. For instance, in the case of fire districts, a more efficient district may have shorter response times while receiving the same amount of revenues from its constituents as another district. In water districts, a more efficient district could treat ratepayers' water to a higher quality standard while charging the same fees as a less efficient one. Second, the cost savings from greater efficiency may be used to reduce the taxes or fees that constituents pay while maintaining the same level of service.

Theoretical Argument for Larger Districts Being More Efficient

There are several theoretical arguments for why larger districts may be more efficient than smaller districts—and therefore why consolidation of smaller districts may improve efficiency. Larger organizations may be better able to realize economies of scale by spreading fixed costs like management, overhead, and infrastructure over more constituents, resulting in lower per capita expenditures. A larger organization may also be better positioned to share resources such as capital assets (like buildings, trucks, or maintenance equipment) over multiple activities, reducing underutilization of those assets. Relative to multiple smaller districts providing the same service, a single larger district can also have lower personnel costs because it may require a single set of personnel to provide administrative functions like information technology (IT), human resources, or budgeting. Consolidation of smaller districts also provides an opportunity to reduce personnel costs by eliminating some high-paying leadership positions such as fire chiefs or general managers and by reducing the total number of board members.

We should note that there is a debate within the academic literature on benefits of larger, consolidated, and multipurpose governments compared with smaller, single-purpose agencies. While some academics argue that consolidation creates the benefits described above, others suggest that those benefits may be overstated, arguing, that inefficiencies can arise from such consolidated government agencies. For example, some have cited the leveling up of wages to the highest levels in the previously separate entities. Skeptics of consolidation also argue that smaller, single-purpose governments can be more efficient than larger, multipurpose agencies because constituents of smaller agencies can more easily review and interpret the activities and decisions of more narrowly focused agencies. This does presume, however, that those constituents are knowledgeable about the agency's activities and decisions and have opportunity to intervene when they disapprove.

Anecdotal Evidence Suggests Consolidation Can Improve Efficiency

In all three counties we visited, as well as in other counties around the state, we came across numerous anecdotal examples of small districts that faced challenges to operating efficiently, and in many of those cases, LAFCO recommended some sort of consolidation. We also found examples of consolidations that appear to have succeeded in improving the efficiency or level of services in the area.

As one example of a consolidation done to achieve improved efficiency, in 2005, a reorganization of several fire protection districts in the county was approved by the San Bernardino LAFCO after it became clear that the organizational structure at the time had led to significant financial troubles for many of the districts. The LAFCO approved the consolidation proposal and created a single county-wide district whose boundaries cover all unincorporated areas in the county. This consolidated fire district is now called the San Bernardino County Fire Protection District (SBCFPD).

The creation of SBCFPD was expected to result in savings in administrative costs and in improved service delivery throughout the county, and in the view of the county, those ends were achieved. Many administrative functions like budgeting and human resources are outsourced to the county for a lower cost than before, and the district is now able to offer a range of services that include fire suppression, emergency medical services, HAZMAT response, rescue operations, flooding and mudslide response, and terrorism response at the same cost as the lesser services provided by smaller independent districts in the county. In fact, several independent districts and cities throughout the county now contract with SBCFPD for their fire services because they receive higher levels of service for a lower cost than they could provide it themselves. According to county and LAFCO executives, coordination has also been enhanced by having a single county-wide district. For example, SBCFPD felt that their response to the 2007 wildfires in Southern California was enhanced by having a consolidated district. In contrast, we heard that the response to those fires in the unincorporated areas of San Diego County may have been hindered by less efficient coordination among the various districts in those areas of the county, resulting in the over commitment of resources to the first of several large fires while leaving other areas vulnerable. Consequently, some San Diego County fire districts indicated that the 2007 fires caused some districts to reevaluate the potential for consolidation, something the San Diego County LAFCO had been working towards for years.

Testing the Relationship Between District Size and Efficiency

While we heard many cases of consolidations designed to improve efficiency or quality of service, we were limited in our ability to empirically test or quantify those efficiencies, for several reasons:

- First, as described above, efficiency improvements can manifest themselves in terms of improved service delivery—something that can be difficult to measure—instead of fiscal savings or rate changes. This complicates attempts to quantify efficiency gains because there may be no observable cost decrease from a consolidation.
- Second, in order to quantify the efficiency gains, it is necessary to have data on both the level of service provided and the cost of that service. Data on the budgets of all special districts across the state can be found in the SCO's special district annual financial report, but the report does not describe the level of services provided by districts. In addition, data were lacking at the individual district level; the districts that we contacted had not tracked their service levels over time in a way that would allow

us to quantify the efficiency gains from consolidation. The LAFCOs also did not quantify efficiency gains. We note that in some cases districts pursuing a consolidation through LAFCO may quantify anticipated efficiency gains in a document called a "plan for service." However, we are unaware of any attempt to verify whether those efficiency gains occurred.

- Third, in the case of water supply districts, for example, there can be significant variations in the cost of the inputs (such as the water that is treated and then sold to end users), making it difficult to isolate the effect of size on a district's costs from other sources of variation. For instance, water purchased from the State Water Project makes up 60 percent to 80 percent of the operating costs of some water districts in Southern California, but in Northern California many districts have their own supplies and thus can avoid costs associated with importing water. In addition, energy costs incurred as a result of pumping water are a significant component of water districts' operating expenses, and an agency's expenditures on energy can vary significantly due to the geographic features of its service area. As such, relatively high water rates for a given district may reflect factors that are independent of its size or how efficiently the district is operated.

Wastewater Districts. In many respects, however, wastewater districts do not share these data limitation problems. The State Water Resources Control Board periodically prepares a report that provides data on all wastewater agencies in the state, including cities, counties, special districts, and Joint Powers Authorities (JPAs) that have wastewater responsibilities. These data are comprehensive and encompass many of the factors that might significantly influence the cost of wastewater service, including the population served, the size of treatment plants (as measured by the average daily flow, which is a rough approximation), the level of treatment applied to waste, whether debt service is included in the rates, and whether the agency received any form of state or federal grant at any point since 1972. It also lists monthly fees for a typical household and fees for new connections to that agency's water system. These data allow us to empirically examine whether larger districts that provide wastewater service charge lower fees.

Wastewater agencies are uniquely suited to this type of empirical analysis because their fees are a reasonable measure of relative efficiency. Unlike districts that provide water supply services, the cost of wastewater agencies' inputs does not vary significantly according to geography. These agencies receive wastewater for free and they typically do not incur significant energy costs to move the wastewater because treatment plants are generally positioned downhill of the sources of wastewater (thus using gravity to move the wastewater). Because these costs do not vary, fees are more readily comparable.

We found two indications that larger wastewater agencies are more efficient than smaller agencies. First, we found wastewater fees charged by agencies to be lower the larger the agency, whether measuring the size of the agency by district population or volume, even while controlling for other factors such as other revenue sources, treatment levels, and inclusion of debt service in monthly fees. For example, the smallest wastewater agencies serve populations of less than 1,000 customers and charge an average of $45.55 per month, while the largest agencies serve more than 500,000 customers and charge an average of $16.21 per month. Second, we found that wastewater agencies with larger populations treated their water to a higher level while charging similar fees to their customers. In summary, therefore, we found that in the case of wastewater agencies, larger districts appeared to both provide services at a lower cost, as well as provide a higher quality of service as measured by treatment levels. We should note, however, that district size did not explain all of the variation in wastewater fee levels, and, as we discuss later, there are other factors that may be important in explaining a district's efficiency and rates.

Other Factors Affect District Efficiency and Level of Service

Although there are certainly cases where having larger districts increases the efficiency of special districts, we also found examples of smaller districts that provide high-quality service at a reasonable cost. As such, there are other factors besides size that play a role in the level of service provided and the cost of providing that service.

Geography. One such factor is geography. While smaller districts may charge higher fees (all else being equal), many of these districts are located in remote areas. Consolidation may therefore not be cost-effective because there may not be any nearby districts with which they can connect. For example, we observed a small district providing sewer services in Napa County that had considered connecting with a larger wastewater agency. This district ultimately ruled against building the connection because it was too costly. Therefore, in remote areas where consolidation is a cost-prohibitive option, districts may have to focus on other operational and management changes to improve efficiency.

Type of Service Provided. We heard from several special district and LAFCO representatives that the relationship between district size and efficiency probably depends on the type of service provided by the district. Districts that provide services with a large capital component (such as water supply) may benefit more from consolidation than districts that provide services that rely heavily on personnel (such as fire protection). Infrastructure-intensive districts tend to have high fixed costs that can benefit from economies of scale. Larger districts can spread those fixed costs over a greater number of people, lowering the cost per person. Infrastructure-heavy districts may also benefit from being better able to recruit and retain expensive support staff like engineers. Because they can afford to employ these personnel with specialized knowledge, larger districts may be in a better position to identify cost-effective solutions to issues that arise. Finally, heavy machinery and equipment is often needed to install, maintain, and replace infrastructure. Again, larger districts are in a better position to spread those fixed costs over a larger ratepayer base.

In contrast, there appear to be fewer opportunities for economies of scale in districts that depend heavily on personnel to provide their services, and therefore consolidation may not offer as many benefits for those districts. For instance, one fire chief we spoke with suggested that, as a general rule, fire districts with fewer than three to five stations may operate less efficiently, but once the number of stations exceeds approximately eight, effective coordination of the larger district requires the same number of leadership positions as in multiple smaller districts, thus reducing the potential savings from economies of scale. On the other hand, we also heard that consolidation can improve the "coordination of command" in fire districts by laying out formal command structures that supplant the ad-hoc arrangements that can arise when multiple districts cooperate to fight a large fire. These formalized command structures can improve fire districts' responses by ensuring that all personnel have received explicit direction about tasks and responsibilities.

Access to Resources. Another factor that can affect efficiency and delivery of service is a district's ability to secure adequate financial resources. Fire districts need revenues to cover costs associated with hiring and training personnel and purchasing equipment. Water districts need funds for operating costs and to pay for maintenance and upgrades to infrastructure. Districts of all sizes need resources to absorb increases that happen due to inflationary pressures, changes in district land use or demographics, and increased regulatory requirements. In some cases, smaller districts may have more difficulty raising funds because their smaller constituent base may have lower aggregate income. But districts of all sizes can have difficulty raising funds because the California Constitution requires them to secure the approval of local residents before imposing taxes and assessments and limits their ability to impose fees for purposes other than the direct delivery of property or personal services.

Management Quality. A final factor that we found that affects the efficiency of a district's operations and the level of service it provides is the quality of its management. Good management can lead to positive outcomes, a higher quality of service, effective and efficient use of financial resources and personnel, effective long-term planning, and accountability to the public. Mismanagement can take the form of intentional or unintentional misuse of funds, resulting in higher-than-necessary costs. Mismanagement may also take the form of the failure to engage in effective long-term planning and underinvestment in infrastructure. Based on our conversations, mismanagement appears to be a major factor in many cases of poorly performing districts. Mismanagement occurs in both larger and smaller districts, and therefore size may not be the overriding factor that determines whether a district is managed well. However, most of the cases of mismanagement that we were informed about occurred in smaller districts. Small districts may be more likely to suffer from poor management because they may have difficulty hiring professional managers, and their board members may not be as knowledgeable as those of larger districts. Importantly, we saw evidence that the solution to mismanagement is not necessarily consolidation. We observed various cases where water districts had come close to financial insolvency or had violated environmental laws as a result of poor management. In two of these cases, however, the small water districts replaced their general managers and became financially solvent within a few years of the change. Moreover, in the view of many people we spoke to, consolidation of two poorly managed districts would have resulted in the formation of a larger poorly managed district. Therefore, although poor management can be related in some fashion to district size, consolidation may not solve the issue.

Costs Associated With Consolidations

Even where consolidations have the potential to improve efficiencies, it is important to be cognizant of the potential costs involved.

Implementation Costs. First, there are one-time costs associated with conducting the consolidation process. Entities that initiate a consolidation are generally required to cover the cost of numerous LAFCO studies that accompany the effort, such as updated municipal service reviews, sphere of influence updates or special feasibility studies, which can cost hundreds of thousands of dollars in some cases. Initiating entities also must cover the cost of an election if there is enough public protest to push the proposal to a vote. Small districts, in particular, may not have the resources to pay these costs, although LAFCO can reduce or waive fees for the studies. (We generally did not hear that these costs were truly an obstacle to consolidation.) Districts (and LAFCO) may also incur legal costs if there is resistance to a consolidation.

LAFCO-Imposed Conditions. Second, the conditions LAFCOs approve when enacting a consolidation can add costs that offset efficiencies that would otherwise be achieved. For example, consolidating groups of personnel involves merging compensation packages with differing salaries and benefits. We heard in many cases that when packages are combined, the end result is the inclusion of the highest salaries and highest benefits for the personnel involved, referred to as the "harmonizing" of employee compensation packages. While this harmonization may be a necessary outcome from ensuring support by the districts and their employee groups for consolidation, it has the effect of increasing the cost of service and can offset some or all of the other efficiency gains achieved, at least in the short term. This is particularly prevalent in fire districts, for which personnel are the major expense. As another example, we heard that cost savings from fire district consolidations may be less than anticipated because as part of many final consolidation agreements, no or few fire stations are closed. This can preclude savings from the elimination of overlapping service areas. In the view of the constituents of the district, their local fire station is the symbol of the quality of their service. Therefore, even if there is another station that would be able to provide service as a result of the consolidation, constituents may object.

Initial Investment Costs. Third, agencies absorbing another district through consolidation can face significant up-front costs as they repair aging infrastructure, purchase required equipment, or begin to build a reserve for emergencies or future upgrades. Therefore, providing service in an area previously served by a poorly managed district initially can be more expensive after consolidation. These up-front costs—which may still be offset by longer-term operational savings—are often cited as a barrier to consolidation.

Functional Consolidations Frequently Used to Improve Efficiency

We have thus far described the benefits and costs of "structural consolidations," which are consolidations performed through the LAFCO process and which involved altering jurisdictional boundaries and responsibilities. But we also found that many special districts of all sizes find other ways to realize some of the efficiency improvements associated with structural consolidations *without* going through the LAFCO process. Specifically, we found many cases of districts pursuing "functional consolidations" to improve efficiency. Functional consolidations can take several forms with differing levels of formality and integration: informal memoranda of understanding between districts, contracting for services, and JPAs. We found that functional consolidations frequently involve sharing administrative staff such as budgeting, human resources, legal, and IT personnel. They may also include contracts for the use of specialized equipment or sharing of operational staff such as maintenance workers. Finally, they can include shared purchasing agreements or shared investments in new facilities, thereby allowing smaller districts to achieve some of the economies of scale and potential efficiencies associated with larger districts.

We observed several examples of functional consolidations that were being considered or had already occurred. Several smaller water districts in San Diego County that are currently facing financial constraints are now in the process of agreeing on a functional consolidation that would focus on IT and human resources personnel while also allowing for the sharing of trucks for cleaning sewer systems. This arrangement may take the form of a JPA if it involves joint ownership of equipment. Similar arrangements have been pursued by northern San Diego County fire districts. In addition, Orange County's LAFCO has established a website to help local governments share services to achieve efficiencies. This website allows districts to post resources or assets they have available as well as resources that they are seeking, which it then matches to one another. Finally, as noted above, several cities and independent fire districts now contract with SBCFPD in order to provide lower cost, higher quality fire protection services to their constituents.

The Upsides. Functional consolidations avoid some of the costs and other downsides of structural consolidations. One of the most frequently aired objections to structural consolidation that we heard was that it reduces local control over service delivery, and a major advantage of functional consolidations is that they allow constituents to retain that control. For instance, some fire districts in San Diego County share fire engines that are identified with multiple logos, each corresponding to a district that uses them. Constituents may see the logo of their local fire district and feel like they have a stake in the service provision. In this way, functional consolidations may not be subject to the same political objections as structural consolidations, and as such they may proceed more quickly. Functional consolidations also avoid some of the costs involved in structural consolidations. They may not trigger efforts to harmonize multiple employee compensation packages and they do not require a LAFCO review, with the process costs and the time associated with that process. Functional consolidations also eliminate the possibility that the residents of one district will directly subsidize those in another district, as may occur with structural consolidations. Finally, we heard that an additional benefit of functional consolidations is that they can be used as an interim step on the way to a full structural consolidation by demonstrating some of the benefits of consolidation and building trust between districts.

The Downsides. In practice, functional consolidations may not deliver all of the same efficiency improvements as structural consolidations. Functional consolidations may not result in the same cost savings as structural consolidations because they do not result in the elimination of board members or district heads like fire chiefs or water district general managers. In fact, they may increase the number of managers and administrative staff if a JPA is created with new board members. Functional consolidations may also miss some improvements to service delivery because they may not allow for the same level of coordination of command as structural consolidations of fire districts.

Another trade-off associated with functional consolidations is that efficiency benefits only occur as long as all participating agencies wish to cooperate. We heard from some district representatives that JPAs can function very well as long as priorities among the participating entities are aligned, but they can fall apart if one district decides to move in a different direction. This can be undesirable because it allows such a district to make unilateral decisions that are beneficial for it but potentially detrimental to other districts.

Another issue we heard with respect to functional consolidations is that LAFCOs do not have explicit statutory authorization to review or alter these JPAs, even where those JPAs are providing direct services such as wastewater treatment or water supply. While LAFCOs may as a practice evaluate some JPAs in the course of conducting studies of services or member agencies, it is not clear that this practice is routine or that LAFCOs have authority to directly make the same kinds of changes in boundaries and services as they do for individual government agencies. We heard differing opinions among LAFCO executives about how significant of a problem this is. However, it appears that this lack of authority can become problematic because it potentially allows districts to expand the area over which they provide service without the same level of LAFCO review as the Legislature requires for other local governments. Based on the SCO's list of special districts, there are about 670 districts formed as JPAs in California (though many of these are agencies other than those formed as special districts).

Relationship Between District Size and Accountability

You asked us to evaluate the linkage between district size and accountability. As we discuss in this section, our findings are inconclusive. We found some evidence—both anecdotal and statistical—that small districts can be less accountable than their larger counterparts. However, we also found anecdotal and statistical evidence that smaller districts may be just as accountable as larger districts. Finally, we suggest that, in part, a lack of transparency of special districts may be a more general problem and not limited to just small districts.

Defining Accountability. In our evaluation of how district size affects accountability, we focused on two components of accountability. First, for districts to be accountable, transparency is required. By this we mean that communities have access to information relevant to making informed decisions. This includes information on both which agencies provide services, as well as how well those services are delivered. Second, for districts to be accountable to the public they serve, that public should have access to the decision making process. In our governmental system, this is typically through the election of representatives. Access to the decision making process can also be achieved outside of the elections process, for example through participation at board meetings. Generally, we assume that if the public has access to relevant information (transparency) and fair access to the decision making process (access), special districts and their public officials can be held accountable for their performance.

Linkage Between District Size and Transparency Is Unclear

We would expect that those agencies most accountable to their public would make important information on meetings, budgets, financial audits, and performance readily available. Current law requires all special districts, regardless of size, to make certain information publicly available. This includes holding open board meetings, making available board meeting recordings and materials, and reporting of financial and employee compensation data to the SCO.

We did find some limited evidence that smaller special districts may be less transparent than larger districts. For example, we heard from LAFCO executives and others that small special districts are more likely than larger districts not to have public websites and to fail to meet all public reporting requirements. As another example, we found that there were 20 independent special districts that did not fulfill the requirement to report annual revenue and expenditure data to the SCO for 2008-09. Of these, 17 districts appear to be smaller districts—those with annual revenues of less than $1 million, with a majority taking in less than $100,000. (This analysis excludes special districts listed as not reporting but that appear to be inactive or for which we could not find prior-year revenue data.)

While there is some evidence to support the notion that some small districts are less transparent, outright violations of the law appear to be the exception, not the rule, according to LAFCO executives. In addition, while 17 districts with revenues of less than $1 million did not report financial data to the SCO in 2008-09, approximately 1,600 independent special districts with revenues of less than $1 million did do so as required under current law. In addition, while it appears that small districts are less likely than larger districts to maintain websites, we found some small districts that did so. Perhaps more importantly, however, we could find relatively few examples of small *or* larger districts that provided comprehensive information on their websites—specifically that included all of the following information: meeting agendas and minutes, annual budgets, financial audits, and performance statistics.

Lack of Transparency May Be a Broader Problem. The issue of a lack of special district transparency may be a more general one to consider, rather than simply being associated with district size. Though we could find no survey data on people's knowledge of special districts generally, we suspect that it is common that average citizens may not be easily able to identify all of the special districts within which he or she lives, or whether a specific service is delivered by a special district or a general-purpose government. This is probably particularly true for non-enterprise districts for which residents do not receive a regular bill, as well as for districts in more populated urban areas where the public may assume that the service is provided by a general-purpose government. This general lack of knowledge is probably compounded by the fact that the property tax bill owners receive does not delineate how much of the base 1 percent property tax rate goes to each local government serving that property area. Property taxes make up roughly 10 percent of all special district revenues and a quarter of all non-enterprise special district revenues. It is hard to expect the public to hold local special districts accountable if they do not have complete knowledge of which districts serve them or how much they pay to support each district.

Effect of District Size on Community Access to Decision Making Is Unclear

During our site visits and meetings, we received conflicting information regarding the accessibility of small special districts. Many people suggested that decision makers in smaller districts are *more* accessible to their constituents. If true, this would promote information sharing and help ensure that decision makers are responsive to community needs and preferences. We heard that it is typical for constituents of small districts to use the same neighborhood stores and attend the same social events as board members. We saw an example in the Circle Oaks County Water District (Napa County), where the general manager felt that his ability to walk door to door to communicate to local residents was key to the agency's ability to convince voters to support a rate increase that was instrumental in bringing the district into fiscal solvency. Compared with larger districts, this high degree of interaction between board members and constituents allows constituents to raise concerns in a more informal and accessible environment.

In addition, these informal channels of communication can be an effective means for board members to inform constituents of issues.

In other cases, however, we heard that a special district's small size could contribute to reduced resident access to the decision making process. In particular, we heard that small special districts frequently do not hold elections and that the governing boards are filled with the same individuals year after year. While this could, in some cases, simply reflect an electorate that is generally satisfied with its special district board, the failure to have regular elections runs counter to the idea of a democratic process with regular community access. We even heard that in rare cases, for a variety of reasons, some small districts do not attract enough residents interested in serving on their governing boards to keep their board seats filled. As a result, governing boards of some small districts are filled with individuals appointed by the county board of supervisors or other governing board members.

Measuring Access to Districts. Given the different perspectives regarding special district access, we sought to supplement our review by examining some factors that could be measured quantitatively. For reasons that we describe below, we thought that the following questions could help inform the discussion regarding special district access. Do special districts, particularly small special districts:

- Hold elections regularly?
- Have voter turnout rates that are similar to cities and counties?
- Overcompensate their employees compared with other local governments and the state?

Given time limitations, we focused our assessment on a subset of local governments in San Diego County. Specifically, for our analysis regarding the frequency of elections and voter turnout rates, we looked at local elections there between 2002 and 2010. For our analysis of employee compensation, we examined the compensation provided to the senior managers of 18 water districts there that employ professional staff and the five city departments that supply water to city residents.

Some Small Special Districts Do Not Hold Regular Elections. Accountability is promoted when governing bodies hold regular elections. For our first measure, we examined whether special district elections were taking place in San Diego County from 2002 through 2010. (We used this sample of years from this county because it was the only one of our case study counties with elections data available in database format.)

San Diego County has 52 independent special districts with members elected to the boards of directors. A board member's term is four years and each board has three, five, or seven members. Boards typically have staggered elections—meaning that at least two seats on the board are on the ballot every two years. Since 2002, most San Diego County special districts would have held at least two—and possibly as many as five—elections. Under certain circumstances, state law permits special districts not to hold a regular election. Specifically, a special district need not hold an election if there are the same number of candidates, or fewer candidates, as there are open seats.

Our review of the 52 special districts found that 42 of them—including all of the special districts serving more than 4,000 people—held at least one election since 2002. Ten special districts, in contrast, held no elections at all during the more than eight-year period. Most of the districts that had no elections are very small water or community services districts, typically serving fewer than 1,000 residents and having an operating budget in the range of tens to hundreds of thousands of dollars annually. One of the districts that did not hold an election, however, is a fire district responsible for serving almost 4,000 residents and managing an annual operating budget of about $1.8 million. We also found that some special districts held fewer elections than otherwise would have been expected (based on the term of the special district governing board members).

It is also worth noting that certain types of independent special districts—primarily cemetery districts—have governing boards with board members that are appointed by general purpose governments, usually the county board of supervisors. We estimate that roughly 400 independent special districts in California (about 19 percent of the total statewide) are board appointed rather than directly elected. To the extent that direct public access to local government is a concern, one could ask whether it makes sense to have independent districts without independently elected boards. When we raised this issue in our meetings, it was suggested that these districts might have trouble finding enough people interested in running for board seats if they were directly elected. It is unclear to us, however, why this would be the case for these districts versus other types of districts. Moreover, if that lack of public interest were true, it suggests that there was not a strong interest in local control and, consequently, as strong a rationale for the district to be independent.

Special Districts Voter Turnout Was Similar to Cities and County. While holding elections is an important component of an accountable government, it is not sufficient. Accountability also requires that citizens express their opinions by voting. For our second measure, we examined voter turnout rates (as defined by the number of votes cast relative to the number of registered voters in a jurisdiction). Comparing these voter turnout rates with city and county voter turnout rates helps assess the degree to which residents are engaged in special district governance. In our analysis of San Diego County local governments since 2002, we found that regardless of the size of the district, special district voter turnout was substantially similar to the turnout for city and county government elections.

Water Districts Provided Higher Employee Compensation. Like any organization that uses public funds, special districts have a fiduciary duty to ensure that public funds are spent efficiently and effectively for the public good. Employee compensation comprises a major component of many governmental entities' expenditures. One could reasonably expect that accountable agencies would seek to not overcompensate employees so as to charge customer rates no higher than otherwise necessary.

For our third measure of accountability, we used data collected by the SCO to compare (1) the amount of compensation that 18 water districts in San Diego County provide their general managers with (2) the amount of compensation that five cities in the county provide directors of departments responsible for providing water services. As an additional point of comparison, we contrasted district general manager compensation with the compensation provided by the State of

California to the director of the Department of Water Resources (DWR). We focused on the compensation provided to these top managers because their responsibilities have significant similarities, and the press and residents often follow senior manager compensation levels closely (particularly in the case of enterprise functions, like water, which recoup their costs by charging residents rates). Thus, executive management compensation can serve as an indirect gauge of local oversight. We found that water districts in San Diego County provide greater compensation to their general managers when compared to city department managers and the director of DWR.

While employee compensation levels are a potential indicator of accountability, we would note that it is an imperfect one. Employee compensation levels can reasonably vary due to factors such as cost of living and desirability of different locations. Some, but not all of this variance is controlled by the fact that we looked at districts and cities within a single county.

With the exception of the two smallest special districts (serving fewer than 400 residents), most water district general managers in San Diego County earn about $200,000 and have about 86 subordinate employees. Overall, the variation in general manager salaries (from a low of $160,000 to a high of $270,000) does not appear to reflect the size of the district as measured by the number of district residents or employees. These district general managers are eligible for pension benefits using the “2.5 percent at 55,” “2.7 percent at 55,” or “3 percent at 60” formulas.

Five cities in San Diego County provide water services through their water department or another municipal department. These department directors earn about $150,000 and have 217 subordinate employees on average (though this includes the City of San Diego’s water department, which has about 800 employees). Like their special district counterparts, the variation in directors’ salaries (from a low of $110,000 to a high of $190,000) does not appear to reflect the number of city residents or employees. The directors are eligible for similar pension benefits as special district general managers. In our review of city and special district salaries, we found that district general manager salaries often are more similar to a city manager’s salary than to the salary of a city water department director. This finding is somewhat perplexing given the generally wider range of responsibilities required of a city general manager.

While there is no state employee classification that is directly comparable to a water district general manager, the position of the director of DWR has some similarities. The state director earns $165,000 annually—less than all but three of the water district general managers in San Diego County. The director of DWR oversees a department with more than 3,000 staff, significantly more than any district general manager or city director in San Diego County. The director of DWR is eligible for the “2 percent at 55” pension formula, a less generous benefit than the pension formulas extended to general managers and municipal department directors.

Overall Assessment of Special District Accountability

Conflicting viewpoints about special district accountability prompted us to explore several statistical measures related to accountability. The outcome of this review is inconclusive. One measure (SCO reporting) suggests that the vast majority of special districts, including small districts, report financial data to the state as required. Another measure (voter turnout rates) suggests that special districts, including small special districts, have levels of accountability that are similar to other local governments. Two other measures (holding elections and top management compensation) suggest that there might be some limitations to special district accountability. Given the limited scope and range of our measures, we urge you not to generalize from our findings, but to use the measures as a branching off point for any future legislative hearings on the topic, as discussed later in this letter.

EFFECTIVENESS OF LAFCOS

You asked us to review how well LAFCOs are operating, the degree to which they are evaluating the "right" metrics when considering consolidation, and what barriers they face in initiating consolidations. In this section, we describe our findings that the LAFCOs we reviewed generally appear to be well positioned to review the work of special districts and to consider consolidations. They appear to conduct their reviews in a thorough and professional manner. We also find that LAFCOs vary in how they evaluate when consolidations make sense. This variation reflects the discretion allowed under current law and is probably appropriate. However, we also find that their LAFCOs do not consistently measure efficiency in their evaluations, something that makes it difficult to evaluate and compare how well different districts and general-purpose governments are utilizing public funds. In addition, we find that LAFCOs face some barriers to initiating consolidations and, therefore, are sometimes wary of doing so when the affected districts are likely to be opposed.

LAFCOs Appear to Fulfill Legislative Mission

The Legislature has the authority to create, dissolve, or otherwise modify the boundaries and services of local governments, including special districts. Beginning in 1963, the Legislature delegated the ongoing responsibility for making these determinations to LAFCOs in each county. The responsibilities and authority of LAFCOs have been modified in subsequent legislation, including a major revision of the LAFCO statutes in the Cortese-Knox-Hertzberg Local Government Reorganization Act of 2000 (Chapter 761, Statutes of 2000 [AB 2838, Hertzberg]). The courts have referred to LAFCOs as "watchdogs" of the Legislature (*City of Ceres v. City of Modesto*). According to the courts, LAFCOs were created "to encourage the orderly formation and development of local government agencies…to guard against the wasteful duplication of services that results from indiscriminate formation of new local agencies or haphazard annexation of territory to existing local agencies."

Based on our site visits and reviews of various documents, we found that the LAFCOs in San Bernardino, San Diego, and Napa Counties appear to be fulfilling their legislative mission. In each of these counties, the LAFCOs do the analysis of services and boundaries, produce reports, and make recommendations designed to encourage orderly government. They employ professional staff with backgrounds and training in related fields, such as regional planning. The work of LAFCO staff appears to be deliberative and professional.

We would note, however, that the LAFCO executives we spoke with reported that they are not up to date on having all spheres of influence and municipal service reviews updated every five years, as required by law. We heard from LAFCOs that this is a common problem statewide and is a consequence of the workload being more than their current budgets can support. We also note that our findings on the quality of LAFCO products in these three counties are not necessarily indicative of the quality in all counties. San Diego County and San Bernardino County, for example, appear to be among the best funded LAFCOs in the state, something that could affect the number and quality of staff they are able to hire, as well as the number and quality of service and boundary reviews they are able to complete annually.

LAFCOs Have Discretion in How They Evaluate Merits of Consolidation

It is difficult for us to evaluate whether LAFCOs are using the "right" metrics when evaluating the merits of consolidation proposals, largely because current law does not articulate when consolidations should occur. Current law sets, as a minimum threshold, that LAFCOs must declare that any consolidation (or other reorganization of districts, such as dissolutions or mergers with cities or counties) would result in lower or substantially similar public service costs and that it would promote public access and accountability. However, current law does not say when a consolidation should occur. It does not provide any specific guidance to LAFCOs detailing the criteria under which a consolidation should be approved or when consolidations are likely to promote orderly formation of governments, preservation of agricultural land, and discouragement of urban sprawl as is the mission of LAFCOs.

Possibly because of this lack of statutory specificity, we found that LAFCOs typically evaluated special districts and the possibility of special district consolidation on a case-by-case basis. While LAFCOs generally indicated that there was not a single set of criteria upon which to make consolidation decisions, we heard a couple of common rationales for when LAFCOs believe consolidation of districts is merited:

- LAFCOs recommend consolidations when they believe that a district is not likely to be financially sustainable over the long term and merging that district with another could improve their viability. The evaluation of long-term sustainability could focus on the agency's ability to fund its annual operations costs, as well as its long-term infrastructure needs, particularly in light of how the LAFCO projects population and service needs to grow or change in that area.
- LAFCOs were more likely to consider consolidations in cases where there are overlapping boundaries or duplication of services. This could occur where two districts are providing the same or similar services in the same geographic area, or where there are small pockets of services provided by one district that is wholly or largely surrounded by another district providing the same service.

These rationales seem generally consistent with the mission of promoting orderly government to the extent that it successfully prevents the financial collapse of poorly operating districts or the inefficient duplication of services.

We would note that while current law does not specify criteria for when consolidations should occur, it does require that a consolidation may occur only if that consolidation is consistent with the recommendations or conclusion of a LAFCO study, which is usually an MSR or sphere of influence report (which is produced after or in conjunction with the MSR).

The MSR is required to review and make written determinations in six areas related to an agency's operations:

- Growth and population projections for the affected areas.
- Present and planned capacity, including infrastructure needs and deficiencies.
- Financial ability of agencies to provide services.
- Opportunities for shared facilities.
- Accountability for local service needs, including governmental structure and operational efficiencies.
- Any other matters related to effective and efficient service delivery, as required by commission policy.

As with the decision to approve consolidations, the law does not provide guidance to LAFCOs to instruct them on how to weigh each of the six factors it is required to review. Instead, it leaves this to the discretion of the local LAFCO, effectively making it a decision based on local priorities and preferences. Importantly, the law does not provide guidance on how each of these six factors is to be measured, again resulting in local discretion of what metrics LAFCOs use. This discretion allows LAFCOs to be flexible to their local priorities and preferences. However, we think the variation results in at least one significant trade-off, specifically in the area of measuring efficiency. As we noted earlier in this letter, we found that when evaluating service delivery, LAFCO MSRs tend *not* to focus on measures of efficiency—such a service per amount of cost—instead focusing more often on other measures of service provided. For example, in the area of fire protection, LAFCO MSRs frequently used the number of emergency responses and response time as measures of service delivery. These appear to be typical measures when evaluating the performance of fire departments. However, in no case did we see where fire service data was combined with financial data to give a measure of efficiency. In part, a focus on level of service rather than efficiency appears to be a consequence of the fact that efficiency can be very difficult to measure. The consequence of the LAFCO focus on service levels rather than efficiency, however, is that it makes it impossible to compare the efficiency of service delivery across similar agencies within a county or across counties, or for a single agency before and after consolidation. An inability to compare government efficiency deprives the LAFCO, Legislature, and public with a meaningful way to evaluate how well public funds are spent by their local agencies.

LAFCOs Sometimes Wary of Initiating Consolidations

Current law does not require LAFCO boards to approve a consolidation when staff recommend that action. A common theme we heard in our conversations with LAFCO and special district representatives was that while LAFCOs have the authority to initiate consolidations, they are often reluctant to do so if the special districts subject to the consolidation were likely to be opposed. The view was that the power of special districts to oppose a proposed consolidation was greater than the power of the LAFCO to force it on an uncooperative district. The reasons a district might oppose consolidation are varied and include a desire by board members or general managers to retain their positions, the concern by a well-performing district that taking over a poorly functioning district could increase the costs to its own constituents, and the concern by a district and its constituents that consolidation could reduce constituent access to the district and its board.

Some of the barriers to LAFCO-initiated consolidation are inherent in the law itself. Specifically, the constituents of a district generally can send a LAFCO-initiated consolidation proposal to a public vote if 10 percent of the population in any affected district files a protest. By comparison, the protest threshold is 25 percent if a district initiates the consolidation process. Additionally, the law provides that if a consolidation proposal goes to public vote, a majority of voters in each affected district has to support the consolidation for it to be successful, not a majority of all the voters. In both of these cases, our understanding is that the law is designed to preserve the local autonomy of each affected district and its constituents. In addition, the law requires the LAFCO to pay for all costs for studies and elections if it is a LAFCO-initiated consolidation proposal, whereas the district(s) pay for these costs if they propose or request the consolidation.

In addition to the barriers established in existing law, LAFCOs and special district representatives suggested that there are other tools districts can employ if they oppose consolidation. Many districts have more financial and political resources at their disposal than LAFCOs and may use them to ensure their preservation if they oppose consolidation. We heard examples of public outreach campaigns and lawsuits initiated and funded by special districts to oppose consolidation efforts initiated by LAFCOs. In more than one of these examples, the special district was successful at preventing the consolidation, usually by preventing the LAFCO board from approving the staff recommendation to approve consolidation. We heard of very few examples of consolidations that went to public vote.

Because of the varied ways that a district can oppose a LAFCO-initiated consolidation, LAFCOs frequently take into account the likelihood of opposition when deciding whether to propose a consolidation. In such cases, LAFCOs often prefer to act as a broker for consolidation, working with the different districts to convince them that consolidation is in each of the districts' best interest. In part because of this, consolidations can take a long time to complete. For example, the consolidation of fire districts in the unincorporated areas of San Diego County began with a fire study in 1997, followed by the creation of a task force in 1999 and multiple subsequent reports. The district consolidation was initiated in 2007 and is still in the process of being completed today.

OPTIONS FOR LEGISLATIVE CONSIDERATION

As described in this letter, we did not find conclusive evidence that small special districts are inherently less efficient or accountable than their larger counterparts. However, we find that there are opportunities to improve the accountability of special districts generally, thereby potentially promoting better outcomes and efficiency of many local special districts, including small and large districts. We also find that there may be opportunities to improve the LAFCO process to successfully achieve consolidations when they make sense analytically. In this section, we offer several options you may want to consider to achieve these outcomes.

Increasing Special District Transparency

Efforts to increase the transparency of governments can allow the local public and media to have better information upon which to make informed decisions and hold their elected officials accountable.

Searchable Databases. One way to promote increased transparency would be to make it easier for individuals to know what special districts they live in and what they pay for in those districts. For example, the state or local governments could create searchable databases accessible on the internet where individuals could input their address and be provided a list of all special and general-purpose governments that serve them. Potentially, this list could include contact information for those agencies, as well as links to their websites if they maintain one. The San Diego County Water Authority's website has this functionality for water districts in that county. According to representatives of the California Special Districts Association, they are currently undertaking a project to accomplish something like this for all special districts statewide. It may be worth considering a way to coordinate their efforts with the SCO (which collects annual financial data on all special districts) and LAFCOs (that have to update and maintain data on district boundaries).

Property Tax Bill Information. Another way to promote transparency would be to encourage or require that property tax bills identify how the revenues associated with a property's 1 percent base property tax rate is allocated among all special districts, general-purpose governments, school districts, and redevelopment agencies. Currently, this allocation varies greatly among properties within counties. To our knowledge, no counties put this information on the property tax bill sent to property owners. Consequently, no individual property owner is able to learn from their property bill how their property tax revenues are allocated among different levels of government.

Public Websites. A third way to improve transparency of special districts would be to encourage or require all special districts to maintain public websites and to include certain information on those sites, such as annual budgets, fiscal audits, board meeting notices and minutes, performance data, links to LAFCO reports, and the term of office for current board members. Currently, many districts maintain websites, and many of those include much of this information. However, smaller districts appear to be less likely to have websites, and many districts that have websites do not include all of this information.

In considering ways to promote transparency, we would offer a caution to consider how any legislative actions could result in state-reimbursable mandates. For example, requiring counties to alter their property tax bills to include allocation information probably would result in a state-reimbursable mandate for the costs associated with reconfiguring databases and reporting processes necessary to carry out that requirement. We are wary of recommending actions that could result in state-reimbursable mandates because these are costs that are outside the state's control and can end up being much greater than anticipated. However, in some cases, there are strategies the Legislature can employ to achieve much of the same objective without creating a state-reimbursable mandate. One example of such a strategy would be to make the receipt of certain funding—such as state grants—by special districts contingent on conforming with the desired practice, such as having a website or providing more detailed information on the property tax bill.

Providing Voters With Information When Special Districts Do Not Have Elections

As we note, ten small districts in San Diego County failed to hold a single election during the five election cycles from 2002 through 2010—either because there was only one candidate per board seat or because no one ran for an open seat. One option the Legislature might consider is requiring that all board seats be included in the county voter guide or on the ballot regardless of whether the seat is contested or not. This would provide a measure of increased special district transparency because it would let voters know that they are constituents of this district and who the board member will be (or if the positions will be vacant until they are filled by appointment). By the same logic, perhaps all independent special districts should be elected. As described earlier, there are about 400 independent special districts that have their board members appointed by a general-purpose government, usually the county board of supervisors.

In considering these changes to special district elections, we should note that many provisions relating to elections have been found by the Commission on State Mandates to constitute state-reimbursable mandates. It is possible that requiring special districts to provide this election related information could be found to be reimbursable.

Developing More Consistent Evaluation Metrics

As described above, we find that there is variation in how LAFCOs evaluate efficiency when conducting MSRs, and in many cases LAFCOs do not appear to actually measure efficiency, instead relying on other measures of service delivery such as amount or quality of service. The Legislature might want to promote the use of consistent measures of efficiencies by LAFCOs and the establishment of statewide or regional benchmarks. If LAFCOs used consistent measures in their reports, it would be easier for the public to compare the operations of different special districts and general-purpose governments both within counties and across county lines. Having clearly defined benchmarks also could be a way to hold local governments more accountable to their constituents who would have more information upon which to judge the effectiveness of their service providers.

It is important to note, however, that coming up with such measures would be challenging. As we describe in this letter, measuring efficiency in a service area such as wastewater treatment may be relatively straightforward, but in other service areas measures of efficiency in government operations are often more difficult to determine. For example, how does one evaluate the efficiency of providing park services? Also, meaningful measures of efficiency are going to vary significantly by service type and could, in some cases, vary by region or even within a region or county. For example, measuring efficiency will be very different if one is looking at fire protection versus another type of service, and reasonable expectations for fire response time and costs may be different for urban versus rural areas.

While challenging, we do not believe developing useful metrics for LAFCOs to use is impossible. In fact, the Orange County LAFCO has already begun working in this direction by developing a system on its website that provides multiyear financial data—such as revenues, expenditures, and reserve data—for every agency in that county. While not directly measuring efficiency of each agency, it is clear that the Orange County LAFCO is attempting to find more consistent ways to evaluate the fiscal operations of agencies. Further, by posting that information on its website, that LAFCO is working to increase the public transparency of its districts.

In establishing these types of metrics, the Legislature would need to consider whether the specific standards for each service type should be developed at the state level—for example, by the Office of Planning and Research or various state departments—or should be set at the local level, for example by each county LAFCO. A more decentralized approach potentially could provide greater flexibility for LAFCOs to tailor the metrics to local differences in geography, demographics, or preferences. On the other hand, a more centralized, consistent approach would better allow the public to compare individual agency outcomes across counties. The Legislature also would need to consider whether to make the development and use of these metrics a requirement for LAFCOs or let them be advisory. Given the fiscal constraints LAFCOs face, it may be important for the state to provide some time and technical assistance before making this a requirement.

Given the complexities of developing standardized metrics, we would suggest that, should the Legislature be interested in encouraging more consistent evaluations by LAFCOs, that the Legislature use a process that is inclusive of representatives of local stakeholders, including special districts, LAFCOs, and general-purpose governments. By including the participation of local stakeholders, there is an increased probability that any standards or benchmarks developed would be flexible enough to be useful to local agencies and constituents in different parts of the state with different service priorities.

Reducing Hurdles to LAFCO-Recommended Consolidations and Oversight

As discussed above, we found that there are some legal barriers to consolidations. Specifically, the law provides a lower protest threshold to place a consolidation proposal on the ballot when the proposal is initiated by a LAFCO rather than a district. Also, when consolidation proposals are placed on the ballot, it takes a majority of any single affected district to defeat the measure, not a majority of all affected voters. In both cases, these provisions are designed to protect the ability of the constituents of each affected local government to maintain local control if that is their preference. In effect, these provisions tilt the process *against* consolidation.

In weighing the rights of local citizens to maintain local control of their governments against a desire for more efficient and effective provision of local services, one approach might be to reduce some of these barriers if certain conditions are met. For example, the protest threshold could be increased if LAFCOs demonstrate certain findings related to failures of a district's public accountability (for example, frequently vacant board seats) and/or specific improvements in efficiency or effectiveness that would be achieved (for example, likelihood of meeting minimum water safety standards). By analogy, other successful legislation has been aimed at reducing barriers and expediting the LAFCO process when certain conditions are met. For example, Chapter 109, Statutes of 2011 (AB 912, Gordon), was recently approved by the Legislature for the purpose of expediting special district dissolutions by eliminating the requirement for elections or protest proceedings when certain conditions were met related to (1) how the dissolution was initiated and (2) LAFCO findings.

We would also suggest the Legislature consider expanding LAFCO authority to oversee JPAs. As we describe, LAFCOs have no statutory authority to oversee the JPAs that districts or general-purpose governments enter into. This includes JPAs that are providing services, such as wastewater treatment or water supply. Consequently, LAFCOs have no statutory authority to review the financial and service data of these JPAs to ensure that they are providing services and using taxpayer and ratepayer funds efficiently and in a manner consistent with current law. Nor does a LAFCO have authority to alter a JPA's boundaries or services in the same way that it can do for individual special districts and other local government agencies. We do not think this expanded authority should be undertaken with the intent of discouraging the use of JPAs because those agreements are one strategy that special districts use to achieve higher efficiencies. However, we think that it is important that the entities created under JPAs be subject to some level of oversight akin to the districts and general-purpose governments that utilize them. One suggestion we received was to require districts to provide LAFCOs with copies of all JPA agreements, including amendments.

Increasing Legislative Oversight of LAFCOs and Special Districts

As we note, the Legislature created LAFCOs to fulfill a legislative function, reviewing local government boundaries and services. While there is good reason for this process to remain fundamentally a local one, there may be value in formalizing more legislative oversight over this function. This could involve regular policy committee or oversight hearings where LAFCO and local government representatives from a given county or region come before the Legislature to provide updates on the major issues, challenges, and changes in their area. Alternatively, legislative committees could delve into areas of particular concern, including getting more information and perspectives from around the state on some of the issues and options raised in this letter. For example, should the Legislature be interested in additional oversight or policy hearings, some questions we think would be valuable to follow up on with local agencies and LAFCOs include the following:

- Are there opportunities to encourage the use of functional consolidations to improve efficiencies?
- Would providing LAFCOs additional oversight authority over JPAs improve the orderly formation of governments?
- How common is it for special districts to go multiple election cycles without having board elections?
- Are there other opportunities to reduce election or other barriers to consolidations that make sense analytically?
- Do special districts overcompensate employees compared with general-purpose governments providing the same services?

- What are the best metrics to use in evaluating efficiency and accountability, particularly for different service types? Are there statewide or regional benchmarks that could be used as standards against which to evaluate government performance?

CONCLUSION

I hope that this information has been of assistance in answering your questions on the topics of special districts and the LAFCO process. If you should have any follow-up questions, please feel free to contact my staff. For general questions, please call Brian Brown at (916) 319-8325. For more specific questions related to water districts, call Anton Favorini-Csorba at (916) 319-8336, and for questions on special district elections or employee compensation, call Nick Schroeder at (916) 319-8314.

Sincerely,

Mac Taylor
Legislative Analyst