

Water Replenishment District of Southern California:

***Although the District Has Addressed
Many of Our Previous Concerns,
Problems Still Exist***



June 2004
2002-016

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CALIFORNIA STATE AUDITOR

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June 9, 2004

2002-016

The Governor of California
President pro Tempore of the Senate
Speaker of the Assembly
State Capitol
Sacramento, California 95814

Dear Governor and Legislative Leaders:

As required by Chapter 941, Statutes of 2002, the Bureau of State Audits presents its audit report concerning the operations and management of the Water Replenishment District of Southern California (district).

This report concludes that although the district has implemented many recommendations of our May 2002 report, it has not fully addressed all our concerns. Specifically, our review revealed that the district adopted a reserve-funds policy that calls for increasing its reserve funds, but that policy lacks credibility, largely because since adopting the policy, the district allowed its reserve funds to further deplete. In addition, the district likely overstated its reserve-funds targets by using some faulty assumptions in calculating them. Moreover, although it included goals and objectives in its strategic plan, it did not include outcomes by which the district and public can measure the district's progress in meeting them. Further, the district spent district funds on items such as gifts and flowers that its policies specifically prohibit. Finally, the district incurred costs for items, such as award dinners, catered meals, and snacks and beverages for its staff and others, that do not appear to be the most prudent use of its funds.

Respectfully submitted,

A handwritten signature in cursive script that reads "Elaine M. Howle".

ELAINE M. HOWLE
State Auditor

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SUMMARY

Audit Highlights . . .

Although it has implemented many recommendations of our May 2002 report, the Water Replenishment District of Southern California (district) has not fully addressed all our concerns. Specifically, our review revealed that the district:

- Adopted a reserve-funds policy that calls for increasing its reserve funds, but since adopting the policy, the district allowed its reserve funds to further deplete.*
 - Likely overstated its reserve-funds targets by using some faulty assumptions in calculating them.*
 - Included goals and objectives in its strategic plan, but did not include outcomes by which the district and public can measure the district's progress in meeting them.*
 - Spent district funds on items such as gifts and flowers that its policies specifically prohibit.*
 - Incurred costs for items such as award dinners and food and beverages for meetings that do not appear to be the most prudent use of its funds.*
-

RESULTS IN BRIEF

The voters of Los Angeles County established the Water Replenishment District of Southern California (district) in 1959 to counteract the effects of overpumping groundwater from the West Coast and Central basins (basins). The California Water Code (water code) grants the district broad powers to do what is necessary to replenish and maintain the integrity of the basins. In December 1999, the Bureau of State Audits (bureau) issued a report concluding that the district's poor management had led to its charging an excessively high replenishment assessment rate (assessment rate) to entities who pump groundwater. Because that report raised significant issues, the Legislature amended the water code to ensure that the district implemented the bureau's recommendations. The Legislature also directed the bureau to perform a second audit. In May 2002 the bureau issued a report concluding that since 1999 the district had eliminated excessive water rates, and it had depleted its reserve funds to a level that threatened its ability to maintain the current quantity of groundwater in the basins because it lacked a long-term vision of its finances.¹ We also concluded that the district had not adequately planned for its capital improvement projects nor implemented adequate accounting and administrative controls over its operating expenses. The Legislature amended the water code again in 2002 and required the bureau to perform this follow-up audit of the district's operations and management.

Although it has implemented many of the recommendations of the May 2002 report, the district has not fully addressed all our concerns. We recommended that the district determine its need for reserve funds and adopt a policy to ensure sufficient funds to meet its statutory responsibilities. The district did adopt a policy that calls for increasing its reserve funds, but the policy lacks credibility largely because the district has since allowed its reserve funds to diminish even further. Having established a low assessment rate for fiscal year 2003–04, the district projects its reserve funds will fall to \$3.5 million by June 30, 2004, less than the maximum that the water code currently allows and a fraction of the district's targets of at least \$18.4 million and

¹ In this report, the term *reserve funds* refers to the district's current net assets, or current assets less its current liabilities, that are not legally restricted.

not more than \$28.9 million. The district recently adopted an increased assessment rate for fiscal year 2004–05, one that its general manager asserts will not further deplete its reserve funds. However, unless the new assessment rate is sufficient to cover its planned costs and begins to replenish its reserve funds, we will continue to question the district’s commitment to its reserve-funds policy. Also, the district has likely overstated these reserve-funds targets by using some faulty assumptions in calculating them. Moreover, to fully implement its reserve-funds policy, the district would need a statutory change to increase its reserves from the current limit—a change that the district is not currently seeking. Without a sound reserve-funds policy, the district cannot ensure that it has an adequate amount of reserves to continue to meet its responsibilities.

In contrast, the district’s policy establishing an optimum and minimum quantity of stored groundwater in the basins appears reasonable. Further, the district is discussing with a work group a variety of options for a program to store surplus surface water in the basins for future withdrawal and use. Such a program could change how the district uses storage space in the basins and benefit the entire region, but it is too early to evaluate the outcome of these discussions.

Both our earlier audits highlighted the district’s lack of up-to-date strategic and capital improvement plans and recommended that the district develop them. Although the district has developed strategic and capital improvement plans, both need refinement. The district’s strategic plan includes goals and objectives but lacks outcomes by which to measure the district’s progress in meeting them. In its capital improvement plan—which should prioritize capital improvement projects—the district specifies its funding needs and scheduling of proposed projects as recommended, but does not identify those projects the district believes it should complete first, possible funding sources available for each project other than issuing bonds, and the projects the district’s board of directors (board) has formally approved.

To review the district’s proposed capital improvement projects and provide recommendations to the board, the Legislature created a technical advisory committee (committee) comprising representatives of the ratepayers. The committee has worked with the district to develop a process to review and approve capital projects and to periodically update the capital improvement plan. Recently, the committee completed its initial review of 11 projects, nine of which the district included in

its final capital improvement plan, but the district has not yet had an opportunity to implement the committee's updating procedure. The statute mandating the committee will sunset on January 1, 2005. However, according to the district's general manager, the district intends to revise its administrative code to ensure that the committee remains a part of its process for reviewing and approving its capital improvement projects. If the district does not revise its administrative code and the statute sunsets, the ratepayers may lose important opportunities to provide input to the district on future capital projects and during the district's process for periodically updating the capital improvement plan.

Finally, the district has improved its accounting and administrative controls and made changes to its administrative policies since our last audit. However, the district does not always follow these policies. For example, the district has spent district funds on gifts and flowers, which its policies specifically prohibit. Also, the district lacks thorough accounting policies to control reimbursements to staff and board members, especially for travel costs. Moreover, although the district instituted controls to ensure that its costs are reasonable and necessary, the district incurred costs that do not appear to be the most prudent use of its funds. In reviewing the district's 2003 administrative payments, we found that the district spent about \$1.19 million on legal services, more than \$17,500 on food and beverages for meetings, \$2,250 for award dinners, and more than \$23,000 to send one director to 17 conferences. By modifying its administrative policies to limit or prohibit certain purchases, the district could better control its administrative costs, especially at a time when its low assessment rate is continuing to shrink its reserve funds.

RECOMMENDATIONS

To ensure that the district has sufficient funds to meet its statutory responsibilities and to show its commitment to its reserve-funds policy, the district should do the following:

- Set its assessment rate at a level that will support the district's planned activities and allow it to replenish its reserve funds, if necessary, and keep them at an appropriate level.
- Reevaluate the assumptions that underlie the amount it targets to have available as reserve funds and, if necessary, seek legislative approval to revise the amount allowed as reserve funds.

To ensure that the district and the public can assess the district's progress in achieving the goals and objectives described in its strategic plan, the district should refine its plan to include measurable outcomes.

To make its capital improvement plan more informative to the district and its ratepayers, the district should consider doing the following when it updates its capital improvement plan:

- Rank projects by their importance to identify the projects it believes it should complete first to meet its statutory requirements.
- Include alternative sources of funding for the projects in addition to issuing bonds.
- Distinguish between board approved projects and proposed projects.

To ensure that the district continues to collaborate with ratepayers on projects, it should pursue its plan to revise its administrative code to make the technical advisory committee part of its process for reviewing and approving capital improvement projects. If the district fails to implement this recommendation, the Legislature should consider extending the committee at least until the committee has had the opportunity to participate in the process of periodically updating the district's capital improvement plan.

To strengthen controls over its administrative expenses and to ensure that it uses public funds prudently, the district should take the following steps:

- Reaffirm its commitment to following the policies in its administrative code, and ensure that its staff abides by the policies.
- Perform a detailed review of the reasonableness of the costs for contracted legal services, and consider whether hiring an in-house lawyer is more cost-effective.
- Reassess its use of public funds for such purposes as award dinners, catered meals, high airfares, and lodging for local conferences, and revise its administrative code to limit or prohibit such costs.

- Amend its administrative code to provide better guidance on reimbursable travel expenses, including a limit on the number of conferences staff and directors can attend and a process for justifying exceptions to that limit.

AGENCY COMMENTS

The district indicates that it accepts our recommendations and further states that it has already implemented one of them by extending the life and function of the technical advisory committee. ■

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INTRODUCTION

BACKGROUND

Under the terms of the California Water Code (water code), Section 60000 et seq., the voters of Los Angeles County established the Water Replenishment District of Southern California (district) in 1959. Created to counteract the effects of overpumping groundwater from the West Coast and Central basins (basins), the district's stated mission is "to provide, protect and preserve high-quality groundwater through innovative, cost-effective, and environmentally sensitive basin management practices for the benefit of residents and businesses of the Central and West Coast Basins." The district lies entirely within Los Angeles County and serves 43 cities, including Los Angeles, Long Beach, Downey, and Torrance, as well as many businesses and private parties that hold pumping rights. The district does not directly provide water to customers; rather, it ensures the health of the basins so that groundwater is available to holders of water rights. According to district estimates, nearly 40 percent of the water consumed by the area the district serves comes from groundwater sources. The rest comes from recycled water and water imported from the Colorado River and the State Water Project. Figure 1 on the following page shows the district's boundaries.

A five-member board of directors (board) governs the district, with each director representing a geographical area within the district. The directors serve four-year terms and are chosen at regularly scheduled general elections. The board acts by adopting resolutions at publicly held meetings. No agency, state or local, oversees the district, which has 27 full-time and part-time employees.

THE DISTRICT'S ROLE IN PROTECTING GROUNDWATER

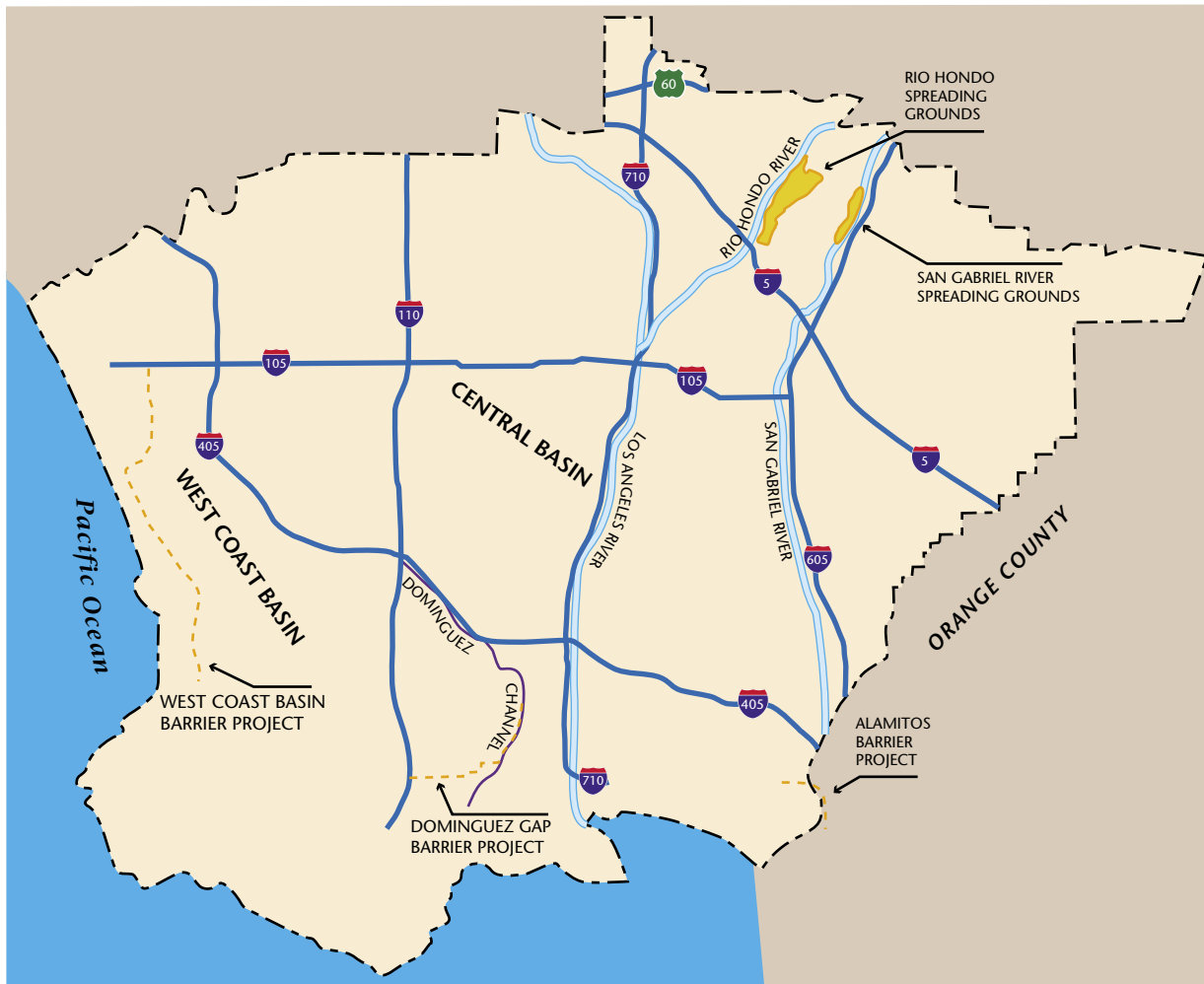
The need for an entity to oversee the replenishment of groundwater in the basins had become clear by the 1950s. The increasing population of the Los Angeles area during the early part of the 20th century had overwhelmed the area's limited sources of surface water, so communities, private water companies, and businesses began pumping groundwater.

Because rainfall in the basins averages only 14 inches per year, it was not long before the pumping outstripped the basins' ability to recharge themselves through natural means. As the groundwater levels continued to decline, some wells went dry and others had to be abandoned because of saltwater intruding into the coastal areas.

Before the district was established, local water agencies tried to manage the groundwater-level issues in the basins. The West Basin Water Association was formed in 1947, and the Central Basin Water Association was formed in 1952. These associations developed a plan to provide supplemental water to their members, limit

FIGURE 1

Water Replenishment District of Southern California



Source: Water Replenishment District of Southern California.

Types of entities that hold the rights to pump groundwater:

- Cities
- Water companies
- Water districts
- Businesses
- Schools
- Cemeteries
- Churches
- Individuals

groundwater extraction, and create a means to provide groundwater-pumping rights to users who lacked access to other water supplies. At about the same time, a number of local entities with an interest in groundwater went to court seeking specific assignments for groundwater rights, which are property rights that can be bought, sold, or leased. In 1961 and 1965, the court awarded groundwater rights to government agencies, businesses, and individuals. During fiscal year 2002–03, 140 parties to the court judgments held a total of 217,367 acre-feet of water rights in the Central Basin, and 60 parties to the judgments held a total of 64,468 acre-feet of water rights in the West Coast Basin.²

By law, the district has broad authority to carry out its responsibilities, which include purchasing water to replenish the basins, administering clean-water programs, and investing in projects intended to improve the reliable supply of clean water at a reasonable cost. The district annually purchases 100,000 to 200,000 acre-feet of water for spreading over the basins or injecting into seawater barrier wells along the coastline. Spreading is the district’s process of piping water to selected areas in the Central Basin where it gradually soaks into the underlying aquifers. Water injected into barrier wells along the coastline forms a dam of freshwater that keeps seawater from flowing into the groundwater aquifers in areas where groundwater levels have dropped below sea level. Los Angeles County operates the spreading grounds and barrier wells, using water the district provides.

The district also operates several other programs to benefit the basins. Under the authority of 1990 legislation that broadened its mission to include detecting, preventing, and removing contaminants in the groundwater, the district established programs to monitor water quality, treat wellheads, remove contaminants, and mitigate the intrusion of saltwater in coastal areas. In addition, the district is planning programs that are within its statutory authority but fall outside its traditional replenishment role. For example, the district is looking at cost-effective and beneficial uses of available storage space in the basins. According to the district, many groundwater basins

² An acre-foot of water is almost 326,000 gallons, enough to meet the needs of two average families for one year.

currently underutilize their storage capabilities; allowing certain entities to store water in the basins would provide more options during times of shortage or interruption of imported water supplies and would play a vital role in the future health of water supplies in southern California. Currently, the district is involved in a work group made up of the basins' stakeholders, such as its ratepayers, to agree on acceptable methods to maximize groundwater storage, but the outcome of this effort is too early to determine.

THE ECONOMICS OF THE WATER REPLENISHMENT DISTRICT

To fund its operations, the district has statutory authority to set and collect a water replenishment assessment from the government agencies, businesses, and individuals that own or lease water rights (ratepayers) on each acre-foot of groundwater that they pump from the basins. Its primary source of income, the replenishment assessment rate (assessment rate), consists of three major components: funds for replenishment, funds for clean water, and funds for operating costs. As part of the rate-setting process, the district conducts an annual engineering survey to determine the condition of the basins and the amount of groundwater it must replenish each year. The district reports groundwater data annually using the period from October 1 through September 30, known as a water year. The district also determines how much money it needs to fund its programs that protect groundwater quality and to fund its operating costs. The district is required to hold public hearings on its determination of the assessment rate and to have established the assessment rate by its first meeting in May. For fiscal year 2003–04, the district estimates it will collect almost \$30 million from the assessment rate. The district plans to use the funds collected from the assessment rate with other sources of revenue, such as receipts for leasing a water treatment facility, and some reserve funds to finance its \$37.6 million budget.

Even with the assessment rate, the basins are a very economical source of water. For example, for fiscal year 2003–04, the district's assessment rate for groundwater was \$115 per acre-foot. The cost to pump and treat the water to bring it up to drinking-water standards (normally, some treatment is needed) adds slightly to the cost. In contrast, the price for one acre-foot of treated imported water was about \$500, a difference of \$385 per acre-foot.

FINDINGS FROM OUR PREVIOUS AUDITS AND RELATED LEGISLATION

In response to a request from the Joint Legislative Audit Committee for an audit of the district, the Bureau of State Audits (bureau) issued a report in 1999 titled *Water Replenishment District of Southern California: Weak Policies and Poor Planning Have Led to Excessive Water Rates and Questionable Expenses*. We concluded that the district consistently overestimated the amount it needed to collect from ratepayers for replenishment and clean-water programs, maintained excessive cash reserves, and failed to maintain controls over its administrative functions and spending. In 2000, the Legislature passed two bills placing temporary and permanent restrictions on the district's operations. In the first bill, the temporary restrictions, which expired after December 31, 2002, limited the district's ability to raise its assessment rate beyond an annual cap increase and prohibited the district from incurring debt to fund capital improvement projects. The second bill permanently restricted the amount of reserve funds the district can accumulate and revised provisions regarding constructing, leasing, purchasing, or contracting for a capital improvement project. This legislation also imposed requirements regarding district contracts, financial statements, and a water purchasing reserve.

The enacted legislation also required the bureau to perform a second audit, and in May 2002 the bureau issued a report titled *Water Replenishment District of Southern California: Although the District Has Eliminated Excessive Water Rates, It Has Depleted Its Reserve Funds and Needs to Further Improve Its Administrative Practices*. We concluded that the district had eliminated excessive water rates by reducing the assessment rate it charges ratepayers. However, at the same time, the district had depleted its reserve funds to a level that could limit the district's ability to maintain the current quantity of groundwater in the basins. This condition was caused by its lack of a long-term vision of its finances and temporary legislative constraints on its ability to raise funds. We also concluded that the district had not adequately developed processes for planning and implementing its capital improvement projects nor implemented adequate accounting and administrative controls over its operating expenses. In Appendix A we present the recommendations from our 2002 audit and our assessment of the district's efforts to implement changes in its practices.

Recognizing that our May 2002 report identified weaknesses in the district's strategic and capital improvement program, the Legislature enacted statutes in September 2002 requiring the district to develop a five-year capital improvement plan and temporarily creating the technical advisory committee (committee). The committee, comprising six district ratepayers, is responsible for consulting with the district to evaluate projects proposed by the district, including capital improvement projects, and making recommendations to the board. Further, the legislation requires the committee to establish criteria for construction of projects intended to improve water quality. The enacted legislation also requires the bureau to perform this third audit of the district.

SCOPE AND METHODOLOGY

The California Water Code, Section 60233.5, requires the bureau to perform an audit of the district's operations and management. To implement this broad mandate, we focused on the recommendations from our May 2002 report and the legislation that enables the district to administer its water quality and replenishment responsibilities.

To understand the steps the district took to implement the recommendations from our 2002 report and to comply with the requirements of the law, we interviewed district employees. We also interviewed members of the West Basin and Central Basin water associations to gain perspective from the ratepayers on the district's progress in correcting prior deficiencies in its policies and planning.

To evaluate the reasonableness of the district's reserve-funds and stored groundwater policies, we reviewed the assumptions the district used to determine its needs and the documents that supported its assumptions.

To determine whether the district set its assessment rate at an amount that meets its needs, we reviewed and evaluated the district's calculation of its fiscal year 2003–04 assessment rate, which included reviewing the district's budget to determine if it supported its spending needs and ensuring that the district tied its water purchase needs to its spending plan.

We also evaluated the district's newly adopted procedures for budget preparation to determine if the procedures incorporated elements we recommended in our 2002 audit report, including the following:

- An explanation for how managers can use historical cost information as a tool to evaluate their cost estimates.
- Guidelines defining the sort of information that can serve as a reasonable rationale for budget line items.
- A method for properly allocating overhead to programs and projects and for properly identifying costs for replenishment and clean-water programs and projects.
- Guidelines for appropriately classifying expenses for noncapital and capital projects.
- Guidelines for creating a central budget file containing the supporting documentation used to arrive at the estimates for budget line items.

To evaluate how effectively the district plans programs and capital improvement projects, we reviewed its strategic and capital improvement plans and the district's efforts to collaborate with ratepayers in its planning process.

To determine if the district took steps to better control its administrative costs, we evaluated whether it developed policies that, among other things, delegated spending authority and provided better guidance to district staff on allowable and unallowable expenses and reimbursable lodging expenses. We selected and reviewed a sample of 57 payments for services and supplies and reimbursements to employees during 2003 to determine whether the district is prudently controlling its administrative expenses.

Finally, we reviewed the district's efforts to improve its controls over contracting by evaluating revisions to its administrative code and determining if the revisions ensured that the district is maintaining the proper level of control over the services it receives from various consultants. We also assessed if the district assigned contract managers to monitor contractors' performance and if the district implemented procedures to periodically evaluate contracts that require fixed monthly fees to ensure that

it receives services in keeping with the fees it pays. We reviewed a sample of 10 contracts approved or active during 2003 to determine if the district's contract management had improved. ■

CHAPTER 1

The District Has Adopted Policies for Its Reserve Funds and Stored Groundwater Quantities but Continues to Deplete Its Reserve Funds

CHAPTER SUMMARY

As recommended in our 2002 audit report, the Water Replenishment District of Southern California (district) has established policies related to its reserve funds and groundwater reserves.³ However, the district's actions have undermined the credibility of its reserve-funds policy, which calls for a minimum reserve of \$18.4 million, more than double the \$7 million reserve funds present on June 30, 2003. Despite this policy, the district set its fiscal year 2003–04 assessment rate at a level that will not fully cover this year's expenses and further depletes its existing reserve funds to a projected \$3.5 million by June 30, 2004, causing us to question its commitment to the policy. Without a sound reserve-funds policy, the district cannot be sure it has sufficient funds to meet its statutory responsibility of ensuring an adequate supply of safe groundwater. Further, the \$18.4 million reserve-funds minimum is likely overstated because of some faulty assumptions the district used to calculate the funds it requires. Finally, although the amount of the planned reserve funds exceeds a statutory limit of \$10 million, the district is not currently seeking legislation to change the limit.

Unlike its calculation of the reserve-funds policy, the district used a reasonable method to develop the optimum and minimum quantities for its policy on groundwater reserves. However, the district is currently discussing with a work group a variety of programs to store surplus surface water in the basins for future withdrawal and use. Although such programs could change how the basin's storage space is used, it is too early to evaluate the outcome of these discussions.

³ In this report, the term *reserve funds* refers to the district's current net assets, or current assets less its current liabilities, that are not legally restricted.

THE DISTRICT'S RESERVE-FUNDS POLICY LACKS CREDIBILITY

In March 2003, to ensure adequate funds to meet its statutory responsibilities, the district adopted a policy that targets a minimum of \$18.4 million and a maximum of \$28.9 million in reserve funds. However, since that time, the district has allowed its already depleted reserve funds to decline by adopting an assessment rate that is insufficient to cover its expenses, bringing into question the district's commitment to its policy. Further, we question the amount of the reserve itself, which is based on some faulty calculations and assumptions and considerably exceeds a statutory limit of \$10 million. By failing to establish appropriate targets for its reserve funds and an adequate assessment rate to maintain the minimum level, the district will face one of two problem situations: If the reserve-funds target is too high, the district will charge its ratepayers an inflated assessment rate to increase its reserves. If the reserve-funds target is too low, the district may not be able to ensure that it will continue to meet its statutory responsibilities.

The District's Actions Are Inconsistent With Its Reserve-Funds Policy

The district's reserve-funds policy establishes the minimum reserve-funds level at \$18.4 million, which equals 50 percent of the district's operating budget; the maximum reserve-funds level of \$28.9 million equals 85 percent of the district's operating budget. According to its reserve-funds policy, the district will evaluate the policy annually when preparing its budget and its engineering survey report with the goal of eventually reaching the necessary balance of reserve funds. However, after adopting the reserve-funds policy, the district set its assessment rate at a level that neither covers its expenses nor provides additional funds to increase reserve funds. As a result, the district's reserve funds, at \$7 million as of June 30, 2003, will drop to an estimated \$3.5 million by June 30, 2004. Although the district would not be expected to replenish its reserve funds in a single year, by acting contrary to its new reserve-funds policy, the district shows a lack of commitment to maintaining reserve funds at the targets set by that policy. Also, by setting its assessment rate at a level that further depletes its reserve funds, the district might not have sufficient reserve funds to meet unforeseen occurrences that could threaten the groundwater supply.

As a result of setting its fiscal year 2003–04 assessment rate at a level that neither covers its expenses nor provides additional funds to increase its reserve funds, the district's reserve is expected to drop from \$7 million on June 30, 2003, to a projected \$3.5 million by June 30, 2004.

Following our 1999 audit report, the Legislature passed laws limiting the amount of the district's reserve funds to \$10 million but allowing the district to adjust the amount in subsequent years to reflect changes in the annual cost of the district's water purchases. The new legislation also temporarily limited the amount the district could raise its assessment rate to 5 percent annually. By the time we conducted our second audit in 2002, the district had allowed its reserve funds to decrease from a high of \$67 million in 1998 to a projected amount of slightly more than \$6 million by June 30, 2002. It did this by significantly lowering its assessment rate from a high of \$162 per acre-foot in fiscal year 1996–97 to a low of \$112 per acre-foot in fiscal year 2001–02, and significantly accelerating its spending for capital improvement projects beginning in fiscal year 1998–99. Because the lower assessment rate did not generate sufficient revenue to cover all of its operating costs, the district used reserve funds to pay the shortfalls. Concerned that the restriction on the district's ability to raise its assessment rate could hinder its ability to recover from past financial decisions and affect its future plans, we recommended the district adopt a minimum reserve-funds policy.

After following our recommendation and adopting a reserve-funds policy on March 17, 2003, the district prepared to set its fiscal year 2003–04 assessment rate. In a preliminary cost estimate that included funding for certain capital improvement projects, district staff submitted four proposals with assessment rates ranging from \$115 to \$165 per acre-foot. Even at the highest proposed assessment rate of \$165, the district planned to use \$1.8 million of its reserve funds, although at the high rate, the district did not plan to issue debt to finance capital projects. Ultimately, believing that the lower assessment rate was adequate to meet its needs, the district adopted a final assessment rate for fiscal year 2003–04 of \$115 per acre-foot. At this assessment rate, the district also proposed using \$1.8 million in reserve funds but planned to delay some capital improvement projects and proposed debt financing for others. Consequently, the district projects that it will have reduced its reserve funds to \$3.5 million by June 30, 2004, about one-third the maximum currently allowed by the California Water Code (water code) and a fraction of the \$18.4 million the district's reserve-funds policy targets as a minimum.

The district projects it will have reduced its reserve funds to \$3.5 million by June 30, 2004, about one-third the maximum currently allowed by the water code and a fraction of the \$18.4 million the district's reserve-funds policy targets as a minimum.

According to the district's general manager, the long-term goodwill the reduced assessment rate created with the ratepayers was more important to the district than the benefits of increasing the rate. The general manager also stated that

the amount was sufficient to accomplish the projects and programs the district considered priorities. Nonetheless, by failing to implement its new reserve-funds policy when setting its assessment rate for fiscal year 2003–04, the district showed a lack of commitment to its policy. Following the completion of our fieldwork for this audit, the district set its assessment rate for fiscal year 2004–05 at \$128.25 per acre-foot, an amount the general manager asserts will not further deplete the district’s reserve funds. We did not review the new assessment rate. However, unless the new assessment rate not only covers its fiscal year 2004–05 expenses but also begins to replenish the depleted reserve funds, we continue to question the district’s commitment to its new reserve-funds policy.

The District Used Some Flawed Assumptions to Calculate Its Reserve-Funds Policy

Our review shows the district may need to reevaluate some assumptions it used to calculate its reserve needs. The district established six separate categories, shown in Table 1, to account for its reserve funds. For the operating and the overdraft

TABLE 1

The District’s Reserve-Funds Policy by Purpose

Category*	Description	Minimum Fund Balance Needed (in Millions)	Maximum Fund Balance Needed (in Millions)
Water purchase	Carryover unused funds the district budgeted to purchase water from the current year to the ensuing year.	\$ 4.5	\$ 6.3
Operating	Cover 30 to 60 days of its operating needs during those times when cash outflows are greater than its cash inflows.	2.8	5.5
Overdraft reduction	Purchase excess replenishment water when offered at a lower rate.	6.0	12.0
Capital replacement	Replace worn-out equipment for its capital project facilities, as needed.	1.2	1.2
Emergency cleanup	Promptly respond to groundwater contamination in the basins, if needed.	0.8	0.8
Rate stabilization	Meet year-to-year fluctuations in operating requirements with little or no effect on the assessment rate.	3.1	3.1
Totals		\$18.4	\$28.9

* Listed in order of the district’s priorities, from highest to lowest.

reduction categories, the district used assumptions that inflate the needed amounts. Overdraft reduction is adding groundwater to reduce the difference between the historical high and the current water level. By using more reasonable assumptions for the two categories, the district would need \$2.1 million to \$4 million less for the operating category and \$3.5 million less for the overdraft reduction category.

The district describes its operating reserve funds as the amount needed to cover 30 to 60 days of its operating expenses when its cash outflows are greater than its cash inflows. The district based its calculation of operating reserve funds on total budgeted expenditures for fiscal year 2002–03 of \$35 million, which included \$25 million earmarked for water purchases. Consequently, the district calculated operating reserve funds ranging from \$2.8 million for 30 days to \$5.5 million for 60 days of operations. However, the district already considered fluctuations or uncertainties in its water purchases by including reserve funds to cover these situations in two other categories: overdraft reduction and rate stabilization. Therefore, we believe the operating reserve funds should not have included water purchases. Using the district’s projected expenses minus water purchases, we calculated that the district’s operating reserve funds ranged from \$800,000 for 30 days to \$1.6 million for 60 days. Moreover, because the district could potentially hold a minimum of \$15.6 million and a maximum of \$23.4 million in its other reserve-funds categories, the district should already have enough in reserve funds to cover shortfalls in cash flow.

By using the optimum water level, instead of the historical high, to calculate the reserve funds for overdraft reduction, the district would reduce the reserve-funds amount from the current calculation of \$6 million to \$2.5 million.

To calculate reserve funds for overdraft reduction, the district determined how much it would need annually over the next 20 years to purchase enough water to bring basin levels up to their historical high. It used the historical high instead of the lesser optimum level set by its policy on stored groundwater quantities because in March 2003, when the district adopted the reserve-funds policy, it had not yet established the optimum level. The district established the optimum level of stored groundwater on June 18, 2003. However, using the historical high as the basis for calculating reserves for overdraft reduction seems unreasonable given the district’s belief that bringing the basins up to that level would result in excessively high water levels that could have adverse consequences. Instead, it would be more reasonable to establish the reserve for overdraft reduction using the optimum level adopted by the district a few months after it established its reserve-funds policy. By using the optimum water level instead of the historical high, to calculate

the reserve funds for overdraft reduction, the district would reduce the reserve-funds amount from the current calculation of \$6 million to \$2.5 million. We discuss the optimum level of stored groundwater in more detail later in this chapter.

As previously stated, the district established a reserve for the rate stabilization category to ensure that it has sufficient funds to meet year-to-year fluctuations in operating expenses with little or no effect on the assessment rate. In addition, to compensate for any unforeseen increase in the cost of water, the district could use the rate stabilization reserve rather than increasing the assessment rate. However, although the entities that hold groundwater-pumping rights are the prime beneficiaries of rate stabilization, two water associations—the Central Basin Water Association and the West Basin Water Association—representing 79 percent of the water rights in the basins believe there is no justification for the district to maintain reserves, including a reserve to stabilize their rates. Therefore, although we believe the district should maintain an appropriate reserve, it should also consider the two water associations' perspectives.

The district's calculation of its reserve needs for water purchases and emergency cleanups appeared reasonable. Further, we found only minor problems with the district's assumptions in calculating its reserve needs for capital replacements.

The Minimum Reserve-Funds Balance Set by District Policy Exceeds the Statutory Limit

Although its policy calls for a minimum of \$18.4 million in reserve funds, state law limits the district's reserve-funds balance to \$10 million.

Although the district's policy calls for a minimum of \$18.4 million in reserve funds, state law limits the district's reserve-funds balance to \$10 million and permits annual adjustments that can only reflect changes in the annual cost of the district's water purchases. As discussed earlier, the district may have overestimated its minimum reserve funds needs; however, the district remains limited to the reserve cap the water code establishes. By not establishing its reserve-funds policy at an appropriate level, the district risks either charging its ratepayers an inflated assessment rate to raise its reserve funds too high or being unable to ensure that it can meet its responsibilities because reserve funds are too low. State law also requires that the district earmark 80 percent of its reserves for water purchases, with the remainder for all other purposes, yet its reserve-funds policy does not provide for this earmarking of reserves for water purchases. In February 2003, the district pursued changes in legislation to establish a reserve fund in

an amount not to exceed \$15 million, but the legislation did not pass. The district can only exceed the current legal cap on reserve funds by asking the Legislature to raise the cap. The general manager says the district intends to seek changes in the next legislative session and will base its reserve levels on amounts needed to support its capital improvement plan.

THE DISTRICT HAS ADOPTED A POLICY ON OPTIMUM AND MINIMUM QUANTITIES OF STORED GROUNDWATER

Our review of the district's new policy that establishes an optimum and minimum quantity of stored groundwater in the basins found the policy to be reasonable.

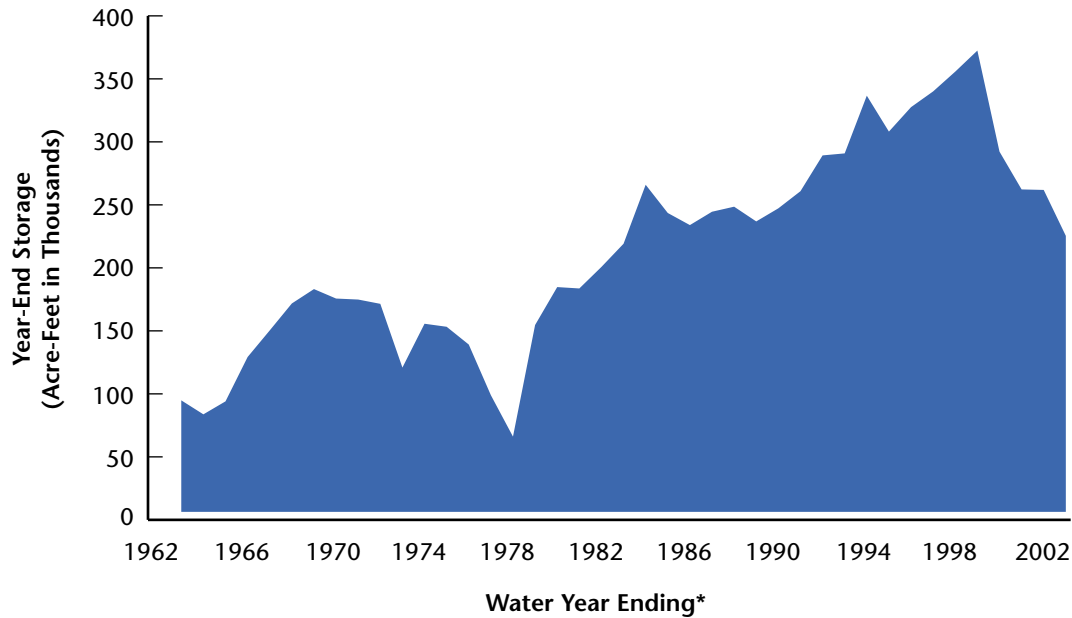
Our review of the district's new policy that establishes an optimum and minimum quantity of stored groundwater in the basins found the policy to be reasonable. Currently, the district and a work group are reviewing a variety of programs to add water beyond the optimum level by storing surplus surface water in the basins for future withdrawal and use. Such storage innovations have the potential to benefit all basin users, but it is too early to evaluate that potential.

In our 2002 audit report we noted that the quantity of stored groundwater declined by more than 110,000 acre-feet between October 1998 and September 2001. With a primary objective of ensuring an adequate supply of groundwater, the district's greatest expense is purchasing water to replenish the basins. The district's 2003 annual engineering report shows that the quantity of stored groundwater declined by more than 147,000 acre-feet between October 1998 and September 2002, eroding about 40 percent of the progress made in replenishing the basins since 1962, as shown in Figure 2 on the following page.

In our 2002 report we found that despite a decline in stored groundwater and an increase in use, the district had not set optimum and minimum quantities of stored groundwater to ensure an adequate supply to basin users. Strategically important, an optimum groundwater quantity gives the district a clear objective for making decisions on various issues, such as water purchases and assessment rates. A minimum groundwater quantity provides the district with an early alert when usage and replenishment factors combine to stress the condition of the basins. Moreover, without targeted levels for groundwater quantities, the district cannot fully justify its planned water purchases.

FIGURE 2

**Changes in Stored Groundwater in the West Coast and Central Basins
1962 Through 2002 (as of June 2003)**



Source: Water Replenishment District of Southern California.

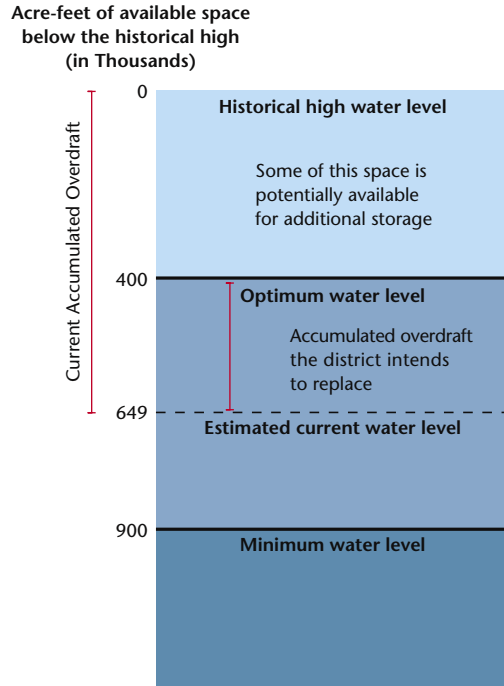
* A water year is the period from October 1 through September 30.

As our 2002 report recommended, the district has established optimum and minimum quantities of stored groundwater, as shown in Figure 3. The district measures the basin's water level against a 1904 historical high and refers to the difference between the historical high and the current water levels as the accumulated overdraft. The district established the optimum level of stored groundwater at 400,000 acre-feet below the historical high and the minimum level at 900,000 acre-feet below the historical high. As of 2002, the quantity of stored groundwater in the basins is 649,000 acre-feet below the historical high, but the district plans to replenish the basins only to the optimal level of 400,000 acre-feet below rather than at the historical high.

The district set its optimum level to provide enough groundwater in the basins to meet the pumping demands that users would make during a major three-year drought without falling below its minimum level. By using this assumption, the district told us it is establishing its optimum and minimum quantities of stored water at a conservative level. The district's

FIGURE 3

**Groundwater Storage Space in the
West Coast and Central Basins
as of June 2003**



Note: Total pumping allowed by court judgments is about 282,000 acre-feet per year, which is approximately 52 percent of natural replenishment.

engineering survey report showed that in the last 41 years, a major three-year drought resulting in a 500,000 acre-foot water loss has not occurred. The amount of water stored in the basins has decreased by only 65,450 acre-feet in the last 10 years. However, according to the district, the availability of imported water in the future is uncertain due to reduced imports from the Colorado River and increased demand. Therefore, it is appropriate for the district to be conservative in ensuring that water resources are available during drought years.

Between the basins' optimum level and the historical high is potential space to store additional water. The district is currently discussing with a work group a variety of programs allowing the storage of surplus surface water in the basins for future withdrawal and use. The district would obtain the additional water from seasonally available surplus water. Comprised of the district and representatives from various rate-paying communities the district serves, such as major cities and public

and private water agencies, the work group wants to maximize all available sources of water, including surface and underground water, by having all those involved in the discussions reach an agreement on issues including underground water storage. This agreement may allow other entities, including the district's ratepayers, to store surplus surface water in the groundwater basins to meet increasing water demands or use the water during periods of drought. Consequently, the entire region could benefit from groundwater storage by having water stored for future use.

RECOMMENDATIONS

To ensure that the district has sufficient funds to meet its statutory responsibilities and to show its commitment to its reserve-funds policy, the district should do the following:

- Set its assessment rate at a level that will support the district's planned activities and allow it to replenish its reserve funds, if necessary, and keep them at an appropriate level.
- Reevaluate the assumptions that underlie the amount it targets to have available as reserve funds and, if necessary, seek legislative approval to revise the amount allowed as reserve funds. ■

CHAPTER 2

Some Key Information Is Missing From the District's Strategic and Capital Improvement Plans

CHAPTER SUMMARY

To further its mission of managing groundwater in the West Coast and Central basins (basins), the Water Replenishment District of Southern California (district) is authorized to charge a replenishment assessment rate to the entities and individuals that pump groundwater (ratepayers), and use the assessments to establish various water programs and build capital improvement projects. In previous reports, we recommended the district develop and update strategic and capital improvement plans to identify and prioritize projects that further the district's mission and to identify the funding sources and scheduling for the infrastructure required. On September 3, 2003, almost four years after we first made our recommendations, the board adopted a strategic plan. However, the district continued to present the strategic plan to the public as a draft because it intended to update the project and program list after completing the capital improvement plan and obtaining approval from the district's board of directors (board). The board adopted the capital improvement plan on May 3, 2004.

We reviewed the district's strategic and capital improvement plans and found that the district could improve both of them. Specifically, although the strategic plan includes goals and objectives, it does not provide outcomes by which to measure the district's progress in meeting its goals and objectives. The district's capital improvement plan includes the funding needs and scheduling of the district's proposed projects as recommended, but it does not prioritize projects to identify those it believes it should complete first or identify alternative funding sources for the projects in addition to issuing bonds.

As required by state law, a technical advisory committee (committee), made up of six individuals representing the ratepayers, has consulted with the district in evaluating its capital projects. However, although the committee has developed a process for reviewing and approving the district's

capital improvement projects and a procedure to periodically update the capital improvement plan, the district has not yet had the opportunity to implement the updating procedure. Currently, the statute requiring the committee sunsets on January 1, 2005. According to the district's general manager, the district intends to revise its administrative code to make the committee part of its process for reviewing and approving capital improvement projects. However, if the district fails to do so and the statute sunsets, ratepayers may lose important opportunities to provide input to the district on future capital projects and during the district's process for periodically updating the capital improvement plan.

STRATEGIC AND CAPITAL IMPROVEMENT PLANS ARE ESSENTIAL TO GUIDE THE DISTRICT IN ACHIEVING ITS MISSION

The district's stated mission is "to provide, protect, and preserve high-quality groundwater through innovative, cost effective and environmentally sensitive basin management practices for the benefit of residents and businesses of the West Coast and Central basins." In response to 2002 legislation that requires the district to develop a five-year capital improvement plan, the district developed and its board adopted strategic and capital improvement plans.

A strategic plan specifies the goals and strategies that further the district's mission; a capital improvement plan identifies the funding sources and scheduling for the infrastructure required to support the strategic plan.

A strategic plan specifies the goals and strategies that further the district's mission. Ideally, a strategic plan should also describe the processes, skills, technologies, and various resources the district will use to achieve its goals and objectives. Finally, it should include measurable outcomes for the district and the public to use to assess the district's progress in achieving its goals and objectives.

A capital improvement plan identifies the funding sources and scheduling for the infrastructure required to support the strategic plan. Identifying any long-term projects the district is planning to build, the capital improvement plan should provide a framework for prioritizing projects and describe potential funding sources and financial constraints that could affect the projects' viability. The capital improvement plan can also be an important tool for giving ratepayers a clear view of the district's long-term direction and a better understanding of the district's needs for revenue to fund capital improvement projects.

MORE THAN FOUR YEARS AFTER OUR INITIAL RECOMMENDATIONS, THE DISTRICT ADOPTED PLANS THAT NEED IMPROVEMENT

The district's board adopted a strategic plan on September 3, 2003, and recently adopted a capital improvement plan. However, both plans need refinement. The strategic plan does not include outcomes the district could use to measure its progress in meeting its goals and objectives. The capital improvement plan does not identify those projects the district believes it should complete first, possible funding sources available for each project other than issuing bonds, and the projects the district's board has formally approved.

After adopting the strategic plan, the district continued to present it to the public as a draft because, according to the district's general manager, the district wanted to update the project and program list in the strategic plan after the district had completed and the board had adopted the capital improvement plan. Nine months later, on May 3, 2004, the board adopted the district's capital improvement plan—more than four years after we first recommended it do so. The district then updated the project and program list in its strategic plan to reflect the capital improvement plan, and according to the general manager, the district now considers the strategic plan finalized.

The District's Strategic Plan Does Not Specify Measurable Outcomes

The district's strategic plan includes goals and objectives, but lacks outcomes by which to measure the district's progress in meeting them.

Developed with input from its stakeholders, the strategic plan the board adopted in September 2003 appropriately includes goals and objectives; however, it lacks outcomes by which to measure the district's progress in meeting those goals and objectives. Without measurable outcomes, the district and the public cannot assess the district's progress in achieving its goals and objectives or assess whether the resources allocated to priority projects is sufficient.

The district included its stakeholders in the development of the strategic plan. For example, it held two public workshops to allow for input from its ratepayers, and to oversee the process and work with district staff to refine the plan's elements, the board created an ad-hoc committee for strategic planning. The resulting strategic plan appropriately included goals and objectives as well as a list of priority projects and programs the district is considering to meet its goals and objectives.

However, the district could further refine its strategic plan to include outcomes the district and the public could use to measure the district's progress in achieving its goals and objectives. Such measurable outcomes are currently missing from the district's strategic plan. For example, one goal in the strategic plan is "to provide basin replenishment," with an accompanying objective to ensure that water sources are available to replenish the groundwater supply. To achieve that goal, the plan states, recycled water will play a more significant role in future basin replenishment, but the plan does not give any outcomes by which to measure the district's progress in maximizing its recycled water use. To provide a meaningful measure of progress, the plan could specify the amount of the water used for replenishment purposes that the district will get from recycled sources and the period in which it will do so. For example, the measure might say that the district will increase the use of recycled water by at least 25,000 acre-feet by 2007. Then the plan would need to identify the projects or programs the district would use to achieve this goal, such as working with the California Department of Health Services to increase the permit that currently limits the amount of recycled water the district may soak into the underlying aquifers from 50,000 to 60,000 acre-feet per year based on a three-year average.

The District Should Consider Making Some Refinements to the Capital Improvement Plan When Updating It in the Future

In May 2004 the district's board adopted a capital improvement plan. Our review of the district's capital improvement plan revealed that it is missing certain information. First, the district did not prioritize the projects according to their importance in helping the district meet its statutory requirements. Second, the funding portion of the plan does not specify possible funding sources other than issuing bonds. Finally, the capital improvement plan does not identify the projects that the board has formally approved.

On May 3, 2004, the district's board adopted a capital improvement plan, which includes nine projects the district intends to pursue over the next five years.

After the board adopted the district's strategic plan in September 2003, the district began the process of developing a five-year capital improvement plan to further evaluate the costs and benefits associated with the priority projects and programs identified in the strategic plan. On May 3, 2004, the board adopted the district's capital improvement plan, which includes nine projects the district intends to pursue over the

next five years. In addition to a general funding plan for all projects and a timeline for each project that assumes all projects are ultimately funded and approved, the capital improvement plan outlines the associated costs, benefits, and environmental considerations affecting the viability of each project. For six of the nine projects, the plan provides a detailed cost-benefit analysis.

The district did not prioritize the projects in its capital improvement plan, which would provide the district and its ratepayers with a clear view of the long-term direction of the district and a better understanding of its ongoing revenue needs.

All nine projects included in the capital improvement plan were mentioned in the strategic plan as being priority projects. The district's capital improvement plan should have prioritized the projects according to their importance in meeting the district's statutory requirements. However, the district did not identify those it believes it should complete first. Considering its limited resources and the level of debt financing it secures in the future, the district will need to determine which projects to pursue first. Prioritizing the district's projects would provide the district and its ratepayers with a clear view of the long-term direction of the district and a better understanding of its ongoing revenue needs.

Further, although the plan indicates that the district is considering issuing bonds to fund its capital expenditures, its funding plan does not provide information on other possible funding sources. For example, district staff indicated in a memo to the district's board that the district might be able to obtain federal funding to use in its expansion of the Leo J. Vander Lans Water Treatment Facility, one of the projects included in the capital improvement plan. Although the capital improvement plan contains a general reference to these federal funds in the section discussing the costs of this expansion, it does not identify the amount it could receive nor is this information included in the section identified as its funding plan.

Additionally, the capital improvement plan does not distinguish between projects the board has formally approved and those it has not approved. In fact, the board has formally approved only two of the nine projects included in the plan—the Safe Drinking Water Program and the San Gabriel River Rubber Dams. According to the district, the board's approval of the capital improvement plan does not constitute approval of the projects specified in the plan, and final board approval is needed before beginning construction on each project. However, to ensure that it fully discloses this information to its ratepayers, the district should clearly identify the board-approved projects in the capital improvement plan.

THE TECHNICAL ADVISORY COMMITTEE'S EVALUATION OF CAPITAL IMPROVEMENT PROJECTS IS INCOMPLETE

As a result of disputes between the district and its ratepayers about a long-range plan for managing the basins' resources, the Legislature authorized a committee to consult on projects proposed by the district, including but not limited to, capital improvement projects. Although the committee has completed an initial review of the district's proposed projects, it did not make a final ruling on all of them. In addition, the district has not implemented the procedure for updating the capital improvement plan that the committee and the district have been working on.

The committee's six members, appointed by both the Central Basin and West Basin water associations, are responsible for making recommendations to the board and establishing criteria relating to the construction of projects intended to improve water quality. Although the board is not required to follow the committee's recommendations, the committee gives the district's ratepayers an official forum to provide input on the district's activities and their impact on the basins.

As required by statute, the committee, in cooperation with district staff, developed a process for reviewing and approving the district's capital improvement projects, including assessing the technical, legal, and financial risks associated with each project. In March 2004, the committee completed its initial review of 11 capital projects, approving four projects, conditionally approving one, not approving one, and deferring its ruling on five.

Although the statutes also require the district to consult with the committee to implement a procedure to periodically update its capital improvement plan, the district has not yet had the opportunity to implement the updating procedure. The statute that requires the committee will sunset on January 1, 2005; however, according to the general manager, the district intends to revise its administrative code to ensure that the committee remains a part of its process for reviewing and approving its capital improvement projects. If the district does not do so and the statute sunsets, ratepayers may lose important opportunities to provide input to the district on future capital projects and during the district's process for periodically updating the capital improvement plan.

The statute that requires the technical advisory committee will sunset on January 1, 2005.

RECOMMENDATIONS

To ensure that the district and the public can assess the district's progress in achieving the goals and objectives described in its strategic plan, the district should refine its plan to include measurable outcomes.

To make its capital improvement plan more informative to the district and its ratepayers, the district should consider doing the following when it updates its capital improvement plan:

- Rank projects by their importance to identify the projects it believes it should complete first to meet its statutory requirements.
- Include alternative sources of funding for the projects in addition to issuing bonds.
- Distinguish between board-approved projects and proposed projects.

To ensure that the district continues to collaborate with ratepayers on projects, it should pursue its plan to revise its administrative code to make the technical advisory committee part of its process for reviewing and approving capital improvement projects. If the district fails to implement this recommendation, the Legislature should consider extending the committee at least until the committee has had the opportunity to participate in the process of periodically updating the district's capital improvement plan. ■

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CHAPTER 3

Although the District Has Improved Its Accounting and Administrative Controls, Some Problems Remain With Purchases, Reimbursements, and Contracts

CHAPTER SUMMARY

In response to our previous audits, the Water Replenishment District of Southern California (district) amended its policies to enhance its accounting and administrative controls. However, it could further strengthen its controls over spending on goods and services as well as reimbursements to staff, consultants, and members of the district's board of directors (board). Tighter controls over incurred costs are necessary to ensure that the district uses public funds properly. By improving and following its policies, the district could better control its costs and earn the trust, confidence, and support of ratepayers.

Despite improving its administrative policies to include more detailed guidance on allowable expenses and reimbursements, the district has not consistently followed the policies. For example, the district purchased gifts, which its administrative code does not allow, and did not obtain the appropriate approval for some purchases as required by its purchasing policies. The district also lacks sufficient control over reimbursements to its staff and board members because its policies do not require staff to match approved travel documents to expense claims, to ensure the district does not duplicate payments for travel expenses. Additionally, directors do not always use the business expense form the district developed to ensure reimbursable costs are for the district's public purpose.

The district also instituted controls to ensure that costs it incurs are reasonable and necessary; nevertheless, the district incurred a number of costs in 2003 that do not appear to be the most prudent use of its funds, especially in light of its decreasing reserve funds and its commitment to keeping the replenishment assessment rate at a lower level. For example, the district spent about \$1.19 million in legal costs but has not performed a detailed review of its legal services since 2000. Also, other

costs the district incurred—such as \$17,500 for catered meals, snacks, and beverages and \$23,000 for one director to attend 17 conferences in one year—may not be the most prudent use of public funds.

Further, even though the district made some improvements to its contract management practices, the district needs to make an additional refinement to ensure that it pays only for services it actually receives. Although the district entered into agreements with four legislative advocacy firms for fixed monthly fees of up to \$10,000 per month, it did not require the consultants to submit written monthly reports detailing their activities.

DESPITE AMENDING ITS POLICIES, THE DISTRICT COULD FURTHER TIGHTEN ITS CONTROLS OVER PURCHASES AND TRAVEL REIMBURSEMENTS

Since our last audit, the district strengthened its purchasing procedures but could add further controls over purchases of goods and services as well as over reimbursements to its staff, consultants, and board members. Our review of 40 vendor payments and 17 employee reimbursements during 2003 revealed that the district did not always follow its purchasing policies, making purchases not allowed under its administrative code or not approved by appropriate staff. The district could also provide better guidance on procurement, particularly for purchases that seem excessive or not the best use of the district's funds, by modifying its administrative code and accounting procedures to limit or prohibit certain purchases.

The District Has Established Purchasing Procedures but Has Not Adequately Enforced Them

The district amended its administrative code in January 2003 to provide better guidance to staff on allowable and unallowable expenses. However, because the district does not always follow its policies, it incurs costs that may not further its public purpose. We reviewed 57 district payments to employees and vendors and found that, in violation of its own code, the district has purchased gifts and paid for questionable telephone expenses. Also, the district has not always followed its cash disbursement and purchasing procedures, failing to properly approve eight of the 57 payments.

Our review of 57 district payments to employees and vendors found that, in violation of its own code, the district has purchased gifts and paid for questionable telephone expenses.

In January 2003, the district adopted revisions to its administrative code that specifically prohibit gift purchases. However, our sample of 40 vendor payments during 2003 showed that for three of these payments, the district spent a total of \$194 on flowers and gifts for a director and a person who was not an employee. Although the district said one of the board's directors instructed staff to make some of these purchases, the district's administrative code clearly states that neither employees nor the district's board should obligate the district for any unallowable expenses, such as gifts. We believe these payments are gratuities and thus may be an unconstitutional gift of public funds.

The district further amended its administrative code in February 2003 to provide a \$200 monthly communications allowance for the directors. According to the administrative

Our review of 57 payments the district made during 2003 to vendors and employees revealed the following weaknesses:

- Two payments were for employee reimbursements that an authorized person had not approved.
- Three payments were for invoices that an authorized or responsible person had not approved.
- Three payments were for purchases that were not approved in advance.
- Four payments were for goods that the district's administrative code prohibits.
- Five payments included reimbursements of telephone calls to directors who already received a communications allowance.

code, the communications allowance covers equipment and services such as cellular phones, cellular service, and fax machines. It also states that directors are to use this allowance in lieu of payment or reimbursement for any telephone calls, Internet fees, or similar expenditures. Nevertheless, the district reimbursed or paid \$921 in 2003 for telephone calls directors made when they were traveling on district business, even though these directors also received the \$200 monthly communications allowance. District staff stated that the communications allowance does not apply to telephone calls the directors make when traveling because cellular connections may be poor outside of the local area. However, the administrative code does not specifically address reimbursements for telephone calls when traveling; rather, it clearly states that directors may choose to receive either a flat monthly communications allowance or reimbursement for

actual communications expenses incurred in connection with district business.

In our 2002 report we noted that the district lacked written accounting procedures to govern cash disbursements and purchasing. Although the district has since adopted procedures, it does not follow them consistently, thereby diminishing their value. During our review of 57 of the district's payments, the district did not appropriately approve eight of the payments. For example, the district reimbursed an employee \$333 for medical expenses without

obtaining the approval of the district's general manager, as required by the district's administrative code. Also, the district reimbursed its general manager almost \$100 for meals purchased for district staff and consultants, even though the payments were not properly approved by the finance committee. The administrative code requires that the finance committee approve meals purchased by a district employee for other persons as long as the meals further the district's business.

For three payments totaling \$6,425, the district did not obtain the appropriate approval until after the purchase was made or the goods were received.

Finally, the district's purchasing guidelines require that staff obtain certain approvals before making purchases exceeding \$250. However, the district did not always follow this policy. In fact, for three payments totaling \$6,425, the district did not obtain the appropriate approval until after the purchase was made or the goods were received. When staff fail to follow these guidelines, which are in place to ensure that funds are used to further the district's purpose, the district cannot be certain the purchases are appropriate.

The District's Administrative Code Could Provide Better Guidance on Reimbursements

Other inappropriate payments result from weaknesses in the district's accounting policies. Although it amended policies related to reimbursements since our 2002 audit, the district could set stricter controls over reimbursements to staff, consultants, and board members, particularly for travel costs. As we mentioned in our 1999 and 2002 audit reports, the district's accounting policies do not require staff to match approved travel documents to expense claims filed by board members or district staff. Adding this requirement to the process of reviewing expense claims is a simple control to ensure that the district pays only for authorized travel and does not duplicate payments. However, the district never addressed our concerns by revising its accounting policies or its administrative code. Absent an adequate review policy, the district reimbursed one director twice for a \$550 conference registration fee, as we observed in our sample of 17 employee reimbursements. After we notified the district of this error, it was corrected, but such oversight could be easily prevented by accounting controls. Although the district states it reconciles travel documents with expenses for district staff, we could not locate that procedure in the district's accounting policies, nor did we find evidence that the district performs a similar reconciliation process for directors' travel expenses. According to the district's general manager, when directors travel out of state, staff attach a

copy of the board minutes that shows the board approved the travel as support for the travel reimbursements. However, we did not see this attachment when we found out-of-state travel reimbursements for directors in our sample. Also, the district's informal procedure does not apply to in-state travel costs that do not require advance board approval.

The district's board members do not consistently use the business expense form, which the district developed to ensure that out-of-pocket expenses are business related or benefit the district's public purpose.

According to district policy, costs its directors and staff incur must be reasonable and necessary. To ensure that out-of-pocket expenses are business related or benefit its public purpose, the district developed a business expense form for board members and staff to use when requesting any reimbursement for this type of expense. Although the district's finance committee requested that board members use the form, we found that the directors do not consistently do so. Three of the 17 reimbursements we reviewed related to this issue, and in all three cases, the directors did not complete the expense form for reimbursements totaling \$503, including \$148 for local meals and meetings between two directors or a director and staff. Without these expense forms, the district cannot be sure it has benefited from costs it reimburses.

The District Has Incurred Costs That May Not Be the Most Prudent Use of Its Funds

During our review of the district's administrative costs, we identified various expenses that may not be the most prudent use of the district's public funds, especially given the district's decreasing reserve funds and its desire to maintain a low replenishment assessment rate. Such expenses include those for outside legal services for matters not under litigation, catered meals for staff, uneconomical airfares, and directors' expenses for numerous conferences in one year.

During 2003 the district spent approximately \$1.19 million on its legal costs for contracts with two legal firms that split the district's work according to their expertise and the district's needs. From documentation the district provided, we found that a significant amount of its payments for legal services were for legal advice related to matters not being litigated, such as district projects, contracts, employment, personnel, and administrative code changes. In fact, according to the district, it paid approximately \$618,000 for litigation services and \$571,000 for nonlitigation services. Because the fees for nonlitigation services amount to about 2,075 hours, the district might consider whether hiring an in-house lawyer is more cost-effective. Additionally, the district should perform a detailed

review of its legal costs, which it has not done since 2000. In April 2004, to better manage and reduce the legal fees it pays, the district developed a policy for contacting legal counsel, limiting who can contact legal counsel and requiring staff to use in-house resources first. Although this policy may reduce future costs, a detailed review of the reasonableness of its legal costs would further ensure that the district does not use public funds unnecessarily.

The district used public funds to pay \$2,250 for award dinners hosted by community organizations and more than \$17,500 for catered meals and other snacks and beverages for its staff and others during 2003.

Although the district's administrative code provides some guidance on allowable and unallowable expenses, the guidelines provide significant latitude on the types of expenses that are appropriate. We found that the district used public funds to pay \$2,250 for award dinners hosted by community organizations and more than \$17,500 for catered meals and other snacks and beverages for its staff and others during 2003. Although these types of expenses might be allowed under its administrative code, we question whether the district was prudent when it used its public funds to pay for them. The general manager explained that attending these award dinners enhances the public's awareness of the district's function and that approval of these events is publicly noticed, open for discussion at board meetings, and voted on by the directors. Although we recognize the importance of enhancing the public's awareness of the district's function, we question whether the district could achieve this same purpose without spending funds in this manner. The general manager also stated that because the district hosts lunches for representatives of other water agencies and those districts host lunches when meetings are held at their headquarters, such hospitality is appropriate and costs are not excessive. While acknowledging that these types of expenses may be customary, we question whether the district is using its funds in a responsible manner by providing staff and others with meals, snacks, and beverages at the public's expense.

Moreover, the district incurred unnecessary costs from poor management and planning of its travel needs. According to the district's administrative code, directors are to use the most economical mode and class of transportation consistent with scheduling requirements. However, the district spent more than \$7,000 on economy flights for three directors to travel to Washington, D.C., to meet with legislators, while the combined airfare of the other two directors making the same trip was less than \$800. According to the general manager, the district always

selects the most economical flights given constraints such as the availability of directors to fly from certain airports, to stay over the weekend, and to attend previously scheduled local meetings. However, we believe that it is the responsibility of directors as public officials and as trustees of the district and its revenues to compromise on their preferred itineraries and change travel times or departure sites to achieve the best use of the district's resources.

Finally, the district's overall costs for conferences may be unreasonable. When a director attends a conference, the district pays for the registration fee, transportation, meals, and lodging, and the director receives daily compensation. Some of these costs are fixed amounts; for example, directors were compensated \$170 each day of attendance at a conference in 2003, which increased to \$199 as of December 2003, and up to \$100 each day for breakfast, lunch, and dinner. Other costs such as registration fees, lodging, and transportation are not as limited; for example, conference registration fees in 2003 ranged between \$125 and \$960.

During 2003, four directors attended up to four conferences, whereas one director participated in 17 conferences at a cost totaling more than \$23,000, not including the director's daily meeting compensation.

Despite these costs, the district's travel policies are vague on the number of conferences directors or district staff may attend each year. Our review found that in 2003, four directors attended up to four conferences, whereas one director participated in 17 conferences at a cost totaling more than \$23,000 for meals, lodging, transportation, and registration, not including the director's daily compensation. Although these conferences appeared to relate to the district's purpose, the itineraries for some of the 17 conferences attended by the director revealed some overlap in the topics discussed. The district's administrative code prohibits directors and staff from attending repetitive seminars or educational courses on the same topic or issue but does not limit the number of conferences they may attend. Furthermore, the district spent more than \$800 for one director's four nights' lodging at a conference held only 12 miles from the district's headquarters. Although the district's administrative code allows this type of expense with proper approvals, we question whether this and other conference costs are the most prudent use of the district's funds and believe that the district should consider establishing more specific policies related to conferences the directors and staff may attend. Appendix B summarizes the annual compensation for the district's directors, including reimbursements for conferences.

THE DISTRICT HAS IMPROVED ITS CONTRACT MANAGEMENT PRACTICES BUT CAN IMPROVE IN ONE AREA

The district entered into agreements with four legislative advocacy firms for fixed fees of up to \$10,000 a month for each firm, but did not require the consultants to submit written, detailed monthly activity reports to enable the district to evaluate whether the value received was consistent with fees paid.

Although the district has improved its process for managing contracts, our review of 10 contracts found that it could improve its administrative practices in one area. We found that the district entered into agreements with four legislative advocacy firms for fixed monthly fees of up to \$10,000 a month for each firm, but did not require the consultants to submit written, detailed monthly activity reports to enable the district to evaluate whether the value received was consistent with the fees paid. By not requiring the monthly activity reports, the district is not obtaining documentation of the services it receives to justify the fees it pays.

During 2003 the district paid four legislative advocacy consultants, with each receiving a fixed monthly fee ranging from \$4,583 to \$10,000, plus expenses. The district also includes in one of its legal firm contracts a provision for legislative advocacy services, at the direction of the general manager, at a cost of \$10,000 per month. Our review of these payments revealed that because the district does not require consultants who are paid a fixed monthly fee to submit detailed monthly activity reports, the district has little documentation of what the consultants are actually doing for the district. Although the district incorporated in the legislative advocacy contracts a requirement for monthly reports of the status and progress of the services it receives, these reports may be in either written or verbal form. According to the general manager, its legislative advocacy firms routinely report to the general manager and external affairs staff, often several times a week, on activities they undertake for the district or on developments that affect the district. With this constant communication, the general manager believes the district can make informed decisions to terminate or renew these contracts based on performance. Also, an appropriate staff member approves the invoice before the district pays the firm for its services. Although the district's discussions with these contractors and its approval of the invoices are forms of contract management, these procedures do not provide assurance to those who may scrutinize the district's expenses that the district received services to justify payments in excess of \$272,000 during 2003.

RECOMMENDATIONS

To strengthen controls over its administrative expenses and to ensure that it uses public funds prudently, the district should take the following steps:

- Reaffirm its commitment to following the policies in its administrative code, and ensure that its directors and staff abide by its policies, especially policies defining unallowable purchases such as gifts, use of the communications allowance, and obtaining appropriate approvals.
- Update its accounting procedures to require staff to match travel expenses to approved travel documents.
- Amend its administrative code to require board members and staff to consistently use the business expense form to document the public purpose of any out-of-pocket expenses.
- Perform a detailed review of the reasonableness of its costs for contracted legal services, and consider whether hiring an in-house lawyer is more cost-effective.
- Reassess its use of public funds for such purposes as award dinners, catered meals, high-cost airfares, and lodging for local conferences, and revise its administrative code to limit or prohibit such costs.
- Amend its administrative code to provide better guidance on reimbursable travel expenses, including a limit on the number of conferences directors and staff may attend, and a process for justifying exceptions to that limit.

To ensure that it appropriately manages its contracts for professional services, the district should require contractors to submit detailed, written monthly activity reports for professional services at fixed monthly fees.

We conducted this review under the authority vested in the California State Auditor by Section 8543 et seq. of the California Government Code and according to generally accepted government auditing standards. We limited our review to those areas specified in the audit scope section of this report.

Respectfully Submitted,

A handwritten signature in black ink that reads "Elaine M. Howle". The signature is written in a cursive, flowing style.

ELAINE M. HOWLE
State Auditor

Date: June 9, 2004

Staff: Denise L. Vose, CPA, Audit Principal
Peter A. Foggiato III
Avena DeMesa
Pamela M. Immordino
Erin L. Oviedo

APPENDIX A

Summary of Progress Made by the Water Replenishment District of Southern California Toward Implementing Recommendations From the 2002 Report by the Bureau of State Audits

The Bureau of State Audits (bureau) made a variety of recommendations to the Water Replenishment District of Southern California (district) in its May 2002 report. The following table shows the bureau's recommendations and the district's progress towards implementing those recommendations.

TABLE A.1

Recommendations	District's Progress
<p>The district should adopt a policy on a minimum reserve fund balance that should specify the amount of reserves it requires to meet all of its expenses including those associated with its operations, the stabilization of its assessment rate, its ability to promptly respond to contamination issues, and its ability to repair and replace facilities and equipment.</p>	<p>Partial corrective action taken. As discussed in Chapter 1, the district adopted a policy on minimum reserve funds that addresses the areas specified in the recommendation. However, we question the district's commitment to the policy as well as the amount of the reserve itself, which is based on some faulty assumptions.</p>
<p>If the district determines that it needs more reserve funds than the California Water Code (water code) currently permits, it should consider seeking legislative approval for an increase in the allowed level.</p>	<p>The district pursued a change in legislation in 2003 through Senate Bill 906. However, the bill did not pass. According to the general manager, the district intends to seek legislation in the next legislative session for a level of reserves that will be supported by its capital improvement plan.</p>
<p>To ensure an adequate supply of water for the basins' users, the district should establish an optimum quantity for stored groundwater that can serve as a target for its water purchases. It should also establish a minimum quantity below which it should not allow the basins to fall.</p>	<p>Implemented. As discussed in Chapter 1, the district established 400,000 acre-feet below the historical high as the optimum level and 900,000 acre-feet below the historical high as the minimum level of stored groundwater. The district is currently in discussions with a work group that would allow other entities such as ratepayers to store surplus surface water in the groundwater basins for future withdrawal and use.</p>
<p>The district's board should set the annual replenishment assessment rate (assessment rate) at a rate that will support the district's planned activities and ensure that it maintains the level of reserve funds it needs to meet its statutory responsibilities.</p>	<p>Partial corrective action taken. As Chapter 1 discusses, the district set the fiscal year 2003-04 assessment rate at a level that does not cover its expenses, further depleting its reserve funds. According to the district's general manager, the district set its assessment rate for fiscal year 2004-05 on May 3, 2004, at \$128.25 per acre-foot, an amount that he asserts will not further deplete the district's reserves.</p>

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Recommendations

District's Progress

If the Legislature extends restrictions on the district's ability to raise funds for its operations, capital improvement projects, and reserves beyond December 31, 2002, the district should pursue the following modifications to the restrictions:

- It should request more flexibility in setting its assessment rate to ensure that it is able to replenish groundwater and fund clean water programs.
- It should seek changes in the factor that controls annual rate increases to one more closely linked to the changes in its costs.
- It should seek relaxed prohibitions on debt to allow it to participate in government-operated loan programs.

The Legislature did not extend legal restrictions on the district after they expired on December 31, 2002.

The district should implement comprehensive written procedures for preparing its annual budget. These procedures should include the following:

- An explanation for how unit managers can use historical cost information as a tool to evaluate their cost estimates.
- Guidelines regarding the sort of information that can serve as a reasonable rationale for budget line items.
- An administratively feasible method for properly allocating overhead to programs and projects.
- An administratively feasible method for properly identifying replenishment and clean water program and project costs.
- Guidelines regarding the appropriate classification of non-capital and capital project expenses.
- Guidelines regarding the creation of a central budget file containing the supporting documentation used to arrive at the estimates for budget line items.

Implemented. The district recently adopted written procedures, with all the elements we recommended, for its staff to follow when creating budgets.

To allow for a thorough public discussion of the district's proposed assessment rate, staff should tie the district's spending plan to its calculation of the rate. The district should distribute this presentation to the board for public hearings and should distribute to attendees a presentation that includes, at a minimum, adequate data to support the proposed rate. This data should be drawn from the district's engineering report, proposed budget, and capital improvement plan.

Partial corrective action taken. The district tied its calculation of the assessment rate to its planned spending needs by using its engineering survey report and proposed budget. Additionally, the district held public budget workshops where it distributed presentations that included adequate data to support the proposed rate. However, as Chapter 2 discusses, it did not have a capital improvement plan in place until May 2004. Thus, its proposed assessment rate for fiscal year 2003-04 does not reflect projects that the district would eventually include in its capital improvement plan. However, according to the district, it considered capital improvement projects when setting its fiscal year 2004-05 assessment rate.

To identify the programs and capital improvement projects that will aid it in fulfilling its mission, the district should continue to create an updated strategic plan and capital improvement plan. Specifically, the district should incorporate the following activities in their development:

- It should assess all activities it performs and their priority to the district's role versus those of other water agencies in the region.
- It should ensure that the plans clearly identify which projects are ongoing and prioritize the proposals in the order of importance to meeting the district's statutory requirements.
- It should share with ratepayers the appropriate level of information on proposed programs and projects, including cost and benefit estimates.
- It should adopt a policy to periodically update its strategic and capital improvement plans to ensure that it bases decisions for future projects on appropriate and current information.

Implemented. The district adopted strategic and capital improvement plans. However, as Chapter 2 discusses, both plans need refinement.

Recommendations	District's Progress
<p>The district should establish a standardized approach to evaluating and selecting capital improvement projects. At a minimum, the approach should include the appropriate steps to identify legal, technical, and financial risks of proposed projects.</p>	<p>Implemented. As Chapter 2 discusses, in cooperation with a technical advisory committee, the district adopted a process for evaluating and selecting capital improvement projects.</p>
<p>The district should implement a cost-benefit analysis methodology that (1) defines standards and assumptions to use when evaluating replenishment projects and (2) offers a process for weighing alternative solutions to contaminant mitigation issues.</p>	<p>Implemented. The district has established a method for evaluating cost-benefit analyses, which uses a present-worth analysis on all projects being considered.</p>
<p>The district should quickly define potential resolutions to the water rights issue involving the Goldsworthy Desalter facility (desalter), and it should implement the most suitable solution to put the desalter to work permanently removing the saltwater from the West Coast Basin.</p>	<p>Implemented. The district made modifications to the well at the desalter, which increased chloride levels at the desalter above the minimum the water code requires.</p>
<p>The district should promptly come to agreement with Los Angeles County to resolve the third-party compensation issue that could potentially prevent the operation of Alamitos Barrier project.</p>	<p>Implemented. The district entered into an agreement on July 16, 2003.</p>
<p>To ensure that it maintains the proper level of control over the services it receives from various consultants, the district should improve its contract management procedures by taking the following steps:</p> <ul style="list-style-type: none"> • Develop scope-of-services provisions for its contracts that clearly define the tasks it requires from contractors and provide the district with criteria for evaluating the contractor's performance. • Ensure that the district and professional services contractors sign a written agreement. • Specify a duration that identifies a starting point and ending point in all contracts. • Ensure that it enters into contracts that are consistent with the board's directions and that contracts are signed only by those authorized to do so. • Separate contracts into active and inactive files to facilitate identification of contracts under which it may have obligations. 	<p>Implemented. We selected and reviewed 10 contracts and found that the district has improved its management of contracts in the areas listed in the recommendation.</p>
<p>The district should renegotiate existing contracts so that they are consistent with current minimum standards that the Legislature mandates, which require scope-of-service, duration, and payment terms.</p>	<p>Implemented. We reviewed active contracts that the district renegotiated and found that the district had included these factors in the contracts.</p>
<p>The district should assign staff of appropriate levels to serve as contract managers. Their responsibilities should include monitoring the contractors' performance and ensuring that the district receives the services and products that the contracts specify.</p>	<p>Implemented. According to the district, it has assigned contract managers to better manage contracts.</p>
<p>The district should implement procedures to periodically evaluate any contracts that require fixed monthly fees to ensure that it receives services in keeping with the fees it pays.</p>	<p>Implemented. The district annually evaluated contracts that require fixed monthly fees.</p>
<p>To allow more efficient contracting practices, the districts should seek legislation to amend the water code to provide the board with the authority to delegate the approval and signing of contracts below certain dollar thresholds to the district's general manager.</p>	<p>The district pursued a change in legislation in 2003 through Senate Bill 906. However, the bill did not pass. The district is currently pursuing legislation in 2004 through Senate Bill 1165, which would allow the board to authorize by resolution a district manager or other representative to sign contracts, not to exceed \$25,000, and other documents in the name of the district.</p>
<p>The board should further amend the district code through the following actions:</p> <ul style="list-style-type: none"> • Make it consistent with requirements of the water code. • Relax its requirements for written requests for proposals for bids for all service contracts under \$25,000 and expand its informal bid policy to cover purchases of services that fall under the new threshold for formal competitive bidding. • Exclude small purchases of materials from its informal bid solicitation process. 	<p>Implemented. The district revised its code to comply with our recommendation.</p>

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Recommendations	District's Progress
<p>To better control its administrative costs, the district should continue its development and implementation of written accounting procedures. It should ensure that these procedures require it to do the following:</p> <ul style="list-style-type: none"> • Delegate spending authority to ensure that management approves purchase of goods and services exceeding a specific threshold before obligating the district. • Allow only authorized managers to approve payments to vendors or consultants. • Maintain documents that demonstrate efforts to ensure that the district receives value for purchases that do not require formal bidding. 	<p>Implemented. The district has developed accounting procedures that address the recommendations. However, as discussed in Chapter 3, it does not always follow its approval policies.</p>
<p>Before approving reimbursement for travel or conference costs for its members, the district's board should ensure that the travel or conference will benefit the district's purpose.</p> <p>The district should amend the district code to provide the following:</p> <ul style="list-style-type: none"> • Requests for proposals do not effectively eliminate bidders. In addition, it should prohibit altering material factors that could affect the evaluation of bids after it has issued final requests for proposals. • Better guidance to district staff on allowable and unallowable expenses. Specifically, the board should adopt a policy regarding the types of expenses it believes promote the public purpose of the district. • Better guidance for reimbursable lodging expenses, including dollar thresholds and a process for justifying charges in excess of those thresholds. • A policy ensuring that it holds contractors to the same reimbursement guidelines as district staff. 	<p>Partial corrective action taken. As discussed in Chapter 3, we still have concerns related to travel and conference costs.</p> <p>Partial corrective action taken. The district has amended its code to include these factors but did not implement a process for justifying charges in excess of thresholds. Additionally, as Chapter 3 discusses, the district does not always follow its new policies related to allowable and unallowable expenses.</p>
<p>To provide reliable information on its operations, as the Legislature intended, the district should take the necessary steps to ensure it complies with the reporting requirements of the water code. It should include in its audited financial statements an accurate and complete list of capital improvement projects and their funding sources as well as a report on the propriety of the district's operating expenses. In addition, the district should ensure that it accurately calculates any disclosure of reserve funds it includes in its audited financial statements.</p>	<p>Implemented. The district's auditor included the amounts the district estimated it would spend on capital improvement projects and a report on the propriety of the district's operating expenses in its standard audit report for the fiscal year ending June 30, 2003.</p>

APPENDIX B

Compensation, Allowances, Benefits, and Other Reimbursements for Directors of the Water Replenishment District of Southern California

The members of the board of directors are not full-time employees of the Water Replenishment District of Southern California (district). However, the district provides benefits, compensation, and other forms of reimbursements to each director. As shown in the following table, these payments include some fixed expense allowances, retirement benefits, and travel reimbursements.

TABLE B.1

Director's Compensation, Allowances, and Benefits	
Compensation	Limit
The district compensates a director for each day's attendance at meetings or for each day's service the director renders in representing the interest of the district. Compensation of \$170 per meeting increased to \$199 as of December 2003 and \$205 as of January 2004, for up to 10 meetings per month.	Up to \$24,600 per year
Vehicle Allowance	
A director may receive a vehicle allowance of \$308 a month provided that he or she attends at least one meeting within the month. Alternatively, the director may receive reimbursement for actual mileage at the current rate for business mileage reimbursement allowed by the Internal Revenue Service.	Actual cost or up to \$3,696 per year
Communication Allowance	
A director may receive a monthly communication allowance of \$200 to cover the following: cellular phone service; fax machine; computer and monitor; software; Internet service; all-in-one printer, scanner, and copier; and dedicated phone line and printer and fax supplies. A director may receive this allowance in lieu of reimbursement for any communication-related expenses. A director who does not elect to receive the communication allowance may seek reimbursement for any communications-related expenses actually incurred in connection with district business.	Actual cost or \$2,400 per year
Health Benefits	
The board of directors selects and approves the medical-hospital insurance policy that the district provides to the directors, as well as district staff, at no cost to them. Currently, the district pays up to \$1,032 per month for medical-hospital insurance. In addition, the district pays for medical and dental expenses not covered by the insurance policy up to a maximum of \$3,000 for the director and \$2,000 for each of their dependents in any one year. The district also reimburses a director up to \$1,000 for actual eye-related expenses incurred per calendar year.	Up to \$16,384 per year, not including dependents

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Retirement Benefits	Limit
<p>The district contributes 23.33 percent of the director's compensation towards retirement for three of its directors who started with the district after 1995. For the other two directors who started with the district before 1995, the district contributes 12.357 percent of the director's compensation towards retirement.</p>	Varies
Other Reimbursements	
Conferences	
<p>The district pays for a director to attend conferences, which may include costs for registration fees, meals, airfare, and lodging. There is no limit to the number of conferences a director may attend or how much the district will reimburse the director annually.</p>	Varies
Per Diems	
<p>A director may receive per diem of up to \$100 a day for meals and gratuities incurred while conducting district business outside of the local area, which is 40 miles from the director's residence or the district's office, whichever is farther. Additionally, the director may receive reimbursement for actual meal costs and the cost of meals purchased for other persons, when the meals further the district's business.</p>	<p>Breakfast: \$20.00 Lunch: \$35.00 Dinner: \$45.00</p>

Agency's comments provided as text only.

Water Replenishment District of Southern California
12621 E. 166th Street
Cerritos, California 90703

May 20, 2004

Ms. Elaine M. Howle
State Auditor
555 Capitol Mall
Sacramento, CA 95814

Dear Ms. Howle:

The Water Replenishment District of Southern California applauds the professionalism and competence of your staff in the conduct of the most recent audit of our District.

We are especially pleased by the acknowledgment of the very substantial progress we have made in implementing 22 prior Audit Bureau recommendations. We take pride in the fact that our Board governance and staff management have the District on the right track.

We accept the 12 recommendations contained in this Audit Report. On May 19, the Board implemented one of them---the recommendation to extend the life and function of the Technical Advisory Committee. We look forward to working with the TAC to implement the three recommendations relating to the Capital Improvement Plan.

Nearly a fourth of the Audit narrative is devoted to the District's Reserve Fund, reflecting the complexity of the subject and the difficult balancing act the District has in trying to set an assessment rate that provides a cushion to meet unanticipated expenditures on the one hand, and the demands for a constrained assessment by many of our pumper constituents on the other. A prior Audit Report faulted the District for having a Reserve Fund that was "too low." This Audit Report counsels us to take into account the perspective of pumpers who do not want the District to have a Reserve Fund at all. The policy dilemma is obvious. Nonetheless, we reaffirm our commitment to implement the recommendation to set the assessment rate "...at a level that will support the district's planned activities and allow it to replenish its reserve funds and keep them at an appropriate level."

We appreciate the Audit Report and will use it as a guide to do an even better job for the 4 million people and 110 groundwater pumpers we serve.

Sincerely,

(Signed by: Willard H. Murray, Jr.)

Willard H. Murray, Jr.
President, Board of Directors

cc: Members of the Legislature
Office of the Lieutenant Governor
Milton Marks Commission on California State
Government Organization and Economy
Department of Finance
Attorney General
State Controller
State Treasurer
Legislative Analyst
Senate Office of Research
California Research Bureau
Capitol Press