



## **PLACER COUNTY GRAND JURY**

# **City of Lincoln Water Connection Fund**

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### **SUMMARY**

Lincoln continues to grow as more land is being developed for homes, businesses, schools, and community parks. The grand jury investigated Lincoln's Water Connection Fund (WCF) and the historical events leading to its current balance. Water connections, usage, fees, and water rate structures were examined as well as previous decisions regarding the implementation of the Twelve Bridges Project. The findings show Lincoln ignored governing regulations related to rate-setting and as a result, overcharged developers and homeowners, resulting in an accumulation of a \$41 million surplus in the WCF for the 2018-2019 fiscal year. Further, a portion of this fund was loaned to other funds managed by the city without following proper procedures or ensuring those other funds would be able to repay those loans.

The grand jury recommends Lincoln return fees collected inappropriately and return funds from improper loans. The city council should develop improved oversight of management within the city.

### **APPROACH**

The grand jury conducted interviews of Lincoln city officials and citizens, made site visits, researched legislative documents, reviewed media reports, reviewed a report from the Auditor of the State of California, and city council meeting minutes.

### **DISCUSSION**

In the course of reviewing residential building permits within the county, the grand jury noted select parcels within Lincoln (and, at times, within areas subject to a preexisting Development Agreement), were assessed higher fees for services, such as the water connection fee. All water connection fees are deposited in the WCF which, as of budget year 2018-19, has a balance in excess of \$26 million. In addition, there are approximately \$15 million in outstanding loans from the WCF that were made to other Lincoln city funds. The grand jury initiated an investigation to review the manner in which the water connection fees were established and to verify whether the accumulated fund balance was used in an appropriate manner.

#### **Water Connections**

Lincoln operates its own water department. Water is obtained from both city-owned wells and purchased from the Placer County Water Agency (PCWA). To obtain water from PCWA, the city purchases water connections. Each connection represents usage calculated as an Equivalent Dwelling Unit (EDU) representing 1,150 gallons usage per day. PCWA has a two-tier charge to the city, regulated and unregulated. Regulated is the charge for the majority of properties in Lincoln. They are served through the city water system due to their lower elevation. Unregulated properties are served directly from the PCWA pipeline, due to higher elevation. PCWA charges Lincoln the current rate of \$15,677 per regulated EDU and \$19,339 per

unregulated EDU (Appendix 1). The unregulated connections are at a higher rate to compensate for water storage by PCWA (Lincoln has its own storage for the connections served by its water system). These water connection fees are paid to Lincoln by developers and by homeowners during building permitting.

### **Fees**

Fees collected for water connections are deposited in the WCF and must only be used for specific purposes as set forth in the following city and state laws:

Lincoln Municipal Code 13.04.360 states *“Connection fees for every service connection to the city water system are established for the purpose of providing funds for the payment of the costs for design and construction of the city's water system and to make the required service connection payments to the Placer County Water Agency and in order that such costs be shared by those receiving the benefits.”*

California Government Code 66013(c) states *“A local agency receiving payment of a charge as specified in paragraph (3) of subdivision (b) shall deposit it in a separate capital facilities fund with other charges received, and account for the charges in a manner to avoid any commingling with other moneys of the local agency, except for investments, and shall expend those charges solely for the purposes for which the charges were collected. Any interest income earned from the investment of moneys in the capital facilities fund shall be deposited in that fund.”*

Lincoln has transferred funds from the WCF, in the form of loans, to other city funds including, but not necessarily limited to the following:

- \$5.33 million - Redevelopment agency
- \$5.25 million – Airport
- \$4.16 million – Fire Stations - Fund 242

These loans are not consistent with California Government Code 66013(c). At the time of this report there were no strategies for repayment, and it appears from sources reviewed that the funds receiving the loans may not currently have the ability to be able to repay those loans in any reasonable timeframe.

### **PCWA Water Connection Charge & Rate Structure**

California Government Code 66013(a) states, *“Notwithstanding any other provision of law, when a local agency imposes fees for water connections or sewer connections, or imposes capacity charges, those fees or charges shall not exceed the estimated reasonable cost of providing the service for which the fee or charge is imposed, unless a question regarding the amount of the fee or charge imposed in excess of the estimated reasonable cost of providing the services or materials is submitted to, and approved by, a popular vote of two-thirds of those electors voting on the issue.”*

PCWA did an extensive study in 2017 which resulted in a revised water connection charge structure for its retail customers. PCWA held hearings and ultimately established water connection charges based upon the size of the lot. This new rate structure only applied to PCWA's retail customers. Wholesale customers like Lincoln continued to pay a flat fee per EDU.

In July 2017, Lincoln city officials imposed a new rate structure for its retail water customers modeled after PCWA's. This rate structure was implemented even though Lincoln had not conducted the required studies to demonstrate that these fees did not exceed the reasonable cost of providing the service as required by state law. Lincoln held no hearings and no city council approval was obtained. The net effect of this change increased fees for some properties and decreased others. For example, under the new rate structure, citizens of the Lakeside development were charged fees of \$18,353 per lot whereas under the former rate structure, fees would have been \$15,295, or approximately twenty percent less.

In January 2019, Lincoln's City Council approved changes to Municipal Code 13.04.360 to modify the PCWA water connection fee without first completing a formal study. The City Council was advised by city staff that neither a hearing nor a study were necessary because the new rate structure would result in a reduction of the fees. While this modification did result in reduced rates for some, it did not address or correct the lack of studies for the imposition of the 2017 rate structure which maintained the increased rates for other properties. For example, a home on a 35,000 square foot unregulated lot currently has a connection fee of \$63,983 (Appendix 2). Per the Twelve Bridges agreement the maximum the city can charge is \$45,833 ( $19,339 \times 2.37$ ). The current fee is a forty percent increase. In contrast, PCWA's highest charge for their retail customers is \$48,348.

### **Twelve Bridges Project**

In 1998, the city entered into an agreement with Placer Holdings Corporation to develop the Twelve Bridges project. This project encompassed the land east of Hwy 65 to Sierra College. It included the Del Webb Sun City development as well as several other villages. The agreement specified that each lot would be charged for one regulated EDU. According to the agreement, the rationale for this determination was contained in a study conducted by Lincoln's city engineer. The study could not be located by city officials.

In 2018, an informal study by Lincoln's city engineer examined water usage and found approximately 85 percent of Lincoln's residential lots actually used less than half of an EDU and 40 percent used less than a third of an EDU. These actual usage rates conflicted with Lincoln's 1998 agreement with the developer of the Twelve Bridges project. For example, per that agreement, Lincoln charged each Sun City lot for a full EDU and purchased a commensurate number of EDUs from PCWA. Not only were Lincoln's Sun City citizens charged for more water capacity than they have actually consumed, but Lincoln has purchased far more water

capacity from PCWA than it will use for decades. These overcharges have contributed to the inflation of the WCF to over \$41 million.

The agreement also specified that the units in villages 13-17 and 19 would have a water factor of 2.37 EDU's because they were identified as very low-density parcels as defined by the land development agreement Exhibit M. For undocumented reasons, the city increased the water factor to 2.5 EDUs for parcels in these villages. For a home built in 2016-17, this resulted in an additional \$2,300 charged to the homeowner.

The developer paid for water storage capacity for the development which exempted it from the storage portion of the PCWA water connection fee (Appendix 3). Units in this development were considered regulated connections. In 1999 an amendment to the agreement specified that units in villages 13, 19, 23 and a portion of 18 would be charged the unregulated PCWA rate due to their elevation (Appendix 4). This rate includes the storage portion of the PCWA fee. However, it appears that the city also charged homes built in other villages the unregulated PCWA fee. For example, one home in Village 16, which was built in 2014, was charged \$43,268 ( $\$17,307 \times 2.5$ ). The fee should have been \$32,199 ( $\$13,586 \times 2.37$ ) in compliance with the 1999 amendment. This \$11,069 overcharge was not an isolated event. Several other properties were similarly overcharged.

In response to the above, the city engineer stated the development agreement was “informational only” despite the fact that it was a legally-binding contract. Lincoln justified charging the unregulated PCWA water connection fee since Village 16 is within the higher elevation zone that is served by the unregulated PCWA service. The city could not provide any agreements that modified the terms of its original agreement. Lincoln is bound to its formal agreement with the developer and cannot arbitrarily change its terms. Doing so has resulted in thousands of dollars in overcharges to the citizens of Lincoln.

## **CONCLUSION**

City officials acknowledge that the Twelve Bridges development agreement was too complex for the city to administer effectively. The agreement was flawed in calculating the fees for very low-density high-elevation housing, but the city agreed to those terms and should either abide by them or modify the agreement. The arbitrary changes and establishment of water connection fees in 1997 and 2017 were not done in a manner set forth by law. It seems clear that Lincoln has unlawfully collected water connection fees in excess of its reasonable costs for providing such service. It has not attempted to conduct any studies to justify these actions. For the past twenty-two years there has been insufficient city council oversight of the conduct by unelected city officials. As a result, the citizens of Lincoln have been charged unjustified and excessive water connection fees. Such conduct cannot be minimized by the city's assertion of the statute of limitations.

## **FINDINGS**

The grand jury found:

- F1. The city has repeatedly failed to conduct required nexus studies to determine reasonable costs for the PCWA connection fee.
- F2. The rate modification in 2017 was not done in a manner required by statute.
- F3. Lincoln's 2019 modification of the PCWA water connection fee did not correct the fees that were improperly established in 2017 and also did not comply with statutory requirements.
- F4. Lincoln's unlawful actions resulted in significant over-charges to its citizens.
- F5. Lincoln made loans from the WCF to other city funds with no assurances that the funds receiving the loans will be capable of repayment within any reasonable timeframe.

## **RECOMMENDATIONS**

The grand jury recommends:

- R1. Lincoln refund charges that exceed the regulated and unregulated PCWA connection fees due to modification of the rate structure in 2017, even if it exceeds the statute of limitations.
- R2. Lincoln identify and refund excess water connection charges to homes in low-density villages for wrong EDU water factor even if in excess of the statute of limitations.
- R3. Lincoln identify homes not in villages 13, 19, 23, and portions of 18 that were charged the unregulated PCWA water connection fee instead of the regulated fee, and refund the overcharge even if it exceeds the statute of limitations,
- R4. Lincoln City Council require a review every 5 years for all connection fees to determine reasonable costs.
- R5. Lincoln restructure loans made from the WFC to comply with state regulations or return the funds to the WFC.
- R6. Lincoln City Council conduct a retroactive study of the performance of city officials and initiate systemic corrective actions including closer oversight of city functions going forward.

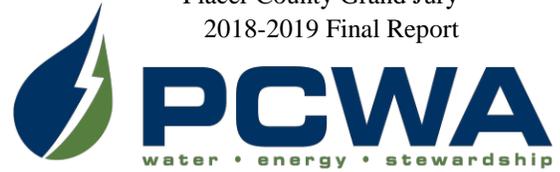
**Exhibit M, 1998 Placer Holdings, Inc. Development Agreement with City of Lincoln detailing the projects EDU schedule.**

**EXHIBIT "M"**  
Project EDU Schedule  
Placer Holdings, Inc.  
Twelve Bridges  
City of Lincoln, Calif.

Land Use Symbol	Description	Unit	Traffic EDU a)	Sewage EDU b)	Water EDU c)	Drainage EDU d)
VLD	Very Low Density	du	1.00	1.27	2.37	1.30
LD	Low Density	du	1.00	1.00	1.00	1.30
MD	Medium Density	du	0.72	1.00	1.00	0.70
HD	High Density	du	0.72	0.60	.057	0.24
VC	Village Commercial	ac	58.33	6.94	5.43	6.40
C	Community	ac	58.33	6.94	5.43	6.40
EC	Employment Center	ac	25.55	6.94	5.43	6.40
P	Parks	ac	1.11	1.59	7.39	2.96
OS	Open Space	ac	0.00	0.00	0.00	0.00
GC	Golf Course	ac	1.11	0.04	0.03	0.03
CC	Community College	ac	5.55	4.96	7.83	4.00
HS	High School	ac	5.55	4.96	7.83	4.00
MS	Junior High School	ac	5.55	3.17	7.83	4.00
ES	Elementary School	ac	5.55	4.76	7.83	4.00
FS	Other Public	ac	1.11	6.94	7.83	2.96

Note:

- a) Traffic EDU/unit based on Fehr & Peer's
- b) Sewer EDU/unit based on LD average day use = 252 gpd
- c) Water EDU/unit based on John Pedri's 11/12/97 max day demands & LD = 1EDU @ 1,150 gpd
- d) Drainage EDU/unit based on City PFE rate
- e) Golf Course (GC) Water demands assumes irrigation is from raw water source



**Appendix 1**

**Water Connection Charges (Effective 1/1/2019)  
Zone 6 - City of Lincoln (for reference only)**

Lower Zone 6 Base Rate Increased 2.5% per ENR CCI (Section 40900(a) of Rules & Regulations) from \$18,867 to \$19,339

**Base Rate WCC for 1.0 Unit of Capacity (UOC):**

Component	Amount for Regulated Meter	Amount for Unregulated Meter
Treatment	\$8,959	\$8,959
Transmission	\$6,638	\$6,638
Groundwater	\$0	\$583
Storage	\$0	\$2,998
Planning	\$80	\$161
<b>Total WCC</b>	<b>\$15,677</b>	<b>\$19,339</b>

**Notes and Definitions:**

- This WCC rate chart is for reference only and is intended to show fees as described in the PCWA-City of Lincoln supply contract. Please contact Lincoln for all development fees and process.
- Per contract with the City of Lincoln, WCC for service through the 18" Regulated Meter is based on the following percentage of PCWA Upper Zone 6 components: 100% Treatment, 100% Transmission, and 50% Planning.
- Units of Capacity purchased for services off of the 8" Unregulated Meter are subject to the full PCWA Upper Zone 6 Water Connection Charges.
- Units of Capacity (UOCs), also known as Equivalent Dwelling Units (EDUs), is defined as 1,150 gallons per day maximum day demand.
- WCC = Water Connection Charge
- GPD = Gallons per Day
- MDD = Maximum Daily Demand (GPD)

## Appendix 2

### CITY OF LINCOLN RESIDENTIAL BUILDING PERMIT FEES

As of February 8, 2019

1. **\*PCWA Water Connection Charge:** *City collects a source water connection charge based on PCWA table (below)*

Total Lot Size (square feet)	Total Peak Day (gal)	PCWA WCC Regulated Meter	PCWA WCC Unregulated Meter
Less than 2,901	250	\$3,324.89	\$4,101.52
2,901 to 4,400	450	\$5,984.80	\$7,382.74
4,400 to 5,500	550	\$7,314.76	\$9,023.35
5,501 to 7,000	700	\$9,309.70	\$11,484.26
7,001 to 10,000	850	\$11,304.63	\$13,945.17
10,001 to 17,000	1200	\$15,959.48	\$19,687.30
17,001 to 35,000	1950	\$25,934.15	\$31,991.87
Greater than 35,000	3900	\$51,868.30	\$63,983.74

## Appendix 3

1998 Agreement - Section 3.3.2 (d)

For a new water service within the City, City charges a city water connection fee ("City Water Connection Fee"). The City Water Connection Fee is comprised of two main components; first, the City's PFE water fees ("PFE Water Fees"), and second, an amount equal to the PCWA Plant Expansion and Replacement Charges fee ("PERC fee" or "Pass Through Fee") for water customers within PCWA's Zone No. 1 from the Foothill-Sunset Water System which is set by PCWA from time to time. PHI shall pay, at the time of issuance of each building permit, the then current City Water Connection Fee including one hundred percent (100%) of the then current PFE Water Fees, subject to the adjustments that may be made pursuant to Sections 2.4, 2.4.1, and 4.2 of this agreement, less a credit for storage facilities constructed by PHI and Webb as provided under Section 3.3.4 of this Agreement, and the then current PERC fee comprising **one hundred percent (100%) of the PERC treatment component, one hundred percent (100%) of the PERC transmission component, subject to adjustment pursuant to Section 3.3.3 of this Agreement, one hundred percent (100%) of the PERC planning component** payable by the City/ and **no percentage (0%) of the PERC storage or distribution component**, all of which

shall be further calculated by **multiplying the sum of the foregoing components by the Water EDU Factor** established pursuant to Section 3.3.9 of this Agreement. In the event that City adjusts its City Water Connection Fee such that the above-stated percentages are reduced, such reduced Water Connection Fee shall apply to the Project and be paid by PHI. In no event shall the Project be subject to City Water Connection Fees in an amount which is more than the City Water Connection Fee charged elsewhere within the City.

#### **Appendix 4**

1999 Amendment - Section 3.3.4(a)

City acknowledges that Villages **13, 23, 19, and a portion of 18** in the Project, as shown on the Large Lot VTM are at a higher water pressure zone and will therefore, connect directly to the new PCWA 30" transmission line to Sunset Water Treatment Plant. **The EDUs comprising Villages 13, 23, 19, and a portion of Village 18 will pay the full PERC fee, including the storage component to City/PCWA.** Consequently, storage demand for these units shall be deducted from the Project for purposes of calculating the water storage demand, as set forth above.

**REQUEST FOR RESPONSE:**

Pursuant to Penal Code §933.05, the Placer County Grand Jury requests a response from the following governing body:

	<b><u>Recommendations Requiring Response</u></b>	<b><u>Response Due Date</u></b>
<b>Lincoln City Council</b> 600 6th St. Lincoln, CA 95648	<b>R1 – R6</b>	<b>August 6, 2019</b>

**Copies sent to:**

**Lincoln City Manager Hanson**  
600 6th St  
Lincoln, CA 95648