

Alternatives to litigation in territorial disputes

As anyone who has heard me speak at a KRWA event, or who has read any of my previous articles will know I am a big believer in water districts and cities setting aside personality conflicts or political agendas and working out voluntary service agreements. As the water wars show every sign of heating up in Kansas, water districts and cities need to remember that the customers are always better served when they can avoid costly legal battles and instead focus on the mechanics of getting the best water service for the lowest cost to the most customers. Both sides must avoid stereotypes. Not all cities are evil empires who want to steal water district customers. Not all water districts want to stifle city growth while they receive handouts from

Washington. Cities need to acknowledge that water districts are challenged with serving far-flung customers and that they are single-interest political subdivisions which lack the economies of scale most cities take for granted.

This is the reason that federal funding was made available in the first place. Most water districts simply cannot afford to lose customers in populated areas, because then the remaining customers will have to service the debt for the whole district. Water districts on the other hand must realize that cities are multi-interest political subdivisions, responsible for providing bundled services to

larger numbers of customers. Cities are apt to be less eligible for federal grants and loans than water districts and must rely on growth and rate increases in order to provide services. Cities are also subject to more intense political pressure from citizens and must maintain several sets of infrastructure. That being said, how do the two sides sit down and come up with a good, shared service agreement which

fact specific that it is impossible to quantify it in that manner. The solution will really depend on the facts of each case, and I will walk you through some questions that can be used as starting points for discussions. Before I do that however, I would like to emphasize the sooner rather than later philosophy. Whoever you are, city or water district, the very best time to work out a shared services agreement is when you

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addresses the needs of both sides? You may notice that I have avoided the word "compromise". In recent years "compromise" has become shorthand in Washington D.C. for "a solution to a problem which the public will hate and which does not really solve the underlying issues but was the result after both parties fought one another to a standstill." Believe me; we can do so much better than that!

So assuming that we have a city and a water district with overlapping territory or that a city intends to annex into a water district's territory, how do the two sides create a shared services agreement? Originally Elmer asked me to give him some material that could be put into a tidy flowchart. I wish it were that cut and dried, but the process is so

have no disputes. Sounds obvious, doesn't it? Well it isn't. Cities and water districts, both of whom are ultimately run by "volunteer" (i.e. elected) boards, rarely want to spend the time and effort to resolve conflicts that haven't popped up on their radar yet. Once I worked with the public works director of a small town to create an outline of the possible territorial issues the town might face with a local water district. We looked at plat maps in order to identify local landowners with large parcels of land, identified the logical areas for future growth, compared city and district water rates, and reviewed the financial reserves of both bodies. (Hint, hint. This is exactly the type of preliminary work you should all be doing!) The public works director and I concluded that there

were some potential problems which could be viewed as excellent opportunities to work together and that the water district manager was a reasonable guy. However, the town decided that it had more pressing problems and didn't want to spend the money on negotiations when they didn't perceive a problem. Sadly, they got to spend lots of money later, when the water district got a new manager who wasn't as cooperative and a new prison suddenly raised the stakes.

So here is a process that will help you start a dialogue. Whether you are a city or a water district, these are questions that need to be answered honestly and objectively. Keep in mind that these same concepts can be used to settle on-going litigation as well. And be flexible and creative. Think outside the box and be prepared to take a concept I might mention and turn it upside down in order to reflect the reality of your fact situation.

1. Where are both sides getting their water and what does that water really cost?

As ridiculous as it seems, cities and water districts will often fight over territory and customers even when one buys water from the other. In reality, this should be the easiest scenario for a shared services agreement because the two parties are already tied to one another economically. If the city is selling the district water, then the city should realize that the district is probably its single largest customer and that the city will also have other sources of revenue once an area is annexed. The city can continue to sell the district water with the idea that any increase in district customers will mean more water sales for the city - without the city having to install and maintain infrastructure. The reverse is true as well. If the water district is selling water to a smaller town, and the town wants to expand, the water district



should keep in mind that the town is probably its largest customer and that even at wholesale rates, the district probably makes more money on the water it sells to the town, than on "retail" water. Both sides have to know the true cost of the water they provide and how much profit they make. Time and time again, I have tried to negotiate shared service agreements only to discover that one or both parties did not know how much money they really made on water. That meant it was difficult to negotiate pricing or to demonstrate that one side would actually make money even after selling water at a discount to the other side.

In fact, as long as the parties are negotiating service to an area, maybe now is a good time to renegotiate the water contract as

well. And while you are at it, take a look at rates. Have both sides stayed current with rate increases? City and district rates will vary, and this in and of itself often allows creative solutions. A good rule of thumb is that district rates are around 3 times higher than city rates. If this is true then a city's regular retail rate might be considerably less than a district's rate and the city may not even need to discount its rate to a district in order to make money by allowing a district to serve or continue to serve an area. The parties also need to consider how rate increases will impact a long term agreement. One agreement I negotiated (city selling district water) worked well until the city started raising its rates and after several years had rates close to the district rates. By then the city's

- graphic by Linda Windler, Thoroughbred Computer Systems

profit margin had shrunk to almost nothing and the city was unhappy with the agreement. Eventually, the city offered to buy the customers in question outright and to compensate the district for its infrastructure. The city and the district also decided to explore a joint venture on a new well, in order to keep water production costs down long term.

Another possible scenario is partial water purchase. Maybe the district buys a portion of its water from a city or vice versa. Better yet, a new service area might lie within district boundaries but be across the road from a city main. The district and the city could enter into a water purchase agreement for just the area in question. If the rate disparity holds true, then the district can buy water from the city more cheaply than it can produce it and the city can still make money on the new customers without having to lay a foot of pipe.

2. Is the service area in question vacant land?

Cities and districts can and should develop long term plans that address growth needs and also acknowledge short term development. More and more cities are concerned about urban growth boundaries and infrastructure planning in areas that may develop first and be annexed later. Cities are tempted by tax revenues but reluctant to accept areas that do not meet building codes, setbacks and other planning and zoning requirements. This is where the district and the city can become allies. Get that plat book out and look at the overlapping areas for future development. Discuss who has lines in the area and who could most easily serve. Are there underserved areas for either party because of lack of infrastructure? Even if the district ends up serving an area, it could require that developers meet city construction specifications that will make it

easier for the city to annex later. The city and the district could work out shared service agreements for water and sewer, so that the city can provide sewer services in an un-annexed area but the parties can cooperate on line locations and easements which may make future annexation easier for the city. Annexation is not a bad thing. Cities have to grow in order to survive. So working together on issues that promote

that the district and the city can create an urban growth boundary (UGB) and allow the city to "buy" that area for a one-time fee. In fact that cost can be passed on to developers when they annex into the city as a development fee that will be payed to the district. As long as the district doesn't have any pipes in the ground, it isn't out any money. Then the parties can agree that any development outside the UGB will be served by

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annexation can be a huge benefit to a city. As long as a district is not harmed financially, it doesn't matter where its customers live.

And let's talk fire flow. Nationwide this has been a big bone of contention between cities and districts. Many districts do not have the flow necessary to provide fire protection due to the fact that historically USDA would not fund lines big enough for fire flow. So we have a city and a district who want to avoid expensive litigation, an area inside district territory that may be annexed, a district that needs customers in order to service its debt and a city that will be required to provide fire protection and wants to keep or improve its ISO rating in an annexed area. Why not agree that the district will size its lines in order to provide fire protection and will buy water from the city for the new customers in the event that it doesn't have sufficient volume? The city should be able to make a small amount of money on the water it sells and it gets infrastructure within the city limits that matches its existing infrastructure. Another solution is

the district and that if the district doesn't have capacity or lines in the area, it can buy water from the city at that time.

Another option of course is for the city to serve an area and to pay the district tap fees and/or a percentage of the revenues generated by water sales. Again, it may be more economical for the city, due its lower water rates and higher profit margin, to invest in the infrastructure outright and pay the district for the right to serve the customers directly. This becomes slightly more complicated when you are dealing with existing customers in a built-out area which is annexed by a city, but it is always possible to come up with a solution. In this situation, the district needs to be compensated for both the investment it made in the infrastructure and for loss of future revenue. But the parties need to be realistic. The developer probably paid for some if not all of the water lines and the district needs to look at net revenues. Remember, it takes many years of water revenue from one or two subdivisions to equal the attorney's

fees in a federal fight over customers. Maybe the district should just continue to serve the customers, but should agree over time to upgrade its lines in order to meet city fire protection standards.

3. Are there hidden benefits from working together beyond avoiding litigation?

Cities and districts would do well to look at the models of 911 services in many parts of the country. Because of the nature of 911 calls in rural areas, many counties and cities have had to work together to provide unified 911 service. In some cases, both parties have contributed to the cost of the equipment which one party operates. Cities and districts need to think about ways in which they can economize by working together. Think regional. Think shared wells or treatment facilities. Think shared billing or even shared O/M. One water district decided it couldn't afford to extend lines because the bids it got were too high. It ended up

negotiating an inter-governmental agreement with the city for construction of the water lines, because the city had its own bids out for similar construction. Both sides saved money and this led to agreements for joint investment in a billing system. Admittedly, neither side was arguing about territory, but their ability to work cooperatively together is a great lesson for us all.

Just as cities can use an agreement to address development issues, water districts also need to keep in mind that they may be able to obtain far bigger benefits in a negotiated agreement than they can even if they were to win a lawsuit. Joint service agreements can be open-ended time-wise, that is they do not have to contain a sunset provision. In contrast, a judgment in a 1926(b) case will only be effective while there is federal indebtedness, and water districts can no longer assume that a loan will remain unexamined for the duration of the loan. USDA's official policy is to review loans every 1-2 years in order to see if

the district can refinance the loan elsewhere. There is pressure from Washington to actively enforce this policy, called a graduation review, because federal funds are increasingly scarce. In the event that a city loses a case, they run the risk of facing a blanket injunction on serving customers anywhere in the district so long as the federal debt remains. With a joint service agreement, the parties can agree in advance on who will serve which areas far into the future. Cities can then incorporate this into long-term comprehensive planning and allocate limited resources.

Clearly, there are many creative ways in which cities and water districts can work together. So do some background analysis and start thinking outside the box. The options are limitless and they only depend on the facts of a given situation and willingness from both sides to look at the big picture and find the ways in which both can benefit from working together.

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