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The Texas Natural Resource Conservation Commission's Oversight of Water Districts and Utilities

December 1996

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Key Points of Report

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Overall Conclusion

Given its limited resources and complex jurisdiction, the Texas Natural Resource Conservation Commission (Commission) meets its essential, minimum oversight responsibilities. In some areas, the Commission can achieve greater impact and efficiency using its existing authority. In other areas, its authority might be enhanced to serve the public interest.

Key Facts and Findings

- The Commission's information on water districts and utilities is kept in multiple databases which lack controls and consistency. The Commission should integrate its technical, financial, and managerial oversight data to reduce fragmentation and inconsistencies. This will help the Commission direct its resources toward the greatest risks and provide greater guarantee of the integrity of local entities.
- The Commission is not organized for the convenience of the entities it oversees. The organization structure may have impaired efforts to integrate data.
- The Commission is passive in its oversight role, possibly because of its complex jurisdiction. It does not have an active program for ensuring the financial, managerial, and technical viability of water utilities. It has also been reluctant to deny petitions for creating new water districts and to dissolve active districts.
- The Commission should develop procedures to control critical processes such as collecting due regulatory assessments and administering technical assistance contracts.
- The Commission and its Water Utilities Division should work with the Texas Legislature to consider:
 - Means of simplifying and standardizing the Commission's oversight of local entities
 - Establishing additional incentives to encourage regionalization of water and wastewater systems
 - Giving the Commission greater flexibility in regulating rates charged by investor-owned utilities
- Summary information on the Commission's jurisdiction and regulated community, including public drinking water systems, districts, and retail public water utilities, is available at Appendix 4.

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Executive Summary

The Texas Natural Resource Conservation Commission (Commission) oversees water-related entities to ensure that citizens will pay reasonable taxes and fees for continuous and adequate water services. It is also generally expected to help ensure each entity's financial, managerial, and operational integrity; however, its jurisdiction depends on multiple, interacting factors.

Given its limited resources and complex jurisdiction, the Commission generally meets its essential oversight responsibilities. In some areas, the Commission can achieve greater impact and efficiency using its existing authority. In other areas, its authority might be enhanced to serve the public interest.

Many of our recommendations ask the Commission to do more than it currently does. Aware of the Commission's limited resources, we have structured our recommendations to be fiscally neutral by recommending operational efficiencies and improvements in fee collections and penalties. A fiscal impact table shown at Appendix 2 identifies recommended revenue increases of approximately \$340,000 and expenditure increases of \$331,635.

Report Highlights

Thousands of entities provide water-related services in Texas. These include:

- Cities (generally not within the scope of our audit)
- Special districts (such as irrigation, drainage, or municipal utility districts)
- Water supply or sewer corporations (nonprofit cooperatives)
- Investor-owned utilities

These entities play an important role in implementing federal and state water laws and policies. They provide water, wastewater, and other services that are essential to public health, and they have a significant local and regional economic impact.

Texas water districts alone have issued debt in excess of \$12 billion. We found that of approximately 970 financially active districts meeting the Commission's reporting threshold:

- 71 districts, having \$320 million in outstanding bond debt, are at high financial risk
- 128 districts are at moderate financial risk

Although it has authority to do so, the Commission does not monitor the overall financial condition of investor-owned utilities. It lacks authority to monitor the financial condition of water supply or sewer corporations.

Integrate Financial, Managerial, and Operational Oversight

If one were to request all the Commission information on a given entity, including its financial activities, boundaries, rates, facilities, complaints, compliance, and operations, the information would take a long time to compile and would likely be incomplete and contain inconsistencies that would hinder interpretation and decision making. The Water Utilities Division alone keeps 27 databases. Many of these databases lack adequate controls and cannot be related to one another. For example:

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- “Deficiency scores,” which are composite indicators of the performance of public water systems, are frequently miscalculated.
- It is not possible to link data on a water district’s financial condition with its performance as a water supplier.

The Commission is not organized for the convenience of the entities it oversees. The organization structure may have impaired efforts to integrate data. For example, though many of the entities that provide drinking water also provide wastewater service, these activities are regulated by different Commission divisions. Thus, entities must routinely interact with multiple locations within the Commission. Even within the Water Utilities Division, the three sections tend to operate independently despite serving common purposes and overlapping communities.

Exercise Regulatory Authority to Ensure Compliance and Prevent the Formation and Continuation of Nonviable Water Systems

Possibly in response to its complex jurisdiction, the Commission has adopted a passive oversight role. For example, it does not have an active program for ensuring the financial, managerial, and technical viability of water utilities and has been reluctant to deny petitions to create new water districts and to dissolve inactive districts. For selected activities, we recommend more rigorous use of the Commission’s existing authority to provide more state assurance of the integrity of local entities.

Strengthen Controls Over Critical Processes

In support of a more active and comprehensive oversight system, we recommend various operational improvements for:

- Collecting due regulatory assessments
- Administering technical assistance contracts
- Monitoring district financial condition
- Reviewing and approving utility rates and plans
- Monitoring public water suppliers

Work With the Texas Legislature to Simplify and Strengthen Oversight Authority

We recommend that the Commission and the Water Utilities Division work with the Texas Legislature to simplify the regulatory system; for example, by aligning requirements for entities of different types. This would allow the Commission to focus on risks rather than on whether it has jurisdiction.

Summary of Management’s Responses

Generally, the report contains useful recommendations that are expected to improve the Commission’s operations in the Water Utilities Division (Division). As the enclosed comments state, the Division will be taking steps to implement many of the recommendations.

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We would like to thank the members of the audit team for their patience and diligence in working with the many complex issues associated with the regulation of water and sewer utilities within the State.

Summary of Objectives and Scope

Our project objectives were to determine whether the Commission's monitoring and oversight over water districts and utilities is efficient and adequate to protect consumers and public health, and whether Commission

controls and jurisdiction are consistent with risks for entities of various types. We focused mainly on the activities of the Water Utilities Division.

Summary information on the Commission's jurisdiction and regulated community, including public drinking water systems, districts, and retail public water utilities is available at Appendix 4.

We appreciate the courtesy and cooperation extended to us by agency personnel throughout this audit.

Overall Assessment

Given its limited resources and complex jurisdiction, the Texas Natural Resource Conservation Commission (Commission) meets its essential oversight responsibilities over water districts and utilities. The Commission:

- Approves district creations
- Approves district bonds
- Maintains district financial data
- Certifies utilities (sets service areas for water supply corporations and investor-owned utilities)
- Permits wastewater utilities
- Reviews engineering plans for new water facilities
- Sets utility tariffs and rates
- Monitors water quality
- Provides assistance to utilities and customers

In preparing for this project, we heard concerns about the proliferation of special districts and utilities. Often, the boundaries of these entities overlap, causing confusion for the average citizen on matters of service, taxation, fees, and governance. A citizen might reside in different service areas for water, wastewater, irrigation, and drainage, where these are overlaid across existing school, city, county, and other political subdivision boundaries. He or she probably does not care who owns or operates these entities, only that the taxes and rates are reasonable and the service is of adequate quality. Legally, though, ownership matters a great deal, since it helps to determine the extent and nature of the Commission's oversight.

However, significant opportunities exist for the Commission as a whole to achieve greater impact and efficiency using its existing authority. In other areas, its authority could be clarified and standardized.

The regulatory environment is complex. This may explain why the Commission appears reluctant to exercise its authority. We recommend that the Commission adopt a rigorous, integrated, data-driven approach to monitoring that builds on local control while providing greater state guarantee of the integrity of local entities.

These entities play an important role in implementing federal and state water laws and policies. They provide water, wastewater, and other services that are essential to public health, and they have a significant economic impact. Texas water districts alone have issued debt in excess of \$12 billion. (The State does not maintain comprehensive information on the financial activities of investor-owned utilities and water supply corporations.)

While the State is not financially liable for the actions of these local entities, it maintains responsibility for public health, consumer protection, and economic development. In helping to ensure the financial, managerial, and operational integrity of these entities, the Commission provides citizens and taxpayers assurance that they will pay reasonable taxes and fees for quality water-related services.

Our recommendations promote a system which:

- Emphasizes similarities, rather than differences, across regulated entities
- Integrates the Commission's financial, managerial, and operational monitoring of water and wastewater utilities, rather than treating these as separate activities
- Moves from event-driven, case-by-case oversight toward active Commission problem identification and resolution

We appreciate the courtesy and cooperation extended to us by agency personnel throughout this audit. Executive and senior staff members had already identified and begun work on a number of the issues and observations noted in this report, including:

- Data integration
- Electronic filing of district reports
- Development of policies and procedures to standardize processes

Section 1:

Integrate Financial, Managerial, and Operational Oversight

Because of the way it tracks information and is organized, the Commission cannot readily compile and report comprehensively on the status of water districts and utilities, including their financial activities, boundaries, rates, facilities, complaints, compliance, and operations. This may result in delayed identification of problems and possible solutions.

Section 1-A:

Improve Data Management

The Commission's greatest barrier to effective, systematic oversight involves data management. Core differences in the way data is tracked make it difficult to relate data across divisions and sections. The Water Utilities Division (Division) alone keeps 27 databases—roughly one for every four employees. Each section within the Division maintains multiple databases which cannot be linked or which can be linked only with great difficulty. Many of the Division's data sets are ad hoc or designed for a specific purpose, and while they may meet that purpose for a one-time report, they are not designed to be updated and referenced to other data sets. Few of the data sets are documented, and much of the information they contain is self-reported and not verified/validated.

In other words, if one were to arrive at the Commission and ask for all the information it has on a given water and/or wastewater entity, including information on financial activities, boundaries, rates, facilities, complaints, compliance, and operations, the

information would take a long time to compile and would likely be incomplete and contain inconsistencies that would hinder interpretation and decision-making.

At present, all data is hand-entered by Commission staff. This approach is prone to errors, especially where input controls are not adequate, and is time-consuming. Electronic filing of reports has been studied but not yet implemented.

The expenditure of resources to improve data management would be more than offset by increases in efficiency and effectiveness. Adopting a data-driven approach could fundamentally change the way the Division operates. For example:

- Financial and facility information on investor-owned utilities could be used to approve or disapprove rate increase requests
- Financial and facility information from districts could be used to streamline the bond approval process
- Reviews of audit reports and engineering plans could focus on the firms that historically have had the most problems
- Entities approaching capacity or having the greatest financial or operational problems could be targeted for either assistance or enforcement

An impediment to this approach is inconsistent reporting requirements for entities of different types and sizes, particularly financial reporting. While districts have extensive financial reporting requirements, the requirements for investor-owned utilities are minimal, and water supply and sewer corporations are not required to report at all. (See the recommendation in Section 4-D for more information.)

While the Commission has a five-year plan for integrating the Division's databases, there is much the Commission can do sooner, using existing data and internal talent.

Recommendation:

- Improve data management at the Division level or higher.
- Ensure that Division-level data management incorporates standards for:
 - Input, data integrity, and processing controls
 - Security
 - Data ownership
 - System and user documentation
- Develop methods for electronic filing of reports.

Management's Response:

The agency agrees that improvements are needed in the data management systems that support the Water Utilities Division. In order to address these issues, the Division has hired a Database Administrator within the Public Drinking Water Section. The responsibilities of the position include oversight of data input and integrity as well as processing controls. This position along with the Division's LAN Manager will be addressing data security and ownership issues.

In addition, the Division has been proactive in seeking ways to integrate its databases. The Division has developed a data model over the last year. In the summer of 1996, the Division participated in a pilot project or "pathfinder" that utilized a new database development methodology "Composer." The Division successfully completed the project and is proceeding on the second phase that will address utility/public water system contacts. An outcome of composer database development is system documentation. Additional funding for improvement of the Division's data systems has also been requested within the report to the Interim Committee on TNRCC funding.

The Division desires to move to electronic filing of reports as quickly as possible. In fact, the Division is actively working to begin electronic filing of drinking water microbiological sampling reports. After the completion of this initiative, the Division will be exploring electronic filing of additional data.

Section 1-B:

Ensure Coordination of Related Functions

The Commission is not organized to provide integrated monitoring and oversight of the local and regional entities over which it has jurisdiction. The existing structure creates difficulties for entities that must answer to multiple Commission locations.

The Commission is organized mainly by media (such as air, water, waste) and by media-specific programs. It recently has moved toward adopting a functional structure (such as enforcement, regardless of media or program). Missing is a structural recognition of the Commission's interaction with local and regional entities.¹

In contrast to the Commission's overall organization, the Water Utilities Division focuses on its clientele (utilities) and thus gives the utilities a primary point of contact. Throughout this project we heard favorable comments from regulated entities about the Division's expertise and assistance.

However, numerous other divisions and sections of the Commission also interact with water-related entities. For example, although many of the same entities that provide water also provide wastewater service, wastewater utilities generally are regulated

¹ A table showing such Commission interactions is located at Appendix 4.2.

outside the Division.² This is of concern because of the general desirability of integrating state and local approaches to water and wastewater.³

The sections within the Water Utilities Division are District Administration, Utility Rates and Services, and Public Drinking Water. These sections tend to operate independently, in accordance with their distinct functions and history, despite facing similar issues, performing similar tasks, and oftentimes serving the same entities. For example:

- The District Administration and Utility Rates and Services Sections both :
 - Approve the creation of service areas
 - Review engineering plans
 - Monitor financial information
- All sections maintain data, respond to complaints, and provide technical assistance.

The efforts of the three sections seem to be driven by history. Each originated in a different agency. The District Administration Section came from the Texas Water Commission, the Utility Rates and Services Section came from the Public Utilities Commission in 1986, and the Public Drinking Water Section came from the Texas Department of Health in 1992. Together, the sections form the Division as it is organized today. However, the State is not yet achieving the benefits of their co-location within the Division.

While there is no one best way for the Commission and the Division to organize, we recommend that the Commission consider ways to integrate its oversight components. For example:

- Consider creating a Wastewater Section within the Division that parallels the Public Drinking Water Section.

The Wastewater Section would process permit applications, monitor compliance with water quality standards, and approve facility plans and specifications. Though many states have housed water and wastewater programs in different agencies, the placement of these two programs within the Commission gives the agency a unique opportunity to leverage its oversight efforts.

- Consider identifying and coordinating approaches to related functions, such as service area creations and financial monitoring, within the Division.

² Wastewater permits are processed in the Agriculture and Watershed Management Division, and other wastewater activities occur elsewhere in the organization.

³ For example, see *Integrated Resource Planning*, a white paper by the American Water Works Association.

Management's Response:

We agree that integration of agency oversight components is important. The agency has been conducting an examination of its water programs. This process was started in the summer of 1996. A major reorganization plan is expected to be completed in December of 1996.

Section 2:

Exercise Regulatory Authority to Ensure Compliance and Prevent the Formation and Continuation of Nonviable Water Systems

Possibly in response to its complex jurisdiction and resource constraints, the Commission has adopted a passive regulatory approach that relies mainly on voluntary compliance. This agencywide policy extends through the Water Utilities Division. While we do not necessarily disagree with this approach as a regulatory philosophy, it has drawbacks, including the proliferation of districts and service areas, inconsistent compliance by entities of different types, and reductions in revenues that otherwise could be used to support the oversight effort.

Examples of the Commission's passive approach include:

- Not taking active steps to prevent the creation of nonviable systems
- Not dissolving inactive districts or restructuring nonviable systems
- Not enforcing or assessing penalties against entities that do not file required reports or pay required fees
 - Not enforcing against or penalizing investor-owned utilities that do not file annual reports; only a 60 percent compliance rate
 - Not instituting collections on entities that do not pay the regulatory assessment; only an 85 percent compliance rate
- Not exercising authority to investigate or audit districts
- Not conducting a timely follow-up on deficiencies noted in audit reports
- Accepting and processing inaccurate rate applications
- Not analyzing or making active use of financial data submitted by districts and investor-owned utilities; infrequent referrals to the technical assistance contractor

Recommendation:

By not setting and holding to a firm regulatory yardstick, the Commission in effect subsidizes low-performing systems. We recommend that the Commission:

- Make active and consistent use of its existing authority by setting and maintaining minimum standards of performance from water systems
- Standards should address the following:
 - Technical capabilities (drinking water quality, deficiency scores, violations, enforcements)
 - Financial stability and integrity
 - Managerial competence, such as compliance with reporting requirements and books/records statutes
- If it is clear that a system cannot meet the minimum standards, even with appropriate technical assistance, assist local residents in arranging for alternative service arrangements

Section 2-A:

Establish a Viability Assessment Program

For various reasons, the Commission currently does not have a comprehensive process to prevent the proliferation of nonviable systems or to restructure existing nonviable systems. The criteria for granting certificates of convenience and necessity (CCNs) and for creating districts provide some basis for this at present; however, Commission staff members do not make active use of the criteria. Commission staff does not feel empowered to deny the creation of districts and have exhibited reluctance to dissolve inactive districts or to decertify poor-performing utilities.

Because the Commission has not officially defined viability, we cannot say what number or percentage of systems are nonviable; however, many current systems might fall under such a definition. (Viability considers each entity's technical, managerial, and financial capacity.)

Without a state-level viability assessment program, nonviable systems may operate in marginal compliance with federal and state requirements, possibly endangering public health. Taxpayers and customers may have to pay more for water services because potential economies of scale have been lost. Also, the presence of approved but inactive districts may impede local planning and regionalization efforts.

The Commission has had statutory criteria for approving certificates of convenience and necessity (CCNs). CCNs are required of water supply or sewer corporations and investor-owned utilities. These criteria might always have served as a viability screening; however, Commission staff members do not document that they have considered them. Before CCNs are granted, the Commission is obligated to consider

In 1994, the Commission formed a Viability Initiative Task Force to address viability concerns. The team has not met since 1995. It was discontinued as reauthorization of the federal Safe Drinking Water Act stalled in Congress.

Reauthorization of the Act in August 1996 requires the Commission to ensure that all new water systems operating after fiscal year 1999 demonstrate technical, managerial, and financial capacity. The re-authorization also requires the Commission to "develop strategies to assist water systems in acquiring and maintaining the means to comply with the Act, and to maintain a list of systems that are not in compliance with the federal regulations."

several factors, including "the financial stability of the applicant." The Commission must further consider:

- The adequacy of the applicant's debt-equity ratio
- Environmental integrity
- The probable improvement of service or lowering of cost to consumers in that area resulting from the granting of the certificate

CCNs generally are not required of districts. Instead, the criteria for creating districts (including those which will provide water and wastewater service) under Section 293.15 of the Texas

Administrative Code, are that the Commission must consider whether the project is "feasible, practicable, necessary, or a benefit to the land in the district . . ." If not, the Commission "shall deny the petition."

The Commission appears reluctant to deny petitions for the creation of districts. Since 1985, the Commission has approved the creation of 189 districts, and it has not denied any creations. Of the 189 districts created by the Commission since 1985:

- 69 are inactive or of unknown status
- 25 have been dissolved
- 2 have filed for bankruptcy
- 2 are financially unstable (not including those in bankruptcy)

Thus, 98 of the 189 districts (52 percent) approved by the Commission since 1985 are not functioning according to the purposes for which they were created.

The Commission also appears reluctant to dissolve districts.⁴ The Commission's authority to dissolve financially dormant districts derives from Section 49.321 of the Texas Water Code.⁵ At present, approximately 224 financially dormant districts have

⁴ We understand, but have not verified, that recent proposed revisions to Section 293.131 of the Texas Administrative Code would give the executive director more discretion to dissolve districts.

⁵ A financially dormant district is one that experienced the following during the calendar year:

- \$500 or less of receipts from operations, tax assessments, loans, contributions, or any other sources
- \$500 or less of disbursements of funds
- No bonds or other long-term (more than one year) liabilities outstanding
- No cash or investments that exceeded \$5,000 at any time during the calendar year

not yet been dissolved. These represent 17 percent of the total number of districts (1304). Of these, 168 (or 75 percent) are municipal utility districts.

If the Commission were to improve its creation and dissolution processes, the State could be assured that all entities are necessary, viable, and will remain so.

Recommendation:

We recommend that the Commission:

- Establish viability screening and assessment processes
- Strengthen and document the processes used to approve CCNs and create districts
- Dissolve financially dormant districts
- Decertify and assist in restructuring nonviable utilities

It has become expensive to comply with the Safe Drinking Water Act, and smaller systems often lack capital to invest in the facility to make necessary improvements. Thus, as the systems age, more may become nonviable over time. By developing a viability process, the Commission will be able to identify marginal systems and assist them either through technical assistance or restructuring.

Examples of restructuring options include merging or consolidating the entity with a nearby system, conversion of its ownership type (such as privatization or conversion from investor-owned to water supply corporation), or contract operation and maintenance.

Management's Response:

We concur with the recommendation that a viability assessment program is needed. The development of this program is required under the newly reauthorized Safe Drinking Water Act. Staff is presently developing recommended changes to Chapter 341 of the Health and Safety Code and Chapter 13 of the Water Code for possible consideration during the upcoming legislative session. If the language changes are passed, the State can begin to develop a program to address the issues of nonviable systems. The program, along with the Safe Drinking Water Revolving Fund, is expected to promote consolidation of utilities.

After notice and hearing, the Commission may dissolve a district that has been inactive for five consecutive years and has no outstanding bond debt.

Strengthen Controls Over Critical Processes

The Commission can improve its operational effectiveness in various ways, including:

- Improve administration of the regulatory assessment fee to ensure that the State receives due revenues.
- Improve administration of technical assistance contracts to ensure that contracts are cost-effective and that contractors are accountable.
- Refocus and expand the general supervision of districts to ensure identification and follow-up on district problems.
- Streamline and standardize approach to rate setting and engineering plan reviews to ensure consistency and efficiency.
- Strengthen management of the public drinking water strategy.

Section 3-A:

Improve Administration of the Regulatory Assessment Fee

Only 85 percent of entities subject to the regulatory assessment fee actually pay it. The Commission does not attempt to collect from nonpayers. In addition, it has allowed a 10-percent discount for entities that pay the fee quarterly; however, the discount is no longer supported by law. As a result, approximately \$280,000 in due revenue is not available to support Commission oversight.

The regulatory assessment fee is the main source of revenue for the Commission's oversight. It dates to a recommendation by the first Texas Performance Review (*Breaking the Mold*) that "the state should require better regulation and oversight of water districts and river authorities." In accordance with that recommendation, the Legislature mandated in 1991 that districts, water supply corporations, and investor-owned utilities collect a regulatory assessment from each retail customer, as follows:

- 1 percent of gross receipts for investor-owned utilities
- ½ of 1 percent of gross receipts for water supply corporations
- ½ of 1 percent of gross receipts for water districts

These fees are to be remitted to the Commission to be used in the regulation of these entities and to provide technical assistance. The Commission has authority to:

- Enforce payment and collection of the regulatory assessment fee
- Assess penalties for late payment of the regulatory assessment fee

The database used to track fees contains incomplete and inconsistent information. Thus, it is difficult to estimate the uncollected amount. While most of the nonpaying

entities appear to be small, some are not. Based on the limited data available, we estimate that:

- 406 providers of water and/or wastewater (270 investor-owned utilities, 70 water supply or sewer corporations, and 66 districts) did not remit fees in 1995.
- At least \$55,197 and \$81,349 went uncollected for calendar years 1994 and 1995, respectively.
- Had allowable penalties been imposed on the nonpayers, the amounts due would have risen to \$71,565 and \$94,172.

The Division has not initiated collections on nonpaying entities. Management has stated that the main reasons for this are the lack of resources due to previous staff reductions and the relatively small amount of money involved. Though authorized to do so, the Commission does not impose financial penalties for late remittance of the regulatory assessments collected by the utilities. In addition, the Commission has not established administrative sanctions such as suspension of other Commission services, including technical assistance and bond application processing.

Currently, the Commission allows entities to remit the collected fees on quarterly or annual basis. It also allows entities that file quarterly to keep 10 percent of the fee for administrative purposes. The discount for quarterly filing was at one time authorized by law; however, the law has now been changed. Elimination of the discount for filing quarterly would increase available revenues by more than \$200,000 annually.

The fees submitted by utilities are self-reported amounts. When a payment is received, it is often not possible to verify whether the amount submitted is accurate because only about half of the investor-owned utilities submit the required financial reports that otherwise could be used to verify the fee amount.

Currently, the remittance status of an investor-owned utility (IOU) may be checked only when the utility files a rate change application. However, 2 out of 11 rate change files we reviewed were processed even though the IOU was delinquent in its fee payments, and 3 additional files had no evidence to show the status of the IOU's fee payment history. To our knowledge, the remittance status of districts and water supply or sewer corporations are not checked before services are provided.

Recommendation:

The Commission should:

- Develop collection procedures to optimize program revenue.
- Impose administrative penalties on nonpaying entities.

- Check remittance status before providing services.
- For fees paid by investor-owned utilities and districts, check the reasonableness of the submitted amount against the entity's financial reports. If the entity has not submitted the required reports, assess the additional allowable administrative penalties.
- Eliminate the discount for quarterly filing.

Management's Response:

We generally concur with this recommendation. The regulatory assessment fee collection follow-up and enforcement function was de-emphasized by the Division during the last fiscal year due to higher priorities such as the drought. For fiscal year 1996, resources have been redirected to again follow-up on utilities that are delinquent on their payment of the fee. As a result of this redirection, we will also be exploring ways to ensure that fee nonpayment issues are included in enforcement orders on noncompliant systems. We will also be looking at methods to evaluate when denial of services for nonpayment of the fee is appropriate. The Division is hesitant to completely disallow certain services for nonpayment of the fee, especially for technical assistance, when the assistance may result in improved public health protection. In addition, we are initiating contact with our Financial Administration Division to consider sending "Dunning" letters to non-compliant entities who are delinquent in their fee payments.

Changes or deletion of the discount for quarterly filing of the regulatory assessment fee will be examined following the legislative session due to various proposals that are under consideration to consolidate fees or restructure funding of the agency's water programs.

Section 3-B:

**Improve Administration of Technical Assistance Contracts;
Establish an Active Referral System**

The Commission does not capture sufficient data to monitor two technical assistance contracts costing over \$322,000 per year. As a result, it is difficult to tell whether it is getting its money's worth. The Commission also:

- Pays the contractors to provide assistance to entities that are not subject to or do not pay the regulatory assessment fee, though this is the fee source that supports the contracts
- Has not been active in referring entities to the contractors; thus, the assistance may not be directed to entities facing the highest risks

State law requires that a portion of the regulatory assessment fee be used to provide on-site technical assistance and training to public utilities, water supply or sewer service corporations, and districts. Accordingly, the Commission has developed two technical assistance contracts with:

- Texas Rural Water Association (TRWA), for \$17,000 per month
- Community Resources Group, Inc. (CRG), for \$9,838 per month

Monthly invoices from the contractors do not include adequate documentation to support the number of man-hours billed. Specifically, contractors do not submit their employees' time records to support the number of administrative hours, travel hours, workshop hours, or other hours in their monthly invoice. For the Texas Rural Water Association contract, these unsupported hours currently occupy approximately 82 percent of the total amount billed.

Current Commission policy is that any utilities in need, including small cities and property owner's associations, can receive technical assistance from the contractors whether or not they are subject to the regulatory assessments. Our review of fiscal years 1993 and 1994 technical assistance records showed that approximately 20 percent of the total amount of technical assistance was provided to entities such as cities, which are not subject to the regulatory assessment fees.

The Commission has not been active in referring eligible entities to the contractors. Potential referral sources include results of district and utility financial condition analyses, utility management requests, complaints, and Commission survey and/or inspection results as reflected in deficiency scores. Our review of the first six months of 1996 utility assistance progress reports found that only 26 percent of all technical assistance was either referred or directed by the Commission. Without active analysis and referral, it is difficult for the Commission to know whether the entities receiving assistance are the ones which most need it and whether the Commission's funding might supplant the contractor's regular technical assistance.

The current division of labor may explain why technical assistance is not referral-driven. Contract-related duties are performed by two separate sections within the Division: the District Administration Section administers the contracts and arranges for payment of the contractor invoices while the Utility Rates and Service Section is responsible for daily interactions with the utilities and periodic referrals to the contractors.

Recommendation:

To ensure that the contracts provide the right assistance to the right parties, the Commission should:

- Develop a data-driven approach to monitoring based on compliance reviews, analysis, and complaints; establish an active referral system based on these.

- Require the contractors to submit detailed employee time records and record the number of on-site hours in the technical assistance progress reports.
- Either limit technical assistance to entities which pay the fee or extend the fee to cover all entities. If the Commission plans to continue its current policy, it might seek clarification on the current state law as to whether it can lawfully use the funds to serve nonpayers.

Additionally, we recommend that:

- Since many system problems stem from financial or managerial weaknesses, rather than technical ones, expand training offerings to address these areas as well.
- Establish a conflict of interest provision to ensure that state funds will not be used for the lobbying activities.⁶

A documented, data-driven monitoring and referral system would allow the Commission to direct its technical assistance to the entities at highest risk of failure or noncompliance.

Management's Response:

We concur with this recommendation. An active referral system has been initiated by the Division. The Division has also started to redefine the role of the Oversight Committee which is the control point in the administration of the contracts. A review of the contract oversight will be completed by March of 1997. We will also work closely with the Grants and Contracts Division, Internal Audit Division and the Legal Division in establishing our plan to improve contractor oversight.

Section 3-C:

Refocus and Expand the General Supervision of Districts

The Commission has declined to make active use of its authority to supervise water districts. As a result, the State does not have an early warning system for identifying districts in financial difficulty, nor does it have adequate follow-up mechanisms to ensure that local problems are addressed and resolved.

The Texas Water Code gives the Commission broad authority over districts. This authority includes:

⁶ We have no reason to believe that the TRWA or CRG have misused state funds: we suggest this as a preventive practice when contracting with groups that also serve as lobbyists.

- Right of continued supervision, including audits of district records, review of audit reports, complaint processing, and development of reporting and accounting manuals
- Approval of district creation and dissolution
- Approval of bond issuance for most types of districts

To better meet its oversight responsibilities, the Commission should:

- Analyze and publish district financial data
- Move from compliance review toward follow-ups
- Document and standardize bond review procedures

For the most part, we believe these recommendations are consistent with new directions for the Commission that are already underway.

To illustrate the potential use of the district financial data as a tool for risk-assessment, we developed a preliminary methodology for identifying financial risk. Our risk indicators were: operating deficits (expenditures over revenues) for three consecutive years, a ratio of long-term debt to assessed property valuation greater than 10 percent, a total tax rate of over \$1.00 per \$100 valuation, a negative fund balance or greater than 30-percent decrease in combined fund balance from 1994-1995, a debt service fund balance of less than 25 percent of the subsequent year's debt service requirement, or bankruptcy.

According to these indicators, we found a surprising number of districts to be at financial risk even under the present favorable economic conditions. Of approximately 970 districts meeting Commission financial audit threshold:

- 71 districts are at high financial risk; these have \$321.5 million in outstanding debt
- An additional 128 districts are at moderate financial risk
- 392 districts meet at least one of our financial risk criteria
- 20 districts are currently under federal bankruptcy protection
- 136 districts have incurred operating deficits for the last three consecutive years
- 72 districts had a combined debt service and maintenance tax rate over \$1.50 in 1995
- High-risk districts are typically: municipal utility districts, created by the Commission, providers of water and wastewater, located in the Houston region

Analyze and publish district financial data.

The Commission maintains a database of financial information from water district audit reports; however, it does not routinely analyze the data to assess statewide risks, aggregate and publish the data, or use the data to return useful information, such as benchmarked expenditures, to districts. These represent inefficient use of an existing resource.

State law requires each financially active water district meeting a certain threshold to submit a copy of its annual audit report and supplemental schedules to the Commission for review. The reports contain financial and operational information that Commission staff maintain in a database.

Recommendation:

We recommend that the data be used:

- Internally, as part of a viability assessment program and as a risk assessment tool for identifying entities for follow-up activities
- To publish standard reports, or snapshots, on the financial condition of districts; this information would be of interest to State decision makers

- To return useful information to districts, such as benchmarked expenditures⁷

This analysis should incorporate operating results, financial position, debt service capability, economic factors, and qualitative factors disclosed in the annual audit reports. To properly support the analysis and integrate financial data with other Commission databases, the Commission will need to maintain additional data and clarify some of its existing data elements, including:

- Capture district asset and liability data
- Capture total revenues and expenditures for combined funds
- Capture qualitative information disclosed in the annual audit report, including doubt as a going concern, condition of capital assets, economic dependency, and internal control weaknesses
- Incorporate CCN number and Public Drinking Water identification number, where these are available
- Clarify instructions for reporting single family equivalent connections and overlapping tax rates
- Require supplemental schedules from all districts meeting the financial reporting threshold

We also recommend the Commission use the results of this analysis to:

- Detect potential financial and operational problems
- Initiate appropriate Commission follow-up activities to prevent deterioration of the district's financial condition

Management's Response:

The data collected is available for public inspection. The Agency will explore the feasibility of expanding its educational program to include standardized reports based on financial data it is currently capturing. The Division is hesitant to develop a system to rate districts as this may be viewed as subjective and potentially detrimental to the Districts long term viability.

The Agency supports the use of financial analysis as a tool to quantify information. As dictated by circumstances, appropriate Agency action will take the form of sharing this

⁷ For example, the supplemental schedules contain information on tax rates, debt and various other indicators, as well as expenditures for personnel, audit, legal, engineering, financial advisers, bookkeeping, and other contracted services.

information with a district's board of directors. Although we can make recommendations and offer assistance, they have the ultimate responsibility for a district's operation.

Move from compliance review toward field reviews and follow-ups. A primary Commission monitoring function has been to determine whether district audit reports comply with governmental regulations such as GASB (statements from the Governmental Accounting Standards Board), GAAP (generally accepted accounting principles), and Commission reporting requirements. While this is important, we feel that the Commission can now safely redirect its resources toward higher-value follow-up activities.

At one time, the Commission was required to review all district audit reports for compliance; however, in the last legislative session, the wording of the law was changed from the Commission "shall" review the reports to the Commission "may" review the reports. This gives the agency additional flexibility to focus on risks.

Strengths of the compliance review process include:

- The Commission's Annual Audit Report Requirements manual generally provides adequate guidance to CPA firms
- The quality of the audit reports has improved since we last reviewed this function in 1990
- Commission staff does a good job reviewing the reports for compliance

Weaknesses of the process include the following:

- When a deficiency is noted in an annual audit report, the Commission does not typically require the district to correct it; instead, the district is advised to correct it in the next year's audit report
- Commission staff members rarely conduct field audits. When they do, the audits are limited to the review of the independent auditor's working papers rather than district financial records; thus, there is no independent validation of the information contained in the reports

Commission staff conducted no field reviews in fiscal year 1996 and in general have conducted fewer in recent years.

Recommendation:

We recommend that the Commission redirect its resources from detailed review of compliance toward risk-based follow-up activities, including :

- Review of auditor working papers
- Field audits of district financial records
- Investigative management audits, possibly on a contract basis
- Referral to the technical assistance contractors

Management's Response:

Review of CPA's working papers is a current task. However, during fiscal year 1996 that task was not performed due to staff's focus on higher priority tasks; this task was assigned a low priority. In the past, the selections of the CPA's whose work papers were to be reviewed was subjective. In the future, the selection process will be based on a statistical sample.

Refine bond review procedures. The Commission has authority to approve engineering projects relating to the issuance of bonds for most general and special water districts. To evaluate the projects and bond issuance, the Commission has established economic feasibility rules. The rules have largely been successful in preventing the speculative development that occurred in Texas during the 1980s. However, the rules and review procedures should be refined to prevent:

- Oversizing of water and wastewater facilities
- Approving bond amounts higher than necessary to support proposed projects

Commission staff members have created checklists to use during bond review, but these checklists have not been recently updated. Each reviewer uses his or her own set of procedures to complete the checklist. The 1989 State Auditor's *Report on the Financial Condition, Creation and Bond Approval Processes, and Supervision of Texas Water Districts* recommended that the then Texas Water Commission establish written policies and procedures for bond application review. This has not yet been implemented.

We reviewed the bond applications of five districts known to be in poor financial condition. The applications were approved because the projected tax rates under the proposed bonds were

Commission feasibility rules have two components: engineering and financial. Engineering review determines whether sufficient water, wastewater, and drainage facilities exist to serve all the development used to support the financial feasibility of the proposed bond issues. Financial review determines whether the projected growth in the assessed property value will be sufficient to support the projected debt service payment of the proposed bond issue and all other outstanding debt with the levy of a reasonable tax rate. The reasonableness and competitiveness of the utility rates are determined by comparing the rates to other competitive development located adjacent to the district.

Economic feasibility is influenced by many factors, such as general economic conditions, the real estate market, the number of competing projects, and geographical location. To address these, the Commission has established tax rate ceilings under assumptions of growth and no-growth. Under a growth assumption, the maximum debt service tax rate ranges from \$1.00 to \$1.50 per \$100 of assessed value. Under a no-growth assumption, the range is from \$2.00 to \$2.50, depending on location.

lower than the established feasibility tax rate ceilings. The high caps may have contributed to high rates of bond approval, as shown in the following table.

	1994	1995
Percentage of bond applications approved	99.0	93.6
Percentage of bond amounts approved	93.6	94.7

Additionally, controls may not be sufficient to prevent the oversizing of facilities. In three out of eight (or 37.5 percent) cases we reviewed, water facilities had approximately 2.5 times the size of the facilities to support the projected number of equivalent single family connections. The Commission approval memos stated that “the facility would be more than adequate to serve the number of connections upon which the feasibility of the subject bond is based.” We found three additional instances of approval of proposed wastewater treatment facilities having more than 1.5 times the size of the facilities needed to support the expected number of equivalent single family connections. A net effect of oversizing would be an unnecessarily higher amount of bond approval than needed to serve the number of connections.

Recommendation:

We recommend that the Commission improve the quality of its bond reviews by:

- Documenting and standardizing bond review procedures
- Refining its tax rate caps
- Considering potential oversizing of facilities

Management’s Response:

We agree that it is important to have standardized procedures for conducting bond reviews. We continue to work toward perfecting this. The agency rules on bond review have been drafted in great detail to give specific direction to staff and the regulated community. Also, we have recently updated our application check list, bond application report formats and employee training manual.

The auditor indicates that the high tax rate caps established by rule may have been the cause of the poor financial condition of some districts. While this may be a factor, we do not believe that an adjustment to the maximum feasibility tax rate is necessary. There are many districts which have tax rates that approach this level and are not considered to be in poor financial condition. Based on the 1994 tax year, 58 districts had debt service tax rates exceeding \$1.50. Of those districts, only nine had bonds approved after our feasibility rules (with maximum tax rates) were adopted. Six were approved after waiving the tax rate limits to finance facilities needed as a result of

litigation or enforcement orders. One was approved in 1996 as a result of a substantial increase in assessed valuation and subsequent decrease in tax rates. Only two have not met their growth projections but they are both experiencing a high collection rate on their taxes.

We concur that it is important to check for the over sizing of utilities as a part of our bond review. Many factors are taken into consideration such as the ultimate needs of the district, regionalization, and economies of scale. We will however, take a closer look at the immediate needs in analyzing future bond applications.

Section 3-D:

Streamline and Standardize Approach to Rate-Setting and Engineering Plan Reviews

The Commission has not made full use of the authority granted it under Chapter 13 of the Texas Water Code to ensure that all utilities meet minimum standards; this has contributed to the proliferation and continuation of possibly nonviable entities throughout the State. The absence of documented procedures may have contributed to perceptions of inconsistency in setting rates and reviewing engineering plans.

Under Chapter 13, the Commission executive director and staff:

- Are granted extensive power to establish and enforce a comprehensive system to regulate retail public utilities, and to assure rates, operations, and services are just and reasonable to customers and retail public utilities
- Are given all authority and power of the State to ensure that utilities meet their obligations
- Have a wide array of remedies including fines, placing the utility under supervision, and imposing felony charges

Recommendation:

To ensure a comprehensive regulatory system and to increase efficiency and effectiveness, we recommend that the Commission:

- Redesign annual reporting requirements.
- Develop and document a system of accounts approved by the executive director; give adequate guidance on how to adjust the National Association of Regulatory Utility Commissioners (NARUC) uniform system of accounts.
- Ensure mathematical accuracy in administrative review and ensure compliance with statute and orders related to the preliminary hearing process

- Develop policies and procedures for rate changes and plans reviews.
- Develop a format and review criteria for the 85-percent plant capacity planning report.
- Standardize and publish the rate-setting methodology.

Redesign annual reporting requirements for investor-owned utilities. The Commission requires each investor-owned utility (IOU) to submit an annual report. However, it does not make active or timely use of the reporting requirement to facilitate processes such as rate making. Possibly because IOUs see little value in the reports, compliance with the requirement is low.

The Commission has authority to:

- Design the format of the annual report.
- Set the reporting deadline.
- Use the information gathered to regulate the IOUs.
- Enforce compliance with the annual reporting requirements.

The Commission does not use its authority to ensure that all IOUs comply with annual reporting requirements. The 1993 and 1994 compliance rates were only 60 percent and 40 percent, respectively.

At the time of our audit, the Commission had not requested the 1995 annual reports. IOUs were given until August 15, 1994, to submit their 1993 annual reports and until October 15, 1995, to submit their 1994 reports. Such untimely information is of little value.

The Commission does not consistently use data from the reports to facilitate overall monitoring of the universe of IOUs. It captured 1993 data and prepared a fact sheet but did not use the data to set benchmarks or analyze the financial viability of the reporting IOUs. The 1994 data was not used or entered into the database.

If the Commission were to ensure that all IOUs submit timely reports, it could use the information to facilitate:

- **Rate setting.** Under this scenario, IOUs would only have to submit minimal updating information when requesting a rate change, and a rate setting program could be used to drive rate calculations. This would reduce the number of applications that IOUs must submit as well as staff time spent processing and reviewing the 21-page rate change application.
- **Risk assessment.** The Commission could use the data to monitor trends and patterns for the universe of IOUs, monitor financial conditions, set benchmarks, and direct its audit resources and technical assistance toward

IOUs facing the greatest risk of financial or operational failure. This information could feed directly into a viability assessment program.

Recommendation:

We recommend that the Commission redesign the IOU annual reporting requirement to increase efficiency. Specifically:

- Gather information sufficient to facilitate rate setting and risk assessment.
- Establish a more timely due date for the annual report.
- Capture all annual report data in a database; consider means of electronic submission of data.
- Ensure compliance with the annual reporting requirements.

Management's Response:

We agree with the recommendation of the auditors to design this requirement. This process will require an increase in monitoring and oversight by the Division. Additional staff will be required in both the Water Utilities and Enforcement Divisions. As the agency moves forward to establish a viability program, special emphasis can be placed on improving this aspect of the Division's workload. We will modify the rate of return calculation procedures to recognize compliance with this and other reporting requirements.

Develop and document a system of accounts approved by the executive director; provide guidance on adjusting the NARUC uniform system of accounts. The Commission has not developed a uniform system of accounts for public water and/or sewer utilities, nor has it given utilities adequate guidance on how to adjust the NARUC's uniform system of accounts. It also has not ensured compliance with books and records requirements. As a result, these entities lack clear procedural guidance and may face unnecessary difficulty in filing for rate changes.

Under Chapter 291.72 of the Texas Administrative Code, utilities may choose either:

- A system of accounts approved by the executive director which will be adequately informative for all regulatory purposes, or
- A uniform system of accounts as adopted and amended by NARUC

Recently, the Commission worked with the community of investor-owned utilities to develop a minimum bookkeeping guide for small utilities (fewer than 200 customers) and a survival guide for small utilities which contains a section on keeping records and filing a rate application. While these are steps in the right direction, they do not qualify as a comprehensive system of accounts or provide sufficient guidance on how to adjust the NARUC system.

Commission staff members do not ensure compliance with books and records statutes. During field audits and desk reviews, section staff members find utilities which are not in compliance. For example, during a desk review, Commission staff determined that:

- A utility's books and records were not kept separately from a related company
- The utility had no records relating to plant and equipment maintained

The review letter to the utility owner said, "we suggest that you attempt to separate the records," referred the owner review to the minimum bookkeeping guide, and stated that "no further action is required by this letter." The letter did not cite the legal requirement or require a corrective action plan with an implementation date.

Recommendation:

The Commission should:

- Develop and document a system of accounts approved by the executive director for all utilities.
- Provide utilities guidance on how to adjust the NARUC's uniform system of accounts to the requirements of the rate change application
- Ensure compliance with books and records statutes and consider requiring corrective action plans

Issue for further consideration:

Consider developing a formal certification process for managers of investor-owned utilities. Increasing the managerial competence of IOU owners would reduce the time currently spent by staff subsidizing poor performing systems and providing record keeping assistance to utilities.

Management's Response:

We agree with this recommendation. The staff has developed two alternative systems of record keeping. The Record Keeping Manual for use by the smallest systems which has been available for a number of years was never officially published. It has been revised and updated to more closely tie to the rate application. The staff developed TNRCC chart of accounts which would be suitable for utilities of any size has been reviewed by utility representatives once and the revised version is currently under review by utility representatives. These two documents will be published as Regulatory Guidance Documents in early 1997. With the availability of the TNRCC chart of accounts, only utilities with professional accounting help are likely to use NARUC accounts so additional guidance on the NARUC system is not a wise use of limited staff resources. We anticipate that through the viability program which will be

initiated with federal SDWA funds record keeping issues will be addressed more strenuously. In the interim as a part of rate application review, staff will become more stringent in requiring and assisting utilities to develop and maintain proper record keeping.

This agency has been actively working with Stakeholder groups to move forward on the managers' certification process. The idea has received favorable review. We will continue to work with the stakeholders on this important issue.

Ensure mathematical accuracy in administrative review and ensure compliance with statute and orders related to the preliminary hearing process. Administrative review of rate change applications does not ensure mathematical accuracy of the information presented on the application, and Commission staff members do not enforce compliance with statute and orders related to the preliminary hearings process. These weaknesses may result in additional work by staff and may put customers in an unfair position in the hearings process.

Chapter 13, Section 184(c) of the Texas Water Code states that, in any proceeding involving any proposed change of rates, the burden of proof shall be on the utility to show that the proposed change, if proposed by the utility, is just and reasonable. Additionally, preliminary hearing orders instruct utility owners to bring all books and records to the hearing for inspection.

Customers complain: A utility owner should not be allowed to increase its rates if it files an inaccurate application and does not provide supporting documentation.

We observed a case in which the Commission accepted an application containing incomplete and inaccurate figures. Customers came to the preliminary hearing to review the utility's support for the rate increase. At the hearing, the utility owner did not produce supporting documentation for the questioned items and failed to prove that the rates were just and reasonable. However, the customers were faced with possibly having to pay the utility's legal and accounting cost associated with proceeding to an evidentiary hearing. Because they felt forced to rely on Commission staff's testimony, they settled. In the words of one customer, "**rate-payers were left with no economically feasible method of obtaining adequate information.**"

Each rate change application undergoes an administrative review prior to it being accepted for filing. During the administrative review, staff exercise judgment in determining the significance of any missing and inaccurate information on the rate change application.

Recommendation:

We recommend that the Commission:

- Include mathematical accuracy of the information presented on the rate change application as a criterion for administrative approval.
- Enforce compliance with statute and orders related to the preliminary hearing process.

Management's Response:

We concur with this recommendation. For small utilities, hiring consultants to assist in preparing a rate application is prohibitively expensive for both the utility and customers. Until our technical assistance staff and contractors can get out and work with these smaller utilities, rigidly enforcing requirements and rejecting applications for lack of mathematical accuracy may not be a prudent step because it can leave small systems in financial difficulty rather than helping them increase revenues to a level which can support an improved level of service. The critical issue should be whether information in the applications can support the requested rates and staff are reevaluating the administrative review process to ensure that necessary information is included before administratively accepting applications.

Preliminary hearing notices and requirements are being reevaluated to ensure that information requested in the notice will be available and to remind customers that documentation is available for their review at the utility's office prior to the preliminary hearing. The initial notice of the rate application tells customers that a copy of the application is available at both the utility and TNRCC offices. Staff members have also been reminded that additional preliminary hearings can be requested to address customer concerns. It should be noted that documentation may or may not support settled rates because they are an agreement between the utility, customers and TNRCC staff and there is no burden of proof on a settlement.

Develop policies and procedures for rate changes and plans reviews.

Weaknesses in the processes for reviewing rate change applications and engineering plans allow for inconsistencies across reviewers and inefficient use of staff time. We observed the following:

- No standard set of policies and procedures for
 - Conducting the rate change and plans reviews
 - Work paper documentation
 - Field audits
- Informal training process
- After-the-fact use of the peer review process to ensure consistency

The Commission lacks a standard set of policies and procedures for conducting rate changes and plans reviews. While it has developed various tools for these purposes, including spreadsheets, guidelines, checklists, and standard forms, no system is in place to ensure that staff members have the documents, use them, and receive timely notification about revisions.

Generally, staff members conduct their reviews based on their professional judgement and knowledge of statutes and rules. The knowledge and experience of senior staff represent a valuable resource that is not being fully captured and used, and may be lost if the staff person leaves.

Staff members retain their work paper files at the conclusion of a review, whether for rates or engineering plans. They may keep the files in whatever manner they choose. Usually, they retain no work paper files at all for review of engineering plans.

The rate change review official file lacks documentation to support staff adjustments to costs included in the cost of service rate base. If challenged, the Commission would not have documentation necessary to support the decisions made. We reviewed rate change review work papers which:

- Had no logical order
- Varied in documentation
- In most cases had no support for staff adjustments

One file contained documentation stating that “the staff concluded that this utility cannot justify a rate increase.” However, the rate increase was administratively approved even though the requested rate was higher than the staff’s proposed rate. We found no documentation supporting the rate approval.

The Commission also has no standard policies for selecting and conducting field audits. Accountants and engineers decide if and when they will conduct a field audit, and they are expected to know how and what to audit. They retain no standard audit programs. This approach increases the possibility of inconsistent audit quality and inefficient use of staff time.

Current training methods are informal. They include:

- Observing other staff members’ reviews and hearings
- Asking the right questions
- Reading applicable laws and rules

We found no formal training offered on mediation, writing depositions, or preparing for formal hearings.

The Commission relies on the peer review process to ensure consistency. However, this occurs after the staff members have completed their work, when detecting inconsistencies results in rework. In addition, staff must spend time preparing for and attending the weekly peer review sessions.

Recommendation:

The Commission should:

- Streamline and standardize its approach to rate change and plans reviews by developing a standard set of policies and procedures for these processes, including work paper documentation:

- Establish minimum work paper standards for rate change files, both contested and uncontested; particularly, support for staff's adjustments of costs included in the cost of service rate base.
- Establish minimum work papers standards for review of engineering plans, preferably in a way that facilitates tracking of the performance of engineers and engineering firms. Consider developing a checklist for determining when an engineering firm should be referred to the professional board for substandard performance.
- Ensure that staff members are trained in the policies and procedures and that they implement them consistently. Develop additional training on mediation and legal proceedings.
- Reevaluate the benefit and need for the peer review process once standard policies and procedures have been developed and implemented. Upper-level review of staff work might be a more efficient way to gain accuracy and consistency.

Management's Response:

We agree with the auditors that written procedures are needed where absent or when they need improvement. The Division has been moving forward on this in various areas. A reason there is less emphasis placed on written procedures in the plan review program is the tenure of the current staff. Nevertheless, we will begin looking at the existing staff guidance and improve the current or build written procedures where none exist. This will more than likely result in redirection of resources from other areas until procedures are completed.

Develop a format and review criteria for the 85-percent plant capacity planning report. The Commission has not developed a format or review criteria for the 85-percent plant capacity planning report. Thus, the reporting requirement and the reviewing process cannot be applied uniformly and consistently, and information of value to state and local decision makers may be lost.

Under Chapter 13 of the Texas Water Code, the Commission is responsible for gathering information on facilities that are approaching full capacity. Rather than design a report for this purpose, the Commission has waited to see what types of reports are submitted. If the reports contain different information, the results cannot be aggregated and analyzed for statewide planning purposes.

Recommendation:

We recommend that the Commission:

- Develop a format and review criteria for the 85-percent plant capacity planning report
- Publish the format and review criteria for utility owners' use.
- Develop a process to ensure that adequate policies and procedures are developed for new legislative requirements.

Management's Response:

We concur with this recommendation. A project plan for implementation of the 85 percent rule was developed in October. The project is scheduled for completion in January of 1997. An outcome of the project will be both a published guidance on the format and review criteria for the planning report. The guidance will be available to all utilities.

After the last legislative session, the agency created a legislative implementation plan to cover all aspects needed to fully implement the new statutes. Unfortunately, the 85 percent rule was not fully covered by the implementation plan process.

Standardize and publish the rate-setting methodology. The Utility Rates and Services section of the Water Utilities Division has begun developing a rate-setting methodology for publication and distribution to utilities. The absence of a published methodology has allowed utilities to be uncertain on matters such as allowed costs. The draft manual is a good start. However, additional work is needed to ensure consistency among staff in applying the methodology.

Chapter 13 of the Texas Water Code gives the Commission power to promulgate rules and regulations with respect to the allowance or disallowance of certain expenses for rate making purposes. The chapter states that the Commission shall consider the following factors, in addition to other applicable factors, in fixing a reasonable return on invested capital:

- Efforts and achievements of the utility in the conservation of resources
- Quality of the utility's services
- Efficiency of the utility's operations
- Quality of the utility's management

The draft manual documents the standard practice for determining premium/bonus basis points. The standard:

- Describes the criteria influencing the number of points assigned to two criteria:
 - Risk (economic/demographic/other)
 - Quality of management (separated into three categories)
 - Good quality of service
 - Efficiency of operations
 - Water conservation efforts
- Gives point scale ranges for each influencing criterion
- Gives a scale for making the premium/bonus basis point determination based on total points assigned

However, the standard omits instructions for assigning the point value within each influencing criterion's range of points. The Commission thus cannot ensure consistency among staff in applying the methodology without specific instructions for assigning the point values. Yet IOUs need to know how the Commission will treat certain expenses for rate making purposes in order to make prudent business decisions.

Recommendation:

We recommend that the Commission:

- Develop and publish a rate manual which addresses all aspects of rate setting, including policies and procedures for rate change reviews and hearings.
- Ensure consistency among staff in applying the rate-setting methodology.

Management's Response:

As stated in the report, the Division has begun reducing to writing a rate-setting procedures manual. When completed, the manual will be published and distributed to utilities. Portions of the methodology are scheduled for completion in December of 1996. Other portions will be added as they are developed. The agency has actively solicited comments and input from the regulated community and consumer groups in this process.

Section 3-E:

Strengthen Management of the Public Drinking Water Strategy

No single individual *manages* the Commission's Public Drinking Water program. Funding and staffing for the program are spread among five Commission organizational units: the Public Drinking Water Section in the Water Utilities Division, Legal, Field Operations, Operator Certification, and Enforcement. While the program is *coordinated* by a Public Water Supply System committee, composed of regional, central, and field operations personnel, this effort is not sufficient to ensure that the program accomplishes its objectives. For example, the results of inspections,

expressed as composite deficiency scores, are often incorrectly calculated, and the number of inspections of public drinking water systems has declined over time.

Recommendation:

We recommend that the Commission strengthen management of the program to increase the number of water system inspections and improve calculation of system deficiency scores. We also recommend that the Commission's Internal Audit Department monitor the program's progress in implementing recommendations on data management.

Improve calculation of system deficiency scores. A potentially high percentage of deficiency scores, based on inspections and performance of drinking water systems, have been miscalculated by inspectors and maintained in Public Drinking Water Section databases. The deficiency score is arguably the most important single measure of the performance of drinking water systems. A deficiency score of 20 or higher is the threshold for determining whether a system poses an imminent health hazard to its customers and whether it should be enforced against. In this regard, the Commission lacks important data on which to assess risks and make decisions.

We queried Public Drinking Water data to find systems having deficiency scores higher than 20. The query found that 616 systems, serving roughly 3.5 million Texans, had deficiency scores of 20 or higher. Alarmed, we immediately contacted the State's drinking water coordinator. He noted that the scores might have been miscalculated if the inspector failed to differentiate between items which cumulate (such as violations of water quality standards) and items which do not (such as a certain design flaws). He offered to recalculate deficiency scores for 13 large systems based on original inspection reports. The recalculation found that 10 of 13 deficiency scores had been calculated incorrectly.

This incident reflects shortcomings in the program's data management, including insufficient analysis and use of the data, nonvalidation of data, and the absence of standard reports which otherwise would have identified these errors.

Recommendation:

The Commission should:

- Develop training to ensure that regional inspectors correctly calculate deficiency scores.
- Establish a quality control function to ensure data accuracy and inter-rater reliability.

Issue for further study:

Consider updating and revising the inspection checklist; for example, the penalties associated with lacking a certified operator appear low.

Management's Response:

We agree with this recommendation. This issue has been forwarded to the Public Drinking Water Committee for resolution.

Increase the number of water system inspections. The number of inspections of water facilities has declined over time, partly because skilled inspectors are busy drawing water samples instead of inspecting facilities. Rejected samples, due either to improper sampling procedures or nonpayment of the utility's lab fees, are costing the Commission between \$135,342 and \$270,468. Agency management is aware of this misallocation of resources and has taken preliminary steps to address the situation.

The Commission's 61 regional drinking water inspectors spend a considerable amount of time drawing water samples. This detracts from the time they would otherwise spend inspecting facilities. The number of inspections (also called "sanitary surveys") has declined as chemical sampling activity has increased, as shown in the following table.

Activity For Federal Fiscal Years 1992-1995				
Type of Activity	1992	1993	1994	1995
Samples	14,751	58,425	95,445	77,871
Surveys	4,967	4,464	4,633	4,064

The Commission considers several factors when compiling the sample schedule, including:

- The labs' workload. Only two approved labs in the State are competitive in price with respect to the analysis of water samples: the Texas Department of Health (TDH) lab for organic and inorganic lab analyses, and the Lower Colorado River Authority for only organic analyses. The level of work the labs can handle affects how much sampling is scheduled.
- The systems' sampling requirements. Sampling requirements are annually for surface water systems and once every three years for groundwater systems.

- The results of the vulnerability assessments. The Commission's vulnerability assessment program evaluates the vulnerability of the water source and issues waivers to the less vulnerable wells based on a complex, documented program; this reduces sampling for systems with less vulnerable sources.

Based on these factors, the Public Drinking Water section compiles a sampling schedule and sends a copy to each regional office. It is the region's responsibility to determine how it will accomplish the schedule.

The TDH rejects about 5 percent of samples because:

- The sampler did not follow appropriate collection and preservation techniques
- The water system has overdue accounts with TDH

Samples rejected by the lab are done so at a cost to the Commission. The cost of rejection is estimated at \$33 for nearby systems and \$66 for systems farther away (increase due to travel costs to and from the lab). The Texas Department of Health has estimated that the rejection rate is about 5 percent of total samples. We estimated total samples to be 81,969, of which 4,098 were rejected. Thus, the Commission's rejection cost ranges from as \$135,342 to \$270,468.

The Commission hopes to obtain additional state funds to award a contract of about \$1.1 million (or nearly 1/6th of total program cost) to a vendor to perform sample collections; this would allow inspectors to conduct more surveys. It also is considering risk-ranking facilities for inspections.

Recommendation:

We recommend that the Commission:

- Either (1) contract with a vendor to collect samples or (2) transfer this responsibility to lower pay grade employees

If the Commission decides to continue water sampling, it should provide additional training on proper collection and preservation techniques. If it decides to contract for water sampling, it should ensure that the contractor practices proper collection and preservation techniques.

- Develop a mechanism whereby TDH informs the Commission about which systems have overdue accounts on a monthly basis. This would help the Commission reduce the rate of sample rejection.

Management's Response:

We agree with this recommendation. Procedures have been initiated in cooperation with the TDH laboratory that have significantly reduced the rate of sample rejection.

TDH has also stopped rejecting samples for overdue accounts until an alternate payment scheme can be developed.

The agency is anticipating adding field staff in this fiscal year due to an increase in the Safe Drinking Water Supervisory Grant. Additional field staff and dollars for a sampling contract have been requested in the Division's report to the Joint Committee on TNRCC funding.

Monitor the progress of the public drinking water section in implementing internal audit recommendations. While we gained an understanding of the funding, functions, and organization of the Public Drinking Water Section, we conducted little test work. This is because:

- Our scope focused mainly on matters of financial oversight and general supervision rather than technical matters involving water quality.
- The Commission's Internal Audit Department had recently conducted a thorough and critical review of the Public Drinking Water Section's data management. This would otherwise have been a large part of our work.
- During the time of our review, parts of the State were experiencing drought conditions having serious implications for the provision of safe drinking water to Texas residents. We had no wish to interfere with the Commission's effort to coordinate statewide drought response.

Recommendation:

Given the importance of the drinking water program and its difficulties with data management, we recommend that the Commission's Internal Audit Department conduct a follow-up review of the Public Drinking Water program within the next 18 months. To provide additional assurance, it might expand its scope to include general administrative controls not considered during our review.

Management's Response:

The TNRCC Internal Audit division performs semi-annual follow-ups on all completed audits. The Water Utilities Division has and will continue to provide status updates and supporting documentation to the auditors. Future Internal Audit projects are selected based upon a formal risk assessment process. The auditors will consider the information in this report during their risk assessment.

Work With the Texas Legislature to Simplify and Strengthen Oversight Authority

Regulation of water and wastewater entities is complex, and Commission jurisdiction varies widely according to numerous factors. The net effects of this complexity are that:

- For an individual citizen, the extent to which the State guarantees the integrity of the local utility service provider depends on where the citizen lives.
- The Commission cannot be held accountable for the landscape of overlapping political jurisdictions and service areas.

To some extent, the complexities of local development are unavoidable. However, where it is possible to do so with minor changes, we recommend that the Commission work with the Texas Legislature to establish a more consistent and comprehensive regulatory system. This would encourage the Commission to focus on risks rather than on whether it has jurisdiction.

Under the state drinking water program, the Division regulates nearly 7,000 public drinking water systems. These systems are of four main ownership types:

- Cities (generally not within the scope of our audit)
- Water districts⁸
- Nonprofit water supply or sewer corporations
- Investor-owned utilities

The State also regulates approximately 4,200 active wastewater utilities. These are of 6 main ownership types, including the ones listed above.

The majority of drinking water systems in Texas are either small or very small, according to Environmental Protection Agency (EPA) definitions.⁹ In general, smaller systems face greater difficulty complying with federal and state requirements. Their sheer number drives the Commission's workload.

⁸ The Division regulates 1300 districts of 12 general types; 650 of the districts operate water or wastewater facilities. Districts that do not provide retail water include river authorities and drainage, navigation, and levee improvement districts. Detailed tables on the regulated community are available at Appendix 4.

⁹ In the table at the top of the next page, cities and districts combined are shown as local government. Size categories are based on number of people served:

Very Small (<500)	Small (501-3,300)	Medium (3,301-10,000)
Large (10,000-100,000)	Very Large (>100,000)	

	Very Small	Small	Medium	Large	Very Large	Total
Federal	121	13	2	1	0	137
Investor	3583	63	1	1	0	3648
State	155	9	0	0	0	164
Local Government	920	750	144	64	6	1884
Water Supply Corporation	759	242	11	3	0	1015
	5538	1077	158	69	6	6848

Source: Unaudited data, Public Drinking Water Section, TNRCC

Commission authority and jurisdiction over these water and wastewater entities depend on multiple, interacting factors, including:

- The entity's purpose (such as water, wastewater, or irrigation) and how it was created
- Specific Commission function (such as bond approval, rate making, or general supervision)
- The entity's ownership type (such as city, district, nonprofit water supply or sewer corporation, or investor-owned)
- The entity's service area and its relationship to nearby political subdivisions (within or outside city limits, for example)

The table on page 40 shows a rough outline of the Commission's jurisdiction for various oversight activities. It also serves as a map for a number of our recommendations.

Commission Regulatory Function	Cities	Water Districts	Water Supply or Sewer Corporations (WSC)	Investor-Owned Utilities (IOU)
Monitor compliance with federal and state drinking water quality standards	Yes	Yes	Yes	Yes
Approve service areas (district creation and utility certification)	No	Yes, for most types of districts, per criteria listed at of the Chapter 293 of the Texas Administrative Code; a certificate may be required if serving within another utility service provider's lawful service area ^A	Yes (unless exempt), via Certificates of Convenience and Necessity (CCNs), per criteria listed at Section 13.246 of the Texas Water Code ^B	Yes, (unless exempt), via CCN
Monitor financial condition	No	Yes, from annual audit report, except ground water districts	No ^C	Yes, from annual report
Set/approve rates and tariffs	Appellate jurisdiction, if 10% of customers protest	Appellate jurisdiction, if 10% of customers protest	Appellate jurisdiction, if 10% of customers protest	Original jurisdiction for IOUs outside the city; appellate jurisdiction for IOUs inside a city ^D
Approve bonds	No	Yes, for most districts, except river authorities, drainage, levee improvement, and navigation districts ^E	N/A	N/A
Review engineering plans for water systems	Yes	Yes	Yes	Yes
Review engineering plans for waste water systems	The Commission "may review" ^F	The Commission "may review"	The Commission "may review"	The Commission "may review"
Provide Education and Technical Assistance	Yes	Yes	Yes	Yes
Administer Regulatory Assessment Fee	Not subject to fee; may receive technical assistance funded by fee ^G	Yes, ½ of 1% of gross receipt	Yes, ½ of 1% of gross receipts	Yes, 1% of gross receipts
^A See recommendation on aligning criteria for creating districts and granting certificates (Section 4-A). Districts also may be created by the Texas Legislature and County Commissioners Courts. ^B See recommendation on approach to prevent federal preemption where WSCs have federal debt (Section 4-B). ^C See recommendation on WSC financial reporting requirements (Section 4-D). ^D See recommendation on giving the Commission greater flexibility in setting rates (Section 4-G). ^E See recommendation on clarifying elements from recodification (Section 4-C). ^F See recommendation on integrating oversight of water and wastewater utilities (Section 1). ^G See recommendation on administering the regulatory assessment fee (Section 3-A).				

This table is included only as an indication of the complexity that the Commission faces. It is not all-inclusive of the sometimes subtle differences the agency faces in

exercising its jurisdiction. More detailed information on Commission jurisdiction is shown at Appendices 4.5 and 4.6.

Recommendation:

To assist in simplifying and strengthening the regulatory system, we suggest the following options:

- Align the criteria for creating districts and granting certificates of convenience and necessity to clarify the Commission's obligation to consider alternatives to new creations.
- Where water supply or sewer corporations have federal debt, develop an approach to prevent federal preemption.
- Establish financial reporting requirements for water supply or sewer corporations.
- Clarify elements from the last legislative session's recodification regarding Commission bond approval authority, district competitive bidding requirements, financial reports from groundwater districts, and election provisions for special law districts.
- Require counties to notify the Commission of new districts they have created.
- Require districts to seek multiple proposals in selecting CPA firms.
- Revise Chapter 13 of the Texas Water Code to give the Commission greater flexibility in setting rates.
- Consider establishing incentives to encourage regionalization.

Management's Response:

The agency is committed to working with the Legislature, as requested, to make any statutory changes that may be necessary.

Section 4-A:

Align the Criteria for Creating Districts and Granting Certificates of Convenience and Necessity (CCNs)

Districts may be created by either the Commission, counties, or the Texas Legislature. Most have been created by the Commission or its predecessor agencies. The criteria

for creating a district are that the project is feasible, practicable, necessary, and beneficial to all of the land to be included in the district.

Water supply corporations and investor-owned utilities are required to have CCNs (certificates of convenience and necessity, which are defined utility service areas). The criteria for granting a CCN are more specific. They include:

- Adequacy of service currently provided to the requested area
- Need for additional service in the requested area
- Effect of the granting of a CCN on the recipient of the certificate and on any retail public utility of the same kind already serving the proximate area
- Ability of the applicant to provide adequate service
- Feasibility of obtaining service from an adjacent retail public utility
- Financial stability of the applicant, including debt-equity ratio
- Environmental integrity
- Probable improvement of service or lowering of cost to consumers in that area resulting from the grant of the certificate

As can be seen, the criteria for granting a CCN are more specific and stringent than are those for districts. We suggest aligning the criteria to make clear the Commission's obligation to consider alternatives to new creations.

Issue for further study:

Consider whether to require CCNs from cities and districts. This might provide a partial solution to the Division's efforts to integrate its databases if the CCN number could be used as a master cross-referencing index. CCNs might be required from all districts or from selected subsets, such as county-created districts.

Section 4-B:

Where Water Supply or Sewer Corporations Have Federal Debt, Develop an Approach to Prevent Federal Preemption

In two recent cases, federal courts have struck down efforts by Texas cities to extend their service areas because the extension would have encroached upon the existing boundaries of a water supply corporation (WSC) having federal debt. A number of similar cases are pending.

Since the 1960s many water supply corporations have borrowed money at favorable rates from the federal Farmer's Home Administration (now the Rural Development Administration). As a condition of the loan, the WSC must not change its boundaries in a way that would affect its ability to repay. However, in these cases, as we understand, the federal debt was not at risk since the acquiring entities were willing to assume it.

In any case, it would be preferable for the State and the local governments to make these decisions based on rates and quality of service and other criteria, rather than on the pre-existence of federal debt. We suggest that the State develop an approach to ensure that the federal debt is not placed at risk and thus avoid federal preemption. We recognize that state efforts may not be sufficient to address this issue, since it involves federal statute and court interpretations.

Section 4-C:

Clarify Elements From the Last Legislative Session's Recodification

Senate Bill 626, passed in the last legislative session, went a long way toward promoting procedural uniformity across districts. However, several important controls were omitted during the recodification. Specifically, we suggest the following:

- Restore Commission authority to approve bond applications for drainage districts, levee improvement districts, and navigation districts.
- Restore competitive bidding requirements for district purchases of materials/machinery.
- Restore the requirement that groundwater districts submit annual financial reports to the Commission.
- Remove conflicting election provisions for special law districts.

The Commission's District Administration section can provide additional detailed information.

Section 4-D:

Establish Financial Reporting Requirements for Water Supply or Sewer Corporations

At present, the State does not collect any information on the financial activities of water supply or sewer corporations (WSCs). These entities serve approximately 7 percent of the Texas population. Districts and investor-owned utilities are required to submit financial information; WSCs alone are not. The Commission cannot have a comprehensive, data-driven oversight system until it obtains consistent and comparable information on the financial activities of its regulated community, including WSCs.

While legislation is probably needed for this to occur, the Commission should develop a standard format for the reports and plan for entering and maintaining the data for viability and risk assessment purposes.

Section 4-E:

Require Counties to Notify the Commission of Newly Created Districts

When a district is created by a county, the county, in addition to the district, should notify the Commission of the newly created district so that the Commission can maintain accurate and complete district data. This information can be used to reduce delays in imposing the regulatory assessments on the newly created districts.

Section 4-F:

Require Districts to Seek Multiple Proposals in Selecting CPA Firms

It would be a good business practice to require water districts to obtain multiple proposals before selecting an audit firm. In addition, the law might be changed to encourage districts to rotate auditors after a certain period of time.

Section 4-G:

Consider Giving the Commission Greater Rate-Setting Flexibility

The Commission has original jurisdiction over the rates charged by investor-owned utilities and appellate jurisdiction over the rates charged by districts and water supply or sewer corporations. The Utility Rates and Services Section devotes a large share of its resources to rate making, especially for investor-owned utilities (IOUs). The process is time-consuming and costly for the participants.

Investor-owned utilities pose a special problem in the state system. They tend to be smaller and less sophisticated than other entities. Their deficiency scores, from inspections of their facilities, are nearly twice as high as for political subdivisions, they are enforced against with greater frequency, and they are much less likely to be considered superior water suppliers.

Average Deficiency Scores, Number of Enforcements, and Number of Superior Systems by Owner Type				
Owner Type	Number of Systems	Average Deficiency Score	Number of Enforcements	Number of Superior Systems
Federal	137	6.19	2	1
Investor	3651	10.53	1034	10
State	165	5.20	10	3
Local Government	1902	5.74	178	507
Water Supply Corporation	1017	7.71	131	15

Source: Unaudited data, Public Drinking Water Section, TNRCC

Chapter 13 of Texas Water Code is specific about the criteria for setting rates for IOUs. At present, many IOUs believe that:

- The rates they are allowed to charge, based on depreciation, are not sufficient to cover expenses and ensure return on investment.
- The rate process is costly and punitive.

Current methods of calculating depreciation and return on investment form a disincentive for one system to purchase another, even where the consolidated entity might be financially stronger and provide better service. Possible solutions include:

- Acquisition adjustments that would allow an investor to include the purchase price in the rate base. This would make it more attractive for a strong, healthy utility to buy out a weak one.
- Alternative bases for calculating rates, such as actual cash flow, income, and invested capital
- Allowances for financial reserves
- Allowances for future plant replacement (sinking fund)
- Allowances for debt covenants
- Possible state guarantee of part or all of loans for improvements
- Ability to recover operating losses

Another option is to remove the Commission's original rate jurisdiction over IOUs altogether and redirect those resources toward restructuring nonviable entities. Under this scenario, the utility would file notice of a rate change with the Commission and use those rates unless:

- The rates were to be appealed by customers
- Based on data analysis, the Commission were to determine that the rates were blatantly unfair

While adoption of a "file and use" rate system would lessen protection for consumers in IOU service areas, the law could be strengthened in other ways to compensate. For example, the Commission could be required to investigate if the rate change exceeded certain pre-set limits, or if a given percentage of the utility's customers, possibly ranging from 5 to 10 percent depending on the system's size, were to appeal the rate change. In addition, the Commission could make it easier for customers to appeal by requiring IOUs to maintain and provide comprehensive customer lists on request.

Section 4-H:

Issue for Further Study: Consider Incentives to Encourage Regionalization

The Commission has legislative authority to promote regionalization. However, agency personnel feel the statutes are not sufficient, and they see regionalization as a "loose" goal. We would like to see the Commission and the Texas Water

Development Board be granted explicit authority and incentives to encourage regionalization through their regulatory and financing programs.

Some of the benefits of regionalization include:

- Improve the ability of small water companies to provide service.
- Improve customer service.
- Make it easier to comply with current and future regulations.
- Avoid drastic rate increases.
- Bring the rates of merged systems into parity.
- Improve and consolidate management and operation.
- Promote conservation.

Objectives, Scope, and Methodology

Objectives

The objectives of this project were to determine whether:

- Commission monitoring and oversight over water districts and utilities is efficient and adequate to protect consumers and public health.
- Commission controls and jurisdiction are consistent with risks for entities of various types.

Scope

The scope of this audit included districts, utilities, and public drinking water systems over which Commission exercises oversight. It considered the various processes, policies, procedures, and practices used to monitor these entities. We focused mainly on the activities of the Commission's Water Utilities Division.

Areas addressed during our review included:

- District creation, conversion, bond application, and certificates of convenience and necessity (CCN) approval processes
- District independent audit report review process
- Accounting and reporting manual methodologies for districts and utilities
- Circuit rider technical assistance contracts
- Rate change processes, policies, and practices
- Plans review processes
- Database controls over information maintained by the Division
- Water quality monitoring processes, policies, and practices

We reviewed bond applications and rate case files based on a selection methodology which identified high-risk entities. We also developed a diagnostic system to identify financially unstable districts based on financial ratios and operational factors significant to the industry.

The data obtained from Commission databases was not verified. We wanted to review the controls in place over the data, but realized early on that the Division had already identified areas for improvement concerning information management and was working to address them. However, the data was still used to provide descriptive information about the complicated regulated community.

Methodology

The methodology used on this audit consisted of collecting information, performing audit tests and procedures, and analyzing and evaluating the results against preestablished criteria.

Information collected to accomplish our objectives included the following:

- Interviews with management and staff of the Commission
- Interviews with members of the regulated community, associations, and external parties that interact with the Commission
- Documentary evidence such as:
 - Policies and procedures related to oversight and monitoring practices at the Commission's Water Utilities Division
 - Applicable federal and state statutes and guidelines
 - Bond application and rate case files
 - Technical assistance circuit rider contracts
 - Review of Commission database information on the regulated community and activities of the Division
 - Public water supply system inspection logs
 - Vulnerability assessment program files

Procedures and tests conducted:

- Test of the bond application approval process used by the Commission to determine if feasible bond issues are approved
- Test of rate change approval process used by the Commission to determine if fair and equitable decisions are made to ensure customers receive adequate service at a fair price
- Review of sufficiency and adequacy of reporting and accounting manuals
- Review of the sufficiency of independent audit report review process to determine if it provides adequate information on the financial condition of districts
- Review of district financial information to determine the financial condition of districts
- Review of technical assistance contracts to determine adequacy of provisions and tests of contractor compliance with contract terms

- Review of public water supply system sampling schedule process to determine if most vulnerable systems are monitored more closely than less vulnerable systems

Criteria used:

- Texas Government Code and Texas Administrative Code
- Commission policies and procedures
- Contract management model developed by the State Auditor's Office
- Contract provisions
- 1996 Source Book on Texas Local Government Debt
- Standard audit criteria

Fieldwork was conducted from late May 1996 to mid-September 1996. The audit was conducted in accordance with applicable professional standards, including:

- Generally Accepted Auditing Standards
- Generally Accepted Government Auditing Standards

There were no significant instances of noncompliance with these standards.

The audit work was performed by the following members of the State Auditor's staff:

- John W. Swinton, CGFM (Project Manager)
- Robin K. Key, CPA
- Francine B. Gutierrez, CPA
- Hugh On, CPA
- Barnie C. Gilmore, CPA (Audit Manager)
- Deborah L. Kerr, Ph.D. (Audit Director)

Fiscal Impact of Recommendations

The following table details the fiscal impact of recommendations contained in this report.

	Revenue
Eliminate Quarterly Discount	\$ 200,000
Increase Collections	80,000
Other Efficiencies	<u>60,000</u>
Total Revenues	<u>\$ 340,000</u>
	Expenses
Salaries/Benefits/Administrative	\$ 256,735
Contracted Follow-Up	<u>74,900</u>
Total Expenses	<u>331,635</u>
Savings	<u><u>\$ 8,365</u></u>

Financial Information

The following table includes information on goal B of the General Appropriations Act, which is the Commission's goal for managing water. It provides appropriation information relevant to the Water Utilities Division.

Goal/Objective/Strategies	Appropriations				
	Fiscal Year	1994	1995	1996	1997
B. Managing Texas' water (total for the goal)	\$	37,122,880	\$ 37,023,946	\$ 33,631,309	\$ 33,631,309
B.2 Manage the state's water resources (total for the objective)	\$	14,066,715	\$ 14,080,973	\$ 12,845,255	\$ 12,845,255
B.2.4 Public drinking water (total for the strategy)	\$	6,024,000	\$ 6,043,000	\$ 6,025,788	\$ 6,025,788
Method of Finance for B.2.4					
General Revenue Fund	\$	2,977,000	\$ 2,996,000	\$ 30,750	\$ 30,750
Water Quality Receipts	\$	9,000	\$ 9,000	\$ 0	\$ 0
Water Utility Receipts	\$	136,000	\$ 136,000	\$ 360,288	\$ 360,288
Department of Health Public Health Services Fee Receipts	\$	662,000	\$ 662,000	\$ 2,665,360	\$ 2,665,360
Federal Funds	\$	1,959,000	\$ 1,959,000	\$ 2,127,184	\$ 2,127,184
Water Works Operator Fee	\$	11,000	\$ 11,000	\$ 0	\$ 0
Plumbing Fixture Inspection Fee	\$	70,000	\$ 70,000	\$ 0	\$ 0
Earned Federal Funds	\$	200,000	\$ 200,000	\$ 842,206	\$ 842,206
Total	\$	6,024,000	\$ 6,043,000	\$ 6,025,788	\$ 6,025,788
Object of Expense for B.2.4					
Salaries and Wages	\$	4,450,000	\$ 4,450,000	\$ 4,906,340	\$ 4,906,340
Other Personnel Costs	\$	0	\$ 0	\$ 32,000	\$ 32,000
Operating Costs	\$	1,237,000	\$ 1,254,000	\$ 1,018,738	\$ 1,018,738
Capital Expenditures	\$	337,000	\$ 339,000	\$ 68,710	\$ 68,710
Total	\$	6,024,000	\$ 6,043,000	\$ 6,025,788	\$ 6,025,788

Goal/Objective/Strategies	Appropriations				
	Fiscal Year	1994	1995	1996	1997
B.2.5 Water utility regulation (total for the strategy)		\$ 2,929,000	\$ 2,923,000	\$ 1,755,377	\$ 1,755,377
Method of Finance for B.2.5					
General Revenue Fund		\$ 54,000	\$ 48,000	\$ 304,114	\$ 304,114
Water Quality Receipts		\$ 365,000	\$ 365,000	\$ 0	\$ 0
Water Utility Receipts		\$ 2,086,000	\$ 2,086,000	\$ 1,284,090	\$ 1,284,090
Department of Health Public Health Services Fee Receipt		\$ 417,000	\$ 417,000	\$ 0	\$ 0
Residential Water Treatment Fee		\$ 7,000	\$ 7,000	\$ 0	\$ 0
Earned Federal Funds		\$ 0	\$ 0	\$ 167,173	\$ 167,173
Total		\$ 2,929,000	\$ 2,923,000	\$ 1,755,377	\$ 1,755,377
Object of Expense for B.2.5					
Salaries and Wages		\$ 1,858,000	\$ 1,858,000	\$ 1,284,517	\$ 1,284,517
Operating Costs		\$ 881,000	\$ 881,000	\$ 446,110	\$ 446,110
Capital Expenditures		\$ 190,000	\$ 184,000	\$ 24,750	\$ 24,750
Total		\$ 2,929,000	\$ 2,923,000	\$ 1,755,377	\$ 1,755,377

Fiscal Year 1996 Budget by Section and Expenditure Type	
Category	Budget
Administration	\$ 258,183
District Administration	\$ 1,174,354
Utility Rates and Services	\$ 1,172,090
Public Drinking Water	\$ 1,948,767
Total by Section	\$ 4,553,394

Fiscal Year 1996 Budget by Section and Expenditure Type	
Category	Budget
Salaries	\$ 2,671,296
Professional Services	\$ 764,643
Release Time	\$ 593,450
Temporary/Other Services	\$ 154,049
Travel, in-state	\$ 116,595
Training	\$ 67,826
Supplies	\$ 66,198
Capital	\$ 39,193
Travel, out-state	\$ 36,682
Other	\$ 24,956
Maintenance & Repair	\$ 9,298
Telephone/Utilities	\$ 4,000
Rent	\$ 2,823
Postage	\$ 2,386
Total	\$ 4,553,395

Agency Profile

Mission

The Commission's mission is "to protect human health, environmental quality, and natural resources by ensuring: clean air for Texans to breathe, an adequate, affordable supply of clean water for the benefit of Texas citizens and businesses, conservation of resources and reduction of pollution, and proper and safe disposal of various forms of pollutants, consistent with sustainable economic development."

Background

Since September 1993, the Commission began functioning as a consolidated environmental agency. There were several stages of the consolidation, including acquiring:

- The municipal solid waste and drinking water hygiene programs from the Texas Department of Health on March 1, 1992
- The Water Well Drillers Board and the Board of Irrigators in September 1992
- The Texas Air Control Board and the Texas Water Commission in September 1993

The Water Utilities Division assures the delivery of safe drinking water through the operations of its three sections. These sections came from several different places and are now functioning within the same division. The three sections that make up the division include the District Administration Section, Utility Rates and Services, and Public Drinking Water.

The **District Administration Section** is responsible for the general supervision of water districts. In providing supervision, the District Administration Section:

- Processes petitions to create new districts
- Maintains approval authority over most district bond issues to assure the engineering and economic feasibility of the project
- Has approval authority over many other types of district matters, including standby fees, impact fees, fire plans, and other miscellaneous issues
- Provides educational assistance through a regular newsletter
- Reviews district annual audit and other financial reports
- Responds to complaints and customer inquiries
- Maintains a database on each of the water districts registered with the State

The two teams that perform these tasks include the Reports and Supervision Team and the Creations and Bond Review Team.

The **Utility Rates and Services Section**'s goal is to ensure that water and sewer utilities provide continuous and adequate service to their customers at just and reasonable rates. To carry out this goal, the Utility Rates and Services Section:

- Processes and recommends granting utility service area applications known as certificates of convenience and necessity (CCNs)
- Reviews engineering plans for construction or modification of water systems
- Exercises original jurisdiction over investor-owned utilities (IOUs) requesting rate changes
- Exercises appellate jurisdiction over other service providers requesting rate changes
- Participates in hearings held by the Commission on various applications submitted to this Section, as well as hearings involving utilities referred for enforcement action

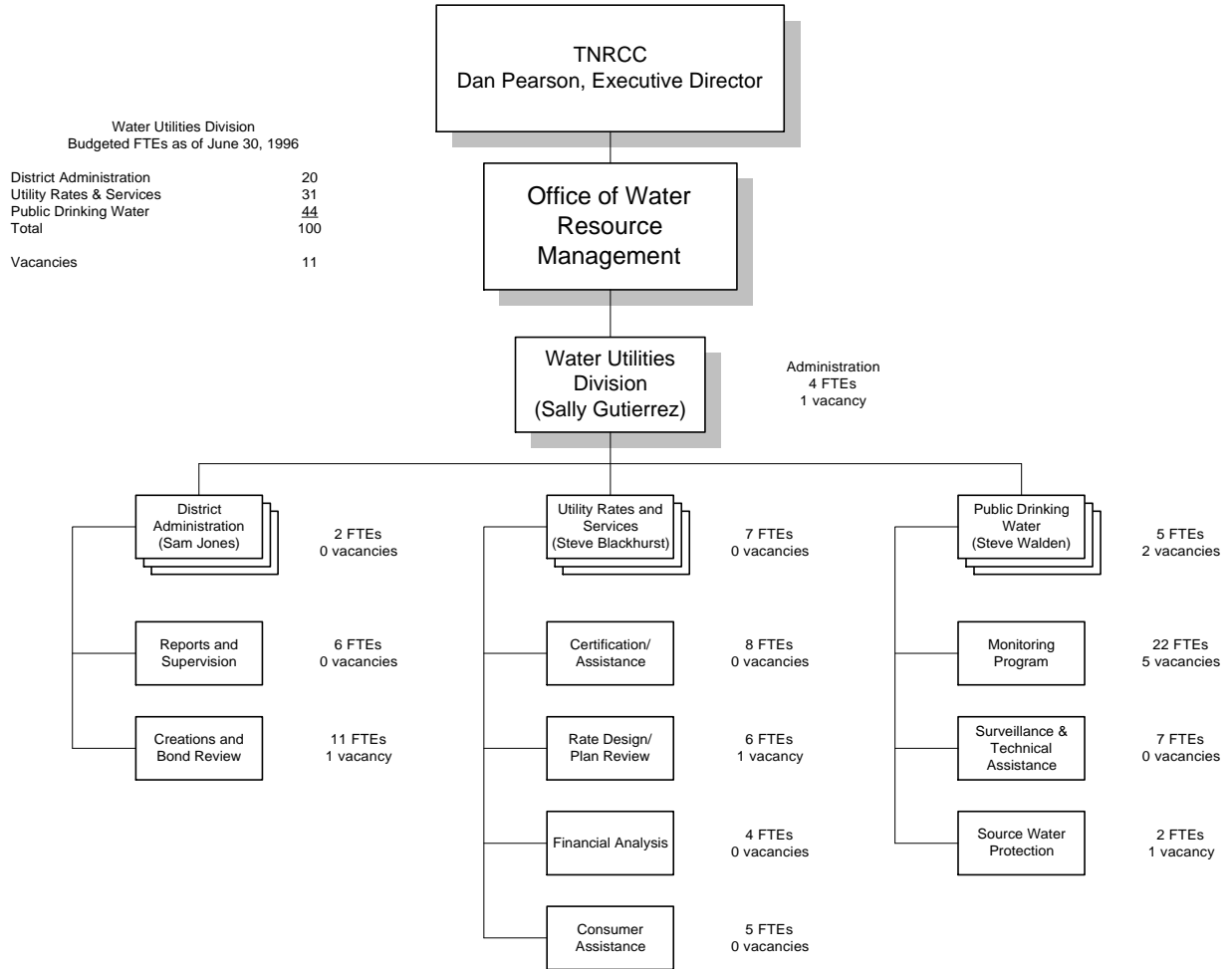
The Utility Rates and Services Section has four teams that carry out the above-noted duties. The teams include the Utility Assistance and Certification Team, the Rate Design/Plan Review Team, the Financial Analysis Team, and the Consumer Assistance Team.

The **Public Drinking Water Section** administers the public drinking water system supervision program and has primary responsibility for the public water system aspects of the federal Safe Drinking Water Act. With the help of the field staff located across Texas at the regional offices, the Public Drinking Water Section performs the following activities:

- Manages the testing and results of monitoring of public water systems for contamination
- Assists local communities in developing drinking water protection programs
- Implements and coordinates the Wellhead Protection Program and provide technical assistance and guidance to communities participating in the program
- Reviews the sanitary surveys of the public water systems conducted by field staff
- Provides technical assistance to the public and other state agencies

The Public Drinking Water Section is comprised of three teams which perform these activities. The teams include the Drinking Water Monitoring Team, the Source Water Protection Team, and the Surveillance and Technical Assistance Team.

Organizational Chart



Reference List

The books, articles, reports, etc., listed below are relevant to the former Texas Water Commission:

State of Texas. Office of the Comptroller of Public Accounts. *Breaking the Mold: Volume 2, Part II*. "The State Should Require Better Regulation and Oversight of Water Districts and River Authorities." 1991.

_____. Office of the State Auditor. *Audit Follow-Up Report on the Supervision of Texas Water Districts*. SAO Report No. 2-150. 1992.

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Glossary

Affected county	A county that has a per capita income that averaged 25 percent below the state average for the most recent three consecutive years for which statistics are available and an unemployment rate that averaged 25 percent above the state average for the most recent three consecutive years for which statistics are available; and, any part of which is within 50 miles of an international border.
Assessed valuation (AV)	The value placed on a piece of taxable property adjusted by any applicable assessment ratio.
Bond	A government-issued, interest-bearing certificate of debt obligating the issuer to make specified principal and interest payments to the debt holders.
Bond application	All documents filed with the Commission for approval of a bond sale
Certificate of Convenience and Necessity (CCN)	Authorizes a utility the right to provide water or sewer utility service to a specific area and obligates the utility to provide continuous and adequate service to every customer who requests service within that area
Community water systems	A public water system that has a potential to serve at least 15 residential service connections on a year-round basis or serves at least 25 residents on a year-round basis. Service connections shall be counted as one for each single family residential unit or each commercial or industrial establishment to which drinking water is supplied from the system.
Connection	A single family residential unit or each commercial or industrial establishment to which drinking water is supplied from the system. As an example, the number of service connections in an apartment complex would be equal to the number of individual apartment units. When enough data is not available to accurately determine the number of connections to be served or being served, the population served divided by three will be used as the number of connections for calculating system capacity requirements. Conversely, if only the number of connections is known, the connection total multiplied by three will be the number used for population served.
Debt service	Legal payments of principal and interest due on public bonded indebtedness, usually in installments collected from ad valorem taxes and other sources
District	Any district or authority created by authority of either Sections 52(b)(1) and (2), Article III, or Section 59, Article XVI, Texas Constitution, regardless of how created

Drinking water	Water distributed by an individual or public or private agency for human consumption, for use in preparing food or beverages, or for use in cleaning a utensil or article used in preparing food or beverages for, or consuming food or beverages by, human beings. The term includes water supplied for human consumption or used by an institution catering to the public.
Exempt IOU or Exempt WSC	A water or sewer utility or water supply corporation with less than 15 potential service connections.
Extraterritorial Jurisdiction (ETJ)	The annexable perimeter surrounding the boundaries of all incorporated cities, towns, and villages; the population level of the municipality determines the width of its ETJ.
Feasibility study	A research report that examines engineering, financial, and other factors to determine whether a potential real estate development project will be an economic success. Also, called market analysis.
General law district	One that is created by the Texas Natural Resource Conservation Commission, a county commissioners court, or to a limited extent, the governing board of a city.
Ground water	The supply of fresh water found beneath the Earth's surface (usually in aquifers) which is often used for supplying wells and springs. Because ground water is a major source of drinking water, there is growing concern over areas where leaching agricultural or industrial pollutants or substances from leaking underground storage tanks are contaminating ground water.
Interconnection	A physical connection between two public water supply systems
Investor-Owned Utility (IOU)	See definition for <i>water and sewer utility</i> .
Noncommunity water system	Any public water system that is not a community system
Nonpoint Source Pollution	Forms of pollution caused by sediment, nutrients, organic and toxic substances originating from land use activities, which are carried to lakes and streams by surface runoff. Nonpoint source pollution occurs when the rate of materials entering these waterbodies exceeds natural levels.
Nontransient noncommunity water supply	A public water system that is not a community water system and regularly serves at least 25 of the same persons at least six months out of the year.
Potable water	Water that is used for or intended to be used for human consumption or household use.

Public water system

A system for the provision to the public of piped water for human consumption. Such a system must have a potential to serve at least 15 service connections or 25 individuals at least 60 days out of the year. This term includes any collection, treatment, storage, and distribution facilities under control of the operator of such system and used primarily in connection with such system; and any collection of pretreatment storage facilities not under such control which are used primarily in connection with such system.

Two or more water systems with each having a potential to serve less than 15 connections or less than 25 individuals but owned by the same person, firm or corporation and located on adjacent land will be considered a public water system when the total potential service connections in the combined systems are 15 or greater or if the total number of individuals served by the combined systems total 25 or more at least 60 days out of the year. Without excluding other meanings of the terms "individual" or "served," an individual shall be deemed to be served by a water system if he resides in, uses as his place of employment, or works in, a place to which drinking water is supplied from the system. A public water system is either a "community water system" or a "noncommunity water system."

Retail public utility

Any person, corporation, public utility, water supply or sewer service corporation, municipality, political subdivision or agency operating, maintaining, or controlling in this state facilities for providing potable water service or sewer service, or both, for compensation.

River authority

Any district or authority created by the Legislature which contains an area within its boundaries of ten or more counties and which is governed by a board of directors appointed or designated in whole or in part by the governor, or by the Texas Water Development Board, including without limitation the San Antonio River Authority, and other river authority or Special district created under Article 111, Section 52, Subsection (b) (1) or (2), or Article XVI, Section 59, of the Texas Constitution that is designated by rule of the Commission to comply with its rules.

Sanitary survey

An on-site review of the water source, facilities, equipment, operation and maintenance of a public water system, for the purpose of evaluating the adequacy for producing and distributing safe drinking water.

Special law district

One that is created by an act of the State Legislature

Surface water	Lakes, bays, ponds, impounding reservoirs, springs, rivers, streams, creeks, estuaries, wetlands, marshes, inlets, canals, gulfs inside the territorial limits of the State, and all other bodies of surface water, natural or artificial, inland or coastal, fresh or salt, navigable or nonnavigable, and including the beds and banks of all watercourses and bodies of surface water, that are wholly or partially inside or bordering the State or subject to the jurisdiction of the State; except that waters in treatment systems which are authorized by state or federal law, regulation, or permit, and which are created for the purpose of waste treatment are not considered to be waters in the State.
Tax base	The total taxable value of all property within a taxing unit's jurisdiction
Tax levy	The gross amount of money a local government can produce by applying its tax rate to its total assessed valuation
Tax rate	A rate determined annually by the board of directors and usually expressed in dollars and cents per hundred dollars of valuation; the tax rate multiplied by the tax base should equal the district's total levy.
Transient noncommunity water system	A public water system that is not a community water system and serves at least 25 persons at least 60 days out of the year, yet by its characteristics, does not meet the definition of a nontransient noncommunity water system.
Viable water system	One that is self-sustaining, and that has the commitment, and the financial, managerial, and technical capability to meet performance requirements reliably on a long-term basis.
Water and sewer utility	Any person, corporation, cooperative corporation, affected county, or any combination of those persons or entities, other than a municipal corporation, water supply or sewer service corporation, or a political subdivision of the state, except an affected county, or their lessees, trustees, and receivers, owning or operating for compensation in this state equipment or facilities for the production, transmission, storage, distribution, sale, or provision of potable water to the public or for the resale of potable water to the public for any use or for the collection, transportation, treatment, or disposal of sewage or other operation of a sewage disposal service for the public, other than equipment or facilities owned and operated for either purpose by a municipality or other political subdivision of this state or a water supply or sewer service corporation, but does not include any person or corporation not otherwise a public utility that furnishes the services or commodity only to itself or its employees or tenants as an incident of that employee service or tenancy when that service or commodity is not resold to or used by others.
Water quality	Term used to describe the chemical, physical, and biological characteristics of water with respect to its suitability for a particular use.

Water supply	A source or reservoir of water distributed and used for human consumption
Water Supply Corporation (WSC)	A nonprofit, member-owned, member-controlled Water Supply or Sewer Service Corporation
Water supply or sewer service company	Any nonprofit, member-owned, member-controlled corporation organized and operating under Chapter 76, Acts of the 43rd Legislature, 1st Called Session, 1933 (Texas Civil Statutes, Article 1434a) that provides potable water or sewer service for compensation. The term does not include a corporation that provides retail water or sewer service to a person who is not a member, except that the corporation may provide retail water or sewer service to a person who is not a member if the person only builds on or develops property to sell to another and the service is provided on an interim basis before the property is sold.
Water supply system	System for collection, storage, treatment, and distribution of potable or other kinds of water from the sources of supply to the customer.

Governmental Controls

Governmental Controls With Reference to Water Districts and River Authorities		Natural Resource Conservation Commission				Attorney General																															
		1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16																				
Water Control and Improvement	1	✓	✓	✓	✓													✓	✓																		
Fresh Water	2		✓	✓	✓															✓	✓																
Municipal Utility	3	✓		✓	✓	✓																✓	✓														
Drainage	4					✓																		✓	✓												
Levee Improvement	5	✓				✓																				✓	✓										
Irrigation	6	✓		✓	✓	✓																						✓	✓								
Navigation, Article 16	7			✓		✓																							✓	✓							
Navigation, Article 3	8						✓	✓																						✓	✓						
Special Utility	9	✓		3	✓	✓																									✓	✓					
Stormwater Control	10	✓		✓	✓	✓																										✓	✓				
Water Improvement	11	✓		✓	✓	✓																											✓	✓			
Underground Water Conservation	12	✓		✓																														✓	✓		
River Authorities	13																																	✓	✓		
Municipal Management Districts	14	✓																																	✓	✓	
Road Utility Districts	15																																			✓	✓
Road Districts	16																																			✓	✓

Governmental Controls With Reference to Water Districts and River Authorities, concluded

<p>County Commissioners Creation - approval Financial - approves bonds</p> <p>City Councils Creation - approval required if district encroaches on city or ETJ Financial and Projects Approval of plans for facilities within city or ETJ (depends on City consent)</p>	Water Control and Improvement	1	✓																	
	Fresh Water	2	✓																	
	Municipal Utility	3																		
	Drainage	4	✓																	
	Levee Improvement	5	✓																	
	Irrigation	6	✓																	
	Navigation, Article 16	7	✓																	
	Navigation, Article 3	8	✓																	
	Special Utility	9																		
	Stormwater Control	10																		
	Water Improvement	11	✓																	
	Underground Water Conservation	12																		
	River Authorities	13																		
	Municipal Management Districts	14																		
	Road Utility Districts	15																		
	Road Districts	16		✓																

Notes:

1. May approve additional road powers for a municipal utility district
2. Limited Right of Supervision
3. Not authorized to issue tax bonds

Commission Interactions With Local and Regional Entities

	River Authorities	Water Districts	Counties	Cities	Interstate Compact Commissions	Council of Government	Soil and Water Conservation Districts	Regional Waste Disposal Authorities	Water Supply Corporations	Investor-Owned Utilities
Commission Interactions With Regional and Local Entities	1	2	3	4	5	6	7	8	9	10
I. Water Planning and Assessment Division										
1. Coordinate/cooperate on data collection and exchange.	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
2. Contract for special projects, joint studies, and services for designated areas.	✓		✓	✓		✓		✓		
3. Contract for assistance in development of water quality management plans (historical).	✓			✓	✓	✓	✓	✓		
4. Provide informal consultation on water quality issues, including proposed Commission rules and regulations.	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
5. Conduct water availability analyses for water rights permit applications.	✓	✓		✓	✓	✓	✓	✓	✓	✓
6. Conduct environmental analyses for water rights permit applications.	✓	✓		✓	✓	✓	✓	✓	✓	✓
7. Develop and update river basin water availability computer models.	✓	✓		✓	✓	✓	✓	✓	✓	✓
8. Review water management, water conservation, and drought contingency plans.	✓	✓		✓	✓	✓	✓	✓	✓	✓
9. Prepare hydrologic evaluations of surface water resources for the administration and enforcement of water rights.	✓	✓		✓	✓	✓	✓	✓	✓	✓

	River Authorities	Water Districts	Counties	Cities	Interstate Compact Commissions	Council of Government	Soil and Water Conservation Districts	Regional Waste Disposal Authorities	Water Supply Corporations	Investor-Owned Utilities
TNRCC Interactions With Regional and Local Entities	1	2	3	4	5	6	7	8	9	10
10. Coordinate and administer Galveston Bay Estuary Program and Corpus Christi National Estuary Program.	✓	✓	✓	✓	✓	✓	✓	✓		
11. Develop and implement Surface Water Quality Standards.	✓	✓		✓	✓			✓		
12. Conduct, coordinate, and manage Regional Assessments of Water Quality as part of the Clean Rivers Program.	✓	✓	✓	✓	✓			✓		
13. Certification of federal permits under Section 401 of the Clean Water Act.			✓	✓						
14. Implement toxicity requirements and wastewater permits.	✓			✓				✓		
15. Develop and manage Texas non-point source pollution control program.	✓	✓		✓	✓	✓	✓			
16. Provide data from TNRCC records to entities or their consultants for use in planning activities.	✓	✓	✓	✓	✓	✓	✓	✓		
Ground Water										
Identify possible critical ground water management areas where underground water conservation districts may be appropriate.	✓	✓	✓	✓	✓	✓	✓			
Weather and Climate										
1. Issue weather modification permits.		✓		✓						
2. Enforce compliance with weather modification permits.		✓	✎	✓						
✎ Potential										

Commission Interactions With Regional and Local Entities		1	2	3	4	5	6	7	8	9	10
		River Authorities	Water Districts	Counties	Cities	Interstate Compact Commissions	Council of Government	Soil and Water Conservation Districts	Regional Waste Disposal Authorities	Water Supply Corporations	Investor-Owned Utilities
II. Agriculture and Watershed Management Division											
Water Rights and Uses:											
1. Process applications for permits to impound, divert or take state surface water.											
2. Process applications for designation as a local sponsor of a water development project proposed by either a federal agency or the Texas Water Development Board.											
3. Maintain permit and surface water use data, including annual water use reports, and ownership and address changes.											
4. Initiate cancellation of unused water rights.											
5. Provide technical assistance to Interstate Compact Commissioners.											
Dam Safety and Floodplain Management:											
1. Review proposed dam projects structurally and hydraulically during the permit and plan review processes.											
2. Inspect existing dams periodically, providing owners with reports and recommendations for correcting any deficiencies.											
3. Review flood control projects and stream channel modifications.											
		✓	✓	✓	✓	✓	✓			✓	✓
		✓	✓	✓	✓	✓				✓	✓
		✓	✓	✓	✓						
		✓	✓	✓	✓			✓		✓	✓
		✓	✓	✓	✓	✓					
		✓	✓	✓	✓						

	River Authorities	Water Districts	Counties	Cities	Interstate Compact Commissions	Council of Government	Soil and Water Conservation Districts	Regional Waste Disposal Authorities	Water Supply Corporations	Investor-Owned Utilities
	1	2	3	4	5	6	7	8	9	10
Commission Interactions With Regional and Local Entities										
4. The Commission has review responsibility over any reclamation projects undertaken by counties and cities where that entity is not in the National Flood Insurance Program.	✓		✓	✓		✓	✓		✓	✓
5. Provide technical assistance to entities on floodplain management and the National Flood Insurance Program.	✓	✓	✓	✓		✓			✓	✓
6. Assist counties in reviewing proposed creations of Levee Improvement Districts.			✓							
7. Provide notice of reclamation projects being reviewed by the Commission and located in that entity's service area.	✓		✓	✓		✓			✓	✓
Plans and Specifications Review:										
Review and approve plans and specifications of domestic wastewater collection, treatment, and disposal facilities.	✓	✓	✓	✓				✓	✓	✓
Wastewater										
Issue permits and registrations for wastewater disposal, municipal sludge, septage disposal, water treatment plant sludge disposal, and concentrated animal feeding operations (CAFO).	✓	✓	✓	✓		✓			✓	✓
Technical Assistance										
Provide technical assistance for watermaster operations.	✓	✓		✓		✓			✓	✓

Commission Interactions With Regional and Local Entities		1	2	3	4	5	6	7	8	9	10
	River Authorities	Water Districts	Counties	Cities	Interstate Compact Commissions	Council of Government	Soil and Water Conservation Districts	Regional Waste Disposal Authorities	Water Supply Corporations	Investor-Owned Utilities	
III. Water Utilities Division											
District Administration:											
1. Provide continuing supervision of districts and certain river authorities through the review of annual financial reports, affidavits, and other information.	✓	✓	✓	✓							
2. Authorize creation of certain types of districts.	✓	✓	✓	✓							
3. Approve bonds for certain types of districts.	✓	✓	✓	✓							
4. Check for required notifications to county and required city's consent (if district is within city's extraterritorial jurisdiction) at time of review of district creation.			✓	✓							
5. Report on the feasibility of Levee Improvement Districts proposed for creation by counties.			✓								
6. Notify counties at time of bond review for MUDs if the district is located outside the ETJ of any city.			✓								
7. Maintain database of district records required to be filed with the Commission.	✓	✓									
8. Check for required city and county approval of plans and specifications at time of bond review.			✓	✓							

	River Authorities	Water Districts	Counties	Cities	Interstate Compact Commissions	Council of Government	Soil and Water Conservation Districts	Regional Waste Disposal Authorities	Water Supply Corporations	Investor-Owned Utilities
Commission Interactions With Regional and Local Entities	1	2	3	4	5	6	7	8	9	10
Utility Rates and Services:										
1. Ensure that adequate and continuous retail utility service is provided within Certificate of Convenience and Necessity (CCN) areas (CCN optional except for counties).	✓	✓	✓	✓					✓	✓
2. Appellate jurisdiction over rates charged by certain entities	✓	✓	✓	✓					✓	✓
3. Original jurisdiction over rates charged by certain entities										✓
4. Review and approve applications for CCNs received from certain entities.		✓	✓	✓					✓	✓
5. Review and evaluate engineering plans and specifications for proposed water system facilities.	✓	✓	✓	✓					✓	✓
Public Drinking Water:										
1. Conduct evaluations of groundwater under the influence of surface water and monitor coliform compliance and surface water treatment reports.	✓*	✓	✓	✓					✓	✓
2. Monitor compliance with inorganic, organic, and lead/copper regulations.	✓*	✓	✓	✓					✓	✓
3. Provide technical assistance regarding system design and operations.	✓*	✓	✓	✓					✓	✓
4. Administer plant optimization program and perform oversight of surface water treatment plants.	✓*	✓	✓	✓					✓	✓

* The Upper Guadalupe River Authority serves as a public water supplier, thus making these Public Drinking Water activities apply to this specific river authority.

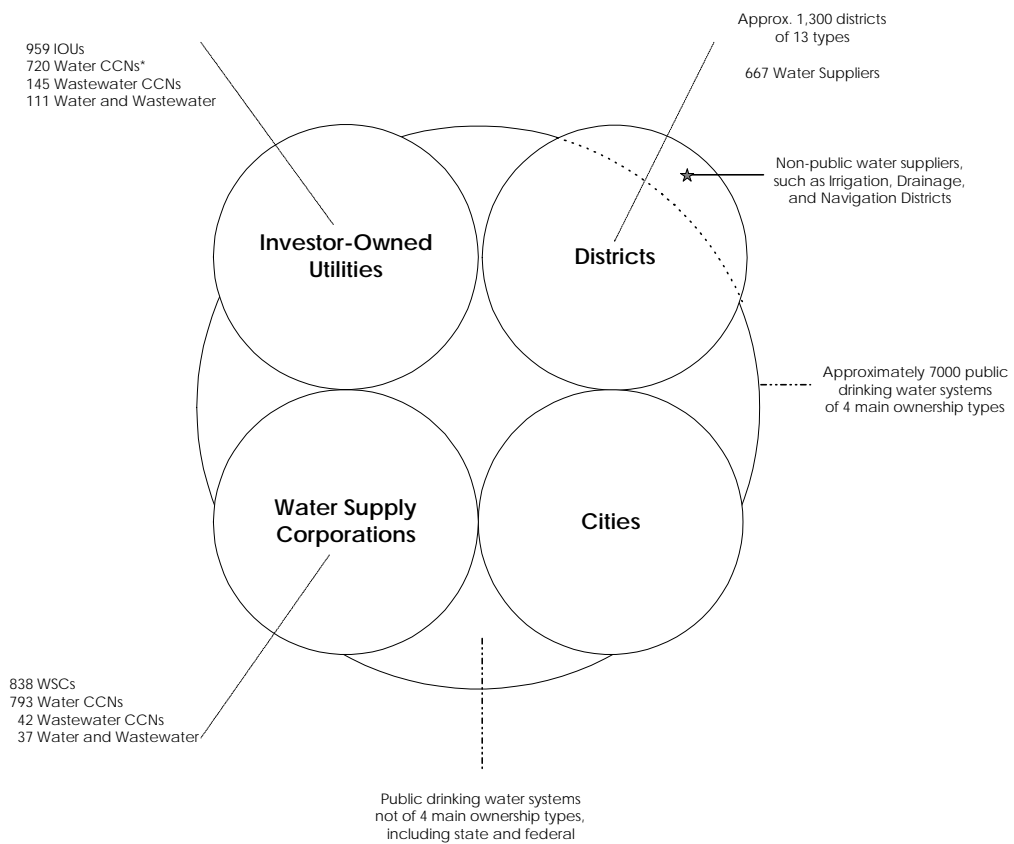
	River Authorities	Water Districts	Counties	Cities	Interstate Compact Commissions	Council of Government	Soil and Water Conservation Districts	Regional Waste Disposal Authorities	Water Supply Corporations	Investor-Owned Utilities
Commission Interactions With Regional and Local Entities	1	✓								
	2	✓	✓	✓		✓	✓			
5. Determine compliance with state and federal drinking water quality standards.	3	✓	✓							
	4	✓	✓							
6. Facilitate development of the voluntary Source Water Protection program at the local level and provide technical assistance to participants; develop plans to protect vulnerable areas near public water supply wells and surface water intakes.	5									
	6					✓				
IV. Petroleum Storage Tank Division	7									
	8									
Register underground storage tanks containing hazardous material or fuels and monitor plans for removal of such tanks or installation of new ones.	9					✓				
	10									
V. Field Operations Division	1	✓								
	2	✓								
1. Conduct construction monitoring inspections and ongoing compliance inspections of wastewater treatment facilities.	3		✓						✓	
	4			✓						
2. May cooperate on responses to pollution incidents, spills, and other emergencies	5									
	6									
3. Receive data from some river authorities that inspect Commission permitted wastewater treatment facilities.	7									
	8									
4. Receive data from river authorities that conduct ambient lake and river monitoring.	9									
	10									
5. Refer certain water quality complaints to river authorities, cities, and counties.	1	✓								
	2	✓								

Commission Interactions With Regional and Local Entities		1	2	3	4	5	6	7	8	9	10
		River Authorities	Water Districts	Counties	Cities	Interstate Compact Commissions	Council of Government	Soil and Water Conservation Districts	Regional Waste Disposal Authorities	Water Supply Corporations	Investor-Owned Utilities
6.	Conduct pollution abatement programs for development over Edwards Aquifer.		✓		✓					✓	✓
7.	Conduct sanitary surveys and collect drinking water samples at public water supply systems.		✓		✓					✓	✓
8.	Investigate citizen complaints and conduct waterborne disease outbreak investigations.		✓		✓					✓	✓
9.	Provide technical assistance to public drinking water systems.		✓		✓					✓	✓
10.	Cities and counties may conduct a municipal pollution abatement program which complements Commission activities in areas such as non-point source pollution control, industrial discharges to a publicly owned sewage treatment plant, solid waste management, and emergency response.			✓	✓						

Commission Interactions With Regional and Local Entities									
River Authorities	Water Districts	Counties	Cities	Interstate Compact Commissions	Council of Government	Soil and Water Conservation Districts	Regional Waste Disposal Authorities	Water Supply Corporations	Investor-Owned Utilities
1	2	3	4	5	6	7	8	9	10
VI. Office of Compliance and Enforcement									
<p>1. Approve certain on-site systems (septic tank) ordinances.</p> <p>2. Enforce permits and registration for wastewater collection, treatment and disposal; for municipal sludge and septage disposal; and for water treatment plant sludge disposal.</p> <p>3. Enforce compliance with authorized rights or applicable statutes through watermaster operations.</p> <p>4. Monitor compliance with Commission orders on water-related issues; issued through the Enforcement Division or the Office of Water Resource Management.</p> <p>5. Issue certificates of competency to operators who demonstrate minimum qualifications and review and approve training for all water operators.</p>									
✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
VII. Office of Chief Clerk									
Notify entities holding surface water rights of application to use water in their basin.									
✓	✓	✓	✓						
VIII. Office of Audit and Evaluation									
Conduct audits of entities receiving state/federal funds passed through the Commission.									
✓					✓				

Water Utilities Division Jurisdiction

Commission Water Utilities Division - The Regulated Community -



*CCNs are Certificates of Convenience and Necessity granted to WSCs and IOUs

Profile - Public Drinking Water Systems

This appendix provides summary information on Texas public drinking water systems. The source of the data is the Public Drinking Water Section of the Commission's Water Utilities Division.

Figure 1

Public Water Systems Total Population and Percent of Population Served by Ownership Type		
Ownership Type	Total Retail Population	Percentage of Population Served
Federal	249,328	1.33%
Investor	974,569	5.22%
State	197,099	1.06%
Local Government	15,874,033	84.98%
Water Supply Corporation	1,382,899	7.40%
TOTAL	18,677,928	100.00%
Source: Public Drinking Water Section, Water Utilities Division, TNRCC		

Notes on the data: The data are unaudited, in that we did not track individual records to source documents. We also found some data problems indicating the absence of input and other controls (see our recommendations in Sections 1-A and 3-E). As a result, the total numbers of systems may not match precisely across the tables. Nevertheless, we found the data adequate to present an overall picture of Texas public water systems.

Systems are of five main ownership types: federal, investor, state, local government (includes cities and special districts such as municipal utility districts), and nonprofit water supply corporations. In the following tables,

cities and districts (such as municipal utility districts) are combined into the Local Government ownership type. Figure 1 shows that cities and districts combined serve 85 percent of the Texas population.

Public drinking water systems are of three main types:

- **Community** - A community system serves at least 25 residents on a year-round basis. Examples of such residential systems include cities, districts, neighborhood associations, and mobile home parks.
- **Transient noncommunity** - A transient, noncommunity system serves at least 25 persons at least 60 days of the year. Examples of such semi-residential systems include recreation areas, hotels and motels, and medical facilities.
- **Nontransient, noncommunity** - A nontransient, noncommunity system regularly serves at least 25 persons at least six months of the year. Examples of such systems include industrial/agricultural, schools, and day care centers.

Figure 2

Public Water Systems Number of Systems by Community and Ownership Type			
Ownership Type	Community	Transient Noncommunity	Nontransient Noncommunity
Federal	32	84	21
Investor	1968	1137	543
State	33	93	39
Local Government	1657	83	146
Water Supply Corporation	875	97	45
TOTAL	4565	1494	794

Source: Public Drinking Water Section, Water Utilities Division, TNRCC

Figure 2 shows the interaction of ownership and community types.

Figure 3

Public Water Systems Number of Systems and Average Retail Population by Commission Region			
Region Number	Region Name	Number of Systems	Average Retail Population
01	Amarillo	178	1,962
02	Lubbock	172	2,109
03	Abilene	215	2,481
04	Arlington	886	5,196
05	Tyler	528	1,858
06	El Paso	109	6,712
07	Odessa	129	2,476
08	San Angelo	77	1,823
09	Waco	443	2,091
10	Beaumont	477	1,582
11	Austin	406	2,776
12	Houston	2284	1,939
13	San Antonio	627	2,924
14	Corpus Christi	234	2,813
15	Harlingen	94	9,884

Source: Public Drinking Water Section, Water Utilities Division, TNRCC

Commission regions differ in the average size of their water systems. While the Houston region has roughly one-third of all the systems in the State, its systems tend to be smaller than those in Arlington or El Paso, for example. The differences reflect different patterns and preferences for local development. Figure 3 shows the number of systems and the average retail population served by the systems for each region.

Most drinking water systems in Texas use groundwater as their water source. Besides being free to the owner, groundwater is less susceptible to contamination than is surface water and thus is easier and costs less to treat. However, groundwater in Texas is susceptible to “mining,” which occurs when withdrawals exceed recharge. Local governments are more likely to operate surface water systems than are other owners. Figure 4 shows the water source for systems by ownership type.

Figure 4

Public Water Systems Number of Systems by Source and Ownership Type					
Ownership Type	Groundwater	Surface Water, Purchased	Surface Water	Groundwater, Purchased	Groundwater under Influence of Surface Water
Federal	123	25	5	8	0
Investor	3873	158	92	62	12
State	141	19	11	9	3
Local Government	2343	440	284	153	5
Water Supply Corporation	1270	264	50	60	8
TOTAL	7750	906	442	292	28

Note: A single system may have multiple water sources
Source: Public Drinking Water Section, Water Utilities Division, TNRCC

Figure 5

Public Water Systems Average Retail Population, Retail Connections, and Production by Ownership Type			
Ownership Type	Average Retail Population	Average Retail Connections	Average Maximum Production (Millions of Gallons/Day)
Federal	1819.91	352.88	0.96
Investor	267.15	68.49	0.33
State	1194.54	119.04	0.38
Local Government	8416.77	2735.68	4.65
Water Supply Corporation	1359.78	448.43	0.71

Source: Public Drinking Water Section, Water Utilities Division, TNRCC

Systems also vary in size, as measured in retail population and connections. Local governments (cities and districts) serve by far the largest retail populations and have the highest production capacity, particularly when compared to investor-owned utilities. Figure 5 shows various size indicators by ownership type.

Most systems in Texas are small or very small according to EPA definitions. Figure 6 shows that 81 percent of systems are very small and that an additional 16 percent are small. Only six systems, all local governments, are considered very large.

Figure 6

Public Water Systems Number of Systems by Size and Ownership Type						
Ownership Type	Very Small	Small	Medium	Large	Very Large	TOTAL
Federal	121	13	2	1	0	137
Investor	3583	63	1	1	0	3648
State	155	9	0	0	0	164
Local Government	920	750	144	64	6	1884
Water Supply Corporation	759	242	11	3	0	1015
TOTAL	5538	1077	158	69	6	6848
According to the following EPA definitions (based on number of people served):						
	Very Small <500	Small 501-3,300	Medium 3,301-10,000	Large 10,000-100,000	Very Large >100,000	
Source: Public Drinking Water Section, Water Utilities Division, TNRCC						

Figure 7 shows various performance indicators for systems by ownership type. In the table:

- Deficiency score is a composite indicator of a system's performance. It incorporates reported water quality violations and the results of facility inspections. A deficiency score of 20 or higher indicates a serious risk to human health; however, we found deficiency scores to be routinely miscalculated (see recommendation on Improve Calculation of Deficiency Scores at Section 3-E for more information).
- Total number of enforcements indicates total Commission enforcements against the system since a new record keeping system was adopted around 1984.
- A persistent violator is one which has 6 monthly monitoring violations (usually for missed sampling) in the last 12 months.
- A superior water system is one that meets primary and secondary water quality standards and exceeds minimum requirements for design, operator certification, and operations.

- Public water systems are required to be operated *under the supervision* of a certified operator; this column shows whether the system has a certified operator according to this definition. Note that certified operators are not required for transient, noncommunity systems and only recently became required for nontransient, noncommunity systems.

Figure 7

Public Water Systems Various Performance Indicators by Ownership Type						
Ownership Type	Number of Systems	Average Deficiency Score	Total Enforcements	Number of Persistent Violators	Number of Superior Systems	Number of Systems Lacking a Certified Operator
Federal	137	6.19	2	20	1	35
Investor	3651	10.53	1034	950	10	1530
State	165	5.20	10	17	3	41
Local Government	1902	5.74	178	96	507	140
Water Supply Corporation	1017	7.71	131	95	15	151

Source: Public Drinking Water Section, Water Utilities Division, TNRCC

In all, the data indicate that Texas has many small systems (generally water supply corporations and investor-owned utilities) serving relatively few people, and relatively few systems (generally cities and districts) serving most of the population. Smaller systems, particularly investor-owned ones, have greater difficulty meeting federal and state drinking water requirements. In sparse, rural areas, these systems are small by necessity. However, in other areas, the presence of these systems reflects local developmental preferences.

Profile - Water Districts

This appendix contains background information on the numbers, types, and financial activities of Texas water districts. The source of the data is the District Administration Section of the Commission's Water Utilities Division.

The following map shows the distribution of water districts of all types across Texas.

Texas has 12 main types of districts. A general law district is one created by the Commission or county commissioners. These tend to have powers and duties associated with their legal type, as specified in multiple chapters of the Texas Water Code. A special law district is one created by a special act of the Texas Legislature. A special law district's powers and duties are dictated by its enabling legislation. A district's name (such as municipal utility district) may not indicate the statute under which it operates. Districts titled "Other" are those not fitting into the other 11 categories, such as districts for waste disposal or downtown management.

Figure 8

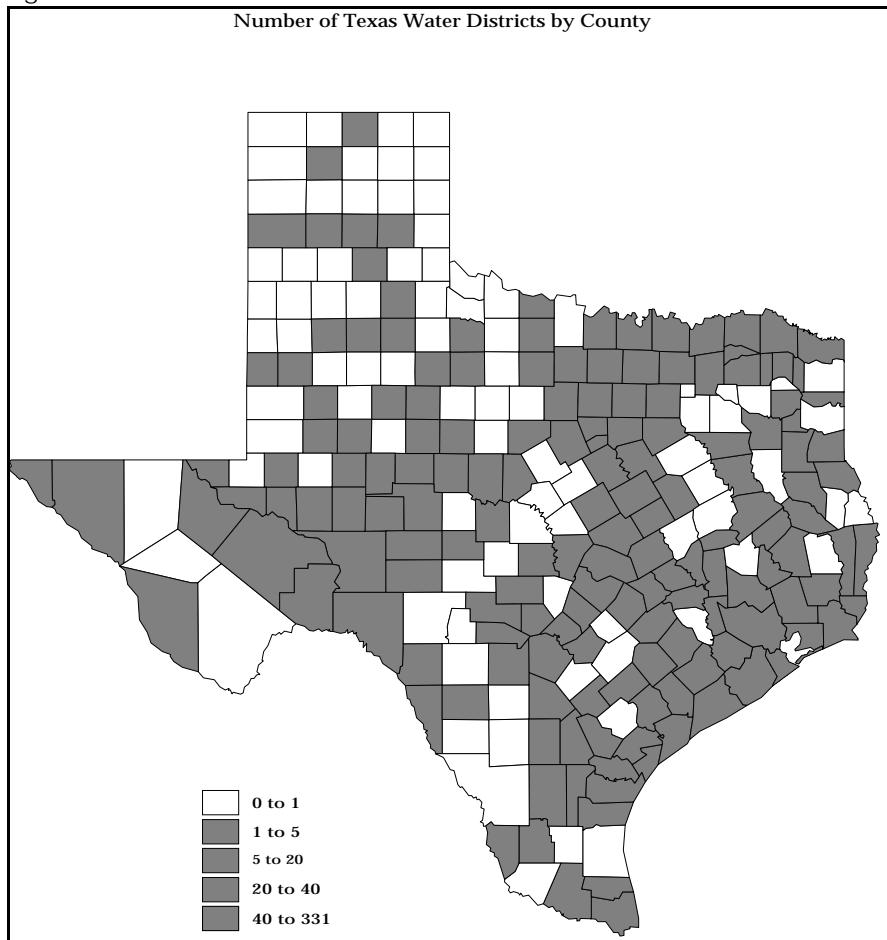


Figure 9 provides summary information on the powers and duties of Texas water districts.

Figure 9

Notes on the data: The data must be accepted “as is.” They are not audited, in that we traced few individual records to source documents. We include this information here to indicate the status of water districts as a whole and to serve as an example for reports that the Commission could develop for local and state decision making purposes (see the recommendation in Section 3-C for more information). The data may not match exactly those reported by the Commission because the Commission has recently recategorized some districts and because districts are routinely being created or dissolved (through annexation by a city, for example); thus, the data are time-sensitive. We also observed some problems with the data itself, including incorrect and nonvalid entries. The following tables contain data merged from two main sources: an official mainframe system containing district demographic data and a PC-based system containing district financial information. We had some difficulty linking the information across the systems.

Finally, not all districts are required to report uniform financial information; for example:

- Ground water districts and municipal management districts are not required to submit annual financial or audit reports.
- Smaller districts have less extensive reporting requirements than do larger ones.
- A number of districts are exempted from filing supplemental schedules to their audit reports.

Figure 10

Water Districts Number of Districts by Type and Status 1995			
District Type	Total	Inactive	Unknown
Drainage District	46	4	0
Fresh Water Supply District	44	5	0
Irrigation District	21	0	0
Levee Improvement District	44	16	2
Municipal Utility District	769	196	6
Navigation District	24	1	0
Other	59	14	2
River Authority	21	0	0
Special Utility District	17	3	1
Underground Water District	43	9	1
Water Control and Improvement District	196	25	3
Water Improvement District	20	0	0
TOTAL	1304	273	15

Source: District Administration Section, Water Utilities Division, TNRCC

Figure 10 shows the number, type, and status of Texas water districts. It shows that a total of 1304 districts have been created and not dissolved. More than half of these are municipal utilities districts, a high percentage of which are inactive. Roughly 22 percent of all officially recognized districts are either inactive or of unknown status.

Figure 11 shows how the various types of districts have been created, whether by the Commission, city, county, or Texas Legislature. The Commission has created nearly half of all districts and over 70 percent of all municipal utility districts.

Figure 11

Water Districts Number of Districts by Way Created 1995					
District Type	Total	Commission	City	County	Legislature
Drainage District	46	0	0	38	8
Fresh Water Supply District	44	0	0	35	9
Irrigation District	21	1	0	17	3
Levee Improvement District	44	0	0	38	6
Municipal Utility District	769	544	0	25	200
Navigation District	24	0	0	18	6
Other	59	2	0	2	55
River Authority	21	1	0	0	20
Special Utility District	17	15	0	1	1
Underground Water District	43	7	0	2	34
Water Control and Improvement District	196	57	1	66	72
Water Improvement District	20	0	0	18	2
TOTAL	1304	627	1	260	416
Source: District Administration Section, Water Utilities Division, TNRCC					

Figure 12 shows aggregated financial indicators for all districts meeting the financial reporting threshold for the last three years. In the table:

- Bonds represent outstanding general fund bond debt.
- Industrial Development Corporation Bonds represent a type of third-party debt for which the district acts as an agent or intermediary on behalf of an industrial development corporation. The district is usually not responsible for the debt and the debt is not shown on its balance sheet

- Beginning and ending fund balances are shown separately for entities using governmental accounting and entities using enterprise fund accounting.¹⁰
- Revenues and expenditures are shown separately for entities using governmental accounting and entities using enterprise fund accounting.
- Assessed value represents the assessed monetary value of the land within the district.
- Tax rates are expressed per \$100 of assessed value.

Figure 12

Water Districts Financial Indicators 1993-1995			
Indicator	1993	1994	1995
Bonds	\$ 5,615,604,792	\$ 6,100,031,353	\$ 6,420,853,019
Industrial Development Corporation Bonds	\$ 4,117,771,786	\$ 4,177,134,445	\$ 5,709,053,292
General Fund Balance Begin	\$ 285,830,662	\$ 316,235,585	\$ 324,237,038
General Fund Balance End	\$ 311,293,696	\$ 344,187,604	\$ 374,382,753
Enterprise Fund Balance Begin	\$ 814,098,018	\$ 718,081,660	\$ 1,119,298,523
Enterprise Fund Balance End	\$ 881,493,149	\$ 784,462,712	\$ 1,227,253,237
General Fund Revenue	\$ 450,967,730	\$ 481,519,245	\$ 495,968,171
General Fund Expenditure	\$ 450,743,715	\$ 446,030,766	\$ 432,109,929
Enterprise Fund Revenue	\$ 320,239,220	\$ 350,281,459	\$ 402,584,158
Enterprise Fund Expenditure	\$ 237,363,891	\$ 230,360,092	\$ 265,531,182
Assessed Value	\$ 88,946,133,097	\$ 102,390,408,517	\$ 98,914,732,903
Average Debt Tax Rate	0.58	0.52	0.47
Average Maintenance. Tax Rate	0.11	0.12	0.13
Average Total Tax Rate	0.69	0.64	0.60

Source: District Administration Section, Water Utilities Division, TNRCC

¹⁰ Districts are allowed to use governmental accounting, enterprise funding accounting, or a combination of the two. In 1989 the State Auditor's Office recommended that Texas Water Commission, the Commission's predecessor agency, strongly encourage all municipal utility districts and water control and improvement districts to use governmental accounting to improve comparability; alternatively, it could gain comparability by requiring supplemental schedules to the audit reports. The Commission opted for the latter approach.

Figure 13 shows bond debt by type of district for 1995. The table shows that 80 percent of district general fund debt belongs to municipal utility districts and river authorities.

Figure 13

Water Districts Bond Debt by District Type 1995			
District Type	Bonds	IDC Bonds	Total
Drainage District	\$ 38,210,407	\$ 0	\$ 38,210,407
Fresh Water Supply District	29,663,597	0	29,663,597
Irrigation District	5,642,793	0	5,642,793
Levee Improvement District	142,515,589	0	142,515,589
Municipal Utility District	2,769,620,338	43,735,000	2,813,355,338
Navigation District	135,271,364	875,398,396	1,010,669,760
Other	515,619,615	1,242,973,815	1,758,593,430
River Authority	2,394,590,714	3,546,946,081	5,941,536,795
Special Utility District	22,274,035	0	22,274,035
Underground Water District	2,954,819	0	2,954,819
Water Control and Improvement District	360,300,206	0	360,300,206
Water Improvement District	4,189,542	0	4,189,542
Total	\$ 6,420,853,019	\$ 5,709,053,292	\$ 12,129,906,311
Source: District Administration Section, Water Utilities Division, TNRCC			

Figure 14

Water Districts Average Tax Rates 1995			
District Type	Average Debt Tax Rate	Average Maintenance Tax Rate	Average Total Tax Rate
Municipal Utility District	\$ 0.77	\$ 0.16	\$ 0.93
Levee Improvement District	\$ 0.29	\$ 0.32	\$ 0.61
Water Improvement District	\$ 0.15	\$ 0.33	\$ 0.48
Water Control and Improvement District	\$ 0.15	\$ 0.08	\$ 0.23
Fresh Water Supply District	\$ 0.12	\$ 0.09	\$ 0.21
Drainage District	\$ 0.06	\$ 0.14	\$ 0.19
Irrigation District	\$ 0.04	\$ 0.02	\$ 0.06
Other	\$ 0.01	\$ 0.03	\$ 0.04
River Authority	\$ 0.00	\$ 0.03	\$ 0.03
Navigation District	\$ 0.00	\$ 0.02	\$ 0.02
Underground Water District	\$ 0.00	\$ 0.01	\$ 0.01
Special Utility District	\$ 0.00	\$ 0.00	\$ 0.00

Source: District Administration Section, Water Utilities Division, TNRCC

Figure 14 shows the average tax rates by type of district for 1995. Because of the wide array of services they may offer (including firefighting, parks, water, wastewater, drainage and flood control) municipal utility districts have by far the highest average tax rates. Special utility districts do not have taxing authority. Only two river authorities levied taxes in 1995; most lack taxing authority. Note too that there may be wide variance around these averages.

Figure 15 shows revenues and expenditures by type of district for 1995. Only groundwater districts as a group showed an operating deficit for the fiscal year.

Figure 15

Water Districts 1995 Revenues and Expenditures				
District Name	General Fund Revenue	General Fund Expenditures	Enterprise Fund Revenues	Enterprise Fund Expenditures
Drainage District	\$ 34,088,623	\$ 30,937,051	\$ 0	\$ 0
Fresh Water Supply District	\$ 12,757,404	\$ 11,338,135	\$ 6,412,871	\$ 5,376,401
Irrigation District	\$ 18,846,779	\$ 16,917,454	\$ 4,820,067	\$ 4,306,154
Levee Improvement District	\$ 2,044,474	\$ 2,316,723	\$ 0	\$ 0
Municipal Utility District	\$ 220,027,740	\$ 207,564,099	\$ 51,272,398	\$ 43,693,648
Navigation District	\$ 17,991,402	\$ 14,519,169	\$ 30,413,820	\$ 32,347,676
Other	\$ 61,864,105	\$ 51,464,995	\$ 108,759,911	\$ 52,406,253
River Authority	\$ 30,583,549	\$ 19,671,032	\$ 141,454,495	\$ 83,976,303
Special Utility District	\$ 0	\$ 0	\$ 13,714,814	\$ 10,307,424
Underground Water District	\$ 9,905,623	\$ 10,549,093	\$ 902,755	\$ 783,787
Water Control and Improvement District	\$ 80,873,774	\$ 60,410,075	\$ 45,671,341	\$ 33,397,965
Water Improvement District	\$ 6,984,698	\$ 6,422,102	\$ 30,255	\$ 28,062

Source: District Administration Section, Water Utilities Division, TNRCC

Figure 16 shows the tax rates for active municipal utility districts by Commission region for 1995. The Houston region has the highest average total tax rates, due mainly to its debt tax rate. The single-family equivalent connections shown in the table are likely understated, since the database showed 77 active districts having either 0 connections or null values.

Figure 16

Water Districts Average Active MUD Tax Rates by Region 1995 ¹					
Commission Region	Average Total Tax Rate	Average Debt Tax Rate	Average Maintenance Tax Rate	Number of Districts	Average Number of SFE Connections
Houston	\$ 1.04	\$ 0.88	\$ 0.16	419	701
San Antonio	\$ 1.02	\$ 0.86	\$ 0.16	6	311
Waco	\$ 0.88	\$ 0.88	\$ 0.00	5	305
Austin	\$ 0.63	\$ 0.33	\$ 0.30	37	826
Beaumont	\$ 0.59	\$ 0.49	\$ 0.10	13	679
Arlington	\$ 0.53	\$ 0.46	\$ 0.07	16	916
El Paso	\$ 0.37	\$ 0.21	\$ 0.16	5	1859
Corpus Christi	\$ 0.19	\$ 0.02	\$ 0.17	8	56
San Angelo	\$ 0.15	\$ 0.00	\$ 0.15	2	115
Odessa	\$ 0.14	\$ 0.00	\$ 0.14	2	0
Harlingen	\$ 0.14	\$ 0.12	\$ 0.02	6	528
Tyler	\$ 0.07	\$ 0.07	\$ 0.00	7	1712
Abilene	\$ 0.00	\$ 0.00	\$ 0.00	2	140
Lubbock	\$ 0.00	\$ 0.00	\$ 0.00	1	0

¹ This table contains known data errors.
SFE = Single Family Equivalent connections

Source: District Administration Section, Water Utilities Division, TNRCC

In summary, Texas water districts come in all shapes and sizes. They can be created in three or four different ways, they may have similar names (such as municipal utility district) yet perform dissimilar functions, and they occupy many different chapters of the Texas Water Code. While the Commission has “general supervision” authority over all the districts, its specific authority, such as for bond approvals, varies by district type.

Profile - Active Retail Public Utilities

This appendix provides background information on retail providers of water and sewer services. The data are maintained by the Utility Rates and Services Section.

Notes on the data: The data are unaudited, in that we did not track individual records to source documents. Throughout the project we had some difficulty linking utility data with other data, including public drinking water systems. Nevertheless, the data are adequate to present an overall picture of Texas retail public utilities.

The key identifier for a utility, depending on its ownership type, is its CCN (certificate of convenience and necessity) number. A CCN is a defined utility service area. The area may or may not be contiguous. The certificate obligates the utility to provide service to the entire designated area.

In addition to certifying utilities, the Commission also has original or appellate jurisdiction over utility rates and tariffs. A tariff establishes the utility's rates, charges, terms of service, and water rationing plan. Figures 17 and 18 show the Commission's jurisdiction over CCNs and rates/tariffs.

Figure 17

Commission CCN and Tariff/Service Jurisdiction		
Utility Service Provider	CCN Required?	Commission Tariff and Service Policies Apply?
IOU - Outside City	Yes	Yes
IOU - Inside City	Yes	Yes If city does not require its own
Exempt IOU	No ¹	Yes
WSC	Yes	No But must file tariff with the Commission
Exempt WSC	No ¹	No But must file tariff with the Commission
District	No ¹	No
Affected County	Yes	Yes
City	No ¹	No

1. Unless serving within another utility service provider's lawful service area.

Figure 18

Commission Rate Jurisdiction				
Utility Service Provider	Retail			Wholesale Appellate
	Original	Appellate	Notice to Customers Required?	
IOU - Outside City	Yes	N/A	Yes	Yes
IOU - Inside City	No Unless city surrenders its jurisdiction to the Commission	Yes 10% customer protest or on request from party to rate case before city	Yes	Yes
Exempt IOU	Yes	N/A	Yes	Yes
WSC	No	Yes 10% customer protest	No	Yes
Exempt WSC	No	Yes 10% customer protest	No	Yes
District	No	Yes In-district customers - 10% Out-of-district customers - 10%	In-district - No Out-of-district - Yes ²	Yes
Affected County	No	Yes 10% customer protest	Yes ²	Yes
City - Only out-of-city customers	No	Yes 10% customer protest	Yes ²	Yes

2. Notice must tell old rates, new rates, and effective date. The Commission recommends the utility notify customers that they may appeal.

Figure 19 shows the numbers of unique CCN service providers by ownership type. Note that this table does not include the universe either of unique utility service providers or of all CCNs. While CCNs are required of investor-owned utilities and water supply or sewer corporations, they generally are not required from cities and districts (see the recommendation in Section 4-A).

Figure 19

Active Retail Public Utilities (as of October 1996)					
Type of Certificate	IOUs	WSCs	Districts	Cities and Others	Total
Water CCN	812	793	105	541	2251
Sewer CCN	145	42	63	442	692
Total CCNs	957	835	168	983	2943