



ANDOVER, ARKANSAS CITY, AUGUSTA, BEL AIRE, BENTLEY, BENTON, BUTLER COUNTY, CHENEY, CLEARWATER, COLWICH, CONWAY SPRINGS, DERBY, EL DORADO, GODDARD, HALSTEAD, HARVEY COUNTY, HAYSVILLE, HESSTON, HUTCHINSON, KECHI, KINGMAN COUNTY, MAIZE, MCPHERSON COUNTY, MOUNT HOPE, MULVANE, NEWTON, PARK CITY, RENO COUNTY, ROSE HILL, SEDGWICK, SEDGWICK COUNTY, SUMNER COUNTY, VALLEY CENTER, WELLINGTON, WICHITA, WINFIELD

**Municipal Utility Growth Issues Special Committee Report
Regional Economic Area Partnership
Water Resources Committee**

Adopted by REAP on September 14, 2009

In June of 2008, the Municipal Utility Growth Issues Special Committee was established by the REAP Water Resources Committee to identify fair and reasonable solutions to service area issues arising between cities and rural water districts in south-central Kansas.

Thirty-six cities and counties in south-central Kansas comprise the Regional Economic Area Partnership, a council of local governments representing a population of more than 730,000. These local governments have voluntarily joined together to guide state and national policies that affect economic development in the region and adopt joint actions among member governments to enhance the regional economy.

In 2007, REAP established the Water Resources Committee (WRC) as a standing committee of REAP with the purpose of serving as a regional alliance for collaboration and information sharing on issues of water supply and water quality in south-central Kansas. The WRC also seeks to identify issues of common interest among member jurisdictions and serve as a regional voice on behalf of members before federal, state and regional agencies.

Rural Water Districts in South-Central Kansas

Cities are established to bring a full range of urban services to their residents. Municipal water systems support city residents by providing water for domestic purposes, wastewater treatment, fire protection and a wide range of commercial/industrial demands. Municipal water systems are essential to urban economic development. Orderly expansion of municipal water systems is critical to the health and vitality of urban areas and the state as a whole.

Rural water districts (RWD) were created to provide domestic water service to residents of sparsely populated, rural areas. Rural water districts meet a critical need: ensuring that rural residents have access to clean water for domestic purposes. Keeping RWDs viable is vital to rural community health and well-being.

Urban growth coupled with expansions initiated by rural water districts that include service to urban-density developments has caused service area conflicts between districts and municipalities. These types of conflicts are on the rise in South-Central Kansas as city boundaries expand and come in contact with a greater number of RWDs. Currently there are fifty-two RWDs in the REAP region, which includes nine counties: Butler, Cowley, Harper, Harvey, Kingman, McPherson, Reno, Sedgwick, and Sumner. Forty-eight of the region's 97 cities have city boundaries within three miles of a RWD. Of those, 24 are REAP-member communities.

In addition, some of the communities adjacent to RWDs are among the fastest growing in the region, including Andover, Derby, Goddard and Wichita. These four communities are within Butler and Sedgwick counties, which experienced a 6% and 5.1% population growth respectively between 2000 and 2007. The potential growth for these and other municipalities in Kansas highlights the importance of a clear statutory framework to guide cities and RWDs through service area disputes.

Recognizing the distinct missions of rural water districts and municipal utility systems is key to the successful resolution of conflict between the entities in moving forward. Service area conflicts often result in high costs for acquisition of RWD territory, costly court procedures, higher costs for ratepayers and a waste of financial resources. REAP communities seek to avoid these issues and determine a fair and reasonable value for assets and property that affected entities can agree upon. While cities and RWDs have diverse interests, a cooperative effort moving forward will benefit all.

Kansas Statutory Framework

State laws have been periodically amended to address isolated issues but have not created a comprehensive solution to service area disputes. Current state statutes provide the following piecemeal approach.

Two sets of state statutes provide avenues for acquisition of RWD territory by a municipality: K.S.A. 12-527, enacted in 1968, and K.S.A. 82a-646, enacted in 2001. The mechanism for establishment of acquisition costs for RWD territory, facilities and improvements annexed by a city are set forth in KSA 12-527. This statute provides that a city shall compensate a RWD for the “reasonable value” of all property, facilities, and improvements used by the RWD and located within the annexed area. Reasonable value is to be determined by three appraisers, but the statute provides little guidance in the determination of what is reasonable. Agreement on the value of a district’s current assets may be calculated more objectively, but determining the value of undeveloped territory is more subjective. With little statutory guidance, appraised values are difficult to predict and often lead to litigation.

K.S.A. 82a-646 provides a framework for the release of lands from a rural water district by action of the RWD board of directors. This statute provides more guidance in that it includes seven factors to be considered, but since the decision is made unilaterally by the RWD board, the potential for disputes remains high. Few cases result in release of lands. While this statute has not been widely used for municipal service expansion into RWD territory, it does play an important role in allowing private landowners to determine the highest and best use of their land.

The 2009 Legislative Session included a bill (SB 51) that incorporated a majority of two previously introduced bills; HB 2283 and SB 332 (drafted by the KRWA) which attempted to address a number of the issues associated with rural water district and city water service area conflicts. The bill was approved by the House and Senate but vetoed by the Governor for reasons unrelated to the water components of the bill. The Water Resources Committee hopes to work with other interested parties under the framework established in SB 51 to draft legislation that creates a comprehensive solution and obtain approval.

U.S. Department of Agriculture Loan Program

Another obstacle to resolving service area conflicts is the USDA Rural Water Grant and Loan program initiated by Congress in 1954 for developing water supply in rural areas. This program has helped to improve the public health and economic stability of rural communities but can be an impediment to orderly urban expansion.

To ensure the ability of RWDs to repay federally backed loans, 7 U.S.C. 1926(b) was added to protect a rural water district from being “unilaterally” annexed by a city or other water system. Congress wanted to insure that the costs of water service to rural residents were minimized, and a water district's ability to repay its debt to the government was strengthened. 1926(b) limits a municipality's legal right to sell water, when the exercise of those powers would result in competition with a rural water district. While REAP recognizes the fiduciary responsibility of the USDA to secure its loans, the service area protection requirement is susceptible to abuse and does not always serve the best interest of the customer.

Outstanding Debt in REAP Region

Consultation with a U.S. Department of Agriculture Rural Development official in Topeka during January of this year identified five current outstanding federally backed loans for RWDs in the REAP region: RWD 5 in Butler County, RWD 7 in Cowley County, RWD 3 in Reno County, RWD 1 in Sedgwick County and RWD 4 in Sumner County. Several RWDs with federally backed loans border REAP member communities, including Andover, Benton, Wichita, Bel Aire, Kechi and Arkansas City. The majority of USDA loans financed for the region’s RWDs over the past 45 years have been paid off.

Regional Response and Public Costs

The inadequate statutory framework for resolution of service area conflicts between cities and RWDs has produced a myriad of service area agreements that resolve short-term conflicts but increase long-term costs to water customers and taxpayers. Examples of long-term costs in the REAP region and in other areas of the state:

- **Urban-density rural development:** Rural water districts have in some cases extended water service to high-density housing developments in unincorporated areas with no provision for fire protection, wastewater treatment, or other urban services. Such developments often result in higher long-term costs to secure such services.
- **Increased costs for housing development:** The absence of a clear statutory formula to determine the cost of acquisition of undeveloped RWD territory by cities frequently adds to the cost of housing development in newly annexed areas. In one instance, a city agreed to pay \$1,000 an acre to obtain undeveloped RWD territory in order to keep a large urban-density development from stalling. That cost was then passed on to the subdivision’s future homeowners and at-large city rate payers.
- **Overlapping governments and duplicative services:** Piecemeal agreements between RWDs and cities have created inefficiencies as urban services are delivered to city residents by overlapping jurisdictions. For example, providing fire protection in urban-density subdivisions serviced by a rural water district may require two separate water distribution systems to serve the same area. Such duplication is costly and unnecessary.

- **Increased insurance costs:** A RWD's inability to provide urban-level fire protection increases risk and lowers ratings by the Insurance Services Office, Inc. (ISO) for the service area, resulting in increased costs for homeowner's insurance in most cases. A decrease in ISO ratings may reach beyond the RWD service area and adversely affect the rating of adjacent portions of the city as well.
- **Litigation costs:** When service area disputes result in litigation, attorney fees and associated costs for both parties can reach into the hundreds of thousands of dollars with no additional services being provided to the customers of either party. In one Kansas case, litigation costs have exceeded \$1 million.
- **Cost to property owners:** Property values may be affected by the water service provider, devaluing property intended for urban-density development. Property owners lose money when land cannot be developed for its highest and best use.
- **Skewed development patterns:** When land sales in the growth areas of a city are altered as a result of the water provider; opportunities for urban development shift, and urban growth gravitates to areas without conflicts over water service.

Committee Recommendations

After studying this issue for over a year, the Committee offers the following recommendations on best practices and public policy with the intent of moving forward with reasonable and fair solutions to service area conflicts. The recommendations are divided into regional, state, and federal categories.

Best Practices

Regional

- Gather documentation of instances where RWDs and cities have successfully worked together to cooperatively resolve service area disputes;
- Gather documentation of instances of conflict between public water suppliers, resulting in unnecessarily increased cost for urban growth in the region;
- Identify and promote best practices in the transfer of rural water district service areas to municipalities and improve communication when RWDs on these practices;
- Encourage county officials to engage cities and rural water districts in the evaluation of RWD service area expansion proposals, especially those within 3 miles of a city;
- Educate developers on available options for de-annexation of service area from RWDs;
- Encourage cities to proactively initiate timely and open communication by and between cities and nearby RWDs, especially with annexing RWD service area;
- Initiate comprehensive regional planning for extension of urban services to unincorporated areas projected for urban density development, such as eastern Sedgwick County and western Butler County; and
- Assemble financial and service profiles of RWDs with service area affected by urban growth.

State

- Regularly inform state legislators in South Central Kansas on issues of municipal growth that affect water supply and water quality in the region;
- Recommend mediation and other Alternative Dispute Resolution (ADR) techniques to encourage RWDs and cities to reach mutually acceptable service agreements; and
- Recommend funding of comprehensive regional planning for urban services affecting water supply and water quality through the State Water Plan Fund.

National

- Collaborate with National Home Builders Association on issues of urban growth affecting water supply and water quality.

Public Policy

Local

- Develop a regional approach to public water supply and wastewater treatment.

State

- Develop and advocate state legislation to establish a formula for determining the value of undeveloped RWD service area;
- Collaborate with representatives from the Kansas Rural Water Association, Kansas Municipal Utilities and the League of Kansas Municipalities to develop a legislative agenda on issues of water supply and water quality affecting municipal growth;
- Develop and advocate state legislation to require mediation or other ADR techniques to establish compensation to RWDs when service area is annexed, potentially under the auspices of the Kansas Water Office; and
- Develop and advocate state legislation to make de-annexation of undeveloped rural water district property more feasible and cost-effective for landowners and developers.

National

- Take action to assure RWDs financed through the U.S. Department of Agriculture comply with federal statutes and administrative regulations and that regional offices of the Department actively enforce federal statutes and administrative regulations applicable to federal loans.