

LACK OF TRANSPARENCY AND DUE DILIGENCE AT THE SANTA MARIA VALLEY WATER CONSERVATION DISTRICT

SUMMARY

Santa Maria Valley Water Conservation District (District) is charged with operating and maintaining the Twitchell Dam and Reservoir (Twitchell) located in northern Santa Barbara County and a small section in southern San Luis Obispo County. It is organized as an independent California special district, and as such is governed by its own elected board of directors that operates independently of any city or county oversight. Given this independent status, full transparency is critical.

The Santa Barbara County Grand Jury (Jury) found the District's transparency lacking both in terms of timeliness and adequacy. The absence of disclosures by the District created a vacuum in the flow of public information, which was filled with incorrect news releases by Western Sierra Resource Corporation (WSRC), a "penny stock"¹ company whose subsidiary, Mitigation Solutions, LLC (MSL), was a party to a contract with the District. The Jury recommends that disclosures on the District's website be enhanced, comparable to those employed by other special districts in northern Santa Barbara County.

¹ Penny stocks are common shares of small public companies that trade for less than one dollar per share.

The Jury also found that financial due diligence was lacking concerning the District’s evaluation of WSRC and MSL’s ability to meet their contractual obligations, specifically regarding their financial condition. The Jury recommended that the District establish and follow policies for vetting the financial capacity and capabilities of parties to all contracts.

INTRODUCTION

A Request for Investigation (RFI) was made to the Jury regarding issues involving transparency relating to the District. The RFI specifically addressed overall transparency and the unique situation created by the contract with MSL for mitigation activities at Twitchell.² The Jury’s report, in response to the request, suggests best practices for disclosures, identifies transparency practices in other districts, and includes an expanded discussion of events surrounding the contract with MSL.

METHODOLOGY

The Jury interviewed directors and legal counsel of the District, reviewed documents obtained from the District, and compared disclosure practices of peer organizations (i.e., other special districts in northern Santa Barbara County). In addition, the Jury obtained and reviewed industry-related resources for relevant disclosure standards for special districts, and reviewed financial disclosures and news releases of WSRC.

OBSERVATIONS

² Mitigation activities broadly include stabilizing Twitchell Dam and removing sediment and debris in and around the Reservoir.

Best practices for transparency

In its own words, “The Special District Leadership Foundation (SDLF) is an independent, non-profit organization that promotes good governance and best practices among California’s special districts through certification, accreditation, and other recognition programs. The SDLF and its activities are supported by the California Special Districts Association and the Special District Risk Management Authority.” The District is a member of the California Special District Association.

SDLF programs include checklists of best practices, one of which addresses transparency; it offers a “District Transparency Certificate of Excellence” to districts that qualify. In addition, the application for the transparency program has an extensive checklist of requirements for a district’s website, including information about the district’s mission, operations, board members and key employees, board meeting schedules, agendas, meeting packets, minutes of meetings, budgets, and financial statements.³

The Jury examined websites of several other special districts in northern Santa Barbara County, which all have transparent websites with links to relevant resources for items such as those mentioned in the SDLF website checklist.

Deficiencies in transparency at the District

The Jury’s first review of the District’s website (SMVWCD.org) in early February of 2023 revealed a dearth of information. During the Jury’s investigation, disclosures have been sporadically added. The investigation of the District’s 2022 meetings revealed that a notice and an agenda were posted. No minutes or document packs were attached for

³https://higherlogicdownload.s3.amazonaws.com/CSDA/feaaf941-6df6-4428-a23c-583379a09704/UploadedImages/PDFs/2023_SDLF_District-Transparency-Application.pdf

Date last viewed May 15, 2023.

any meeting except for a special meeting of the District's Board held on October 19, 2022, with one action item relating to the contract for the mitigation efforts at Twitchell. The sole reference in the minutes reads:

ACTION ITEMS

Twitchell Dam & Mitigation Contract:

District Counsel reported on the changes to the MSL contract; held discussions with Mr. Jones of MSL, revised correct typographical errors raised by Director Hadick. Responded to Director Adam's questions. It was moved and seconded (Flores and Mahoney) to authorize President Hadick to execute and Secretary to attest to the MSL contract. Motion carried: 5-0-0-2.⁴

The contract with MSL

Nothing appeared on the District's website about the nature, scope, or finances involved in the contract with MSL. No local newspaper picked up the story, although some financial service websites did report WSRC's news releases. A web search revealed the only public mention of the contract was in securities filings and news releases by WSRC, which is the parent company of MSL. WSRC's news releases and disclosures were the only publicly accessible sources of information about the MSL contract with the District that the Jury could find.

A news release by WSRC, dated October 25, 2022, valued the contract at \$1.976 billion, and reported that WSRC had \$40 million of equipment financing and a \$150 million line

⁴ <https://www.smvwcd.org/files/f89bdfc92/10-19-2022+Minutes+Final.pdf>
Last read May 15, 2023.

of credit immediately available. The news release also stated MSL would secure federal reimbursement funding for the District.⁵

The contract has been characterized as self-funded, meaning responsibility for performing mitigation activities and obtaining government or other financing for the work rests solely and exclusively with MSL, at a net zero cost and no liability nor obligation to the District.

The District did not establish a value for the MSL contract. The October 2022 contract was for a feasibility study. The final contract in January 2023 incorporated the feasibility study and set the legal framework for the relationship between the parties. Values of the contract will be known only if and when the District initiates specific task orders for work. WSRC's assertion about \$190 million of available financing has not been verified.

Emergency expenditures in response to Winter 2023 storms in California

Winter 2023 storms in California placed Twitchell in emergency mode, and \$13.6 million of disaster expenditures were made through February 2023 via independent contractors. The \$13.6 million amount is far more than the District's funds on hand or its ability to generate additional revenue, and MSL has not provided funding. In a March 28, 2023, letter to the California Office of Emergency Services, the District formally requested advanced funding for those emergency expenditures through the California Disaster Assistance Act.⁶

The District failed to perform financial due diligence regarding the contract

⁵<https://www.otcmarkets.com/stock/WSRC/news/Western-Sierra-Announces-FINAL-Contract-for-15-Billion-Federally-Funded-Project-Through-the-Company's-Wholly-Owned-Subsid?id=377389> Date last viewed May 15, 2023.

⁶<https://www.smvwcd.org/files/cfa2d051e/SMVWCD+Request+to+CalOES+re+Advanced+Funding.pdf> Date last viewed May 15, 2023.

The Jury learned that the District did not initiate the contract with MSL. MSL approached the District. Only cursory steps were taken to vet MSL and its principals. The District did not seek bids because the contract was presented as a net zero cost to the District.

Financial filings and news releases by WSRC have long been publicly available on its website⁷ as well as on OTC Markets Group, Inc.⁸ The websites show that MSL is a wholly owned subsidiary of WSRC⁹. The financial reports and other filings the Jury reviewed revealed a history of unfavorable financial conditions,¹⁰ and do not reflect the availability of the financing resources claimed by WSRC in its October 25, 2022, news release.

CONCLUSION

The Jury found that the District needs to give proper attention to its duty to operate in full public view, thereby supplying the District's constituents with timely and accurate information about developments that may impact them. The Jury also found that the District should thoroughly vet the financial capacity and capabilities of potential parties to all contracts.

FINDINGS AND RECOMMENDATIONS

Finding 1

⁷ <https://westernsierraresource.com/> Last viewed May 15, 2023.

⁸ <https://www.otcm Markets.com/stock/WSRC/overview> Last viewed May 15, 2023.

⁹ MSL and WSRC are separate legal entities, but constitute a single economic entity, therefore financial reports consolidate them.

¹⁰ e.g., Negative working capital of approximately \$12 million and an accumulated deficit from recurring losses of approximately \$29 million.

The Santa Maria Valley Water Conservation District's transparency needs to be improved both in terms of timeliness and adequacy.

Recommendation 1

That the Santa Maria Valley Water Conservation District bring its website disclosures up to best practices comparable to those recommended by the Special District Leadership Foundation and those employed by other special districts in northern Santa Barbara County.

Finding 2

The Santa Maria Valley Water Conservation District's inadequate disclosure regarding its contract with Mitigation Solutions, LLC resulted in Western Sierra Resource Corporation's inaccurate news releases becoming the only public source of information about ongoing mitigation activities at Twitchell Dam and Reservoir.

Recommendation 2

That the Santa Maria Valley Water Conservation District's website report at least quarterly on ongoing mitigation projects.

Finding 3

The Santa Maria Valley Water Conservation District failed to exercise financial due diligence in its evaluation of Mitigation Solutions, LLC's ability to meet its contractual obligations, particularly considering Western Sierra Resource Corporation and Mitigation Solutions, LLC's financial condition.

Recommendation 3

That within six months, the Santa Maria Valley Water Conservation District establish and follow policies for thoroughly vetting the financial capacity and capabilities of potential parties to all contracts.

REQUEST FOR RESPONSE

Pursuant to *California Penal Code Section 933 and 933.05*, the Santa Barbara County Grand Jury requests each entity or individual named below to respond to the enumerated findings and recommendations within the specified statutory time limit:

Responses to Findings shall be either:

- Agree
- Disagree wholly
- Disagree partially with an explanation

Responses to Recommendations shall be one of the following:

- Has been implemented, with brief summary of implementation actions taken
- Will be implemented, with an implementation schedule
- Requires further analysis, with analysis completion date of no more than six months after the issuance of the report
- Will not be implemented, with an explanation of why

Santa Maria Valley Water Conservation District – 90 days

Findings 1, 2 and 3

Recommendations 1, 2 and 3