

**METROPOLITAN DOMESTIC WATER IMPROVEMENT DISTRICT
FINANCE OVERSIGHT COMMITTEE**

**Metropolitan Domestic Water Improvement District
Board Conference Room
6265 N. La Cañada Drive
Tucson, AZ 85704**

April 16, 2012

MINUTES

Committee Members Present: Jeffrey Ratje, Chair
Sheila Bowen, Member
Reb Guillot, Member
Lee Mayes, Member
Jim Stevenson, Member
Clare Strom, Member
Tim Thomure, Member

Committee Members Not Present: Bernie Wiegandt, Vice Chair

District Staff Present: Mark R. Stratton, General Manager
Christopher W. Hill, Deputy General Manager
Warren Tenney, Assistant General Manager
Mike Land, Chief Financial Officer
Charlie Maish, District Engineer
Tullie Noltin, Recorder

I. Call to Order and Roll Call.

Mr. Ratje called the Metropolitan Domestic Water Improvement District Finance Oversight Committee (Committee, FOC) meeting to order at 4:00 p.m. Mr. Ratje, Ms. Bowen, Mr. Guillot, Mr. Mayes, Mr. Stevenson, and Ms. Strom were present. Mr. Wiegandt was not present. Mr. Thomure arrived at 4:01 p.m.

II. Status of Capital Improvement Projects and County Road Projects.

Mr. Maish said Magee Phase 2 is under construction, Cortaro Road from Shannon to Thornydale. A portion of La Cañada south and La Cholla from Magee to Overton are also under construction. The contract has been awarded for the Iberia Avenue Interconnect in the Metro Southwest area. Old Magee Trail well, replacing Matter well, is currently out to bid. The District's miscellaneous design consultant has completed design at Old Magee Trail and is now concentrating on the Riverside well. Once those plans are approved, they will move on to the new well site at Metro Hub. Final approval was received on the design for the Pantano Transmission line, also in the Hub service area.

Approval of the Riverside transmission main was received three weeks ago and planned development in that area near Lulu Walker School will include road realignment and additional parking, which will require more utility modifications. The very basic plans supplied make it challenging for utilities to design the modifications. There is not enough time to put the Riverside Transmission line out to bid, so a change order will be sought on an existing contract to include that work.

Mr. Maish said the District has submitted final plans for the County project on Orange Grove between Camino de la Tierra and La Cholla, which is expected to start in July. Since it is almost May, there is no time to bid and award that project by the County's date, so that project may require another change order to an existing contract. The problem with this one is the work is extensive, estimated to cost about \$350,000, and that might make it difficult for the Board to accept but there are few options if the District is to keep the County's schedule.

Construction is expected to start in the Fall for Magee Phase 3, the portion between La Canada and Oracle. Conflicts are minimal there and approval has been received from the County. District staff has not decided whether to put it out to bid or not, due to the small size around \$30,000.

Ms. Bowen asked about the projects that are being pushed through as change orders. Mr. Maish explained the projects have become more involved because the County continued to improve upon the plans, which were initially calling for widening of existing pavement and now call for the removal of entire pavement sections. Ms. Bowen asked if the District ever considers using the County's contractor. Mr. Maish said the District has never done that before and that would require intergovernmental agreements. That approach would create other problems with regards to control of costs, inspections, and oversight. The County does have such arrangements with Tucson Water but the City of Tucson pays 50% of their costs, so it is a little different for a smaller utility like Metro Water.

Mr. Maish said the parking lot expansion construction on the north side of the District office is being funded with monies budgeted for the current fiscal year. The District's contractor working on the La Cholla road project, Select Development, is the same contractor that was awarded the contract for road improvements on La Cañada from River to Ina. Select Development will also be constructing the new driveway entrance for the District office as a part of the road improvement construction, so we approached them about doing the additional work to expand the parking lot. The Board awarded a change order to an existing contract, La Cholla, to accomplish the expansion.

Ms. Strom asked if the District uses boiler plate language regarding change orders when requests for proposals are put out for bid. She would like the FOC to receive a copy of that to review it. She is hearing there may be some angst with the Board about approving this kind of action. She asked if this approach was done because of the time frame. Mr. Maish said typically change orders are done for smaller increases in the range of 2-5%. Mr. Stratton said standard practice has been that the Board approves the construction bids granting the General Manager authority to approve changes up to a certain amount in the motion and when changes exceed that authorized

amount, they must go back to the Board for consideration and approval. Ms. Strom requested a copy of just the boiler plate language regarding change orders.

Mr. Ratje asked how much the additional work will cost at Lulu Walker, planned as a change order to the Riverside Transmission Main contract. Mr. Maish said the awarded contract was \$140,000 and the modifications to the distribution line will be in the \$25,000 range.

III. Discussion and Direction for Draft Fiscal Year 2012-2013 Budget.

Mr. Tenney said the memo was provided to give the FOC an overview on the budget. In his opinion, this is the toughest budget staff has ever had to draft. There are a number of issues hitting all at once but the biggest issue is revenue. Water consumption is down throughout Arizona, which is good from a water conservation perspective, but the District still has to maintain the pipes, well sites, and staff regardless of how much water is flowing through the system. In addition, the District did not have a rate increase last year for the first time since 1998. Some operating costs are increasing based on inflation, such as parts and materials. Other costs are increasing for other reasons, including health insurance costs, increased utilization of CAP, electricity rates, and regulatory fees. The few projects under construction right now were expected to cost less when they were envisioned a year or two ago, such as the Old Magee Trail well, which is coming in \$300,000 higher than estimated. The agreement with Omni Tucson National to build a reclaim line requires Pima County to pay \$500,000 of the costs but the District has to pay initially and the County has 20 years to repay the District. The District is exploring other ways to fund the reclaim line to avoid having to set aside those monies but that is included in the budget until that can be worked out. Mr. Tenney feels the District is doing a good job of determining “needs” versus “wants” but there are some needs that cannot be funded.

Ms. Bowen asked if the reclaim line would eventually result in a reduction of water use. Mr. Stratton said it would not because the entity benefitting, Omni Tucson National, is not currently a customer. Mr. Maish noted that Pima Community College’s and the park’s reclaim usage would represent a slight future reduction.

Mr. Guillot asked if the Old Magee Trail well overage of \$300,000 could be paid through the RTA fee funds. Mr. Tenney said it could not because the RTA fee is not covering the new well. Mr. Stratton also explained the new well site is larger than Matter Well, with a block wall and landscaping. In addition, the electrical panel at Matter well was marginally meeting code, so the new electrical is costing more because it meets the newer standards.

Mr. Ratje asked if the Board feels any pressure to reexamine the RTA fee and possibly roll it into established rates when it is time to terminate it. Mr. Stratton said the RTA fee pays for the debt service of bonds, so when the revenue source ends the expenditure will have also ended.

Mr. Ratje asked about declining water sales. Mr. Land said it has been difficult to define the correlation between the economy and water use. Mr. Tenney said the District is seeing the decrease continue this fiscal year, as it has over the last 5 years. The average decrease in the

District is 1.7% but some areas are seeing as much as 6% decline. Mr. Ratje said while he understands that a rate increase is the standard way to address declining revenues, he is concerned that raising rates when people using less water removes some of the incentive for customers who want to use less water in order to have lower bills. Mr. Tenney said that concept is something staff has wrestled with too, because customers wonder why their bill is not costing less if they are using less water. Two years ago when the last rate increase was passed the District did adjust the base rate somewhat to try to capture more of the actual costs needed to run the utility. Many utilities made the mistake over the last 15-20 years of trying to have a low base rate and higher commodity rate because it was overlooked that whether there are a million gallons or two million gallons going through the system, the utilities still must maintain pipes, well sites, and operating costs. This is why the District is moving towards a higher base rate but that can be difficult to explain to the general public. Ms. Bowen asked if the base rate is included in metered water sales on the draft budget, and Mr. Land confirmed.

Ms. Strom said meter reads drive the billing and she wondered if there are internal controls like spot checks done through the billing process to ensure customers are accurately billed. Mr. Hill confirmed and explained the planned meter replacements will provide an opportunity to operate more efficiently. Mr. Land noted that sewer rates have gone up substantially in the past few years and this is probably causing customers to try to use less, especially during the winter months when sewer calculations are done.

Mr. Ratje asked if the contingency for sick leave is a new thing. Mr. Land said the sick leave policy has been in place for several years but staff is now recognizing the need to have actual monies set aside to pay out soon. Mr. Ratje asked if the auditors have required a plan to fund the payouts. Mr. Land explained the auditors have been expensing this every year but the District has not been setting aside actual cash. Mr. Stratton said he had a conversation with the Board on this issue and they would like to look at the policy closer. There will probably be changes impacting the bottom line but right now the current situation needs to be addressed. He said the Board has indicated they will be looking at this in the next fiscal year. Ms. Bowen asked if the sick leave monies would be included in the salaries and benefits line item or another area. Mr. Tenney said it would be better to set aside \$244,000 in a separate contingency specifically for the imminent pay outs starting next year. Ms. Bowen wanted to make sure that quarter million covers all employees expected to retire in the next two years. Ms. Strom asked if the Board is looking at changing that benefit over time. Mr. Stratton said the Board has asked him to take a closer look at the policy but some current employees have been counting on that as part of their retirement. Mr. Stratton, Mr. Maish, and Mr. Land are among those who will retire soon. Over the years, there have been changes to the Arizona Retirement System that have affected participants too, but there has been an effort to make those changes gradual.

Mr. Stratton said a wave of retirements is expected to impact the District soon and the majority of those leaving will be from the higher levels. Staff is looking at the value of attrition and training, knowing some benefit can be realized by promoting from within but experienced people from outside can be hired if necessary. Some positions will be replaced at entry level rates rather than top level rates, so there will be some savings.

Mr. Ratje asked what would happen if the District ever came up negative. Mr. Land said the District needs to balance its budget to be able to operate. Several projects have drained the cash flow and some reimbursements are going to come back but cash on hand today is extremely low. Mr. Stratton said the District is somewhat like a fire or school district but instead of tax income, Metro Water relies on meter sales. The District cannot have a negative balance and has the authority to assess tax levies in order to keep operating, although it is doubtful the Board would ever decide to. Mr. Ratje wanted to be clear that he is not advocating such a move but wondered what could happen in a worst case scenario. Mr. Stratton said if the District was ever considered to be insolvent, the Pima County Board of Supervisors would take over the District and levy a tax to operate it. The Board definitely has an obligation to operate the District in the black.

Ms. Strom said from her perspective, the current drain on District resources is due to accelerated RTA progress. Keeping up with their changing schedule has a huge impact on balancing the budget. Mr. Stratton said when the RTA projects were originally pitched, costs for utility relocations were included in the figures. Before the 2006 election, the plan was modified to remove utility relocation work to make the proposal appear more attractive to voters and get a positive vote. More projects were added or modified later within our service area that caused the District to utilize all staff resources and all monetary resources to accommodate their schedule. Mr. Land said the debt service reserve has two more years before it reaches maximum funding.

Mr. Ratje asked if the purchased power line item in the budget includes interruptible rates and Mr. Hill confirmed, noting he is working to get more sites on interruptible rates eventually.

Mr. Tenney said the increase in salaries is mainly because there is now a full year reflected in the positions of Customer Service Supervisor and Civil Engineering Assistant. Also reflected, is a slight increase for a Customer Service Field person, and slight increases for CDL license holders because it is becoming difficult to make sure CDL licenses are carried. Staff is recommending a 2% Cost of Living Adjustment (COLA) to try to retain staff. The consumer price index shows a 2.9% increase, so the 2% is lower than that, totaling \$74,000 in the budget. Mr. Land noted health insurance costs have gone up. The prior provider's premiums went up considerably, so switching back to Blue Cross Blue Shield has resulted in less of an increase. ASRS retirement contributions are going back to 50%-50% from the current proportion of 47%-53%. Ms. Bowen asked if the employees will be reimbursed for that 3%. Mr. Stratton said the ASRS has not responded to our inquiries on how they will reconcile or balance.

Ms. Strom read in the Board meeting minutes about a contractual study to measure efficiencies of staff but she does not remember hearing about this. Mr. Stratton said the discovery of staff processes was hired to see what improvements could be made. The discovery report included recommendations to increase efficiency in a number of areas using the existing IT infrastructure and making software adjustments. Ms. Strom asked if the report could be provided to the FOC. She asked what kinds of findings were discovered, and if it was discovered in the report that if employees are "siloed" and not cross-trained, their longevity has no lasting benefit. Mr. Stratton confirmed and explained sharing the work product with others through IT processes was a large

part of the discussion. In the past, the District has done some cross-training. Ms. Strom asked if the report includes giving field staff devices such as handhelds or iPads. Mr. Stratton said some of the recommendations would require the ability to download from the field, as opposed to driving back and forth between the field and the office. One problem that was discovered was three people inputting the same data into three different databases. The low hanging fruit was identified with varying costs but nothing is included in the budget right now, until we know where we are. Mr. Stratton would like to see it implemented over a 2 year timeframe, starting with \$100,000 this year. At this point, even a portion of the funding would be helpful but this proposal is one of the sacrificial lambs in the budget.

Mr. Ratje asked Mr. Stratton if he had to make a cut somewhere, where would it be. Mr. Stratton said he would not completely cut any one item but he would reduce a few. He cited an example of well maintenance; maintenance for six wells is in the budget and the District could choose 3 or 4 to fund. The problem is delaying things now makes it hard for the District to play catch-up later. CAP water purchases could be cut a little but not too much because he does not want to end up with an obligation to owe the CAGR. Many small adjustments cumulatively could make a dent in the bottom line. Ms. Bowen asked if well maintenance had not been delayed for several years already. Mr. Tenney said when the rates were increased two years ago, one of the main reasons given was the need to start increasing maintenance. Well maintenance was put aside 3 or 4 years ago, when the District really had to cut back to deal with the initial challenges of the recession and relocations. Over the last year, it was decided it was time to ramp it back up.

Mr. Ratje asked when would be a time to dip into the \$500,000 emergency fund. Mr. Stratton said the Board would only consider using those funds late in the fiscal year, if funding was short for something the District really needed. Mr. Ratje asked if it would be appropriate to fund the \$140,000 Riverside Transmission Main project and related work at Lulu Walker from the emergency fund. Mr. Stratton said that work started this fiscal year and the transmission main portion is funded through the current budget but if the construction is not complete by the end of the fiscal year, the Lulu Walker portion could potentially come out of the emergency funds. Mr. Ratje said it might be a good idea to think of alternatives to using operating funds.

Ms. Bowen asked if the capital program is in line with original assumptions. Mr. Tenney said some projects have been pushed back due to the biggest challenge of funding. One area the District needs to keep moving on is CAP utilization because as was explained last month, doing nothing and relying on groundwater still costs money. Some options are more expensive or harder to implement than others but it is important to keep incrementally moving forward.

Ms. Strom asked if the contractors the District is dealing can be required to use Metro Water if their project is occurring in our service area. Mr. Stratton said our projects must use our water but others do not have to. Even if they were required to, it would not have a huge impact.

Ms. Strom thanked staff for all of their work and said the narrative was especially helpful. She asked if anything has been prepared for a proposed rate increase yet. Mr. Tenney said staff has

not yet put any rate increase scenarios together but will soon. Mr. Stratton said once the Board provides direction on how much revenue is needed, staff can start developing scenarios.

Ms. Bowen asked if the District has given any thought to implementing fees to pay specifically for certain items, like what Oro Valley has done. Mr. Stratton said Oro Valley has become innovative with fees for certain purposes but since the District already has the RTA fee, it might be hard to add on another fee. The idea is not out of the question and he would be happy to suggest it to the Board. Ms. Bowen said it might be easier for the ratepayer to understand why they are paying more and gain an understanding of the needs of the District. Mr. Stratton said it is sometimes harder for the District, being a stand-alone utility and not having some of the benefits of a municipality. On the other hand, the District can create its budget focusing on water issues without worrying about town issues.

Mr. Stevenson asked if staff sees a light at end of the tunnel with projects. Mr. Maish said we are almost there now with County road projects. The Orange Grove improvements are the only big portions not yet addressed. If the County builds that, it will be a four-lane divided roadway but so far they have not moved on it.

Mr. Stratton said the next Board study session is April 30, 2012 at 5:30 p.m. If there are specific comments from the FOC they will be passed on to the Board. The FOC are invited to attend and the Board would appreciate any direct input as well. Mr. Ratje thanked staff for their work and encouraged FOC members to look at the draft budget again, in light of the conversation. If any FOC members have comments for the Board of Directors, they can be emailed to Tullie Noltin.

IV. Future Meeting Dates; Future Agenda Items.

Mr. Tenney said the Board will be holding a Study Session on the budget on April 30, 2012, and FOC members are welcome but not required to attend. The next regular Board meeting date is May 14, 2012. The next FOC meeting is scheduled for May 21, 2012. He is not certain where the budget will be at that point. Mr. Stratton said if the Board is satisfied with the budget in May, staff could educate the FOC with a presentation of some sort. Ms. Bowen said one of the things she is interested in is the status of the original capital improvement program.

V. Adjournment.

Mr. Ratje made a motion to adjourn. The meeting adjourned at 5:09 p.m.

Jeffrey Ratje, Chair
Finance Oversight Committee