

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

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

August 19, 2013

MINUTES

Committee Members Present: Jeffrey Ratje, Chair
Sheila Bowen, Member
Jennifer Dussor, Member
Reb Guillot, Member
Lee Mayes, Member
Jim Stevenson, Member

Committee Members Not Present: Tim Thomure, Vice Chair

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

I. Call to Order and Roll Call

Mr. Guillot called the Metropolitan Domestic Water Improvement District Finance Oversight Committee (Committee, FOC) meeting to order at 4:00 p.m. Ms. Bowen, Ms. Dussor, Mr. Guillot, Mr. Mayes, and Mr. Stevenson were present. Mr. Ratje arrived at 4:14 p.m. Mr. Thomure was not present.

II. Approval of Minutes – April 15, 2013 Meeting and May 20, 2013 Meeting

Mr. Mayes made a motion to approve the minutes. Mr. Stevenson seconded the motion. Motion passed unanimously.

III. Status of Capital Improvement Projects and County Road Projects

Mr. Maish said the only ongoing capital improvement projects both involve wells. Riverside Well construction has been under way for quite awhile and is nearing completion. Construction began at Hub 1A Well last month and work is proceeding underground. A block wall enclosure is being constructed around the well site. Project bids on that job were well under the engineer's estimate in the area of electrical costs but the general contractor indicated they could still do the

work. When work got started, the electrical subcontractor pulled out so they are trying to find another and the project has been delayed substantially. Mr. Mayes asked if there is any possibility the contractor could come back and say they could not find another subcontractor. Mr. Maish said they are expected to find a replacement but the contractor is doing as much as he can under his license in the meantime. Ms. Dussor asked if this contract is exclusive to the District and Mr. Maish confirmed.

Mr. Maish said the District is still dealing with County contractors on the road projects to make sure all valve issues are addressed. There are a few difficulties and the County is being supportive but their response has not been timely.

IV. 2013 Water Rates & Revenue Analysis

Mr. Tenney summarized the analysis, which is a follow up to what was done last year. This year's finances look better, primarily because the Board took two critical actions to implement a rate increase to the Water Availability Rate (base rate), establish a Water Resources Utilization Fee, and refinance and restructure the District's debt. The Board's action, supported by the FOC, helped reduce some of the pressure. The analysis shows several projections with various rate increases and also no rate increase. Water consumption is on the decline and a 2.1% decrease annually was used in the projections. That is the primary reason the District could within a few years find itself in the red. There is a need to focus on ensuring revenues will cover the fixed costs through the water availability rate rather than the tiered consumption rates.

Mr. Ratje arrived at 4:14 p.m.

The majority of expenditures are tied to fixed costs. Another area of concern is CAP increases, which have historically added 5% each year but this year increased by 15% increase. The uncertainties CAP is facing with increasing power costs and other issues could mean annual increases of more than 5% in future years. The District's power costs are increasing as well. The District is in a lot better situation than last year but we should continue to be proactive. Recognizing the uncertainties of the declining usage and the impact on the projections, it is better to be proactive and look at modest rate increases now, rather than have to go to customers in three years with a 10% or 12 % rate increase.

Ms. Dussor asked if the District has been able to identify specific communities experiencing similar trends and the range of their declines. Mr. Tenney said the information has been shared through conversations with others in the Phoenix and Tucson water communities. Tucson Water is keeping their financial forecast on a downward trend for at least the next five years. Metro Water, Tucson Water, Community Water of Green Valley, CAP, and ADWR are all helping to fund a study by Gary Woodard of Montgomery and Associates to look at why water usage is down in the Tucson and Phoenix areas. It is not known whether studies are being conducted in other arid regions. National publications have published articles about how lower consumption appears to be the new normal. Mr. Hill noted power industries are also seeing similar trends. Ms. Dussor asked if water community discussions include whether reclaimed water programs play a

role in declining usage. Mr. Tenney was uncertain but said reclaimed water is primarily available to large businesses. Mr. Land said early results of the study are showing that when investors “flip” homes, they are pulling out old irrigation systems and replacing appliances and fixtures to make the homes more attractive to buyers who want to conserve water. Mr. Tenney talked about the impact on water consumption of the recent increases to sewer fees that the District collects on Pima County’s behalf. Wastewater is seeing an impact on sewer flows and revenues as well. Mr. Tenney noted that increases to upper tiers sometimes have an effect on demand and when Tucson Water increased their higher tiers, people reduced their usage so that nobody was in the highest tier anymore and Tucson Water removed it. If you are counting on that revenue, it can be a challenge.

Mr. Ratje expressed concern about rate increases driving demand downward and customers wanting to conserve more because the water costs more. That could place the District in a worse situation and force consumption declines into a faster pace. Mr. Block said that has been discussed in the Ad Hoc Committee for Dr. Woodard’s study but he believes price is not the sole factor. There is speculation that the situation is temporary and once the majority of homes have low flow fixtures, the trend will perhaps curb itself.

Mr. Guillot supports making the Water Availability Rate higher to cover more of the fixed costs. If the District encourages people to conserve but we charge more when water usage goes down, people will start to complain. If we can increase the Water Availability Rate and keep some people on the higher tiers, maybe we will be getting a good compromise that could last awhile and satisfy the concerns of customers.

Mr. Stevenson asked the difference between the Water Availability Rate and the Water Resources Utilization Fee. Mr. Tenney explained the Water Availability Rate is the base rate and the Water Resources Utilization Fee is the 10 cents charged per thousand gallons of water specifically for CAP and effluent projects.

V. Discussion and Recommendation Regarding Rate Adjustment Scenarios

Mr. Tenney went over the various scenarios in the report. Based on comments from the FOC last year, \$1 million in capital projects are factored into the projections. Staff has described a few recommendations that include various rate adjustments and also increases to the Water Resources Utilization Fee because it is important to have monies there for programs related to utilizing CAP water.

Ms. Bowen asked about the 6% scenario. Mr. Tenney explained the first 4% of revenue would come from an increase to the Water Availability Rate and the other 2% would be spread across the three highest tiers, so we could count on the 4% more than the 2%. The 3% scenario and 4% scenario would increase only the Water Availability Rate so the increase would not be subject to future declines in consumption. Mr. Land confirmed.

Mr. Ratje asked if less than a 3% could be considered. Mr. Tenney said less than 3% only carried through 2015-16 before falling short. One thought among staff was that it might be advantageous to go for a larger increase now and reassess next year, rather than have to catch up later. Several small increases would have a compounding effect on revenue assuming the decline in usage starts to taper. Mr. Ratje asked if consumption turns out to be the opposite, would the District consider lowering rates. Mr. Tenney said knowing what the District is dealing with regarding the CAP Utilization and until some of the debt retirements are complete in 2020, it might be prudent to consider not having annual rate increases or lesser amounts but he could not see the District lowering rates. Mr. Ratje said budgets have a way of expanding to fill in the gaps when revenues come in better than expected, and compared the situation with a ratchet only going one way. Mr. Tenney said it will be important for the FOC and Board and staff to continue to look at ways to reduce expenditures and remain vigilant even as things change. Everyone realizes the District cannot revert back to the hay days of the late 1990s.

Ms. Bowen asked how unfunded capital projects will be addressed in the future. Mr. Tenney said Mark Stratton, General Manager, has asked District staff to update the Water Resources Management Plan to see what is needed today, rather than continue to rely on the plan from 1994. Right now there is not a plan to set up a new capital improvement program but there have been discussions about setting money aside to be in a position to fund things as we go. There is also the possibility of going out for a revenue bond for larger needs like CAP Utilization. Mr. Hill said many maintenance projects and operations have been deferred and staff is focused on mission critical work. There is going to be some catch up with that and the District cannot defer things forever.

Ms. Dussor expressed a desire to clearly define capital needs and establish priorities so that we can approach projects from a disciplined perspective when extra money becomes available. Other FOC members agreed. Ms. Dussor asked if it is understood where the 2.1% decline occurs across the tiers. Mr. Land said the decline is spread pretty evenly among the lower residential tiers. There was a discussion about how conservation is easier for higher users. Those in the highest tiers are more likely to have the financial means to deal with extra cost but also have the ability to reduce usage faster. Mr. Land said there have been Board discussions in the past about protecting the low end users so the Board might consider adjusting the first tier to 6,000 to reduce the impact of the increase.

Mr. Guillot asked if the District has seen a change in the amount of bad debt. Mr. Land said yes, the bad debt used to be about \$10,000 on water sales and now it is about \$25,000 on \$15 million of water sales. Mr. Guillot said he is inclined to go with a higher scenario but he likes the idea of not spending money just because we have it. Later the District may be able to coast without any increases or do a slight decrease but he likes the idea of bringing the Water Availability Rate higher to cover fixed costs.

Mr. Tenney noted in addition to adjusting the rate structure, the report also looks at increasing the Water Resources Utilization Fee with a 10 percent annual increase November of each year. Funds generated from that fee would be a good start for CAP Utilization. Each 10 cent increase

per thousand gallons would mean an additional \$1.00 for the average customer who uses 10,000 per month. Combined with the lowest 3% scenario, this would mean a \$3.00 increase per month. Last year, the increases were \$3.50 combined. That was a recommendation this Committee was supportive of last year. Ms. Bowen asked if the District has identified the overall capital need for that program. Mr. Tenney said the District was in the middle of a study by HDR trying to finalize the costs. It could be \$25 to \$40 million, dependant on route selection and other things.

Ms. Bowen asked if the District participates in any low income programs like the County does. Mr. Land said we had once considered piggy backing on the County's program. Ms. Bowen wonders if it would help lower the default rate. Mr. Land said the District does prompt people to call certain charitable agencies that help people with their utility bills.

Mr. Ratje asked if the District has ever considered other ideas to generate revenue, such as charging to include leaflets with our bills. Mr. Land said the District did establish the fire protection fee. Mr. Hill explained the District began charging buildings that had fire riser systems because it costs money to make sure water is available to those systems. Mr. Land said staff also considers the amount we charge Pima County to include their sewer fees on our bill and collect them. Development fees are increasing at Metro Southwest now. About a dozen people have purchased dual meters, as well.

Mr. Ratje asked if users would be able to discontinue use of District service and start their own wells. Mr. Tenney said state laws prohibit doing so within established service areas of a designated provider. The law was passed to make certain all property owners have the benefit of a secure water supply.

Ms. Bowen asked if there are any pending water quality regulations that could add costs. Mr. Hill said the possibility is always there but he does not see it in the near future. She asked if required debt service ratios are maintained under these scenarios, and Mr. Land said yes.

Mr. Guillot made a motion that the Finance Oversight Committee recommends to the Board of Directors that the Board schedule a public hearing to discuss a rate adjustment based on the 6% scenario and a 10 cent increase to the Water Resources Utilization Fee. Ms. Dussor seconded the motion.

Mr. Ratje said he is uncomfortable with the 6% because combining the 10 cent increase of the Water Resources Utilization fee and the adjustments to the Water Availability Rate brings the increase to a minimum of \$3.00 per month for the average customer. Mr. Ratje said he is a little more comfortable with 4% and 10 cents for the future CAP Utilization program, which is really important. He asked if the District has had increases every year and Mr. Tenney said there was an increase every year except 2011 over the last several. The last increase to the base rate marked a shift towards less emphasis on the percentage and more on the dollar amount. Mr. Ratje said the District would be better off not trying to hit the highest water users because they are already paying more per unit. Just as a university wants out of state students who pay higher tuition, we

do not want to ostracize those folks because they use more and then have to charge more to everybody when the high users conserve. Mr. Mayes agreed.

Motion failed, with Ms. Dussor, Mr. Guillot, and Mr. Stevenson voting in favor; Ms. Bowen, Mr. Mayes, and Mr. Ratje opposed.

Ms. Dussor asked about the socio-economic differences between the tier 1 and tier 2 customers. Mr. Tenney said that is hard to determine because other water providers who have implemented low income programs have found that low income customers are not necessarily low water users. Some low water users are retired folks with one or two individuals living in the home but there are also large families in the first two tiers. Usage varies with the age of the house, landscaping and seasons. Mr. Guillot said he uses volumes in the 2nd or 3rd tier in winter and the 5th tier in summer. Mr. Land said the District has some customers who are struggling to pay their bills but using lots of water.

Ms. Bowen made a motion that the Finance Oversight Committee recommends to the Board of Directors that the Board schedule a public hearing to discuss a rate adjustment based on the 4% scenario and a 10 cent increase to the Water Resources Utilization Fee. Mr. Ratje seconded the motion.

Ms. Dussor said sending a split recommendation to the Board is still valuable information. Mr. Mayes said everyone seems to agree there is a need for some sort of increase.

Motion failed, with Ms. Bowen, Mr. Mayes, and Mr. Ratje voting in favor; Ms. Dussor, Mr. Guillot, and Mr. Stevenson opposed.

It was summarized that the Committee members were supportive of a \$2.00 increase to the Water Availability rate and a 10 cent increase to the Water Resources Utilization Fee.

Mr. Ratje said the only other thing the FOC has not specifically put into the recommendation is a common desire to see that all needs to be very well-defined and the District should be guided by a disciplined approach when spending any additional funds that might be generated on capital improvements. If more revenue is generated than is budgeted, we want to make sure we do not spend more and then do not create an opportunity for more rate increases.

Mr. Ratje said this is his last FOC meeting. He has taken another job at the University of Arizona but will still be drinking Metro Water. The Committee and staff thanked him for his service.

VI. Call to the Public

Ingrid Saber, who resides at 6322 N. Barcelona Lane #157, Tucson, Arizona, 85704 asked if staff is concerned about being able to provide for the future, considering everything. She wonders if the District will be able to supply enough water to everyone. Mr. Tenney said the

District is constantly looking ahead to make certain we are prepared. The District wants to bring CAP water to the service area and this is something we are planning for.

Ms. Saber said her sewer bill is now greater than her water bill and there seems to be a gross waste of water on the grounds where she lives. She asked if there is a formula or ratio used to figure out the sewer charge and whether there is a different calculation for private golf courses where the water use is obviously being used to water the greens and is not flowing into the sewer. Mr. Tenney said for residential customers, Pima County uses a formula based on what is typically the lowest indoor water use months: December, January and February. Mr. Land said golf courses have dedicated irrigation meters and dual metering is available to residential customers as well. Ms. Saber said she would follow up on that. Tim Dinkel is the contact person for dual metering.

Ms. Saber wanted to thank Mark Stratton for the information about the conference he attended but she believes the trip was extracurricular in every sense. She thinks it had nothing to do with seeing that this body functions properly, was a fundraising event outside the purview of this entity, and should be paid for by those who participate in it and those who wish to support it.

VII. Adjournment

The next FOC meeting will be held on Monday, September 16, 2013. Mr. Mayes said he will not be able to attend the September meeting.

The meeting adjourned at 5:30 p.m.