

**BOARD OF DIRECTORS
METROPOLITAN DOMESTIC WATER IMPROVEMENT DISTRICT
PIMA COUNTY, ARIZONA**

January 25, 2010

**** Board Room ****

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

MINUTES

Board Members Present: Jim Doyle, Chair
James Tripp, Vice Chair
Bryan Foulk, Member
Reb Guillot, Member
Dan M. Offret, Member

District Staff: Mark R. Stratton, General Manager
Michael McNulty, Legal Counsel
Warren Tenney, Clerk of the Board
Tullie Noltin, Recorder

Regular Session

I. Call to Order and Roll Call

Jim Tripp, Vice Chair of the Board of Directors of the Metropolitan Domestic Water Improvement District (District), called the Board Meeting to order at 5:31 p.m. James Tripp, Bryan Foulk, Reb Guillot, and Dan M. Offret were present. Jim Doyle was not yet present.

II. General Comments from the Public

There were no comments from the public.

III. Status of Northwest Central Arizona Project Water Treatment and Delivery System

Mr. Stratton said the Board of Directors held a study session update on Northwest Central Arizona Project (NW CAP) a year ago. The study session covered treatment, delivery system and reliability for the NW CAP system. Warren Tenney, Assistant General Manager, provided a detailed background report on those three aspects. The Board has been kept apprised of the recent development on system reliability. If the NW Providers continue to pursue a treatment plant, bypassing the CAP pumping stations has been considered an alternative to the reliability

reservoir. The Bureau of Reclamation is estimating the bypass alternative to cost \$18.5 million with the final numbers expected in February.

Mr. Stratton said Tim Thomure of HDR would give a presentation to the Board on treatment options and costs with comparisons to the options in the Carollo report. Mr. Thomure gave a brief Power Point presentation titled “Northwest CAP Implementation Update: Treatment Options and Costs” and a hard copy was provided to the Board Members. He pointed out the data in the cost study is based on actual Metro Water data. The presentation reviewed the option of recharge and recovery as a treatment method rather than a treatment plant. The presentation gave a scenario of how recharge and recovery would be done for the District and looked at projected costs. The capital costs for recharge and recovery are significantly less than slow sand filtration, microfiltration, or conventional filtration.

Mr. Foulk asked about the time frame between phase one and the final build-out. Mr. Stratton said conceptually it is five years but he said timing is dependent on technology advances. Whatever the treatment method, the District would still want to eventually pursue reverse osmosis as a second treatment. The biggest issue with reverse osmosis is brine concentrate disposal, which costs as much or more than the treatment itself. The goal is to reduce the volume or find alternative uses for the brine waste. Evaporation ponds and other energy-intensive methods are costly and research is underway to improve the methods. If the District blends half its supply, that would mean a significant groundwater level decline. Well fields could be better managed and it would allow some rebounding of the aquifer in those areas where the most depletion has occurred. The Oro Valley Utility is looking into the same thing, so the impact on the Canyon Del Oro basin aquifer should be substantially minimized.

Mr. Foulk asked what the customers might think of the taste and odor of blended water. Mr. Tenney said blending is different from direct delivery. Tucson Water blends with groundwater the recovered water it has recharged. They have done taste tests and people did not notice much of a difference between groundwater and blended water. Odor and taste issues are much less under the blending scenario versus direct delivery. Mr. Tenney said the District learned from Tucson Water’s experience that gradual introduction is better. Mr. Stratton agreed that regardless of the treatment process, a slow introduction is beneficial and the District will make sure the system remains stabilized and quality is preserved. Chris Hill, Deputy General Manager, said customer satisfaction is one of the most important things to keep in mind. He said in addition to being sure regulatory aspects are considered, the District also takes steps to maintain the level of aesthetic quality customers are used to. Mr. Thomure added that included in the cost estimate for recharge and recovery is a provision for whatever water conditioning is necessary to ensure the water is compatible when it enters the main system.

Mr. Thomure said the premise for the HDR study was that Avra Valley Recharge Project would be acquired from the Central Arizona Water Conservation District (CAWCD). There is enough capacity at the facility to accommodate Metro Water District's full allocation. There is currently no recovery there, and the purpose of the study was to identify how much it would cost to add recovery. Recharge and recovery technology has been in use for over 50 years as a treatment technology and a reliability feature.

Jim Doyle arrived at 5:54 pm.

Mr. Stratton discussed possible scenarios for developing a recharge and recovery site in the Marana area, which could benefit all NW Providers and not just the District. Mr. Stratton said the Board was also provided with an article from the Arizona Daily Star with interviews from water professionals from our region about the long-term availability of CAP, in the wake of the announcement that there could be a shortage declaration on the Colorado River as soon as 2012. Mr. Stratton's concern with trying to secure financing to build a CAP treatment plant may be a difficult idea to sell when there are articles in the paper about long-term river water shortages and droughts. A system with a built-in reliability feature, especially if storing water, acts as a bank account of stored water that the District can continue to pump. Recovery could be done for a number of years. The investment in infrastructure would provide a little more flexibility in meeting long-term needs if in fact shortages on the river actually occur.

Mr. Offret asked if there are any anticipated environmental concerns with the aquifer or soil conditions. Mr. Stratton said long-term testing on water quality has been looked at for many years. New substances are continually being regulated. Mr. Hill added pharmaceuticals and personal care products are an increasing area of the public interest, and the technology to detect trace amounts advances rapidly so regulatory standards are always changing.

Mr. Stratton said it would be ideal if the NW Providers do continue to pursue the same treatment option. Flowing Wells Irrigation District has some concerns with the O&M costs but the HDR study shows O&M costs to be equivalent with the other treatment options. Power costs are projected to rise substantially so other options like solar power could be alternatives. Capital projections for building a new recharge-recovery facility are still far less than building a treatment plant.

Mr. Offret asked where the other partners would recharge. Mr. Stratton said they would recharge in the same location. Realistically they would not need to build a full facility there because they could still utilize the Lower Santa Cruz Recharge Facility. A recovery well field could be developed in conjunction with the partners for everybody to share.

Mr. Tenney said staff has been working with the other NW Providers to draft an Intergovernmental Agreement (IGA). The treatment method system has not been decided on but the four partners are trying to make sure the IGA is flexible enough to work for either system. Mr. Stratton said he would like to have a recommendation on treatment method to the Board within a six-month period. By that time staff would like to know whether a new recharge facility is needed. If land is to be acquired and it is state land, typically negotiations will take at least a year.

Mr. Stratton said there is also a potential impact to reliability if recharge and recovery is pursued. The District would need to have discussions with CAP and Bureau of Reclamation. Reliability for recharge and recovery would be similar to the type of reliability Tucson Water may want, which would allow for a more unified voice in the region on reliability.

IV. Overview of Draft Financial Plan

Mr. Stratton said after having completed the three financial closings at the end of December, it became apparent staff needed to review the District's long-range financial plan. Two alternatives were provided to the Board in the report. The first is a do-nothing approach with no rate increases. Under that scenario, the District would encounter severe hardship and would be \$12 million in the hole within ten years. The other alternative proposes an annual 4% rate increase. Mr. Stratton said that Mike Land, Chief Financial Officer, made some assumptions that have some bearing on the numbers. Neither alternative includes capital projects, nor could they finance the NW CAP treatment and delivery system. Both alternatives assume the original CAP allocation, not the full amount. There are some unfunded capital projects that need to be done in association with the next phase of the La Cañada roadway. Mr. Land did include expenditure increases protected at a conservative 3%. Capital equipment and vehicles were kept at \$200,000 per year. The three RTA projects in 2011 solidify the need to keep the RTA fee in place to reimburse the District for costs associated with those water line relocations. When the 4% rate increase is considered, the real difficulty lies in the next two to three years. After three years, the reserve fund starts looking better. There will be a need for some revenue increases to meet the requirements. The O&M side of the budget has been very tight for the past two years, and sooner or later the District will be required to spend more on O&M that is currently unfunded.

Mr. Stratton said there are not many bond projects for the Bond Oversight Committee (BOC) to oversee now, yet they have a great deal of talent and have an understanding of finance and utility operations. Mr. Stratton proposed they serve as an Advisory Committee to the Board so that as the financial plan is developed, the Committee can give their input as to what would be acceptable to the general public before recommendations are made to the Board. He said the same process is used at both Tucson Water and Pima County Wastewater, where they have an

advisory committee that discusses the financial plan with staff before recommendations are brought to the Pima County Board of Supervisors. Mr. Stratton feels it is better to have many people involved in the process when dealing with finances; that way ideas can go through a public process in an advisory committee in addition to staff and Board of Directors.

Mr. Land said if there are no rate increases the District will be \$12.5 million in the hole in the year 2019. With a 4% standard increase every year, the District would have over \$15 million, a difference of over \$27 million over ten years. The figures show either a larger rate increase or change in the rate structure is necessary to have enough money for capital projects. Mr. Stratton said the debt service changes dramatically after about 2019. At that time the debt service for the 2002 bonds goes down from \$2 million to just over \$400,000 and the senior debt goes down from \$4.7 million to \$2.7 million. Those significant reductions in debt service will allow the District to regain strength. The District could use the extra \$2-3 million gained on additional debt for a CAP treatment system or capital improvement projects. Using future monies already in the budget to help pay for debt service so not having to raise rates to generate that income is the most appropriate way to keep rates stable.

Mr. Land added both financial plan versions include the Metro-Southwest service area. Mr. Land conservatively estimated the number of new connections in that service area. The County focus is for growth to occur in the area.

Mr. Offret said Oro Valley seems to be increasing their rates every year about 3.5%. He asked if the District has considered any other percentages, such as 3%. Mr. Stratton explained Oro Valley charges a “Groundwater Preservation Fee” which is viewed as a surcharge rather than part of their rates so they can increase their rates less. Marana is doing something similar. Oro Valley believes they have collected enough funds to move forward with the NW CAP System. Mr. Tenney said the options presented are not meant to be the only scenarios but a broad view. Mr. Stratton explained he wanted to keep it in a simple format to illustrate to the Board that if nothing is done the picture is bleak. Mr. Stratton does not want to see double digit rate increases, and feels it would be better to keep the percentages low and restructure the rates.

Mr. Stratton said the District still has the RTA fee of \$3 per month for the typical residential customer. Until we can figure out how much the next three RTA projects are going to cost the District, there is no way to estimate. The County has not provided Mr. Maish updates recently so staff is unable to determine how much water line will need to be moved. Mr. Guillot said it was implied that the RTA fee was for the first segment of the La Cañada road project and that the fee would go away. Mr. Stratton said at the time the fee was implemented, it was generally believed the other RTA projects would be spread out enough that another mechanism could be used later.

Mr. Guillot said the economic climate is not good. Mr. Stratton expressed the District cannot plan anything until the County provides the information.

Mr. Land said many customers complain of increases in their bill when the wastewater rates go up. The customer sometimes does not realize water and wastewater are separate. Mr. Guillot recalled some comments at the last Public Rate Hearing reinforcing that misconception. Mr. Stratton said the County is proposing to increase wastewater fees totaling about 19% at the end of each year, for the next four years. Mr. Guillot said he would like to see a newsletter article about the coming wastewater increases and emphasize it is the County, not the District, raising wastewater rates.

Mr. Foulk said Oro Valley has been raising rates but he understands Tucson Water has not. He asked whether the Northwest Partners' activities will keep rates rising at a faster pace than the City of Tucson. Mr. Stratton said Tucson Water had recently raised its rates. The Tucson City Council typically protects lower income residents and pushes to keep base rates low. Based on 180,000 connections, the Tucson Water base rate does not cover operations costs. Mr. Foulk is concerned about seeing articles in the paper about Tucson Water rates being considerably lower than surrounding areas. The news articles do not always seem fair and he does not want people to get the idea their rates would be lower if the City of Tucson took over. He does not want Metro Water to have the highest rates. Mr. Land mentioned over the 12,000 gallon threshold the comparison changes and Tucson Water rates become more expensive. Mr. Stratton said it is problematic to watch what the neighbors are doing versus paying attention to the District's needs. Basing rates on comparisons with other providers is an artificial way of looking at rates because it is not based on our specific reality. Mr. Stratton said that even with financing \$35-40 million for NW CAP, the debt can be end-loaded so the District will not have to raise rates to pay for that type of improvement and that sets the District in a good position long term.

Mr. Foulk said the District needs to raise money in various ways. He feels it is better to raise the base rate by a small percentage but also implement small fees for specific things. He feels it would be easier for the customer to understand and the end result is essentially the same.

Mr. Tenney said that if the Board is supportive of the concept of having the Bond Oversight Committee also serve in a financial advisory role, it would be introduced as an agenda item in February so the Board can officially restate their role. Mr. Thomure, who sits on that Committee, believes the members are more than willing to revise their role if the Board sees fit.

V. **Approval of Purchase Agreement for Avra Valley Recharge Project with the Central Arizona Water Conservation District**


Mr. Tripp made a motion to approve the Avra Valley Recharge Project Purchase Agreement between the Central Arizona Water Conservation District and Metropolitan Domestic Water Improvement District and that the Board Chair be authorized to sign the Agreement. Mr. Offret seconded the motion.

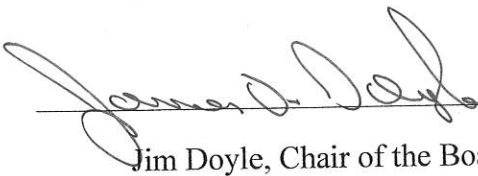
Mr. Stratton said a couple minor changes were made this morning by the attorneys, but nothing substantive. He wanted the Board to be aware the current version is slightly different than what was previously distributed. The District is just waiting to hear back from CAP attorneys that the changes were approved. There might be one or two changes still to come but in the event there are substantive changes, which at this point there should not be, the Agreement would have to come back to the Board.

Motion passed unanimously.

VI. Adjournment

Mr. Tripp made a motion to adjourn. Mr. Foulk seconded the motion. The meeting adjourned at 6:38 p.m.



Warren Tenney, Clerk of the Board

Jim Doyle, Chair of the Board