REGIONAL WASTEWATER RECLAMATION ADVISORY COMMITTEE
Transamerica Building
Pima Association of Governments' 5th Floor Conference Room
177 North Church Avenue
Thursday, January 21, 2010

Committee Members Present:

Jim Barry	Sheila Bowen	Corey Smith	Bill Katzel
Mark Stratton	Jeff Biggs	Mike Gritzuk	

Committee Members Absent:

Brad DeSpain	John Carlson	Barbee Hanson	Rob Kulakofsky
Armando Membrila	Ann Marie Wolf		

Staff Present:

Ed Curley	Eric Wieduwilt	Ron Meck	Melanie Seacat
Diana St. John	Laura Fairbanks	Lillian Von Rago	Lorraine Simon
Jeff Nichols	Mary Hamilton	Tom Burke	Kristen Borer
Jackson Jenkins	Gregg Hitt		
John Warner	Mike Kostrzewski	Charles Wesselhoft	

Guests:

Pat Cunningham
Claire Zucker, Pima Association of Governments

I. **CALL TO ORDER.** Chair Sheila Bowen called the meeting of the Regional Wastewater Reclamation Advisory Committee (RWRAC) to order at 7:51 a.m. A quorum was not met.

II. **CALL TO THE AUDIENCE.** There were no comments from the audience.

Bill Katzel asked to make a comment for the record before the Financial Plan discussion. He is disturbed by the memo dated January 19, 2010 from Chuck Huckelberry, Pima County Administrator (distributed to the Committee). He feels that it is a premature memo to the Pima County Board of Supervisors. It negates what the Committee is trying to do in an advisory capacity. Mr. Katzel feels that Mr. Huckelberry could have waited until the Committee made an official recommendation.

Jim Barry said that the last Committee meeting was on January 14, 2010. The memo is dated January 19, 2010. It is not premature: the Committee had already voted in favor of the Financial Plan (Plan).

Mr. Katzel said that there is a caveat in the memo that it is pending this Committee's recommendation.

Mr. Barry said that this Committee has already recommended the Plan.

Mark Stratton said that there will be a formal recommendation after the public meeting. The Committee agreed to set a public hearing for comment before a recommendation will be made.

Mr. Katzel said that he feels the memo preempts this Committee and the public input.

Mr. Barry said that he disagrees.

III. **DISCUSSION**

A. **Old Items/Updates.**

Financial Update – Financial Plan. Tom Burke, Director of Finance and Risk Management, gave an overview of the FY 2009/10 Financial Plan, referring to the PowerPoint presentation given at the January 14, 2010 meeting. $974 million is needed for improvements over the next eight to 10 years. $812 million is needed in the next for years. The Financial Plan provides an analysis to determine the necessary minimum rates. The Plan recommends the adoption of a four-year rate increase. This facilitates sewer revenue obligation sales over the next several years and the ability to tell lenders that there will be sufficient funds to complete the projects.

The main issue with the ability to raise $970 million is the ability to show the rating agencies and the lenders that there is sufficient cash flow to cover operating expenses, the debt service and the debt service coverage. Two slides show historical revenue. In the past, RWRD has charged rates to cover operating costs but not to cover debt service. RWRD has relied on connection fees to pay for debt service. Rating agencies and lenders consider this risky as connection fees are volatile.

Mr. Stratton said that when looking at development fees to pay for growth-related items, funding all debt service on growth is not necessarily an accurate depiction of what the State statues allow. Mr. Burke said that is correct. Currently $720 million of the current program is just existing facilities with no growth. The remaining balance is needed to meet the needs of existing facilities regardless of growth.

The second slide shows that RWRD has been covering cash needs for operating costs but not the depreciation. That is due to the County historically borrowing debt to cover capital improvements. Connection fees have been sufficient to cover the annual $20 million gap. Connection fees cannot cover the pending debt service of $970 million. Rates will need to be raised to cover the debt service. The next slides show the operating expenditure projections for the next five years. Based on the assumptions, the expenditures increase three to four percent each year. The largest increase in compensation relates to health insurance costs. The increases in operating expenses are related to electrical and chemical costs. These are relatively moderate increases.

Mr. Stratton said that he noticed an eight percent increase in health insurance. His employer saw a 20 percent increase. Mr. Burke said that the County is receiving insurance quotes now, but no decisions have been made yet.

Mr. Burke said the next slide shows the main concern for the rates is capital improvements totaling $812 million in the next four and one half years. The County will need to borrow almost $800 million. Figure 5 shows the annual debt service over the next 10 years. It has been expanded beyond the Financial Plan to show that in the next five years it increases $90 million per year. Shortly thereafter it rises to $127 million per year. Current debt service is $25 million. Debt service will increase by a factor of five.

Mr. Stratton said that, knowing the projection is 15 year notes, this equates to $100 million over the following eight or nine years. Mr. Burke said yes, it will drop down to approximately $90 million and maintain that for several years after the peak.

Mr. Barry asked if this is County-wide or just RWRD debt. Mr. Burke said it is just RWRD debt. Pima County currently has approximately $750 million in outstanding debt. $20 million of that is RWRD debt. By the completion of the Regional Optimization Master Plan (ROMP) and other treatment and conveyance projects, the County will have issued approximately $1 billion in RWRD debt.

Mr. Gritzuk asked if that was total County debt. Mr. Burke said that was just RWRD. The County itself has $400 million in General Obligation debt and has issued Certificates of Participation (COPs) for several buildings. There is no longer time to delay the expenditures that are being faced. Figure 6 shows the debt to be issued in the next several years: $165 million this year and next, $200 million for the following two years, and $67 million the next year. That will raise the necessary funds to pay for the projects that will be done by 2014. After that time there will be more debt, approximately $50 million to $80 million, depending on the projects.

Ms. Bowen said that previous discussions were held regarding why sewer obligation bonds were being pursued, which are less traditional than general obligation bonds. Mr. Burke said that historically, the county has issued two types of debt for sewer obligations. The most traditional is sewer revenue bonds. There were bond authorizations in 2004 and 1997. Last year the last of the available bonds were issued. The County has also borrowed $70 to $80 million from the Water Infrastructure Finance Authority (WIFA). As there was not a 2008 or 2009 bond authorization election, other funding mechanisms have been used to cover the lack of available bonds. In the last two fiscal years, the County has issued $84 million in COPs to cover the cash shortfall. $50 million has been already been repaid. That type of funding is not available for the current need. The County does not have any assets of that value.

Mr. Smith asked why the County did not aggressively pursue sewer obligation bonds for the debt to be incurred beyond 2010. Mr. Burke said that the Bond Advisory Committee recommended to not having a 2008 or 2009 election due to the economy. Mr. Smith said that, as a result of not pursuing sewer obligation bonds, WIFA funds cannot be sought. Lake Havasu, AZ recently received $400 million in WIFA funds at three and one half percent interest. The rates in the Plan are five and one half to six percent. The difference between three and one half and five and one half percent cuts the rate increase required over the next four years in half. It would be interesting to put this before voters in 2010. Otherwise, this completely circumvents voter authorization of the largest debt this County has even seen. Is there a reason why Mr. Huckelberry is opposed to that route? Mr. Burke said that he does not know what Mr. Huckelberry's position is on this. Mr. Smith asked if there was a reason why WIFA was not fully exhausted in the Financial Plan. Mr. Burke said that the Bond Advisory Committee recommended not having a bond election at the time the Financial Plan was being written so WIFA funds were not an available source of funds.

The five, five and one half and six percent projections are high projections as no one knows what interest rates will be in the future. There is also a five percent projection for COPs sales that are being sold today. As of last night bids are coming in at 3.17 percent. Mr. Burke expects that when the sewer revenue obligations are actually sold the interest rate will be four percent, which is lower than projected.

Mr. Smith asked if that the financial projections are overly conservative. Mr. Burke said that the projections are conservative on the interest rate calculations. There has been a decline in flow but no decline in flow is assumed in the Plan.

Mr. Smith asked what Mr. Burke felt the basis point differential between WIFA and COPs would be. Mr. Burke said that COPs are currently being sold at 3.17 percent and the last WIFA loan was 2.7 percent, therefore approximately 50 basis points.

Mr. Stratton said that normally WIFA is 85 percent of a standard revenue bond with a triple "A" rating would have. That equates to a 15 percent reduction in the interest rate by going through WIFA. He understands the need to obtain funding. Mr. Stratton can see obtaining the first $165 million using sewer bond obligations as a bridge until receiving voter authorization for sewer revenue bonds, and then obtaining a lower interest rate. As 2010 is an election year, the cost for holding an election would be significantly less. He feels that getting this amount of money without voter authorization is a bad move. He feels the voters should have a say in how this is financed. If the voters turn it down, the sewer bond obligations are still available.

Mr. Barry said that if the sewer revenue obligations are done now, then voter authorization is received for sewer revenue bonds, does that change the status of the sewer revenue bonds. Mr. Burke said that it does change. Sewer revenue bonds and WIFA loans have equal status as far as lien rights. The sewer revenue obligations sold would be junior to those due to covenants in the bonds and WIFA loans that require that no other debt be issued at the same parity. Subordinate debt can be issued, but WIFA and bond holders are paid first, then sewer bond obligations would be paid second. This would have to be disclosed in the official statement telling potential buyers that their position may become more inferior. This will raise the interest rates.

Mr. Gritzuk asked how much the interest rates would go up. Mr. Burke said that he did not know. Both of Pima County's financial advisors have taken the position is that Pima County should make the commitment that we will not issue superior debt.

Mr. Barry said that he feels that, from a political point of view, that November 2010 is a terrible time to go to the voters for sewer revenue bond authorization. If there is a commitment to go to the voters, then wait until 2012. November 2010 will be extremely volatile.

Mr. Stratton said that he agrees, but sewer revenue obligations should be a fall-back position until an election could be held. Circumventing voters is not a wise political move.

Mr. Barry said that taking an issue to voters that there is a better than not chance of losing is also not wise public policy either.

Mr. Stratton said that the message to the voters is "this has to be done one way or the other." It is only a matter of how it can be done with the least expense to the voters.

Mr. Barry said that, hypothetically, assume the voters say no. Has anything been gained by letting the voters say no?

Mr. Katzel said that is the voters right to say, “No.”

Mr. Barry asked if anything was gained by having the voters say, “No.” The goal is $800 million. Going to the voters in 2010 is, in his opinion, politically the wrong choice.

Ms. Bowen said this Committee is reviewing and approving the Financial Plan – the needs, the costs and the operation – not the funding mechanism.

Mr. Stratton said that he believes the Committee has an opportunity to comment on the funding mechanism.

Mr. Smith said that he has asked for the charter for the Committee. Found on the website from 2002 forward, “The WMAC is charges with the evaluation of the Department’s program and policy decisions as well as short term and long term capital and operating funding needs.” It talks about need. The Committee has defined the needs: $812 million. He feels that there are other committees in the County, namely the Bond Advisory Committee, that are in a better position to evaluate how this is funded.

Mr. Barry asked if the Financial Plan include the assumption that sewer revenue obligations will be used, and the rates are based on that. Mr. Burke said that was correct. Selling sewer revenue bonds was not an option at the time the Plan was written. If sewer revenue bonds were authorized, they would still be sold at five to five and one half percent as that is what the current analysis is for debt service for the County debt.

Mr. Smith said that written into the instruments that are sold are covenant restrictions and covenant ratios that rate increases will be put into effect to cover the need. This will be superior to what ever the Committee decides.

Mr. Barry said that if the Committee approves the Financial Plan, the Committee is saying that they agree that there is $800 million worth of needs, and this Plan is what is necessary to pay it. The Committee is not saying “how.”

Mr. Smith said the Financial Plan presumes “how” through rates. He feels that there should be far greater emphasis in other Committees or the Board of Supervisors to pursue the funding mechanisms and the least-cost basis.

Mr. Barry said the Committee should stay out of that.

Ms. Bowen said that the Committee in years past has understood the capital needs to fund ROMP. That has always been a priority. “How” the County has decided how to move forward with funding is now impacting the proposed rates. That is her concern as far as this Committee and its relationship to the Financial Plan.

Mr. Katzel agrees that the discussion of this Committee is warranted around what the user pays. It is all tied together. If the Committee did not discuss the rates and the rates were not variable according to the mechanism. Mr. Smith said that the rates are tied to the financing mechanism. Mr. Katzel said it is the Committee’s legitimate concern as to the rate the consumer pays.

Mr. Smith said that it would be interesting for the other Committee members to look at the Bond Authorization Committee’s website. There is a letter submitted by their Chair, Larry Hecker, to [Board of Supervisors] Chair Elias questioning the purpose of the [Bond Authorization] Committee. After all they do and recommend, the Board says “no.” There is reply from Chair Elias. It is similar to the discussions in this Committee that they go through machinations and the Board of Supervisors goes a different direction or uses a different financing mechanism. He recommends the Committee read the two letters.

Mr. Katzel said that is true of any advisory committee. The word “advisory” is paramount.

Mr. Smith said that is the [Bond Advisory] committee, which [Larry Heckler] characterizes as dysfunctional, that he feels should be reviewing this very subject.

Ms. Bowen said that there was a motion and approval at the last meeting that this Financial Plan be approved. There was also discussion of the funding mechanism that basically yielded the user fee, recognizing that there are issues outside the Committee's control. Given that, she asked for discussion as to how the Committee sees that process.

Mr. Burke said that the financial advisors expect the sewer revenue obligations to be sold at the same rate as bonds, as the covenants are essentially the same. What will be driving the [interest] rates is the County's ability to pay, the County's ratings from the rating agencies and the projected revenue sources.

Mr. Gritzuk asked if that was about four percent. Mr. Burke said yes. Our estimates are high due to the uncertainty of the future bond market. The same projections are used for the County's General Obligation debt service, which has a better bond rating than sewer debt.

Mr. Gritzuk asked if the COPs were selling at three and one half percent. Mr. Burke said that in closing COPs sales today, they are expecting to be sold at 3.2 percent. Mr. Gritzuk asked how much in outstanding COPs were against RWRD. Mr. Burke said that as of June 30, it was about $22 million. Mr. Gritzuk asked if that would be paid off by the end of this fiscal year. Mr. Burke said that they will be paid off at the end of this fiscal year or the beginning of next fiscal year. There are several overlapping on the properties. Mr. Gritzuk asked if that enabled RWRD to do more COPs. Mr. Burke said no as the closing today for $20 million is on that same asset in order to purchase another asset.

Jeff Nichols said that in 2006 the Financial Plan assumed there would be a $565 million bond authorization in 2008 and a $310 million bond authorization in 2012. Those numbers have remained relatively constant with this Financial Plan. The Committee was also told in 2006 that the average bill at the end of ROMP would be $45. This Plan shows $44. The typical customer is now paying $29.

Mr. Barry said the difference is not going out to the voters. Mr. Nichols said yes.

Mr. Katzel said that that the difference is also the level of public awareness of what is happening with the rates. Mr. Nichols said that customer service staff knows that the public is very aware of the rates.

Mr. Stratton said that user rates will increase approximately $15 in five years. There was a comment in Mr. Huckelberry's memo, "This will accelerate debt repayment and allow reductions in sewer user fees and rates after FY 2015/16." Why put the increase in the rates as opposed to a separate fee or surcharge that identifies it as debt service for ROMP that would be easily earmarked and reduced instead of blending it in with the O&M costs? Ms. Bowen said that was discussed at the last meeting: it is similar to the service fee charge. Mr. Burke said it would be very easy to do that. The graph showing what the revenues produced will be. By 2014 there will be an extra $79 million per year, $12 million for O&M costs. It would be easy to split how much of these fees are related to debt service.

Mr. Barry asked if they meant a separate line item on a user's bill. Mr. Stratton said yes. It would identify the debt service for ROMP. When ROMP is done, it would be easy for the Board of Supervisors to remove that line showing debt service. Mr. Burke said that is how GO debt is handled. The debt service is a separate tax. Mr. Stratton said that it would be easier to explain to customers why their rates go up.

Mr. Katzel said it would be a good educational tool.

Ms. Bowen asked for further questions and discussions.

Mr. Smith said that at the last meeting that one annual increase of 10 percent instead of two six and one half percent increases was discussed. He said that, even though it can not be voted on today, the language should specify they track the market: If the interest rates in fact are four percent instead of the projected five percent there would be a reduction in the rate increase. Mr. Burke said that the County is required to do a rate analysis and financial plan every year. If the rate is split so that a portion is related just to debt service, that should be easy to analyze each year. Mr. Smith said that the Committee should be very explicit in the recommendation to the Board of Supervisors. A 50 percent rate increase over five years presumes an interest rate of five and one half percent. If, in fact the first $165 million is borrowed at 4.2 percent, it should be eight and one half percent the first year, not 10 percent. The Committee needs to be clear that the focus should be on rate reduction and rate control.

Ms. Bowen said that the obligations will be sold in March and the 10 percent rate increase would go into effect July 1. If this was a separate debt service line item, it would also go into effect in July.

Mr. Barry asked if this assumes annual sales. Mr. Burke said yes. The plan assumes a sale in January of each year. Financial statements would be completed for the prior year. Typically sales are done in the spring of each year. Mr. Barry asked when the first payment would be. Mr. Burke said that the first payment would be in July. The Plan assumes six months of interest in any given year.

Mr. Stratton said that he agrees with the concept. It may be better to initiate what is here then, as debt is issued, look at reducing future rates. Mr. Smith said that what will happen is an accrual of a large amount of cash. Mr. Stratton said if the interest rate goes up so will the next issuance. It might produce a steadier flow.

Ms. Bowen said that a vote was taken at the last meeting to be ratified at this meeting. The consensus at the last meeting was that the Financial Plan be recommended to the Board of Supervisors with the caveats that the user fee increase be combined to one annually, that the debt service be separated out on the bill, and future rate adjustments made on actuals.

Mr. Barry said that he feels that it is important to recognize that there is an $800 million need that will not go away. It has to be faced and we have to come up with the best way to finance that need.

Mr. Smith asked that the Charter of the Committee be reviewed to make certain that they are not overstepping their responsibilities.

Ms. Bowen said that she applauds RWRD for bringing the information to the Committee early on. The Committee has been aware of this need. RWRD has been very forthright with the information. This has to be funded. The funding mechanism is what is out of our control.

Mr. Barry said that it was clear from the Committee that the issue of having an election or not having an election did not have to be addressed by Mr. Burke. He felt that if this was done as a bridge measure and an election was held, and the voters said no, we would have to come back and do it the other way. That is a recipe for ignoring the voters. We have to be careful. The issue of a vote has to be addressed. There has to be four votes from the Board of Supervisors. Mr. Burke said for a rate increase there has to be three votes. For a sale of debt there must be four votes as the rates cannot be held for 30 days like a normal ordinance.

Mr. Gritzuk said that when Mr. Burke goes to the Board of Supervisors with this Financial Plan, the rate increase only requires three votes. Mr. Burke confirmed that the rate increase only requires three votes. It is like an ordinary ordinance. The sale of debt will require four votes.

Mr. Stratton asked what happens if four votes are not received. Mr. Gritzuk said that if there is no sale of debt there is no money to proceed with construction. Contracts have been awarded and are under construction. If construction has to stop, the financial impact would be severe. Mr. Burke said it would impact both sewer and GO debt. If there are no funds to pay for projects, even though sewer debt is paid through sewer revenues, it is looked at in the overall County rating for GO bonds as well.

Mr. Gritzuk said that with Ina Road upgrade and expansion underway, they are 75 percent done with the design of the facility. The contractor is now developing guaranteed maximum price (GMP) proposals for the largest portions of the construction. RWRD will be in negotiation with the contractor in a few weeks. The proposals are for more than $170 million. To meet the regulatory schedule, RWRD must move rapidly and reward the GMP to the contractor. If the debt sale does not go through, RWRD will be back at the drawing board.

Mr. Barry asked how quickly the regulatory agencies would take action against RWRD. Mr. Wesselhoft said that they can not do anything until there is an actual permit violation. The contract for work at the Roger Road facility needs to be done by 2011. Once RWRD misses that date, the regulatory agencies can start taking action. Mr. Barry asked if completing ROMP is part of RWRD’s permit. Mr. Wesselhoft said that if we back out of the Ina Road contract the regulatory agencies may find a way to say that RWRD is in violation of the permit.

Mr. Gritzuk said that there are many examples of that around the country. RWRD is the last in this state to comply with regulatory requirements. Pima County will not see much relief from regulatory agencies.

Mr. Barry asked if there was a date set for the public meeting.

Ed Curley said that, after taking a survey, Tuesday, February 9, 2010 appears to be the most convenient for the Committee.

Ms. Bowen said that there are 13 voting members but there are two vacancies. Is a quorum of seven still required? Mr. Curley said yes. Ms. Bowen confirmed that letters have been sent to the appointing authorities that have the two vacancies.

Mr. Gritzuk asked if February 9 has been set. Mr. Curley said that is the staff recommendation. Ms. Bowen asked the Committee to be available if possible due to the vacancies and difficulty getting a quorum.

Mr. Barry asked what the Committee's role is at the public hearing. Mr. Curley said that after the Committee hears the public comments, they convene a meeting to make a formal recommendation to the Board of Supervisors regarding the details of the Financial Plan. Mr. Barry asked about the length of a public hearing. Mr. Curley said that longest part is the presentation to the public. Ms. Bowen asked the location of the public hearing. Mr. Curley said it will be here, in the Pima Association of Governments large conference room on the 5th floor. Mr. Stratton said that historically, there has not been a large public attendance.

Mr. Gritzuk asked if the current Plan was in draft form, and what steps need to be taken to finalize it. Mr. Burke said that a few modifications will be made, such as the Committee recommendation. Mr. Curley said that the Plan needs to be sent to the public libraries by February 2, so a revised copy will be needed before the public hearing. Mr. Burke said that a copy of the proposed ordinance amendment is needed from the County Attorney's office. Mr. Burke confirmed that the Committee previously recommended an annual one step increase. Mr. Curley said that some wording regarding the separate debt service component is needed as well.

Mr. Gritzuk asked if a final or draft Plan will be presented to the Board of Supervisors. Mr. Burke said a final Plan. Mr. Barry asked if it would be for the Board's approval. Mr. Burke said yes, it will contain the Committee's recommendation and commentary from the public. Mr. Curley said that any verbal or written comments will be summarized and included.

Mr. Barry confirmed that the timing anticipates a sale in March if the Board of Supervisors approved the Plan. Mr. Burke said yes. Mr. Stratton asked when this Plan will be put on the Board of Supervisor's agenda. Mr. Burke said probably the first meeting in March. There is a 15 day publication requirement before the meeting.

IV. FUTURE AGENDA ITEMS. Mr. Barry asked when the next regular Committee meeting would be held. Ms. Bowen said on February 18. Mr. Curley said that the Committee has the option of cancelling that meeting and resuming in March. Mr. Barry said that he would like to discuss the mandate and Charter of this committee and have an update on the Water/Wastewater Study. Mr. Curley said that that there was also a request for an update on the drug take-back program. Ms. Bowen suggested that the February 18 meeting be skipped and the Committee act on the January 14, 2010 minutes on February 9, 2010.

V. CALL TO THE AUDIENCE. There were no comments from the audience.

VI. ADJOURNMENT. The meeting was adjourned at 8:50 a.m.