



Water Department

**Water Commission**  
7:00 p.m. –February 1, 2016  
**Council Chambers**  
809 Center Street, Santa Cruz

### **Minutes of a Water Commission Meeting**

**Call to Order:** Chair D. Baskin called the meeting to order at 7:02 p.m. in the City Council Chambers.

#### **Roll Call**

**Present:** D. Baskin, D. Schwarm, A. Schiffrin, W. Wadlow, L. Wilshusen, and D. Engfer  
**Absent** D. Stearns (with notification)

**Staff:** R. Menard, Water Director; H. Luckenbach, Deputy Director/Engineering Manager; T. Goddard, Administrative Services Manager; D. Culver, Chief Financial Officer; N. Dennis, Principal Management Analyst, A. Poncato, Administrative Assistant III

#### **Election of Officers:**

Chair Baskin opened the floor for nominations for Water Commission Chair.

Commissioner Schiffrin nominated Commissioner Wadlow.

Commissioner Schiffrin moved to close nominations and by acclamation elect Commissioner Wadlow as Water Commission Chair for 2016. Commissioner Wilshusen seconded.

VOICE VOTE: MOTION CARRIED

AYES: D. Baskin, D. Schwarm, A. Schiffrin, W. Wadlow, L. Wilshusen, and D. Engfer

NOES: None

ABSENT: D. Stearns

Chair Wadlow opened the floor for nominations for Water Commission Vice-Chair.

Commissioner Schiffrin nominated Commissioner Wilshusen.

Commissioner Schiffrin moved to close nominations and by acclamation elect Commissioner Wilshusen as Water Commission Vice-Chair for 2016. Commissioner Baskin seconded.

VOICE VOTE: MOTION CARRIED

AYES: D. Baskin, D. Schwarm, A. Schiffrin, W. Wadlow, L. Wilshusen, and D. Engfer

NOES: None

ABSENT: D. Stearns

**Others:** 3 members of the public.

**Presentation:** There were no presentations.

**Statement of Disqualification:** There were no statements of disqualification.

**Oral Communications:** Oral communications made by D. Spelce.

**Announcements:** None

### **Consent Agenda**

1. City Council Actions Affecting Water
3. Landscape Ordinance

Commissioner Schiffrin moved the consent agenda as amended. Commissioner Baskin seconded.

AYES: D. Baskin, D. Schwarm, A. Schiffrin, W. Wadlow, L. Wilshusen, and D. Engfer

NOES: None

ABSENT: D. Stearns

### **Items Removed from the Consent Agenda**

2. Approve the January 4, 2016, Water Commission Minutes

### **Commission Questions/Comments**

- Correct the spelling of CEQA under general business item 3. Water Supply Augmentation Strategy, Initial Work Plan.
- Correct the sentence in the first comment under general business item 3. Water Supply Augmentation Strategy, Initial Work Plan to state, "We are working to finalize CEQA if California Fish and Wildlife lets us finish the process to be able to start a trial in February, assuming we have water."
- Correct the sentence in the third comment under general business item 1. Cost of Service Analysis and Rate Structure Design to state, "In other words, once we have a methodology for the cost of service it won't matter what the revenue requirements are. Different revenue requirement levels would affect what the cost is but not the way it's going to be distributed."

Commissioner Schiffrin moved the minutes as amended. Commissioner Baskin seconded.

VOICE VOTE: MOTION CARRIED

AYES: All.

NOES: None

ABSENT: D. Stearns

#### 4. Update Initial Water Supply Outlook

##### Commission Questions/Comments

Should we seek to extend the petition that allows us to reduce our required flow release amounts and if we realize that we do not need the extension can we advise the Board, rather than the other way around? How does staff conclude that we do not need another extension when the data presented appears as though we may need another extension?

- The feedback we received from the State suggests that they would not be open to another extension at this point. We can request an extension in the event we realize that we need one and can have it in place within two to three weeks after we submit a request.

Can you project when Loch Lomond would spill?

- We are unable to make that projection at this time.

What information do we have about the flows on North Coast streams?

- There are stream gauges on the north coast but the data are not summarized in the same way - in terms of mean monthly flow – as they are as on the San Lorenzo River, however, we will focus more on the north coast in March when we create a water balance for 2016.

It seems as though we have been able to get more water out in greater drought conditions than in the past. How have we been able to effectively optimize our take from the river in terms of the ability to pump water this year? Does the strategy tie into the analysis from Gary Fiske, and has it provided any information that might tell us how we can continue in this direction going forward?

- One of the issues that Mr. Fiske brought to our attention was the first flush constraint, as mentioned in his evaluation presented to WSAC. We also have a constraint on the pipe that runs from the Felton Diversion to Loch Lomond which prohibits us from pushing large amounts of water to Loch Lomond. Additionally, it is unknown what the quality of the water is after the first flush. All of these factors are on the radar of things to keep an eye on, but the most important improvement that has helped us optimize our use of the river is that staff is more aware of how much water can be taken at the Felton Diversion and pumped into Loch Lomond.

Is that different than what has been occurring?

- The data we have has shown that the Felton Diversion was seldom used over the past 10-15 years. The dam was inflated during this period but the pumping did not occur. Maybe the water was not pumped during that timeframe because it was spilling, but we do know that the Felton Diversion was not routinely used over the past 15 years.

##### Additional Comments

- We are pumping water from the Felton Diversion Dam to Loch Lomond storage when we can.
- As of January 26, 2016, our region was downgraded from Extreme Drought to Severe Drought on the US Drought monitor.

Commissioner Schiffrin moved the staff recommendation. Commissioner Wilshusen seconded.

VOICE VOTE: MOTION CARRIED

AYES: All.

NOES: None

ABSENT: D. Stearns

## **General Business**

### 1. Inputs and Outputs of Capital Financing Plan and Water Rate Increase Work:

Ms. Menard provided a brief presentation summarizing the Capital Financing Plan and Water Rate Increase work. Ms. Menard, Mr. Culver and Brian Thomas of Public Financial Management responded to Commission questions.

#### Commission Questions/Comments

- The Rate Increase information is not available at this time.

#### Appendix A Questions and Comments

Line 26 Ending Cash Balance: Since these totals are what are carried over, shouldn't the Ending Cash Balances in both the 2017-2021 and 2017-2026 columns be \$0?

- Yes, they should be zero.

Line 27-28 Debt Service Coverage & Targets: Are these numbers going to be expressed as percentages or as a ratio?

- They will be expressed as a ratio so the number should be 1.5 times.

Lines 17 – 19 Capital Project Costs & Funding: The capital expenditure estimates change frequently over a number of years in this spreadsheet. The amounts in this section are far different than indicated in the current fiscal city budget. Please explain how these match the city budget.

- The numbers do not match the current city budget because the work that was done to create this plan was being fine-tuned during the fiscal year. Our goal is to create a consistent financial plan beginning FY 2017.

Line 17 Capital Project Costs & Funding: Once we get into the out years, after 2019, the capital improvement budget balloons from 83% to 120% of the total operating budget. Please explain.

- There are two major projects in years 2019 – 2021 and 2023 – 2025, which are having this impact: the dam repair project and the water supply project. The repair of the dam is scheduled to occur over 3 years but will likely be finished in 18 months – 2 years. We hope construction of the water supply project to be complete in 3 years, but the water supply project has not been defined yet so it is difficult to say. Something the department is looking into is how to deliver these two projects that are anomalies. We don't necessarily want to staff up for this relatively brief timeframe. One example may be hiring construction/program managers.

Do we worry about going to the market too often?

- No, given the nature of the work we're doing, going to the market every two years would be considered normal.

Line 4 Volumetric Revenue from Rate Increases w/Baseline Demand: What percentage increase was used for these calculations?

- 15% for the first year and 8.5% for the other years.

If the operating, maintenance, and capital improvement cost estimates are realistic, aren't the rate increases going to have to be something along this line?

- Yes and no. Yes, because we need to generate this sort of money. No, because the price per unit will change dramatically based on the cost of service and the amount of water we estimate we are going to sell.

Line 21 Debt Service as a % of Rate Revenue: Is there an industry standard of what the debt service as a percentage of rate revenue should be?

- No, there is not.

Shouldn't the total for Line 19 Debt Funded 2017-2021 be the same amount indicated in Table 4 on page 70 for Total Uses in years 2017-2021?

- This apparent disconnect is the result of issuing debt in 2021 and some of the proceeds not being spent until 2022.

Line 21 Debt Service as a % of Rate Revenue: What are the key factors that are considered by rating agencies and can we have a list of those factors in the future?

- Cash reserves, debt service coverage ratios, the relative age of our facilities, history of rate increases, willingness and ability to raise rates, and affordability. They will look at the water bill as a percent of median income in our service area. The higher the bill, the worse it is for your credit rating because there is more pressure not to raise rates.

Are non-financial factors that are considered?

- Yes, such as the board, council, and management of the utility.

Do they look at our ability to produce water?

- Yes.

Line 19 Debt Funded: There is \$7.4 million dollars debt funded in 2017. Is this amount a portion of the \$25 million dollar I-Bank loan?

- Yes.

#### Appendix B Questions and Comments

Included in the financial plan, there should be language that states what factors lead to issuing debt. What are the triggers for issuing debt?

- Generally the debt is issued in lump sums of \$25 million dollars. The debt will be issued when we are ready to generate \$25 million worth of constructions costs.
- The utility should also utilize reimbursement resolutions as a tool for the timely issuing of debt to make sure that debt is not issued and then not properly spent because this results in paying interest on money you're not using.

The numbers for Aquifer Storage and Recovery for 2016 in Appendix B show \$535,000 but the numbers in the Capital Improvement Plan we received at the last Water Commission meeting state that the Aquifer Storage and Recovery numbers were \$350,000. The Recycled Water numbers in Appendix B state \$480,000 but the numbers in the Capital Improvement Plan we received at the last Water Commission meeting stated \$160,601. Why are the numbers so different?

- The numbers that the Water Commission saw in January were draft budget estimates used as placeholders while the contracts were being negotiated with Pueblo Water Resources for Phase 1 of the ASR work and Kennedy/Jenks for the recycled water work, both of which were approved by City Council at their February 9<sup>th</sup> meeting. These are both two year studies and it may be worth noting that the spreadsheet included in the Water Commission's packet in January on this topic spread the draft budget estimates over two fiscal years to reflect spending. The draft budget estimate for ASR was \$370,000 and for RW \$325,202.

There are no Water Supply, Collection, Treatment, or Storage projects budgeted in fiscal years 2022-2026 and no money set aside for any projects. Should we put a generic placeholder in those years to set aside money for future, unforeseen, projects?

- This model is structured to complete critical projects at the front end while continuing to plan for future projects in the first five years. The second five years will be focused on construction of water supply project(s). One of the benefits of the debt service coverage ratio is that it requires us to generate additional revenue each year that is not allocated to any specific project and is available to be used the following year. We can use this generated revenue to help us get debt service coverage to fund pay as you go capital on an on-going basis.

Is the \$9.6 million dollar fee for the Water Treatment Plant Tank Assessment the cost of the entire project or just the assessment?

- The amount is a total cost for the assessment, the preliminary design, design and construction, and all associated consolidated costs. The assessment portion of this project is complete and in the next fiscal year, we will spend \$600,000 on the design of the new tanks. The \$9.6 million dollars if for the entire project.

### Final Comments

Are we comfortable with the 1.5 ratio?

- When you issue debt, you are going to have a debt covenant in which you will agree that you will always maintain revenues sufficient to cover your costs and typically some specific debt service coverage ratio (DSCR) service. The debt service coverage will range between 1.15 times coverage to 1.25 times coverage. Having a policy to maintain

1.5 x DSCR means you have a margin of safety so that if something unexpected happens you won't find yourself in technical default.

By debt covenant, do you mean an agreement with our lenders as to what our default standards are?

- Yes, that is your legal pledge.

In regards to coverage targets, when we talk about revenue, are we talking about net?

- Yes, net operating revenues divided by your debt services.

Please explain: Pay-as-you-go capital funding versus debt-financed capital – There is no industry standard or best practice for this metric. The factors that should be considered are debt capacity, day's cash on hand and intergenerational equity.

- Debt capacity goes back to our previous discussion about what bonding companies want from us. Day's cash on hand is making sure we have enough cash on hand to pay the bills. Intergenerational equity is spreading the cost of the reinvestment cycle over a longer period of time so that the people who benefit from them will pay a portion of the cost of that reinvestment.

Does each additional capital improvement become added intergenerationally and backed into the rate structure?

- Yes.

How important is it for us to meet the July 1, 2016, rate implementation deadline?

- That is unknown at this time.

I-Bank was presented as a reimbursement but it is not clear what it is reimbursement for.

- In April 2014, we took a reimbursement resolution to the city council to debt finance any additional capital costs that were generated from that day forward. At that time, we were in the middle of the 2<sup>nd</sup> phase of the Bay Street Reservoir project and we were preparing for the filter rehab project. We expect to receive reimbursement for both of these projects.

We are applying for a \$25 million dollar loan from I-Bank with \$15.5 million going towards replenishing the fund balance and two reserves which will leave us with \$9.5 million left. How will that \$9.5 million be spent?

- Think of the I-Bank package as two parts: one part is reimbursement for capital expenditures that we have already made, which is the \$15.5 million dollar figure, and the second part is for capital expenditures we plan to make in the coming 18-24 months. The I-Bank loan is going to three areas:
  1. build up the fund balance to repay the fund balance for capital projects already spent,
  2. create reserves to reach our reserve goals,
  3. fund capital projects in 2017.

Please explain the percentages of Annual Inflation Factors in Table 2 on page 66.

- The numbers are estimates drawn from historical experience and industry trend. Operating Supplies & Chemicals along with Energy expenses have traditionally increased at a rate greater than inflation. Some of these numbers came from the rate model we worked on several years ago. Employee benefits include PERS and health care costs. Personnel costs include employee salaries. Due to several failed recruitment and/or retention issues, the City recently completed an assessment and implemented compensation changes for our many of the positions within our Operations, Production, Water Quality, Distribution, Conservation, and Recreation Divisions by increasing salaries to retain good employees. These numbers were budgeted into the future forecast with the addition of 3 additional positions each year for the first 3 years.

Requests for Follow Up:

- Provide year to year percentage growth figures and percentage of revenue in key accounts.
- Insert footnotes explaining why budget numbers for projects have changed from month to month.
- Define projects so Commissioners know what they are.
- Separate the CIP project from the new water supply when the financial planning and rate discussion items return.
- Present CIP existing facilities and CIP new facilities with a comparison of what the impacts of those two different capital improvement plans are going to have on the overall revenue needs and rate increases.
- Add a fourth primary goal to the draft financial plan to include rate affordability.
- Separate operation and capital costs.
- Add both reserve numbers to the spreadsheet A.

Commissioner Schiffrin moves that the Water Commission accept the draft Financial Plan and request the staff to include the following when the Plan returns:

1. Incorporate a trigger for issuing debt;
2. Consider the addition of a rate payer affordability policy;
3. Clarify the distribution of the I-Bank loan;
4. Separate the CIP into existing capital projects and new capital projects;
5. Include a sensitivity analysis, and
6. Incorporate other Commission comments and respond to Commission questions;

Commissioner Wilshusen seconded.

AYES: D. Baskin, D. Schwarm, A. Schiffrin, W. Wadlow, L. Wilshusen, and D. Engfer  
 NOES: None  
 ABSENT: D. Stearns

4. Cost of Service Analysis and Rate Structure Design:

Ms. Menard provided the presentation summarizing the Cost of Service Analysis and Rate Structure Design and responded to Commission questions.

Commission Questions/Comments



- In the recommended motion, the word ‘transparency’ should be replaced with ‘clearly defined’.
- Add a fourth bullet to state: “Results in sufficient revenue to fund ongoing operations and to accomplish the department’s financial plan”.

Commissioner Schiffrin moved to accept the staff recommendation with the following changes to the bullet points to say:

- Methodologies used in the analyses are clearly defined and legally defensible;
- Results are equitable and likely to be perceived to be fair by customers; and
- Results effectively encourage water conservation and efficient use while reflecting cost of service;
- Results in sufficient revenue to fund ongoing operations and accomplish the department’s financial plan;

Commissioner Wilshusen seconded.

AYES: D. Baskin, D. Schwarm, A. Schiffrin, W. Wadlow, L. Wilshusen, and D. Engfer  
 NOES: None  
 ABSENT: D. Stearns

**Subcommittee/Advisory Body Oral Reports:** None

**Directors Oral Report** No action shall be taken on this item.

- Last month Ms. Menard presented information about the Water Supply Advisory Committee recommendations to the Board of Directors for Soquel Creek Water District and Scotts Valley Water District and received a friendly reception.
- In regards to the supply augmentation project, we have several contracts moving forward. ASR is in phase 1 and the recycled water project is an analysis of all alternatives using recycling water. Additional information will follow in March when we present our quarterly report.

Request

- Include updates on the progress of WSAC projects in the next quarterly report.

**Adjournment** Meeting adjourned at 10:31 p.m. The next regular meeting of the Water Commission is scheduled for March 7, 2016, at 7:00 p.m. in the Council Chambers.

Respectfully submitted,

**Amy Poncato**

Digitally signed by Amy Poncato  
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Staff