SUMMARY NOTES OF THE FINANCE COMMITTEE
ZONE 7 BOARD OF DIRECTORS

August 28, 2014
3:30 p.m.

Directors present:	Sandy Figuers Angela Ramirez Holmes Sarah Palmer
Staff present:	Jill Duerig, General Manager Tamara Baptista, Finance Manager Mike Wallace, Staff Analyst Judy Rector, Board Secretary

Director Figuers called the meeting to order at 3:30 p.m.

Director Figuers asked the other committee members, Directors Palmer and Ramirez Holmes, about reorganization of the Finance Committee. They both agreed that the Committee can remain as it currently is with Director Figuers as the Chair.

1. Public Comment – None

2. Agreement in Principle Concerning Extensions of the State Water Project Water Supply Contract (Theresa Lightle - State Water Contractors)

Jill Duerig welcomed Theresa Lightle to Zone 7 and Mike Wallace introduced her. Mr. Wallace gave a brief description of Ms. Lightle's background with the State Water Contractors and the Department of Water Resources. Ms. Lightle, Senior Financial Management Analyst representing the State Water Contractors, discussed the contract negotiations between California's Department of Water Resources (DWR) and the State Water Contractors (SWC's) with Zone 7 as one of the 29 contractors taking part in the negotiations.

Ms. Lightle explained that the Agreement in Principal (AIP) is the foundation the lawyers will use to draft the contract amendment. The amendment extends the current contract, which expires in 2035, to 2085 and will secure continued water supply services to 2085. This will create the ability to finance facilities beyond 2035 and ease financial burdens on SWC's. By amending the contract, the state would continue water services for fifty more years and DWR would provide capital financing with bonds to fund projects, which would eventually lower periodic payment amounts for SWC's. What is important to DWR at this point is that the Agreement-in-Principle is ratified so they can use it as a project description for the environmental review. There is nothing in the amendment about the BDCP and it is strictly regarding the financial articles of the contract and how the SWC's are billed. DWR's goal is to get everyone to support the AIP. The contract extension is being done now to focus on capital financing beyond 2035 and avoid financial compression and escalation.

Ms. Lightle explained the contract extension process timeline, the implementation of "Freeze-Go" or "Pay-as-You-Go" billing methodology, creation of a State Water Resources Development System (SWRDS) Finance Committee, Cash-Flow & 51(e) Revenues, and answered questions by the Directors.

General Manager Jill Duerig asked the Finance Committee for direction. Directors Palmer and Figuers agreed that the item asking for signatory authority to sign the Agreement in Principle amendment should go to the full Board at the September board meeting. Director Ramirez Holmes noted that it should be a full board discussion and not on consent so the public can comment. She would like to hear the General Manager's thoughts on "truing up" of costs with DWR. She also suggested that there should be a conversation on tunnels so people know what is being signed. Ms. Lightle reiterated that the BDCP and the Delta Conveyance are not part of the AIP.

3. Water Rate Design & Process

Ms. Duerig introduced consultant Lori Rose whose goal is to step back and make suggestions on ways to make things better. Ms. Rose said she and Tamara Baptista, Finance Manager, had been working on water rates and looking at things that might improve the process of determining rates including a normal rate and a drought rate. This allows flexibility to establish a regular rate and a drought rate under Zone 7's 2010 Urban Water Management Plan.

Multiple alternatives for rates were developed for the Board in the past and presented over two Board meetings, but data isn't fully available until late August. Both the Finance Committee and the Retailers prefer to have more time for discussions prior to the Board adopting the rates in October. Director Palmer agreed that compression made things fall through the cracks.

Director Ramirez Holmes says she has always pressed for more communication with the Retailers but is opposed to reducing the number of public hearing meetings because the public has to be able to weigh in. She noted that she would personally like to see a public meeting/workshop entirely on budget. She asked about the process and timeline for working with the Retailers and what we are waiting on before starting those conversations with Retailers. Ms. Baptista replied that staff analyzes a large volume of data including the demand projections submitted by the retailers and water operation expenses. The Directors discussed the timing of meetings and Ms. Duerig reminded them that a date for a Special Board Meeting is set up every month in advance, if needed.

The Joint Liaison Committee proposed a Water Policy Roundtable on September 27. The purpose would be to begin discussions on balancing competing policy priorities for rates, financial sustainability, water reliability and water quality. Another reason for not coming back to the full Board before the October meeting was so staff could process what happens on September 27th and come up with a proposal to the Board. There is also a Finance Committee meeting scheduled for September 8th.

Director Figuers said using reserves in a drought is like a drought rate but if we have another two to four years of drought, do we want a contingency for back-to-back drought years? We have never had a plan for an extended drought. He asked if the Board would want to deplete reserves or create a Stage 2 Action specific plan, which ties our hands.

Director Ramirez Holmes said we should declare a drought for emergency projects but don't do an automatic surcharge.

Ms. Duerig said that the Urban Water Management Planning Act requires a five-year update next year. Use of the drought reserve, as outlined in the 2010 Urban Water Management, can be revisited.

Director Palmer said we could adopt a plan that is not automatic but goes through the Board, has a deadline and a sunset, and the Board's hands are not tied. The Directors agreed that a drought surcharge should not be automatic but available if the Board needs to impose one and that is why a policy is developed to address the issue. Director Ramirez Holmes asked if retailers are charging a surcharge in order to be made whole financially, and if Zone 7 adds one on top that would mean paying more for less water.

Director Figuers noted that by March we know if we are going to have a drought but Ms. Duerig said it is more about what Zone 7's state allocations going to be. This year we knew it was going to be low because it was set at 0% in January but rains significantly improved the allocation. Ms. Rose said the drought rate can be calculated if there is a reduction in volume, i.e., if the rains come, you go back to a regular rate by late April. The Sustainability Report in April or May analyzes whether we need conservation that year or not. Ms. Duerig said if you have the rules upfront and adopted in advance, then everyone knows what Zone 7 is likely to do.

Dan Martin, City of Pleasanton, said residents are not upset with the increase but more with the reasoning behind it and ask why the increase? City of Pleasanton follows a guiding principle of not charging people more money and having small increases over time based on the Consumer Price Index. Director Ramirez Holmes asked about significant revenue losses for Pleasanton. Mr. Martin responded that with the structure of the Pleasanton revenue stream, their largest cost component is purchasing water from Zone 7 but they have reserves to make up any revenue shortfall.

John Archer from DSRSD said the drought rate process was easy this year because of working in advance. The Board takes the action, the Board has to continue the action, and the Board has control over when to start to decide the action, it is not a staff decision.

Director Ramirez Holmes said she does not like something that automatically goes into effect even if we don't need it. The reserves worked exactly as intended. She is concerned about Retailers adding drought surcharges when people are doing their best to conserve, so she doesn't want Zone 7 to also add a surcharge.

The Directors discussed having the option of having a policy with a rate structure and multiple levels of options based on the severity of the drought but not tier-based.
Ms. Duerig said that because untreated customers would still be a pass-through, if they take less water, we get charged less and any drought surcharge is hard to justify. We have a lot more

fixed costs on the treated water side for treatment plants and even if we are treating less water, any savings are balanced by increased energy costs at the wells. Director Palmer noted that sometimes you have to do more treatment because the water quality is worse.

Director Figuers said he would prefer to start the process early, have meetings early, such as mid-April, so if staff declares a drought, it is not compressed into the last month and there is more time for public hearings knowing that it is going to be a tough year.   Ms. Duerig explained that if you have the rules adopted in advance, then everyone knows what Zone 7 is going to do.

The Committee agreed that a policy should be set up with options that state "if we have a drought, these are the steps we are going to take" and put things in place ahead of time such as a rate structure built on multiple levels based upon the severity of the drought.

Ms. Duerig said there are two separate proposals. The first one about the drought rate and staff will come back with a proposal as there is no urgency except to complete it before the Urban Water Management Plan.   The second proposal is to change the process to present the rates at one Board meeting (October) which would allow more time for the Committee, staff and the Retailers to meet.
Director Figuers restated that he would like to see the Committee get involved earlier, hear the rates at a regular board meeting and then choose if a second meeting is necessary.

4.   Finance Policies, Part I (DRAFT Operating Budget Policy)

Lori Rose told the Committee that it is important to have policies and give guidance to the General Manager and staff on how to implement the Board's expectations. The Operating Budget policy lays the groundwork for the upcoming budget process. This will also establish a two-year budget cycle for Zone 7. Director Palmer asked about the point in the agenda item on authorizing the General Manager to make budget transfers as appropriate within the same fund. Ms. Rose explained that this allows Ms. Duerig to make budget transfers within approved limits.

Director Ramirez Holmes said one of the challenges at Zone 7 is so many funds and having to add funds. In the audit they summarize all this and some of the numbers jumped out last year and she asked how to prevent this? She said that the auditor said there are budget variance controls that should come back for discussion. Director Ramirez Holmes said a policy is needed and wanted to make sure there are budget variance controls over 5% to 7% so there are no surprises. This gets back to roles and responsibilities and focusing on the level of control. The Board is looking for simple explanations. The auditor's report did not show a lot of detail and added up to a larger amount. Ms. Duerig said this is how staff came up with the monthly format to show budget expense vs. expense to date and add text to show a proper policy level and keep the Board in the loop. Director Ramirez Holmes said most of the discrepancies were with transfer and project overruns to cover shortfalls.

Director Figuers asked about the term "structurally balanced" used in the agenda item. Ms. Rose said it means having a plan and using resources to look at all factors and pieces for a responsible budget and not draining reserves. He also asked about "operating budget carryovers." Ms.

Duerig explained that if you don't buy as many chemicals one year as budgeted, you don't get to carry over that money into the next year.

Dan McIntyre, City of Livermore, said the two-year budget works great for the City of Livermore. He suggested that minimum and maximum amounts in policies are good, too, because it creates a floor and a ceiling.

Director Ramirez Holmes said that she does not see Board empowerment to do the Budget, it says General Manager. She likes the DSRSD policy on accountability where the Board is mentioned and is the body that sets the goals and objectives. She also mentioned that budget principles should have the phrase "unless the Board decides otherwise" for consistent terminology assuming all of the principles would be different if the Board chose otherwise.

In referring to the section on Reporting, she said she would like an actual quarterly staff discussion explaining changes and saying "here is where we are" as opposed to a report in the packet. Because the Monthly Staff Report is at the end of the meeting, there isn't a lot of time left to ask questions.

Ms. Duerig said at the last Board meeting, President Greci directed that the role and frequency of meetings be on a future agenda.

5. Verbal Reports

Director Ramirez Holmes requested that a work plan for the year be developed so the directors know what to expect and have an idea of what the Finance Committee plan is for the year.

6. Adjournment

Since there were no further issues or comments, the meeting was adjourned at 5:35 p.m.