SUMMARY NOTES OF THE FINANCE COMMITTEE
ZONE 7 BOARD OF DIRECTORS

September 10, 2015
4:00 p.m.

Directors present:	Angela Ramirez Holmes Dick Quigley Bill Stevens
Staff present:	Jill Duerig, General Manager Osborn Solitei, Assistant General Manager, Finance Tamara Baptista, Finance Manager Linda Van Buskirk, Acting Board Secretary

Director Quigley called the meeting to order at 4:00 p.m.

1. Public Comment on Items Not on the Agenda:

Leonard Olive, City of Pleasanton. After a meeting between staff from Zone 7 and the Retailers on September 8th to discuss the Cost of Service Study, Mr. Olive wanted to express some concerns on the presentation that was given to the retailers.

Osborn Solitei, Assistant General Manager, Finance, responded to the issues raised by Mr. Olive and stated that when meeting with the Retailers the understanding was that the assumptions and data were preliminary, not even close to being final yet, and the information was presented only for discussion of concepts.

Director Ramirez Holmes said she would like a copy of the preliminary information that was given to staff from the Retailers.

Director Quigley thanked Mr. Olive, but noted the item was not agendized. He applauded that kind of work between staff stating that he thinks it is very effective to filter out errors and omissions at the staff level before bringing to the board.

2. Discussion of 14-15 Audit Approach and Status

Osborn Solitei introduced David Alvey from Maze & Associates, our auditors for FY 14-15.

Mr. Alvey distributed a three-page outline entitled “Audit Planning Meeting Agenda for the Year Ended June 30, 2015” and discussed the audit procedure. Audit standards require the auditors to communicate with “those charged with governance” to discuss the audit process including audit scope, audit timing, management representations and fraud considerations. Mr. Alvey said that Maze will also be assisting in preparation of a Comprehensive Annual Financial Report (CAFR).

Mr. Solitei said that prior to the audit, Mr. Alvey would be sending an email to Finance Committee members with questions and they can respond back to him directly. Director Stevens asked what the questionnaire would be regarding. Mr. Alvey informed the committee members that Statement of Audit Standard (SAS) #99 requires auditors to ask management questions about their awareness and understanding of fraud. Auditors will then make a decision as to whether they need to 'educate' management about fraud and the types of controls that will deter and detect fraud. The standard also requires auditors to make inquiries of the audit committee, internal audit personnel and others within the entity. As an example, a couple of areas they deem automatically high in the fraud risk area would be improper revenue recognition and management's ability to get in and change the internal control process. He directed the committee members to the last page of his handout at Paragraph 2(b) "Areas to be Discussed" for a list of questions.

Director Stevens asked if this is a federal or industry-wide standard. Staff replied that it is not federal but it is required by the American Institute of Certified Public Accountants (AICPA).

Director Quigley asked if there are any audit regulatory changes since last year and if those will be addressed. Mr. Alvey responded that yes, just like the tax code, every year there are changes to it, and that Maze always keeps updated on the standards.

Director Ramirez Holmes thanked Mr. Alvey very much, and said that she appreciates that the audit plan and process has gotten better. She then asked if there is going to be a status report between the audit and final presentation, as last year they received a spreadsheet which listed the questions that were asked back to staff. Mr. Alvey said he can do that if the committee would like.

Director Quigley asked if the audience or staff had any further questions, and then thanked Mr. Alvey for his presentation.

3. Review of Impacts on Assumptions for Cost of Service Study of Possible Rescheduling of Certain Capital Improvement Program Projects, as recommended by Water Resources Committee:

Mr. Solitei handed out a table entitled "Fund 120 – Renewal/Replacement and System-wide Improvements - Proposed Deferrals" and discussed the dollar amount difference from year to year as a result of deferring projects totaling $14,700,000.

Ms. Duerig explained that the Water Resources Committee went through the individual CIP projects at its September 9, 2015 meeting. This is not really an elimination of projects. There is one slight modification in tackling one project sooner, but everything else has been deferred or broken into phases. So for instance, if staff had a project that had three filters being rehabilitated in the same year, staff might have moved them so that each filter was in a different year to spread the costs. This was done at the request of Raftelis. They wanted a reduced CIP number to use in the model they are developing. The staff-recommended deferrals were endorsed by all three Water Resource Committee board members.

Director Stevens said he was in that committee meeting. The proposed deferrals are pretty innocuous. All staff is doing is taking a project and delaying it and spreading it out over a few years. He pointed out that these deferrals mean that our maintenance costs will go up, so they will be included in the next budget round. Whenever you defer a project, now you have to maintain it to keep it operational. He referred to the FY 18-19 column which shows that Zone 7 will spend more than was budgeted due to "playing catch up." The bottom line is this year Zone 7 needs to save money because of the fact that everything has come together to create a perfect storm and Zone 7 must survive this year. That is one of the reasons for the rush on the analysis and the reason why deferrals are needed. Director Stevens thinks deferrals are a great answer to how to keep Zone 7 whole financially.

Director Ramirez Holmes asked for an explanation on the chart and staff clarified such issues as the difference between the Subtotal (in Millions of Dollars) which represents the adjusted FY budget amount and the Former Subtotal (15/16 CIP) which represents the approved budgeted amount for CIP. Director Ramirez Holmes asked how much carry over Zone 7 had from the CIP spending in FY 14/15. Mr. Solitei responded that approximately $2,800,000 was carried forward.

Director Ramirez Holmes asked how the new legislation on chromium 6 affects Zone 7's plans for chromium in the CIP. Staff responded and explained that it gives us some breathing space in terms of determining the most economical solution.

Director Quigley commented that it pleases him as a committee member to see the $19,870,000 figure move to $7,000,000 due to the proposed deferrals. He is comfortable recommending this to the full board, but would like to hear comments from the Cities and DSRSD. Director Stevens added that he is comfortable supporting, as well.

Director Ramirez Holmes said she felt uncomfortable making any kind of suggestions without full information. She trusts staff's decisions and is pleased, but would like to see more impactful information.

John Archer with DSRSD said there are two components of Zone 7's rates which are the drought component and the capital needs component, and both pieces of this come together in setting the rates. DSRSD asked staff to look at deferring and maybe spreading projects out a little longer since that is where it impacts the finance side.

Director Quigley agreed that the CIP element certainly is a significant component of Zone 7's rates. He then thanked Mr. Archer for his input.

Leonard Olive, City of Pleasanton, said that the rationale behind deferring CIP projects certainly is very sound. He said the City supports this concept. In reference to the FY 17-18 and FY 18-19 columns of the chart where the subtotal bumps up to $22,000,000 and $23,000,000, he questions if Zone 7 can really deliver that amount of projects in those particular years.

Ms. Duerig clarified the biggest expenditures in the water treatment facilities seen on the chart spread over the four years, is basically a single project at each plant – the ozone project. Director Quigley said the committee is in accord with moving forward and that they look forward to hearing more at the full board meeting.

4. Proposed 2016 Municipal & Industrial Water Connection Fee

Mr. Solitei explained that in 2002 the Board adopted the Connection Fee (Resolution 02-2450), increasing connection fees by the Construction Cost Index (CCI), as published in the Engineering News Record, with periodic detailed reviews to determine if other adjustments are needed. The most recent periodic review was performed in 2011 and the next one is due in 2016. Based on that, the staff recommends adjusting the current fees to keep pace with inflation, based on the ENR CCI from September 2014 to September 2015. Although staff does not have the information for September 2015, the August 2015 index is at 2%. As soon the figures for September 2015 become available, that will be included as part of the submittal to the Board for adoption at the October meeting.

Director Stevens asked if the ENR CCI is an industry standard or if there is another standard. Staff could review it in the connection fees study to see if another index is appropriate and bring it forward at that time.

Director Quigley remembers over the years having homebuilders in a room talking about using and adopting this index. His inclination is to stick with it.

John Archer said that DSRSD uses the same index for inflation on projects.

Director Ramirez Holmes said that building has slowed down tremendously. She thinks that when staff re-does the plan, the projections will be slightly less.

Mr. Archer said that mathematically the big risk is you are adding new projects that you weren't anticipating. DSRSD is going through that process right now. They can't start on the connection fee side until they are finished with the Master Plan, but which one goes first? The inflationary factor hopefully keeps you in the ballpark. It doesn't cover new projects.

Director Stevens suggested that when staff does create the study that they keep in mind one of the biggest factors -- When do you apply that connection fee? Is it when you get the building permit? When you turn on the faucet? When you sell the home?

Director Ramirez Holmes said the City collects it when they pull the building permit with all the other city fees. Ms. Duerig said Zone 7 has agreements with the cities to collect fees on our behalf. Mr. Olive is 55% sure it is when the meter is set. Mr. Archer thought at one time it was when they pulled the map.

Director Quigley said that this item is asking for Finance Committee concurrence on the 2%. He concurs because big builders who have been here over the years can adjust quickly to a routine 2% tied to the CCI. It makes sense to them. Director Stevens also concurs and recommends approval to move forward on the proposed municipal industrial water connection fee.

5. Verbal Reports:

Ms. Duerig said that President Palmer is at the Alameda County LAFCo meeting. Zone 7, along with DSRSD and the Cities of Pleasanton, Dublin and San Ramon are being awarded plaques for a Good Governance Award presented by the California LAFCo. That plaque will be presented at the board meeting.

Director Ramirez Holmes noticed that the monthly budget report that is normally in the agenda packet was not in the August packet and asked if there will be one in September.

Mr. Solitei responded that a quarterly revenue and expense report is more user friendly and accurate as it actually projects out to the year end. Zone 7 staff recommends changing it from monthly to quarterly. Staff will prepare a full report to the Board in October.

Director Ramirez Holmes said that an August budget report is useful because it shows the carryover, while waiting until October when the audit is in November is not very useful for the committee studying numbers when they must talk about rates and yet they have not received any budget information prior to that time except what has been provided for this rate study and the assumptions, but assumptions of what?

She expressed concern that the Finance Committee must make sure that they are doing their job of financial oversight while making these decisions about rate studies and assumptions. For her, not getting a report until October is not ok because that does not provide enough information. She wanted to make a request in the verbal report piece because she thinks that it is important to have the information before next week's meeting where the committee is supposed to give its input about real numbers.

Director Quigley said that every three months makes sense. He also pointed out that the annual report that just came out has a section entitled "Managing Your Water Resources" which shows a way to go back 10 years on the large numbers and is quite revealing. He then said that a report every three months could help simplify things as a committee and certainly for the public. He applauded the Retailers for working with Zone 7 to refine numbers and increase transparency.

Director Stevens said that this is a water agency where the board approves a budget every year and quarterly reports are fine because they show what has been budgeted, what has been spent, and what is projected.

There being no further business, Vice President Quigley adjourned the meeting at 5:02 p.m.