MINUTES OF THE BOARD OF DIRECTORS
ZONE 7
ALAMEDA COUNTY FLOOD CONTROL AND WATER CONSERVATION DISTRICT

REGULAR MEETING
September 16, 2015

The following were present:

DIRECTORS:	SANDS FIGUERS JOHN GRECI JIM McGRAIL SARAH PALMER RICHARD QUIGLEY ANGELA RAMIREZ HOLMES BILL STEVENS
DIRECTORS ABSENT:	
ZONE 7 STAFF:	JILL DUERIG, GENERAL MANAGER KURT ARENDS, ASSISTANT GENERAL MANAGER, ENGINEERING OSBORN SOLITEI, ASSISTANT GENERAL MANAGER, FINANCE LINDA VAN BUSKIRK, BOARD SECRETARY
COUNSEL:	DAVID ALADJEM, DOWNEY BRAND

Item 1 – Closed Session

(a) Conference with Legal Counsel - Significant exposure to litigation pursuant to Gov't Code Section 54956.9(d) (2): 3 cases

(b) Conference with Legal Counsel - Potential litigation pursuant to Gov't Code section 54956.9(d) (3): 2 cases

(c) Conference with Legal Counsel - Existing litigation pursuant to Gov't Code Section 54956.9(d) (1): Alameda County Flood Control and Water Conservation District, Zone 7 v. Pleasanton Gravel Co., Alameda County Case No. HG14724177

(d) Conference with Labor Negotiators:
Agency Negotiator: G.F. Duerig
Employee Organizations: Alameda County Management Employees Association; Alameda County Building and Construction Trades Council, Local 342, AFL-CIO; International Federation of Professional and Technical Engineers, Local 21, AFL-CIO; Local 1021 of the Service Employees International Union, CTW; Unrepresented Management.

Item 2 – Open Session and Report Out of Closed Session

The Board came out of Closed Session at 6:45 p.m. and President Palmer said that no reportable actions had been taken.

Item 3 - Call Meeting to Order

President Palmer called the regular meeting to order at 6:59 p.m.

Item 4 - Pledge of Allegiance

President Palmer led a salute to the flag.

Item 5 – Citizens Forum

Alan Burnham said he has written a two-page document about how wholesale water rates should be structured. President Palmer advised Mr. Burnham that this is an agenda item.

Item 6 - Minutes

a. Minutes of the Special Meeting of August 17, 2015: Director Stevens moved that the minutes be approved, and Director Figuers seconded the motion. The motion passed by a vote of 6-0-0-1, with Director McGrail abstaining.
b. Minutes of the Regular Meeting of August 19, 2015: Director Ramirez Holmes moved that the minutes be approved, and Director Quigley seconded the motion. The motion passed by a vote of 7-0.
c. Minutes of the Special Meeting of August 26, 2015: Director Stevens moved that the minutes be approved, and Director Figuers seconded the motion. The minutes were approved by a vote of 7-0.

Item 7 – Consent Calendar

Director Quigley moved to approve Consent Items 7(a) through 7(c) and Director Ramirez Holmes seconded the motion. The items were passed by a voice vote of 7-0.

Resolution No. 15-85	Proclaimed the week of October 19-24, 2015 to be Flood Preparedness Week (Item 7a)
Resolution No. 15-86	Approved request for out-of-state travel to attend the annual AWWA Cal-Nevada Section Fall Conference (Item 7b)
Resolution No. 15-87	Authorized the General Manager to negotiate and execute an Agreement with DWR for construction of the new Olivina Turnout and any other related documents (Item 7c)

Item 8: Staffing Update

Ms. Duerig announced that the July Employee of the Month was Anthony Choi, Account Clerk, who works for Margaret Chun. Anthony is one of those delightful people who always helps employees who are trying to figure out all the nuances of accounting, whether it’s timesheets or vacations, challenges with the software, or anything else. He is always willing to share his knowledge. The Board applauded Mr. Choi in absentia.

Item 9: Commercial Septic System, Nella Terra Winery

Kurt Arends, Assistant General Manager, Engineering introduced the application for a new septic system at the Nella Terra Winery and Event Center in Sunol. The existing septic system onsite currently supports the rural residents and commercial wine tasting room. There is a temporary events center which is basically a tent, and the attendees and guests and employees currently use a portable toilet system. The winery is proposing to construct a permanent event center with permanent restrooms. This is their application for a second onsite septic system that would support the event center, guests and employees. Zone 7 Resolution 1165 prohibits commercial septic systems unless an exception is granted by the Zone 7 Board. The policy also restricts onsite loading to a maximum of one rural residential equivalence per five (5) acres. This is a 100-acre parcel which is not located over the Sunol or Livermore groundwater basins.

Director Stevens asked if the site drains into the Zone 7 basin. Mr. Arends confirmed that it is within our service area, so Zone 7 is responsible for reviewing the application.

Director Figuers asked if an owner or somebody who is familiar with this system is present. He asked how deep are the native soils in that area and how deep will the leach field be.

Gerry Beemiller, owner of the property and owner of Nella Terra Winery, explained that they have done some soil testing. The soil in the area where they propose a septic system is around 10 feet or so before getting into any rock, so it percolated really well.

Director Ramirez Holmes asked why this item is coming before the Board as it is obviously an existing commercial development. Is it deemed “new commercial development”? Mr. Arends explained that it is a new commercial septic system. Board Resolution 1165 states that there shall be no new commercial septic systems without Zone 7’s approval. Actual permitting of the system is through Alameda County Department of Environmental Health, so they will be the ones reviewing the design and issuing the actual permit.

Director McGrail moved for approval of the motion and Director Ramirez Holmes seconded. The motion passed with a roll call vote of 7-0.

Resolution No. 15-88	Authorized the commercial use of a septic system at Nella Terra Winery

Item 10: Cost of Service Study

President Palmer introduced Osborn Solitei, Assistant General Manager, Finance, to provide background on the financial presentation. She instructed everyone present to allow him to go through the presentation completely first and then questions would be taken.

Mr. Solitei Osborn gave a brief background for the Cost of Service Study. Mr. Solitei then introduced Sanjay Gaur with Raftelis to review the primary drivers for the numbers and to give a presentation on the Cost Study.

Considerable discussion ensued regarding Zone 7’s budget and projections for Fund 100 – the Water Enterprise (water rate fund) , and Fund 120 – Capital RR & SWI including reserves, maintaining infrastructure, the Asset Management Plan and the Capital Improvement Program, financial components, the rate design which includes both fixed and volume-based variable components, along with the respective retailer impacts. Rate structure case studies from Metropolitan Water District: Fixed and Volumetric, and Santa Clara Valley Water District: Take-or-Pay were discussed. Mr. Gaur emphasized throughout the presentation that we do not pay for water; we pay for the having water available at any time and the ability to use water when we want it.

Mr. Gaur suggested that Zone 7 can resolve the shortfall associated with conservation by implementing a temporary (2-1/2-year) conservation surcharge to cover O&M as follows:
Starting in January 2016 -

FY 15-16: $3.5M (collected over 6 months)
FY 16-17: $7.0 M
FY 17-18: $5.0 M (sunsets on June 30, 2018)

The consultant also suggested incurring debt within two years.

Mr. Solitei emphasized that if the board decides not to increase rates, the financial future of the agency will be grim. Fund 100 ending balances are projected to be:

FY 2015-2016 = $5,361,941
FY 2016-2017 = ($7,422,087)
FY 2017-2018 ($19,951,958)

These balances, combined with losses in the Fund 120 balances, would produce total combined ending balance in FY 2019-2020 of ($58,580,099).

Director Stevens asked about the variable rate. Are we setting a rate for three years or are we going to change the variable rate next year? Mr. Gaur said the rate would increase each year by 10% above inflation.

Director Ramirez Holmes asked for clarification on the fixed cost because she said that it doesn't appear fixed at all. Mr. Gaur replied that it is called a fixed variable. The idea of a fixed variable is that you are creating an incentive for other agencies to look at alternative supplies, potentially looking at storage facilities in the summer time because they could potentially lower their fixed costs. The fixed cost is a percentage and is determined based on a three-year rolling average.

Director Figuers asked if there is are any critical projects still included. Ms. Duerig responded that staff did a risk analysis that was shared with the Water Resources Committee which went through each project and what deferring it meant. In some cases it was possible to defer, although it would increase maintenance costs in the short term and some of the items are related to being able to distribute the water. The Asset Management Plan is based on projected failures and proactively fixing things before failures happen. Director Figuers then asked if there are there some projects that staff thinks are more important than others? Yes, and that is how staff came up with the list of deferrals. Ms. Duerig stated that the ozone project should not be deferred any longer, if Zone 7 is to successfully accomplish its mission, which is to serve high-quality water.

Director McGrail asked if Zone 7 is pursuing any type of grant money for ozone or has the agency explored selling some bonds? Ms. Duerig said that she is unaware of any grant programs that would pay for ozone. There is a state revolving fund but there are limited funds and it usually pays for systems that are not currently meeting drinking water standards. Luckily, we are not in that situation. To the second question, the $43M of debt that is proposed in Year 3 of this program is in fact selling bonds, so that is what staff is recommending so that the ozone project can be built.

President Palmer asked how much this plan will cost the individual household. Mr. Gaur directed the board to Slide 33 showing the estimated pass-through per CCF amount to be $3.15. Right now Zone 7 is charging $2.36, so that a $0.79 increase. For the average customer then, they can see how much water they use, multiply that by $0.79 and that would be the impact.

Alan Burnham, 4221 Finley Way in Livermore handed out a two-page letter to the Board entitled "Towards a Moral Wholesale price Structure for Zone 7". It detailed that in the long term, California has a water supply problem. He believes that there has been inadequate attention to diversifying supply. As he reads the Zone 7 reports, he is very encouraged, but what he heard tonight is very discouraging. He said there has to be a lot more attention to spending what is necessary to assure capacity to actually supply the water that people want. A 33% increase in fees to him is trivial. Not having enough water to the point of losing trees and vegetation could cause hundreds of dollars of damage. He said the emphasis needs to be is making sure the people understand that if they want to have water, they are going to have to pay for it.

Detlev Tiszauer, 5168 Norma Way in Livermore, thanked the Board for a great, detailed presentation, which he liked. His question is on the pro forma rate changes. He sees a 10% increase going forward in the total expenses year after year, but doesn't understand why, with a decrease in water delivery, the expenses increase at a 10% rate. A lot of companies have had to deal with the downturn in business and how they deal with it is they cut costs – they cut their expenses. He would like to see where the agency can cut expenses so that revenues and expenses balance. He would like to see the detail on the expenses and a better explanation for the increase of 10% every year.

Karla Brown, Vice Mayor of the City of Pleasanton recognized the Zone 7 Board and their staff for the leadership throughout the fourth year of this historic drought. She said that some of the things in the presentation have been a great education for those in the audience. As an elected Pleasanton representative, she voiced some concerns that the City of Pleasanton has for the proposed increases focusing on three things: rate restructuring, the two and a half year drought conservation surcharge and an ongoing rate increase. On the matter of a rate change, Pleasanton currently does not support the idea that a proposed rate change is not the same for all retailers. Pleasanton encourages Zone 7 to go back to the drawing board and develop an approach where all retailers have the same rate per unit. Regarding large capital projects, perhaps more projects could be deferred. The $30M ozone project is a clear need. The city also believes that Zone 7 should consider taking full advantages of bonds. Right now interest rates are very low. Pleasanton supports the idea of a temporary drought surcharge, but asks that Zone 7 consider sun-setting it on an annual basis and reviewing it to extend further. It should be evaluated very carefully instead of automatically looking at a 2-1/2-year drought surcharge. Pleasanton is sensitive to Zone 7's needs and they city understands the agency's loss of revenue. We are all in this together. We want to work together. Thank you.

Leonard Olive, City of Pleasanton. Mr. Olive commended the efforts of stretching the capital plan out, but would also like to clarify that a lot of the projects are not failing pipes that are ready to blow up or fail. He spoke specifically about the ozonation projects for the treatment plants. Even back seven or eight years, this technology was a little bit risky. Mr. Olive said that the benefits of this project are aesthetics. The agency would use ozone for only half a year when algae is present. The cost for this treatment would be about $40M if you started building in '17-'18. According to Mr. Olive, the cost to maintain a plant like this by then will be about $5M/year. Mr. Olive stated that he believes in doing capital projects, and in preserving our assets. Mr. Olive said that we need to do this, but considering ozone today is ludicrous. He suggested staff go back and take a look at what the real priorities are today in a drought year. Treatment for taste and odor aesthetics is not needed. At a cost of $40M today, he recommends a "no" on that. The last thing he suggested staff consider is Zone 7's project execution track record at about $8M/year at best, so Zone 7 needs to consider how it will execute this volume of projects.

John Archer of Dublin San Ramon Services District said that DSRSD appreciates the opportunity to give Zone 7 these comments and they also appreciate the opportunity to work with staff and the consultants over the last few weeks on this project. DSRSD understands the need for the drought surcharges. DSRSD mentioned in the Finance Committee and to the Board last year that they support a surcharge of some type but DSRSD specifically recommends that it have a sunset – a very specific date so that the customers understand that it's not going to be there forever and ever. That's something that DSRSD has heard at its board meetings. As to the fixed component and restructuring, they understand the comments about having a fixed component, but from their standpoint the rate is blending in and it's a line item in their rates. A deadline of January 1 is troublesome and DSRSD is willing to consider waiving the contract requirement to allow more time. DSRSD supports the effort to use debt to help fund the big projects.

Kathy Narum, Councilwoman from the City of Pleasanton, said that the rate that Pleasanton is currently paying is a blended rate of the tiers at $2.31, going up to $3.20. By her math, that is a 38.5% increase, and a really tough sell to Pleasanton residents. She said that the new rate structure is complicated and the public is not going to understand it, especially if Zone 7 doesn't do a drought surcharge with a sunset at the end of year and then reevaluate the position. Pleasanton supports and will certainly defend the fact that Zone 7 needs to have operating reserves. Pleasanton had the same issues in its enterprise funds. Regarding the rate structure, Ms. Narum asked that staff take more time working with the retailers to ensure it is fair and equitable.

Alfred Exner, 266 Sanderling Way in Pleasanton, thanked the Board and staff, saying that this presentation was much better than the original workshop. As he understands it there are about 70 entities that get untreated water. He wonders if there a methodology for splitting the fixed costs and the variables costs between these two entities, untreated and treated water.

Ms. Duerig clarified that untreated water is not part of this study. Untreated users are served straight off the South Bay Aqueduct. The untreated water customers pay for their own turnout maintenance and turnout construction. Zone 7 basically does a pass through, charging them what the state charges Zone 7 plus a small administrative charge. Zone 7 has no pipes to them, no treatment plants and no pump stations, nothing. It's a direct charge. This study is more about the treated water system and the kinds of projects needed to maintain, improve or operate the treated water system.

President Palmer pointed out the Water Resources Committee notes from the September 9th meeting included in this agenda packet, where the fourth page outlines possible rescheduling of capital improvement projects. That information includes a discussion of risk of delays.

Director Stevens recommended that staff look at the situation realistically while planning ahead. He suggested going to a tiered system next year, but plan five years in advance for a one year rate increase. Reserves must be in the middle, not at the minimum level. If that means a 42% increase, then it's a 42% increase. He urged staff not to cut corners. Director Stevens said that Zone 7 should have raised rates last year. Staff should consider doing it simply as requested by the retailers.

Mr. Gaur clarified that the first year is an overall 33% increase in revenue with the drought/ conservation surcharge, then the following year it is a 9% increase, including the surcharge and the third year is 7%, including the drought surcharge. It is not 33% each year. This is the year we bite the bullet and then the increases stabilize. The agency can accomplish this in two ways: a percentage increase to increase the revenue or a drought surcharge. The beauty of the surcharge is it is temporary and can sunset. When you do a percentage increase usually it is usually permanent.

Mr. Solitei further clarified in the chart, the rate increase of 33% will actually use an extra $4M of reserves of the fund balance. One of the components of issuing debt is to have reserves, and if you don't have reserves, you can't issue debt. The reason we are going to the third year is because we don't have reserves and cannot issue debt with no reserves.

Director Ramirez Holmes said the numbers have to support whatever change we make. She can support a drought surcharge to cover where we are, as long as staff is responsible for overages and expenses over and above what the Board budgeted. She is in favor of increasing operational reserves and covering that piece, recovering the amount we need. She is uncomfortable with and does not support the 33% increase for 90% of it to sit in a reserve account. She said if Zone 7 is going to charge the rates, they should translate to operational reserves. The drought surcharge should cover the shortfall due to the drought. She will support one year, then looking at it annually. She supports the amount built in for the debt service because Zone 7 will have to have that budgeted as a line item so that Zone 7 can go out for debt. On the expense side she directed staff to tighten up the CIP figure for the actual projects that staff will complete because that will impact what we do. Director Ramirez Holmes requested staff to address the City of Pleasanton's comment about issuing debt. Pleasanton included an entire paragraph about their assessment in its letter to the Board. Mr. Solitei agreed to address that with them.

Director Quigley recommended that staff look at the rate increases of other agencies for comparison. He said that had Zone 7 moved like some of the other water agencies in the neighborhood who had significant increases, we would not be in such a hole now. Zone 7 needs to repair our fixed costs because they represent a majority of our budget. We also have to pay the good folks that keep our system together.

Director Quigley applauded staff and the consultants for what they've put together, particularly page 5 referencing the cost cutting measures and CIP deferrals. The importance of this slide is that it shows how rapidly the reserves have been depleted and the urgency needed to rebuild them. He is in favor of looking at taking a 3-year approach with a sunset.

President Palmer agreed with Director Quigley. Determining what other agencies are actually doing in terms of is informative and necessary. President Palmer suggested looking at a one-year plan with revisit, and to also go across the board for all retailers in terms of spreading it out evenly. Consider what the impact of that would be and is that fair?

Director McGrail said he is really uncomfortable with a 38% increase. He said that the proposal is confusing and suggested going back to the drawing board and explaining in common sense terms that a layperson can understand. What is this going to cost the average Livermore resident for their water? Is it going to be $44 a month or $144?

Mr. Gaur noted that the challenge is that a cliff is coming and it is important to move as fast as possible so we don't jump off of that cliff. Zone 7 is in a "perfect storm" because its rates are 100% variable, California has had the worst drought in recorded history, and on top of that the agency has a large capital improvement need. He appreciates the comments from the board.

Director Greci noted that, unfortunately, we are in the same boat as all other California water agencies. If you don't sell water, you don't make the money you need to cover your costs. We have a mission statement to be reliable. Reliability requires infrastructure. If infrastructure fails, it's going to be worse than a drought. You won't have any water. You can't get carried away and defer a lot of the CIP projects. Our system is antiquated – it needs constant maintenance and updating. In this CIP plan there is no gingerbread. We have analyzed it and deferred projects for the last two years to cut costs, to deal with the shortfall of funding. You have to draw a line in the sand where you stop cutting costs on maintenance. That is as important as getting the water from the state. If the state doesn't supply the water to us, which is what has happened the last three years – they've been cutting way back because they don't have it – we've done proactive things like storing water because our valley has the capability to recharge our basin. That's our most important reserve, not money. It's another reserve that we have to draw on, but we can only draw so much before we have to replenish. Reserves are important to keep the business going. A sensible reserve in this situation – how do you say what's sensible? We are dealing with a lot of variables tonight. This is a variable business. It varies on the amount of water we sell, it varies on the amount of water we get from the state, and it varies on how much water the people use. Our community has been extremely prudent in conservation – this whole valley – way beyond what the state mandated – some cities as high as 34% to 37% cutback. We encourage conservation and that may sound kind of stupid, but we encourage people not to buy water. That hurts us. Are we smart enough business people that we can deal with that shortfall? We try to be. One of our big mistakes is we didn't implement a bigger rate increase the last go around when it came before this board. We should have and we learned a lesson from it. We wouldn't be as bad off as we are now if we had implemented that rate increase last year. This is more difficult because it's so complicated. Director Greci added that he has been on this board for 21 years and thinks this is the most trying time in his history on this board. He then applauded Director Ramirez Holmes for her attention to detail and intelligent questions. Director Greci agreed with Director McGrail that the proposal is very complicated. We need to recharge our basin and that means buying more water and spending more money. We've been pulling on our reserves for the last couple of years and now they're getting low. Director Greci said we need to catch up on revenues and we need to rebuild our financial and groundwater reserves. He'd like to see more information and to have the proposal in a more simple form because people come and ask for explanations. Director Greci said that we get out of this board room and you're visiting with people or they call you up and say what's going on? You're going to charge a 33% increase over three years? Director Greci said that everyone in this room is on city water – most of board members, too – but board members understand the need for increases. We didn't do it last year but a consultant tells us that's what we really need to do now, so we better do it.

<u>Item 11 – Committees</u>

Water Resources Committee Meeting – September 9, 2015 – notes
Finance Committee Meeting – September 10, 2015 – notes pending

<u>Item 12 – Reports – Directors</u>

a. Verbal comments by President:
b. Written report by Director Quigley
c. Verbal reports

President Palmer said that she went to a LAFCo meeting this week and Zone 7 received an achievement award from the Board of Directors of the California Association of the Local Agency Formation Commissions. CALAFCo presented the Government Leadership Award to Zone 7 and its partners, the Cities of Dublin, Livermore, Pleasanton, San Ramon, and DSRSD for developing the Tri-Valley Intergovernmental Reciprocal Services Master Agreement, as an example of working together and furthering good government efforts. The award will now become part of the Zone 7 wall of fame.

Item 13 – Items for Future Agenda - Directors

Director Figuers suggested that staff put an item on the agenda for next month to discuss eliminating the Drought Contingency Fund. Ms. Duerig recommended bringing the item to the Finance Committee first before bringing the item to the full board so that there can be a full discussion of the reserve policy.

Item 14 – Staff Reports (Information items. No action will be taken.)

a. General Manager's Report
b. Legislative Update
c. Outreach Activities
d. School Report
e. Drought Update
f. Verbal Reports

Director McGrail asked who Cota Cole Attorneys are. David Aladjem, Counsel, replied that Derek Cole with Cota Cole is an attorney who specializes in SMARA, and staff is trying to get additional information in how they might deal with some of the Chain of Lakes issues.

Director McGrail asked if Zone 7 has completed the lease on the Del Valle property. Ms. Duerig responded that it has not yet been executed; however, negotiations are proceeding and it seems to be getting close to the point where at least staff is comfortable and will be able to share with the attorney who has not yet seen it. Director McGrail said he would like to see the lease before it is executed.

Item 15 – Adjournment

President Palmer thanked everyone present for attending the meeting. There being no further business, President Palmer adjourned the meeting at 9:38 p.m.