

TO: BOARD OF DIRECTORS
FROM: BRUCE BUEL *BBB*
DATE: AUGUST 8, 2008

AGENDA ITEM
E-4
AUGUST 13, 2008

OPTIONS FOR PROVIDING WATER SERVICE TO BLACKLAKE

ITEM

Receive report from Finance and Audit Committee and consider options for providing water service to Blacklake [PROVIDE POLICY GUIDANCE].

BACKGROUND

On July 23, 2008, your Honorable Board referred the development of a scope of work and options for providing water service to Blacklake that avoid negative rate impacts on Town water customers to the Finance and Audit Committee. Attached are the minutes from the Committee's August 5, 2008 Meeting. The Committee is scheduled to meet again on Friday August 8, 2008 and staff will forward minutes of that meeting to the Board prior to the August 13, 2008 Board Meeting. Director Vierheilg and/or Director Harrison may wish to comment at the Board Meeting.

From staff's perspective none of the four proposal currently under consideration address the fundamental issue of potential negative impacts on Town Water System customers. Each option may provide one data point to plug into a larger examination of negative impacts (See attached July 14, 2008 Reed proposal as an example of such a study). Staff expects that Bob Reed will be available when this item is considered to discuss options for quantifying this issue. It may be possible to limit the scope of the study to reduce cost yet provide the needed information.

RECOMMENDATION

Staff recommends that your Honorable Board receive the Committee's reports; interact with Bob Reed and then provide policy guidance regarding next steps. Should your Honorable Board wish to pursue the larger study at this time, staff respectfully requests guidance on negotiations with Mr. Reed or development of an RFP.

ATTACHMENT

- Minutes from August 5, 2008 Finance and Audit Committee Meeting.

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MINUTES OF THE 8/5/08 MEETING OF THE FINANCE AND AUDIT COMMITTEE

1. CALL TO ORDER, ROLL CALL AND FLAG SALUTE

Chairman Vierheilg called the Special Meeting to order at 1:00 p.m. in the NCSD Board Chambers. Both Chairman Vierheilg and Director Harrison were in attendance along with staff members Bruce Buel and Lisa Bognuda. There were also six members of the public present, including Ian Wallace, Curt Curtis and Bill Petrick as representatives of the Blacklake Village Master Association Board of Directors and Pat Eby, Cliff Trotter and Bill Nelson as individuals.

2. DEVELOPMENT OF MERGER STUDY SCOPE OF WORK

- A. RECOGNIZE BLACKLAKE REPRESENTATIVES – Chairman Vierheilg recognized Ian Wallace, Curt Curtis and Bill Petrick and thanked them for their service.
- B. SET GROUNDRULES FOR DISCUSSION – Chairman Vierheilg announced that this meeting was a “Brown Act” meeting and that the two NCSD Directors were compelled to comply with state law. He further stated that he was suspending the three-minute rule as it applies to public comment.
- C. DEFINE OUTCOME/GOAL FOR STUDY – Larry Vierheilg proposed that the goal of the study was to achieve an equal starting point so that neither fund subsidized the other. He also hoped that this process would produce a proposal acceptable to Blacklake’s property owners so that the second protest proceeding would be the last. Ian Wallace objected to the work “subsidize” and requested a definition. General Manager Buel indicated that the Board’s definition was a proposal that avoided an increase in combined system water user fees above the user fee that either fund would pay as a stand-alone system. Curt Curtis objected to that goal stating that it was beyond the group’s ability to calculate. Jim Harrison supported the goal of finding a buy-in charge that had no negative impacts. Bill Petrick objected to paying any more to consultants to achieve an outcome.

Pat Eby objected to the work “Merger” and expressed her belief that the two systems were already merged. She proposed that the group use the word “Combined”.

- D. DEFINE STANDARDS FOR DETERMINING OUTCOME/GOAL – Chairman Vierheilg proposed that proposals focus on determining the amount of funding necessary for the two divisions to achieve an equal starting point. Bill Petrick proposed that the outcome be measured in hard data and not hearsay.

Pat Eby proposed that the group agree that Blacklake is fully built-out and that the Town has some expansion capability. Jim Harrison inquired about the Rossi

development proposal and questioned the relevance of making the requested findings. Committee discussion followed on Rossi's proposal.

- E. DISCUSS APPLICABILITY OF TOWN WATER CAPACITY FUND 700 – Curt Curtis expressed his opinion that inclusion of Fund 700 in the Town's Asset balance was not fair or equitable given that Blacklake had no ability to grow. Bill Petrick agreed with Curt Curtis but observed that Town's Fund 700 was only relevant if an asset evaluation methodology was used. Curt Curtis stated that Blacklake felt that there was an implied agreement between the NCSD Board and the Blacklake Village Master Association Board in early 2007 to merge the two systems without a Buy-In Charge and that NCSD had told Blacklake that there were sufficient funds in the Blacklake Water Fund to avoid a buy-in charge. Bill Petrick proposed that the NCSD Board cause District Legal Counsel to opine on whether or not there was an implied agreement and if so, whether Blacklake had any obligation to pay any buy-in charge. Bruce Buel summarized the history of NCSD's efforts to process the merger and indicated that Blacklake representatives participated in the development of the scope of work for the Reed Equity Surcharge calculation before the Blacklake Village Master Association Board wrote its April 2007 letter agreeing to further evaluation of the potential merger. Bill Petrick stated that the only cost that NCSD ever proposed for the merger was the \$180,000 in plumbing costs set forth in Boyle's February 12, 2007 Comparison Memo. Jim Harrison disagreed with Bill Petrick and expressed his opinion that the February 12, 2007 Comparison Memo focused only on plumbing and not the total merger cost. Bill Petrick argued that Blacklake would get no benefit from Town's Fund 700 assets. Jim Harrison disagreed and cited the proposed use of Fund 700 funds to pay for the Frontage Road upgrades as part of the Waterline Intertie Project as an example of how Blacklake would benefit from these assets if the two systems were merged. Chairman Vierheilig agreed to request that the NCSD Board pay District Legal Counsel to render an opinion on whether or not there was an implied agreement between NCSD and the Master Association such that the merger would occur without a buy-in charge.

Pat Eby requested that NCSD document who paid what and when so that all Town System Fund 700 assets are tracked. She also expressed her opinion that Blacklake would derive no benefit from Town's Fund 700 assets should the two systems be merged.

- F. DISCUSS BLACKLAKE WATER CAPACITY FUND 700 – Chairman Vierheilig distributed a 7/29/08 memo from Lisa Bognuda documenting the history of funding for the construction of the Sundale Well and the 4" intertie. Discussion followed on the use of the fund and the short-term nature of the fund.
- G. DISCUSS SUNDALE WELL – DEFINE ISSUES; OBTAIN DATA – Committee discussion followed on water production from the Sundale Well and the limitations on that production. Curt Curtis objected to limiting Blacklake's access to the Sundale Well for emergency use only. Jim Harrison likened the Sundale Well to an insurance policy – the subscriber pays for the premium even though payout only occurs when there is an emergency. Bill Petrick expressed his opinion that the limitations were a gray area subject to interpretation.

Pat Eby requested more time to review the Bognuda Memo and asserted that NCSD should pay Blacklake for use of Blacklake's water. She also asserted that Blacklake has reduced its aggregate consumption by 15% and Blacklake should not be required to participate in payment of the Waterline Intertie Project. Bruce Buel noted that the Court Settlement called for NCSD to reduce its aggregate pumping by 83% and that all NCSD customers would be required to pay for the new supply.

Bill Petrick indicated that the Technical Group could increase or decrease the amount of supplemental water to be imported.

Bill Nelson indicated that his previous statements regarding Villagio's contribution to the Sundale Well should have been the Oaks and Estates.

- H. DEFINE APPROACHES TO ACHIEVE OUTCOME/GOAL – Ian Wallace asked that Defensibility be added to Applicability and Reasonability as review criteria. Curt Curtis proposed to re-look at the Reed Study with subtractions of all or some of the Town Water Fund 700 from the Town's asset total. Bill Petrick agreed with Curt Curtis and added that the Reed Study could be simplified by eliminating select rows and discounting the value of Town's Fund 700 assets.

Pat Eby distributed spread sheets illustrating her proposal to base the buy-in charge on the differential between what Blacklake and Town water customers paid historically.

- I. DISCARD NON-VIABLE APPROACHES – Curt Curtis proposed that NCSD look at modifying the Reed Study. Larry Vierheilig observed that agreement needed to be reached regarding the base period for evaluation of alternatives. Bill Petrick argued for June 2006 as the agreed upon base period and observed that later base periods included the expenditure of Blacklake funds on the 8" intertie.

Pat Eby indicated that modifications to the Reed Study would not be acceptable to Blacklake and that her proposal was simpler and more easily understood.

- J. EVALUATE REMAINING APPROACHES – Chairman Vierheilig asked Bruce Buel if the Committee had achieved the Board Goals. Bruce Buel answered that the Board had expected the Committee to propose options and to propose a mechanism to examine whether or not those options avoided subsidies. Jim Harrison and the Blacklake Representatives agreed that the Committee needed to at least list options so that the Board could comment.

- K. DISCUSS PROCESS FOR REACHING CLOSURE – Following extensive discussion, the Committee agreed to discuss at least the following four options:
1. Implied Agreement that there be no buy-in charge
 2. Modifications to Reed Study
 3. Pat Eby proposal
 4. Larry Vierheilig II Proposal

In regards to the Larry Vierheilig II Proposal, Bill Petrick requested that 2006 be used as the base period and that both the Blacklake and the Town reserves be evaluated.

Bill Petrick indicated that he favored #2 or #3 over #4 and he felt that #4 may not be necessary given that #2 and #3 would likely come out with the same approximate Buy-In Charge as #4. He indicated that the likely consensus Charge appeared to be around \$300 per equivalent 1" meter. Bruce Buel indicated that any such convergence would also need to be evaluated for subsidies to comply with the Board's objective. Curt Curtis objected to evaluation for a subsidy on the basis that such a study was beyond the capability of the Committee. Bill Petrick expressed his belief that it would not be possible to determine if rates would be higher given the magnitude of the budgets involved compared to the aggregate contribution resulting from a buy in charge.

3. SET NEXT MEETING DATE

The Committee agreed to meet again at 1:00 p.m. on Friday August 8, 2008.

The meeting was adjourned at 3:45 p.m.

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July 14, 2008

Bruce Buel
Nipomo Community Services District
148 South Wilson Street
P. O. Box 326
Nipomo, CA 93444-0326

Subject: Proposed Contract Amendment for Water System Financial Plans and Equity Analyses

Dear Bruce,

The Reed Group, Inc. has been working with the District to prepare a variety of water and sewer financial plans and rate/fee updates. Recently, you asked that we amend the scope of services to include developing financial plans to evaluate the potential implications of combining the Town and Blacklake water systems, relative to maintaining two independent systems. A description of the proposed scope amendment, along with cost and schedule information, is presented below

Scope of Services - Water System Financial Plans and Equity Analyses

In 2007, The Reed Group, Inc. assisted the District in preparing a five-year financial plan and rate recommendations for a combined water system. Findings and recommendations of that effort were contained in a report dated September 14, 2007. Since that time, the District has been further evaluating the advantages, disadvantages, and potential impacts of the proposed consolidation of the Town and Blacklake water systems. As a result, further analyses are needed to fairly and comprehensively assess the potential financial implications of combining the two water systems (including assessing a potential Blacklake equity surcharge). At this time, the District would like to prepare 5-year financial plans for the Town and Blacklake water systems as independent utilities (status quo), as well as for a combined water system. The proposed contract amendment would cover this new task.

Specifically, this contract amendment will include:

- Developing five-year financial plan models for (1) the Town water system, (2) the Blacklake water system, and (3) a combined water system using the FY 08-09 budgets, FY 07-08 year-end fund/reserve balances, capital improvement plans, and other



information provided by the District. The models will be extended through FY 12-13 and will be used to assess issues related to the proposed consolidation.

- Using the financial plans to determine annual water rate revenue requirements under each financial plan. Consideration will be given to operating and maintenance costs, capital program needs, debt obligations, reserves and reserve policies, potential equity surcharges, and other issues identified by the District.
- Developing water rate schedules for each financial plan. Rate schedules will be based on the current rate structures and revenue requirements determined from the financial plans.
- Making presentations in up to three meetings with the Board of Directors and/or community meetings with customers.
- Preparing a draft report describing financial plan assumptions and information, and describing findings and conclusions. The report will describe the potential financial impacts of combining the two water systems from perspectives of both Town and Blacklake customers.
- Finalizing the water system financial plan analyses and conclusions in a final report based on staff comments and Board direction.

Estimated Cost for Water Rate Structure Analysis

At this time, we estimate that the cost of the requested water system financial plans and equity analyses to be \$22,000, including expenses. Expenses for three trips to the District are included in this estimate. However, in an effort to minimize travel costs, we will strive to conduct the study such that an initial meeting with the Board of Directors to identify water system consolidation issues occurs on the same day the Board is considering water system capacity charges (currently scheduled for August 13, 2008). My hourly billing rate for 2008 is \$215 and is subject to revision each January. As you know, it is our practice to bill only for the actual time and expense required for the project subject to the not-to-exceed limit of our agreement.

Information Request

In order to facilitate the start of this project, below is a list of information that will be needed to begin the water system financial plan and equity analyses study. We have already received the proposed FY 08-09 budget document.

- Town and Blacklake customer data from the utility billing system including APN, location, water class code, and 12-month usage history (FY 07-08).
- Five-year Town and Blacklake water system capital improvement plans.



Other information may be requested once we begin the study.

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If the above work is approved it would amend, and be completed in accordance with other terms of, the Agreement for Rate Studies approved by the District on May 9, 2007. Please let me know if you have any questions regarding this proposal. We appreciated the opportunity to be of continued service to the District.

Sincerely,

Robert Reed
The Reed Group, Inc.