

# BAWSCA

Bay Area Water Supply & Conservation Agency

## BOARD POLICY COMMITTEE

December 12, 2012

1:30 p.m.

BAWSCA Offices, 155 Bovet Road San Mateo, 1<sup>st</sup> Floor Conference Room  
(Directions on page 2)

### AGENDA

<u>Agenda Item</u>	<u>Presenter</u>	<u>Page #</u>
<b>1. <u>Call To Order, and Roll Call</u></b> Roster of Committee members ( <i>Attachment</i> )	(Klein)	Pg 3
<b>2. <u>Comments by Chair</u></b>	(Klein)	
<b>3. <u>Public Comment</u></b> <i>Members of the public may address the committee on any issues not listed on the agenda that are within the purview of the committee. Comments on matters that are listed on the agenda may be made at the time the committee is considering each item. Each speaker is allowed a maximum of three (3) minutes.</i>	(Klein)	
<b>4. <u>Consent Calendar</u></b>	(Klein)	
A. Approval of Minutes from the October 10, 2012 meeting ( <i>Attachment</i> )		Pg 5
B. Appointment of BAWSCA Representative and Alternate to ACWA/JPIA ( <i>Attachment</i> )		Pg 29
<b>5. <u>Reports and Discussion Items</u></b>		
A. Mid-Year 2012-13 Work Plan and Budget Review ( <i>Attachment</i> ) <u>Issue:</u> What adjustments are needed to complete planned and anticipated work during FY2012-13? <u>Information to Committee:</u> A memo and oral presentation on FY 2012-13 Work Plan and budget, projected year-end spending, the estimated year-end General Reserve balance and the need for and timing of decisions for managing the General Reserve balance. <u>Committee Action Requested:</u> Discussion	(Jensen)	Pg 33
B. Fiscal Year 2013-14 Work Plan and Budget Preparation <u>Issue:</u> What critical results need to be achieved next year and what resources will be required? <u>Information to Committee:</u> An oral report on challenges that must be considered in preparing the FY 2013-14 preliminary Work Plan and budget. <u>Committee Action Requested:</u> Discussion of issues that must be addressed during FY 2013-14.	(Jensen)	

**6. Reports****(Jensen/Sandkulla)**

- A. Bond Issuance to Prepay Capital Debt Owed to SFPUC – Status Report
- B. Long-Term Reliable Water Supply Strategy – Pilot Water Transfer Status Report
- C. SFPUC Water Supply Improvement Program – Status Report
- D. Board Policy Calendar (*Attachment*)

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**7. Comments by Committee Members****(Klein)**

- 8. Adjournment to the next meeting on February 13, 2013 at 1:30pm in the 1<sup>st</sup> floor conference room of the BAWSCA office building, at 155 Bovet Road, San Mateo.**

**(Klein)**

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**Directions to BAWSCA**

From 101: Take Hwy.92 Westbound towards Half Moon Bay. Exit at El Camino Northbound (move into the far left Lane) Left at the 1<sup>st</sup> stop light which is Bovet Road (Washington Mutual Building will be at the corner of Bovet and El Camino). Proceed West on Bovet Road past Albertson's to two tall buildings to your left. Turn left into the driveway between the two buildings and left again at the end of the driveway to the "Visitor" parking spaces in front of the parking structure.

From 92: Exit at El Camino Northbound and follow the same directions shown above.



**BAY AREA WATER SUPPLY AND CONSERVATION AGENCY**  
**BOARD POLICY COMMITTEE**

**Committee Roster:**

Larry Klein, City of Palo Alto (Chair)

Rob Guzzetta, California Water Service Company (Vice-Chair)

Ruben Abrica, City of East Palo Alto

Robert Anderson, Purissima Hills Water District

Randy Breault, City of Brisbane/GVMID

Jamie McLeod, City of Santa Clara

Irene O'Connell, City of San Bruno (BAWSCA Vice Chair)

Tom Piccolotti, North Coast County Water District

Barbara Pierce, Redwood City (BAWSCA Chair)

John Weed, Alameda County Water District

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**BAY AREA WATER SUPPLY AND CONSERVATION AGENCY**

**BOARD POLICY COMMITTEE**

**October 10, 2012 – 1:30 p.m.**

**BAWSCA Offices, 155 Bovet Road, San Mateo, 1<sup>st</sup> Floor Conference Room**

<b>MINUTES</b>
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**1. Call to Order: 1:30 p.m.**

Committee Chair Larry Klein called the meeting to order at 1:30 pm. A list of Committee members present (8) and absent (2), and of other attendees is attached.

The Committee took the following actions and discussed the following topics:

- 2. Comments by Chair:** Chair Klein noted that the agenda includes a significant item on the bond issuance. He wants the committee to feel comfortable with its recommendation to the Board, and therefore expects a thorough discussion.
- 3. Public Comments:** There were no public comments.
- 4. Consent Calendar:** Approval of Minutes from the August 8, 2012 meeting.

**Director Anderson made a motion, seconded by Director O’Connell, that the minutes from the meeting of August 8, 2012, be approved. The motion carried with one abstention (McLeod).**

**5. Action Items:**

A. Potential Bond Issuance to Prepay Capital Debt Owed to SFPUC: Mr. Jensen pointed out additional details on the set of recommendations being presented to the Committee. He explained that:

- 1) Work is continuing and the recommendations that will go to the Board in November will have more detail than what is currently available for presentation to the Committee.
- 2) There are certain things that cannot be known or may remain unknown even by the November Board meeting. For example, Mr. Jensen noted that after the preliminary credit assessment becomes available, there may be potential opportunities to enhance the bond structure to improve the final credit rating. BAWSCA and its Finance team are working to set parameters that would need to be met before moving forward with a bond issuance.
- 3) Lastly, one recommendation requests the authorization of the CEO/General Manager to execute financing documents at the appropriate time conditioned upon satisfaction of specified criteria. While the specified criteria were noted in the

memo, they were not included in the motion. Following discussion of the item, the Committee will be asked to act on the recommendation as listed on the agenda, but with the addition of 2 conditions:

- a) The bond interest rates and final financing structure will need to result in a net present value savings of not less than \$20 million over the term of the bonds.*
- b) San Francisco must provide, in advance of receiving any funds, a written pledge to use bond proceeds in a manner consistent with federal laws and regulations.*

Mr. Jensen stated that his presentation will go through the key issues of interest to the board members and each agency's financial representatives, as well the current structure of the financial plan. There are some questions on which input is needed from the committee as an advisory body to the CEO and the Board.

Mr. Jensen began his presentation by emphasizing that the objective of the bond issuance remains the same; to help water customers by saving them money on cost of water purchased from San Francisco. This can be achieved if the following conditions are met:

- The bond issuance complies with all relevant laws and rules.
- By securing the best practical credit rating, issuing bonds at the lowest practical interest rates, and with the allocation of debt service being reasonably distributed among the member agencies.
- Financial risk to BAWSCA and its member agencies is low, or significantly greater than under the "no action" alternative.
- A guiding principle is whether the results compare favorably to the "no action" alternative, which is continuing to pay San Francisco at an interest rate of 5.13%.

Mr. Jensen emphasized that the credit ratings and interest rates must be practical because the goal is to strike a balance in enhancing credit ratings and lowering interest rates without spending too much money to do so. He also emphasized his choice of using the word reasonable over fair in reference to the allocation of debt among the member agencies, because the final results should be reasonable for all the member agencies.

In highlighting the objective of keeping the financial risks to BAWSCA member agencies low, and having the results comparable to the "no action" alternative, Mr. Jensen summarized the history of the existing \$360 million debt being repaid to San Francisco through wholesale water rates.

Background -- presentation on source or debt to be paid:

In 1984, Wholesale Customers signed an agreement to pay San Francisco for their share of investments to the capital facilities. The method of repayment preferred by San Francisco at that time was Utility Method, in which San Francisco pays for facilities using current revenues or issuing bonds, and is responsible for paying the bonds off. The wholesale customers would repay San Francisco by paying depreciation and rate of return over the life of facility. A pumping unit has a 15 year lifetime, while a dam may have a lifetime of 200 years or more. Under the Utility Method, Wholesale Customers would repay San Francisco for facilities over several generations.

During the negotiation of the new Water Supply Agreement (WSA), KNN did a study that looked at changing from the Utility Method to a Cash Method. With the Cash Method, Wholesale Customers would pay San Francisco a proportionate share of revenue funded projects and a proportionate of debt service, if the SFPUC issued debt. The payments would be in real time.

At the time the old agreement was about to expire and the new agreement take effect, there was an unpaid debt of about \$360 million for facilities that San Francisco had constructed, and for which the Wholesale Customers had not yet completely paid their share under the old contract. The member agencies and the SFPUC agreed to amortize the remaining debt over the 25-year term of the new agreement at an agreed upon interest rate of 5.13%.

The 2009 Water Supply Agreement also provided that the Wholesale Customers could prepay that debt through BAWSA, in whole or in part, without penalty.

In the fall of 2011, San Francisco proposed that BAWSCA examine prepaying the debt. San Francisco needed the money, and BAWSCA was likely able to borrow money at an interest rate less than 5.13% thereby saving the Wholesale Customers money.

Mr. Jensen clarified that the 5.13% interest rate is NOT a bond interest rate, but an interest rate that is embedded in the Wholesale Customers' agreement with San Francisco.

Director McLeod asked that if the bond issuance moves forward, would BAWSCA member agencies have influence on what San Francisco spends the money on? Mr. Jensen stated that BAWSCA can impose certain requirements: 1) The money cannot be spent on investments that will have a net effect of increasing Wholesale Customers' rates, and 2) there are legal restrictions that San Francisco will have to abide by in the use of tax-exempt proceeds.

Director McLeod asked if there are any other major winners in this transaction besides San Francisco and the Wholesale Customers. Legal Counsel, Allison Schutte, and Fi-

nancial Counsel, David Brodsky, stated that BAWSCA and the SFPUC would get the direct benefits of the bond issuance.

Director Weed commented that in an auditor's perspective, it can be anticipated that San Francisco will have a separate account for the bond funds, which can report how the money in the account is being invested. Mr. Brodsky stated that he expects there would be a separate account for tax purposes since the funds would be subject to rebate.

Ms. Schutte explained that as part of the closing, San Francisco will be required to sign an agreement that dictates where the money will be spent. There will be a suite of projects in the agreement, and BAWSCA will be checking in on San Francisco to ensure they adhere to the terms of the agreement.

Mr. Jensen explained that the bond issuance is for Wholesale Customers to pay the money they owe San Francisco. If BAWSCA and its member agencies choose the "no action" alternative, San Francisco will still receive payments from the Wholesale Customers and spend the money at its own discretion. BAWSCA's requirement of how San Francisco spends the funds from the bond issuance is to the extent that San Francisco complies with the law so that it does not violate BAWSCA's bond covenants.

Ms. Schutte stated that there will be a reporting requirement for San Francisco that can be further highlighted for the Board in November.

Director Weed expressed his concern that the funds will be spent in such a way that will increase wholesale water rates, and suggested to restrict the use of funds on the WSIP projects only.

Mr. Jensen stated that wholesale water rates will be affected if the money is spent on the regional water system for expenses that have not already been anticipated in the rate projection. BAWSCA is working with San Francisco so that there are no unintended consequences that results to higher rates for the Wholesale Customers. Mr. Jensen stated that there will be an attachment to the agreement with San Francisco listing what the expected expenditures will be.

The committee agreed with Director Breault's summary that the intention of the bond issuance is to get the Wholesale Customers' debt to San Francisco acknowledged as "paid" without an unintended consequence of Wholesale Customer rates going up.

Mr. Jensen reported that BAWSCA and its financial team are working to ensure written documents for the bond issuance comply with all applicable laws and rules. The staff memo provided to the Committee identifies the various necessary documents, and included drafts of the Revenue Bond Indenture, First Supplemental Indenture, and Continuing Disclosure Certificate for the Committee's review.



An action item for the Board in November is to authorize the CEO/General Manager to select a Trustee through an RFP process, and authorize the selected Trustee to receive the money. The relationship with the Trustee is codified in the Revenue Bond Indenture.

BAWSCA is securing the best practical credit ratings to ensure member agencies are able to save money. BAWSCA has asked the bond rating agency to evaluate a conservative structure and provide a preliminary credit assessment. Possible enhancements could be considered before requesting a final credit rating.

Some of the characteristics for achieving a positive credit outlook include having a reserve balance equal to 50% of the maximum annual debt service and a secure revenue stream. Mr. Jensen explained that having a secure revenue stream was the reason behind AB 2167. The legislation allows the BAWSCA Board, if it chooses, to authorize San Francisco to do the revenue collection. This is important to the bond buyers as San Francisco's historical billing system is seen as a secure revenue stream.

Mr. Jensen emphasized that the preliminary credit assessment will provide a basis for evaluating potential credit enhancements. BAWSCA wants to issue bonds at the lowest practical interest rate.

In response to Director Klein's question, Mr. Brodsky said that it is not yet possible to know how the bonds will be rated. He reported that Standard and Poor had a positive reaction with BAWSCA's credit picture, and Mr. Brodsky stated that he is confident BAWSCA will get an A or A+ rating.

Mr. Brodsky stated that to get a higher rating, it might be at an additional cost or at the expense of a portion of the savings, and since the goal is to maximize savings as opposed to getting the highest bond rating, a bit of compromise with the rating is practical.

In response to Director O'Connell's question, Mr. Brodsky confirmed that Cal Water has an A+ credit rating. Mr. Brodsky briefly explained that a rating methodology for some entities involves a "bottom-up" look where individual member agencies are looked at for their average credit rating. BAWSCA's bond issuance will be looked at "Top-down" as it is a regional water agency that provides the service to a sizable, productive and largely affluent region.

Mr. Jensen went over a table of the Overall Plan of Finance reflecting assumptions and market conditions as of September 25<sup>th</sup>. The total proceeds of \$383 million from the bond issuance are broken down into Tax Exempt and Taxable Bonds. The total proceeds from the prepayment funds amount to \$367 million. The difference between the bond proceeds and the prepayment funds covers the estimated \$2.1 million cost of issuance and a stabilization fund. Mr. Jensen noted that the stabilization fund is 50% of annual debt services. He emphasized that it is a revenue stabilization fund as opposed

to a rate stabilization fund, and noted that the revenue stabilization fund is important to rate agencies and bond buyers when assessing the risks, determining the credit rating, and establishing interest rates.

The net present value savings for member agencies is estimated to be \$20-\$34 million over the 21 ½ year term of the bonds. The annual present value savings is \$1.0 - \$2.1 million spread out among the 26 member agencies.

For comparison, Mr. Jensen noted that the Wholesale Revenue Requirement that San Francisco collects each year is currently in the neighborhood of \$200 million and will be going up to \$300 million and above, as the WSIP is completed. The repayment of the \$360 million is approximately 10% of the current annual Wholesale Revenue Requirement.

Mr. Jensen stated that an important discussion is how the debt service, and therefore savings, is distributed among the agencies. BAWSCA and the financial team are working to ensure the allocation of debt service is reasonably distributed.

Mr. Jensen continued his presentation explaining that there are two issues to be considered.

The first issue is how to set a surcharge for recovering the debt service from member agencies. The second is how to allocate the interest expense among the member agencies.

Two contrasting methods can be used for setting the surcharge. One method would be to use a volumetric approach, where each agency is charged based on the amount of water purchased during the year. A second method would be to charge each agency a fixed amount, regardless of how much water were used in a particular period.

Each method has advantages and disadvantages.

San Francisco currently uses a volumetric approach to allocating the Wholesale Customers' payments for use of the Regional Water System, including repayment of old debt. The SFPUC's current method for setting wholesale water rates allocates costs proportionate to the amount of water purchased by each agency.

This method can result in under or over collection of revenue, depending on how much water an agency purchases in a given year. Wet years, dry years, economic boom or decline, and conservation efforts can all affect the amount of water purchased. The potential under collection of revenue is seen as a risk to the bond buyers.

A more appealing method to bond buyers would be for agencies to be charged a fixed amount, regardless of how much water is purchased. This approach is certain to recover the necessary revenue each year. This method, however, would differ significantly

from the “no action” alternative in that agencies might pay more or less than they would have paid the SFPUC under the “no action” alternative.

Mr. Jensen presented a slide demonstrating that each individual agency’s percentage of total purchases from San Francisco changes overtime, but cannot be predicted.

The Financing Team has come up with a method that exhibits the advantages of both approaches. The recommended and an anticipated approach to pursue is a modified volumetric approach, in which fixed allocations are set each year, and reconciled the following year based on how much water each agency actually purchased from the SFPUC.

The surcharge could be set for each agency by multiplying the (fixed) annual debt service by each agency’s percentage of total purchases in a prior year (also a fixed, known number).

Each spring, the surcharge could be calculated. Because the amount of revenue received from each agency would not reflect that agency’s purchases made during the current year, reconciliation would be made so that all members would pay their fair share over the term of the bonds.

Mr. Jensen stated that this approach would appeal of the low risk to the bond buyers, and should result in a low bond interest rate. The method should also appeal to the member agencies because the percentage of the debt they would pay would more closely match the percentage they would pay San Francisco under the base case.

Mr. Jensen emphasized that the agencies’ total purchases from San Francisco changes over time because their usage varies over time. Whether it goes up or down, how much agencies are charged will be adjusted. If for example, San Francisco interrupted water service to San Jose and Santa Clara, the amount they had been paying would have to be made up by the remaining agencies. Director Breault commented that it would be the same scenario with the existing revenue requirement, only at a 5.13% interest rate. Mr. Jensen agreed.

Mr. Jensen noted that in developing a structure for setting the charges, it is important to have a plan that works today and that can be modified in the future. If, for example, Santa Clara and San Jose’s services were interrupted, or ACWD’s consumption goes down as much as 50%, the board should have the ability to consider revisions to the method for setting surcharges.

Mr. Jensen noted it would be to the member agencies’ advantage if the allocation of debt service was not a part of the bond covenant. If it were, it would be locked in for 21 ½ years and cannot be changed. Additionally, if the board chooses to finalize the allocation of debt service before it acts on the bond issuance, the potential chances to enhance the credit rating would be eliminated.

Director McLeod asked about the potential loss of the interest earnings if there is a major difference between agencies' payments and later adjustment. She noted that if an agency takes a big step down, they are going to lose the value of that money for the next 2 years, and get the old value following reconciliation.

Mr. Jensen stated that such effects should be relatively small and that the value of fine-tuning the calculations would be less than the effort to do so.

Director Guzzetta suggested the Committee keep in mind the magnitude of the dollars being discussed in comparison to the \$300 million revenue requirement that Wholesale Customers have to pay San Francisco every year. That amount increases every year. The distribution of savings amounts to less than 2%.

Director McLeod stated that for some jurisdictions and their annual budget, some of those small incremental numbers mean whether or not to close a library. It is worth having the discussion and having everyone realize and agree in the end, that the money could be lost over time. Director McLeod pointed out that even though it's an incremental amount of money, it's real money for some jurisdictions.

Mr. Jensen acknowledged the importance of the dollars for each jurisdiction, and noted that the Board will be provided information that shows the estimated savings to each agency.

Director Guzzetta stated that while he understands that one can look at the dollar savings in the context of their annual budget, it would be difficult to estimate the demand within the level of accuracy of what this dollar savings will be.

Director O'Connell commented that without the bond issuance, BAWSCA member agencies will have no savings, plus an increasing revenue requirement every year.

Mr. Jensen continued his presentation explaining the second issue is how interest expenses could be distributed among the member agencies.

Mr. Jensen noted that BAWSCA's bond issuance will include both taxable and tax-exempt bonds, which have different interest rates. The question is how should interest costs be allocated to member agencies.

Mr. Jensen explained that San Francisco has been generally able to issue tax-exempt bonds for nearly all the cost of the WSIP because the total purchases of Cal Water and Stanford from the Regional Water System amount to less than 10% of system-wide water sales. San Francisco has issued a small amount of taxable debt in recent years.

BAWSCA would not be able to do issue only tax-exempt bonds because Cal Water and Stanford's purchases from the Regional Water System amount to more than 20% of the purchases of the BAWSCA agencies alone (not counting San Francisco). As a result, BAWSCA's bond issuance will need to issue some taxable debt.

With a uniform distribution of interest payments among all the members, publicly-owned agencies would pay a portion of the higher taxable interest rates. BAWSCA and the Finance Team analyzed the significance of the different types of approaches.

A comparison was made between a blended or uniform debt service allocation and a non-blended debt service allocation, where public agencies would pay the tax-exempt interest rate and Cal Water and Stanford would pay the taxable interest rate. The difference in savings represents \$5 million in present value over the 21 ½ years.

The exact size of the additional increment to public agencies depends on various factors including how the debt service is allocated.

Mr. Jensen presented a table that showed the comparison of savings for the public agencies and the private agencies when using the blended versus non-blended debt service allocation.

Mr. Jensen stated that he is presenting the conclusions and considerations gathered from the analysis to provide the committee with objective information and to obtain the Committee's input to the CEO and the Board.

The analysis shows that all agencies would save money with either approach under current market conditions. Currently, the taxable and tax-exempt interest rates are fairly close. If the taxable interest rate were to rise significantly, it would be less advantageous for Cal Water and Stanford to participate. In the extreme, they might be better off continuing to pay San Francisco 5.13% interest. This possibility appears unlikely at this time.

Mr. Jensen went over the following issues that should be considered before making a decision:

- What is the principal behind privately-owned utilities being charged a different interest rate?

The simple answer is because they are profit-making organizations. However, under California Public Utility Commission (CPUC) regulation, privately-owned utilities are only allowed to make a rate of return on capital investments they make in their own water systems, as an incentive to maintain and improve their infrastructure. The CPUC does not allow privately-owned utilities to mark-up operating costs, such as the cost of buying water from the SFPUC. Those costs are passed on directly to the residential or business customers. Because BAWSCA's surcharge to pay debt service would be considered an operating cost, Cal Water will make no profit from BAWSCA's issuance of bonds.

- Does the SFPUC issue taxable debt and how are interest costs allocated?

Mr. Jensen reported that San Francisco has issued taxable debts in the form of commercial paper. The difference in interest rates, while small, has been allocated to all Wholesale Customers through the uniform wholesale water rates set by the SFPUC.

- What would be the significance of interest rates to a typical residential water bill?

The difference between a blended and non-blended interest rate for a typical residential water bill would be about \$0.25 per month. That value represents an average over the service area, based on average water use in FY 2010-11.

- Are there other inherent subsidies in the existing SFPUC rates, and in any water utilities' rates?

Mr. Jensen stated that while this is not an issue over which BAWSCA has authority, it is important to recognize that Wholesale Customers currently pay a uniform rate to San Francisco to cover all costs of running and maintaining the Regional Water System, including their two-thirds share of the \$3.6 billion for rebuilding the system.

Mr. Jensen noted that the Board has never had to deal with the issue of interest rate allocation before. In the past, the board has set charges by allocating costs in proportion to usage amongst the membership, as has been done for annual assessments, and as was done for the water management charge. On other issues, such as subscription water conservation programs, the Board has allocated costs to the beneficiaries of those programs. The Board retains the authority over how future water management charges might be allocated.

Mr. Jensen asked for the Committee's comments and discussion of the issues presented.

Director Klein stated that he had the same concerns that were raised by Committee members during the presentation, but feels that when taking into account the present value, some of the fine tuning of the process would require more accounting expense than the savings. He stated that government subsidies widely exist, and that at some point the analysis should stop so that the quest for a perfect result does not prevent achieving a good result.

In response to Director Weed's questions, Mr. Brodsky stated that the bond issuance will be two series of bonds, one tax-exempt and one taxable. Both series of bonds will be secured by the same revenue pledge. Mr. Brodsky stated that one large pool would create a stronger credit than two entirely separate pools.

From the standpoint of the taxable bonds, Director Weed asked if there would be some way that the issuance of bonds for privately-owned entities could be structured as a

capital investment, on which they would pay higher interest but be able to make a rate of return.

Mr. Brodsky stated no, for the same reason that the expense is going to be viewed as an operating cost for both the publicly-owned agencies and the privately-owned agencies, rather than as a capital investment.

Director Weed pointed out that in the overall structure, San Francisco is still going to get the money and have the freedom to spend it, with limited restrictions.

Director O'Connell noted that the bond issuance is to pay money owed to San Francisco that Wholesale Customers would be paying under the "no action" alternative. The difference is, it is at a better interest rate for the Wholesale Customers.

Director Weed stated a traditional bond is pledged against a certain asset. Even though it stays within the water enterprise, as Mr. Brodsky stated, the money San Francisco gets from the bond issuance is still not pledged against an asset, which is what a traditional use of a bond is.

Director Anderson commented that the important point he got from reading the documents is that the agencies are not individually liable. The rest of the reading requires professional explanation but he feels comfortable to make a motion for recommendation #4A) authorize the GEO/General Manager to execute these financing documents at the appropriate time conditioned upon satisfaction of specific criteria.

Mr. Jensen clarified that recommendation #4A includes two provisions which are conditions on the CEO/GM to enable or trigger the bond sale.

The two provisions are:

*1) The bond interest rates and final financing structure will need to result in a net present value savings of not less than \$20 million over the term of the bonds; and 2) San Francisco must provide, in advance of receiving any funds, a written pledge to use bond proceeds in a manner consistent with federal laws and regulations.*

For the first criterion, Mr. Jensen asked for input on what number might represent the lowest acceptable net savings for proceeding with the bonds. He said the lower estimate of potential savings is \$20 million, but it would not make sense to abandon the effort if the savings would be only \$19.9 million. Should the Board consider \$10 million? Mr. Jensen stated that the number can't be determined on a savings per agency basis but rather, on the aggregate. Whatever the number is, it ought to be several times larger than the cost of issuance estimated at \$2.1 million.

The second criterion relates to tax laws that restrict how San Francisco may use proceeds from tax-exempt bonds. The criteria can reference the agreement BAWSCA is

currently negotiating with the SFPUC. This provision of that agreement will protect BAWSCA and its member agencies against unintended consequences.

Director Guzzetta pointed out that if Cal Water were charged the higher interest rate, it would have no effect on the company or its shareholders. It would affect its customers because the cost is a simple pass through from Cal Water to its customers. The fairness issue is that Cal Water customers should pay the same as all the other customers.

Director Pierce commented that all Wholesale Customers are currently paying its debt owed to San Francisco at a uniform 5.13% interest rate.

Director O'Connell noted that the recommendation does not include a decision on setting the rates, and asked when it will be brought to the board.

Mr. Jensen explained that the Board will receive a specific recommendation at its November meeting. At this time the matter before the Committee does not include a recommendation on the how debt service should be allocated because work has been ongoing and input from the Committee is desired at this time.

Mr. Jensen also stated that the Board should not take an action that might limit BAWSCA's ability to enhance its credit rating once the preliminary credit assessment has been received. If there are opportunities to enhance the credit rating, it would be in the agencies collective interest to allow the CEO/General Manager to achieve that. The wording of recommendations to the Board should avoid limiting the Board's ability to make prudent revisions over the 21-year term of the bonds.

Mr. Jensen stated that he is not asking the Committee or the Board to provide an open-ended authorization, nor is he intending to take a move or action that would be perceived as unfair to any of the agencies. But it is in the agencies' collective interest not to restrict its flexibility by being overly specific at this time.

Mr. Brodsky stated that the modified volumetric approach is technically the stronger credit and will translate into additional savings. It might be in the form of a higher credit rating or a lower reserve requirement, or even in the form of market recognition. But, to be able to confidently present to the rating agencies will bring a positive credit result.

Mr. Brodsky added that the tax issue will not be a credit factor for the rating agencies. The rating agencies' investors will care about how they get paid back. They will not necessarily care how what the method of pay back is, but if we want to have the advantage of the modified volumetric method, BAWSCA would have to commit to a billing system in which a fixed amount is levied against each member every year.

Director Klein expanded on Mr. Jensen's comments and stated that while there are four specific recommendations for the Committee to act on under the agenda item #5A, ad-



ditional motions or motions to amend a recommendation by members of the Committee is appropriate.

Director Weed made 3 points of clarification. First, that the proposed savings be expressed as a percentage with an approximate dollar value. A percentage is an easier reference point than just a dollar amount. Second, to clarify that the length of the bond is the same as the length of payback, which is 21 ½ years. Third, that BAWSCA should have the ability to refinance the bonds in 10 years.

After discussion, the committee agreed to amend the wording of the first criteria under recommendation #5A-4 based on Director Weed's clarification point about the percentage of savings.

**Director Weed made a motion, seconded by Director McLeod, to amend the first criteria under recommendation #5A-4 so that it states that the result savings will include a percentage value of 4% of the present outstanding debt owed to San Francisco, or \$15 million. The Committee approved the motion with 7 ayes and 1 abstention (Anderson).**

Director Weed added that in November, the Board should be presented with the anticipated bond structure with a term equal to the payback length of 21 ½ years, and with the ability to refinance after the standard period of 10 years. This is a guideline as opposed to conditions.

Ms. Schutte noted that these issues are fundamental to the structure of the bond deal and will be in the draft bond documents. She will work with Mr. Jensen to ensure that in November, the Board is presented with the clear structure of the bond, including the term, call provisions and other critical items.

Director Breault made an observation about the table that compares the blended and non-blended approach for allocating interest. The blended approach provides public agencies that represent 75% of water purchases, with 75% of the savings. Cal Water and Stanford represent 25% of water purchases, and would receive a 25% of the savings. The non-blended approach provides Cal Water and Stanford with a 10% savings, and the public agencies with 90% of the savings. Director Breault suggested the savings be presented in a way that reflects the effect on retail water customers.

**Chair Klein brought back the motion made by Director Anderson, seconded by Director Pierce, that the Committee recommend Board approval of four actions in November.**

*Discussion on the motion:*

Chair Klein noted that the blended versus non-blended rate is not a part of the motion. It is for a later time, unless a member of the committee wants to make a motion to give direction to staff, that would be appropriate.

Director Breault stated that the motion implies that the committee is not directing the CEO/General Manager whether to use the blended or non-blended approach. He pointed out that whether or not this item will come back for the Committee's discussion, it is best to be clear with what the Committee advises the CEO/General Manager.

Director O'Connell pointed out that the motion includes no recommendation on the surcharge setting or interest expense allocation.

Mr. Jensen stated that if the Committee wants to act on the debt service allocation, he recommends the Modified Volumetric approach on the matter of setting the charge, provided that the Board does not act on it as a condition for the sale of the bonds. Doing so will remove the Board's ability to change it later, and set it for the next 21 ½ years. It could be added to the recommendation as #5.

On the matter of using a blended versus non-blended approach for the allocation of interest expense, he would need a clear recommendation from the Committee or the freedom to act in the best interests of all member agencies.

Chair Klein will open further discussion on the debt service allocation, following a vote on the motion at hand: **Director Anderson's motion that the Committee recommend Board approval of four actions in November, with the revisions to 4A, seconded by Director Pierce:**

**Chair Klein called for a vote on the motion:**

- 1. Authorize the CEO/General Manager to amend the contract with KNN for their financial advisory services until the completion of the financing.**
- 2. Authorize the CEO/General Manager to appoint a bank to be selected through a RFP process as the Trustee for the bonds.**
- 3. Adopt a Resolution approving in substantially final form the various financing documents, including the Revenue Bond Indenture, First Supplemental Indenture, the Continuing Disclosure Certificate, the Preliminary Official Statement, a Prepayment and Collection Agreement with the SFPUC and the Bond Purchase Agreement.**
- 4. Authorize the CEO/General Manager to execute these financing documents at the appropriate time conditioned upon satisfaction of specified criteria.**

- a. The bond interest rates and final financing structure will need to result in a net present value savings of not less than 4% or about \$15 million over the term of the bonds.
- b. San Francisco must provide, in advance of receiving any funds, a written pledge to use bond proceeds in a manner consistent with federal laws and regulations.

**The motion carried unanimously.**

**Director O'Connell made an additional motion to provide an advisory to the CEO/General Manager to pursue the modified volumetric approach. Director Pierce seconded the motion. There was no discussion on the motion. The motion carried unanimously.**

Director Pierce commented that the presentation to the Board in November should be done in a way that allows people to understand the information within the context of the memberships' current percentages in savings. She noted that rate payers are currently paying equally, and if that can be continued, or not, the information should be presented both ways so that the Board can make the necessary policy decisions.

Mr. Jensen appreciated the questions and comments from members of the Committee, and noted that it was critical to present the methodologies and the numbers for the Committee's discussion, as well as the Board's consideration in November. He acknowledged Director Breault's suggestion to present the information based on the percentages of savings distributed in the context of the end-user's perspective.

Mr. Jensen will work with Legal Counsel in determining whether the methodologies should be included in the motion, and whether it is included or not, the information will be presented to the Board so that there is transparency and the opportunity to discuss.

Chair Klein stated that the interest expense allocation and whether to use blended versus non-blended is a policy issue, and is a matter that should be discussed and decided by the Board.

**Chair Klein made a motion that the Committee make a recommendation that the Board adopt the blended approach in allocating the interest expense. The motion was seconded by Director O'Connell.**

Discussion on the motion:

Director McLeod stated that private and public agencies function differently with different drivers and issues. There is the overall concept of rate structures and changing rates to customers. She expressed her concern that there has not been enough discussion and additional factors should be considered by the Committee for it to make a recommendation to the Board about the methods. She felt that more information should

be provided and that the item should be deferred for further discussion by the full Board.

Mr. Jensen explained that the ability to move quickly to issue the bonds in January is for the purpose of taking advantage of the market conditions. He and the financial team agree that the BAWSCA Board should make fully informed decisions and that additional information can be brought to the Board in November. While there are no indications that market conditions will change in the January, deferring decisions to the January Board meeting would have adverse impacts.

**Director McLeod made a substitute motion that information be provided to the Board for further discussion at the November Board meeting, with no recommendation from the Committee. Mr. Anderson seconded the motion.**

*Discussion and Comments on the substitute motion:*

Director Guzzetta believed that the Committee should provide some guidance to the full Board. He noted that the current process for the existing obligation is that everybody pays the same. Using a method other than the blended method will be a major change in the way member agencies have been servicing the existing debt with the SFPUC. Director Guzzetta stated that it would be appropriate to make a recommendation to not change the process, and allow the full Board to make the decision to support the recommendation, or not.

Chair Klein stated that he will vote against the substitute motion because the Committee's role is to make recommendations to the full Board.

**Chair Klein called the vote on the substitute motion. The motion failed by 5 noes (Breault, Guzzetta, Klein, O'Connell, Pierce) , and 3 ayes (Anderson, McLeod, Weed).**

**Chair Klein brought back the main motion he made to recommend the blended approach to the Board.**

In response to Director McLeod, Director Guzzetta further explained Cal Water's rate structure and how it will be affected by the bond issuance. He stated that with a non-blended allocation of interest expense all member agencies would save money, but Cal Water's customers would save less than customers of a public agency.

Mr. Jensen clarified that the details being presented to the Committee about the rate setting and interest cost allocation became available after the staff memo was finalized for the committee. These details will be included in the memo for the board in November.

Mr. Jensen acknowledged Director McLeod's comments about the inherent differences in the make-up of private and public agencies, and suggested the underlying policy is-

sue is whether the company would experience financial gain at the expense of public agencies.

Mr. Jensen asked Director McLeod if it would be helpful to provide, in the memo to the Board, clarification that Cal Water's rates are regulated such that Cal Water does not make profit from the interest rate allocation, and that the impact would be directly on the rate payers, businesses and residence served by both the public and private agencies. Director McLeod agreed that would be helpful.

Director Pierce noted that including the similarities and differences of the methods and how the debt has been paid for by the agencies in the past would be a helpful comparison for the Board in looking at the blended and non-blended analysis.

**The motion carried with 5 ayes (Breault, Guzzetta, Klein, O'Connell, Pierce), 2 noes (McLeod, Weed), and 1 abstention (Anderson).**

B. Amendments to the BAWSCA Investment Policy:

Mr. Jensen reported that the Investment Policy must be consistent with the Bond documents. The Committee is being asked to recommend Board adoption of the proposed revisions.

Mr. Jensen stated that the revisions maintain the objectives the Board established when the policy was first adopted. The objectives, in the order of priority, are Safety of principal, Liquidity, and Return on Investment.

Ms. Schutte reported that the current policy is extremely conservative and serves the function of a bank account in Local Agency Investment Fund (LAIF). She went over the four categories that would need to be added to the Policy, as noted in the staff memo. They include:

1. Federal Securities,
2. FDIC insured deposits,
3. Bonds, debentures, notes or other evidence of indebtedness issued or guaranteed by federal agencies, and
4. Money market mutual funds rated AAA by Standard and Poor's or Moody's.

Ms. Schutte explained that these categories continue to be conservative. The policy comes to the Board for review each year, and the Board can choose to review and revise the policy more often, if it chooses.

**Director O'Connell made a motion, seconded by Director Anderson.**

Discussion on the substitute motion:

Director McLeod suggested the Committee consider including social responsibility as an additional investment objective. She recognized that doing so can put the policy in the political realm, but, it provides a way to identify an issue of concern, subject to the Board's further discussion. It also provides general guidance to staff in looking at potential portfolios, and establishes a clear direction that social responsibility is a consideration in the use of public funds.

Director Guzzetta commented that it can really complicate things when it comes time to invest, and questioned what criteria would be used to identify the areas of concern in a portfolio?

In response to Director Guzzetta's question, Ms. Schutte stated that in her experience with other agencies, social responsibility has not been a part of their investment policies.

Director Klein questioned the purpose of the four categories. Ms. Schutte explained that the categories need to be added to the policy to make it consistent with the Bond Indenture. Because the current policy is so conservative, it wouldn't allow BAWSCA to take advantage of many the investment possibilities contained in the Bond Indenture.

Ms. Schutte further explained that since BAWSCA has never issued bonds before, the categories being added were not necessary in the current policy.

Mr. Brodsky clarified that the bond proceeds will result to at least \$13 million in the reserve that will be with the bond trustee. The bond trustee is subject to BAWSCA's investment policy.

Mr. Jensen stated that the Committee does not have to act on a recommendation to the Board. He proposed to move the item to the Board with further information and the revised and red-lined version of the policy for the Board's discussion and consideration in November.

Given the pressing time to complete all requirements for the bond issuance, Mr. Jensen suggested taking the issue of social responsibility under discussion at a later time.

Director O'Connell stated that it's not clear from the memo that if the Investment Policy does not include the four categories being proposed, the \$13 million from the bond issuance will sit at conservative interest rates. To best address the bond issuance, staff is recommending that the four categories be added. With that in mind, Director O'Connell moved to add all four categories to BAWSCA's Investment Policy. Director Anderson seconded.

Director McLeod made a friendly amendment to the motion, that when the item comes back to the Board in November, that there be some potential discussion on the issue of

social responsibility in the policy. She is concerned that the issue will get lost, and would like to see some direction for the staff to make the referral.

Chair Klein and Director Pierce suggested that a separate motion be made.

Mr. Jensen pledged to note in the staff memo for the Board, that there was discussion of whether or not the investment policy, now or in the future, should include a consideration of social responsibility. He would need to review how the issue has been treated by other agencies and become familiar with it before committing to include the issue in the policy's objective.

The Committee agreed to include the issue in the next BPC agenda.

Director Klein stated his concern with the obscurity of the language used in the four categories. He pointed out that Federal Securities is very broad and noted that some are riskier than others. There are some federal securities that are not secured by the full faith and credit of the United States, and it is unclear whether those will be excluded. He has similar concerns with the mention of bonds, debentures and notes issued or guaranteed by federal agencies. There can be real differences between ones that are issued, but not guaranteed.

**Director Weed made a substitute motion to revise the recommendation to say, "The types of permitted investments may be revised to be consistent with the Revenue Bond Indenture." and that the details on investment provisions will be further discussed at the Board meeting. The substitute motion was seconded by Director Anderson.**

*Discussion on the substitute motion:*

Director O'Connell stated that the revisions to the policy have to satisfy the objectives established by the Board; Safety, Liquidity, and Return on Investment. She argued that if there was a federal security that was not secured, that would be disqualified because it does not satisfy the policy's objective for Safety.

Director Klein stated that while that is a valid point, BAWSCA may not want to be as aggressive as the bond holders would like to allow us to be.

Director Guzzetta felt that the Committee does not have the information to make a logical recommendation on what appropriate investments should be. There were some good points raised and questions left unanswered. The Investment Policy must be a document that provides good guidance for BAWSCA, and while he is not against revising the policy, he cannot support the proposed revisions without further discussion.

Director Weed suggested that it would be most efficient for the Committee to develop the definitive language of the investment policy for the Board's consideration. In response to his question of when the policy needs to be finalized for the purpose of the

bond issuance, Mr. Brodsky stated that the policy should be finalized before the bond issuance.

Director McLeod said that the item should come to the Board in November as a potential item for action, and not just as an informational item, so that if the Board feels confident in moving forward with the additional information provided, then action can be taken.

The Committee concurred.

**Chair Klein made a motion, seconded by Director O'Connell, that the amendments to the Investment Policy be forwarded to the Board in November as a report with potential for action by the Board if it so chooses. Otherwise, the item will go back to the Committee for further discussion in December and the Board's final action in January.**

**The motion carried unanimously.**

- C. Authorization to Negotiate and Execute a Contract Amendment with PG&E for the Washing Machine Rebate Program: Ms. Sandkulla reported that the administration of the Washing Machine Rebate Program (WMRP) is included in the FY 2012-13 work plan adopted by the Board in May. The action before the Committee is to recommend Board authorization to negotiate and execute a contract amendment with PG&E to extend its administrative services for the implementation of the WMRP.

Ms. Sandkulla explained that PG&E's contract is on a calendar basis, and will end as of December 31, 2012. The contract includes a 6 month closeout period of up to June 30, 2012.

The contract amendment will extend PG&E's administrative services to implement the WMRP through calendar year 2013. There are no major program changes expected, and rebate levels will stay the same.

Ms. Sandkulla reported that the program has grown from issuing 1,000 rebates per year in 2002, to a current 7,000 rebates per year among all participating agencies. Participation is at a 100% among the BAWSCA membership, with Santa Clara agencies participating through SCVWD, and ACWD participating independently.

**Director Pierce made a motion, seconded by Director McLeod, that the Committee recommend the Board to authorize the CEO/General Manager to negotiate and execute a contract amendment with PG&E for administrative and rebate processing services through June 30, 2014 associated with implementation of the Washing Machine Rebate Program from January 1 through December 31, 2013; and offer participation to member agencies through June 30, 2014. The motion carried unanimously.**



**6. Brief Reports:**

- A. Proposal to Drain Hetch Hetchy: Mr. Jensen stated that BAWSCA's position remains the same. He reported that he spoke on BAWSCA's position with Cities Association of Santa Clara County (CASCC), and will be making the same presentation to City/County Association of Governments (C/CAG) on October 11<sup>th</sup>. Mr. Jensen noted that he is happy to speak to interested groups in the service area of Hayward and ACWD.
- B. Mid-Year Budget Review: Mr. Jensen reported that an assessment of the budget will be provided to the Board Policy Committee in December highlighting the progress made in the current fiscal year. Any adjustments or additions to the work plan will be included in the report, and recommendations as to what to do with the General Reserve will be addressed during the budget process.

7. **Comments by Committee Members:** Director Weed noted that the Calaveras Dam project is relocating approximately 3 million cubic yards of additional earth, which would need approval from the Division of Safety of Dams (DOSD). He expressed his concerns with the implications to Wholesale Customers that might result from the SFPUC's bond issuance against a project that does not have state approval for the construction.

Ms. Sandkulla explained that the additional grading work is to move a hill on the left abutment because it was determined that during a seismic event, that hill would become unstable and hit the Dam. The SFPUC is working very closely with DSOD through the entire process and they have received staff and expert approval on their approach.

Ms. Sandkulla has discussed the issue with the SFPUC several times, and the SFPUC is confident that DSOD is on board with their approach. DSOD has not issued a written approval because their process requires them to make their own assessment, and this can take time. While there is a slight risk to moving forward without the written approval, the alternative is to wait and stop.

Ms. Sandkulla further explained that the SFPUC has been issuing bonds since the beginning of the WSIP, and there were no approval to do a majority of the projects at the outset of the program. The WSIP was launched without approval by any of the CEQA documents, DSOD, Fish and Game, and Fish and Wildlife. And only just recently did the SFPUC get approval from DSOD for the Calaveras Dam Project. While this is an issue of concern, the SFPUC has had significant records of issuing bonds in advance of getting final approval for their projects.

BAWSCA will continue to follow the Calaveras Dam Project and will provide a report to the Board in November.

8. **Adjournment:** The meeting was adjourned at 4:11pm. The next meeting is December 12, 2012.

Board Policy Committee Minutes

October 10, 2012

Respectfully submitted,

Arthur R. Jensen, Chief Executive Officer and Secretary

ARJ/le

Attachments: 1) Attendance Roster

**BAY AREA WATER SUPPLY AND CONSERVATION AGENCY**

**BOARD POLICY COMMITTEE – August 8, 2012**

**Roster of Attendees:**

**Committee Members Present**

Larry Klein, City of Palo Alto (Chair)  
Rob Guzzetta, California Water Service Company (Vice-Chair)  
Robert Anderson, Purissima Hills Water District  
Randy Breault, City of Brisbane/GVMID  
Jamie McLeod, City of Santa Clara  
Irene O’Connell, City of San Bruno (BAWSCA Vice-Chair)  
Barbara Pierce, Redwood City (BAWSCA Chair)  
John Weed, Alameda County Water District

**Committee Members Absent**

Ruben Abrica, City of East Palo Alto  
Tom Piccolotti, North Coast County Water District

**BAWSCA Staff:**

Art Jensen	CEO/General Manager
Nicole Sandkulla	Water Resources Planning Manager
Anona Dutton	Water Resources Planner
Christina Tang	Sr. Administrative Analyst
Lourdes Enriquez	Assistant to the Chief Executive Officer
Allison Schutte	Legal Counsel, Hanson Bridgett, LLP
David Brodsky	KNN Public Finance (by teleconference)

**Public Attendees:**

Tarun Narayan	City of Palo Alto
Nico Procos	City of Hayward
Michelle Sargent	San Francisco Public Utilities Commission
Michael Yee	Alameda County Water District

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**BAY AREA WATER SUPPLY AND CONSERVATION AGENCY**

**BOARD POLICY COMMITTEE MEETING**

**Agenda Title:**        **Appointment of BAWSCA Representative and Alternate to ACWA/JPIA Board**

**Summary:**

On July 1, 2012, the Association of California Water Agencies (ACWA) Health Benefits Authority (HBA) transitioned its Employee Benefits program to the ACWA Joint Powers Insurance Authority (JPIA). The ACWA JPIA issued a directive instructing organizations who previously received benefits through ACWA HBA, and now the ACWA JPIA, including BAWSCA, to appoint a Director Representative and an Alternate Representative to the ACWA/JPIA Board.

**Fiscal Impact:** Expenses, per diem, and fees incurred by the appointed Director to attend the Board meetings and the ACWA conferences are the responsibility of their respective districts. In the event the Board's appointed Director Representative, or the Alternate, attends JPIA Board meetings at the ACWA conference, expenses, per diem and fees incurred would be BAWSCA's responsibility.

**Recommendation:**

**That the Committee recommend that the Board appoint the BAWSCA Chair as the Director Representative to the ACWA/JPIA Board, and the CEO as the Alternate Representative.**

**Discussion:**

ACWA JPIA member agencies are entitled to be represented on its Board of Directors. The representative must be a member of the agency's elected board. Each member agency also has the right to appoint one alternate who may be an officer, a member of the governing board or an employee of the member agency. The Directors and Alternates serve until a successor is appointed and at the pleasure of the Member by which he or she has been appointed. Each Director representing a Member, or his or her Alternate, shall have one vote.

Appointing the representative and alternate by position, rather than by name would eliminate the possibility of frequent reappointments. The recommendation is to appoint the BAWSCA Board Chair as the Director Representative and the BAWSCA CEO as the Alternate Representative.

The JPIA Board of Directors' meetings are held twice a year, during the Spring and Fall ACWA conferences. While the Directors and/or their Alternates are encouraged to attend these Board meetings, the JPIA understands that it is not always possible.

**Attachment:**

1. ACWA/JPIA Board of Directors powers and functions.

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The Board of Directors of the ACWA/JPIA shall have the following powers and functions:

- (a) The Board shall elect from its voting members pursuant to Article 10 of this Agreement an Executive Committee.
- (b) The Board may review all acts of the Executive Committee, and shall have the power to modify and/or reverse any decision or action of the Executive Committee upon a majority vote of the voting Directors present at any Duly Constituted Board Meeting.
- (c) The Board shall review, modify if necessary, and approve the annual operating budget of the Authority, prepared by the Executive Committee pursuant to Article 11 (d).
- (d) The Board shall receive and review periodic accountings of all funds under Articles 17 and 18 of this Agreement.
- (e) The Board shall have the power to conduct on behalf of the Authority all business of the Authority, including that assigned to the Executive Committee, which the Authority may conduct under the provisions hereof and pursuant to law.
- (f) The Board shall have such other powers and functions as are provided for in this Agreement or in the Bylaws.
- (g) Meetings – The Board shall provide for at least one annual regular meeting. It may also provide for the adjourned regular meetings, special meetings, or meetings upon call of the President of the Board.

Additional information about ACWA/JPIA may be obtained at their website:  
<http://www.acwajpia.com>.

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**BAY AREA WATER SUPPLY AND CONSERVATION AGENCY**

**BOARD POLICY COMMITTEE MEETING**

**Agenda Title:**           **Mid-Year 2012-13 Work Plan and Budget Review**

**Summary:**

To ensure continued access to reliable supplies of high quality water at a fair price, four issues require serious attention during the second half of this fiscal year. The resources to address these issues and produce necessary results can be provided within the currently approved Operating Budget for FY 2012-13 of \$2,715,504.

This memorandum presents: 1) the proposed changes to the annual Work Plan, 2) proposed reallocation of funds within the existing Operating Budget, and 3) the projected balance of the General Reserve.

**Fiscal Impact:**

As a result of the mid-year Work Plan and Budget review, no changes are requested to the currently approved budget at this time. Minor budget reallocations are needed to complete work through the remainder of FY 2012-13 within the currently approved Operating Budget. None of the modifications require Board action.

**Recommended Committee Actions:**

**That the Committee recommends:**

- 1. Board approval of the following revisions to the FY2012-13 Work Plan:**
  - a. Investigate a potential pilot subscription program that would provide customers with water use information designed to promote water conservation, with all costs to be borne by participating member agencies.**
  - b. Pursue agreement with San Francisco or legislation to protect customers outside SF, with costs funded by reallocating funds within the existing budget.**
  - c. Complete the sale of bonds to prepay capital debt owed to San Francisco and implement monitoring and reporting measures to ensure proper management of bond proceeds.**
  
- 2. Board review and discuss alternatives for managing the General Reserve balance at the March 2013 Board meeting, and consider taking actions at the May 2013 Board meeting in conjunction with the consideration and adoption of the FY 2013-14 budget.**

**Prior Board Approved Budget Actions for FY 2012-13**

Board authorized budget actions to date are as follows:

- A. On May 15, 2012 the Board approved the FY 2012-13 Operating Budget of \$2,585,504.**
- B. On July 19, 2012, the Board approved an increase to the Orrick contract of \$15,000, the funding for which was taken from the budgeted contingency, resulting in no change to the Operating Budget.**
- C. On September 20, 2012, the Board authorized the following budget actions which increased the Operating Budget by \$130,000, for a total Operating Budget of \$2,715,504.**
  - 1. Transfer \$130,000 from General Reserve to the Operating Budget to develop a Pilot Water Transfer Program:**
    - a. CDM \$72,000 for technical support**
    - b. Hanson Bridgett \$58,000 for legal support**

2. Transfer \$120,000 from General Reserve to pay Moody's and S&P to pay the costs of a preliminary credit assessment, provided the cost would be paid from bond proceeds if bonds were issued. The issuance of bonds now appears very likely, and this transfer is not expected to be needed. If bonds are issued, the money will remain in the General Reserve and the Operating Budget will not be increased by \$120,000.
3. Amend Contract with Hanson Bridgett to add \$65,000 from the unspent balance of the Water Management Charge to complete re-programmed work on the Long-Term Reliable Water Supply Strategy. This transaction does not affect the Operating Budget or General Reserve Balance.

The existing budget for the Long-Term Reliable Water Supply Strategy remains sufficient to complete that study. The subscription water conservation programs are funded with revenues from participating member agencies.

**Discussion:**

The mid-year review included examining progress toward completing the Work Plan as adopted, and considering anticipated work that should be performed during the balance of this fiscal year. The relatively minor Work Plan modifications are presented in Table 1 (attached), which shows the progress on selected items and new results to be achieved this year.

Following Work Plan review, the budget review included estimating spending on ongoing programs through the end of this fiscal year, savings that are expected to result from completed or delayed activities and the resources needed to achieve any results not already reflected in the approved budget. Possible budget adjustments were then considered, as well as potential sources of funds: the Operating, the Long-Term Reliable Water Supply Strategy, subscription conservation programs, and the General Reserve.

This review provided an informed assessment of resources needed to complete the work envisioned for the balance of the year.

Overall Status of Results to be Achieved During FY 2012-13. The major items in the approved Work Plan are on schedule as of December 6, 2012. The priorities for several efforts have shifted during the summer and fall of 2012. The investigation of issuing bonds to save customers money led to Board approval for an expected issuance in January 2013. Resources were also devoted to protecting water customers against possible negative impacts of draining Hetch Hetchy.

These major efforts diverted time and resources from other efforts, such as initiating negotiation of amendments to the Water Supply Agreement (See items 5 a and b in Table 1, "Results to be Achieved in FY 2012-13"), and preliminary examination of Wholesale Customer interest and issues related to changes to wholesale water rate structures (See item 9 in Table 2, "Activities Not Included in Proposed Operating Budget for FY 2012-13").

In addition, the status or pace of work by outside entities, such as FERC, results in some activities needing fewer resources than originally estimated, at least in this year.

Work Plan Modifications and Proposed Budget Revisions. Table 1 presents the Board-approved Work Plan of results to be achieved during FY 2012-13, and highlights recommended revisions to the Work Plan. Explanations for the changes and budget reallocations appear below.

1. Consistent and defensible water supply planning. The Board-approved Work Plan for this fiscal year included selection of a consultant to prepare consistent and defensible water demand projections throughout the BAWSCA area (See item 1.c in Table 1). An RFP was released in October, and proposals have now been received. Once a consultant has been selected, work could begin this fiscal year, but would require Board authorization of the consultant contract and Board allocation of additional funding. This cost for this effort is expected to be large, and using a portion of the General

Reserve balance may prove to be the best alternative for funding this one-time effort. No funds are requested at this time. A recommended schedule and possible actions will be brought to the Board Policy Committee in February 2013.

2. Potential additional subscription-based water conservation program. BAWSCA is investigating a pilot program for interested members that would provide web-based information to water customers, including their water use, how it compares to their neighbors' use, and options for reducing their use (See item 2.b in Table 1). Such systems have demonstrated water savings of up to 5%. An RFP issued in January 2013 would permit selection of a vendor in February/March and initiation of a pilot program in July. Several agencies have already indicated interest in this type of program.

3. Protect members' interests in a reliable water supply. Proponents of draining Hetch Hetchy Reservoir state they plan to continue their campaign to drain Hetch Hetchy Reservoir and reclaim Hetch Hetchy Valley even though San Francisco voters failed to pass their ballot measure this November. If successful, the resulting changes to the water system could affect the reliability, quality and cost of water. Even if not successful, the ongoing efforts create uncertainty for communities that would be affected but currently have no role in the decision making and no other means of protection.

BAWSCA intends to pursue its goal of protecting the water customers' interests by pursuing an administrative or legislative protections (See item 4.a in Table 1 and item 4 in Table 2). Additional legal support can be provided within the existing contract for legal services; the lower than expected level of activity in the FERC process permits budget to be reallocated within the contract limit. Additional strategic counsel services will be needed, the level of which will depend on which approach needs to be taken. Additional support for an administrative solution can be funded within the CEO's discretionary spending limit of \$25,000 using funds from the contingency budget. If a larger effort is needed, a request for additional authorization could be brought to the Board in March.

4. Ongoing administration of the 2009 Water Supply Agreement. Work continues to resolve outstanding issues related to San Francisco's allocation of costs to Wholesale Customers. As usual, efforts are directed toward resolving issues within contractual deadlines. In the event that issues cannot be resolved, the Agreement provides for arbitration of disputes. If arbitration is pursued, resources beyond those available in the budget may need to be allocated to this effort (See item 7 in Table 1 and 11 in Table 2). The Board will be informed if and when this need arises.
5. Manage activities related to revenue bonds series 2013 A&B to prepay capital debt owed to San Francisco. None of the related activities this fall were included in the original Work Plan, and funding was authorized by the Board in September and November. Additions to the Work Plan include final preparations to issue bonds in January and pricing bonds at appropriate time to ensure the greatest savings to BAWSCA's member agencies. In addition, staff is making necessary administrative changes to maintain proper accounting transactions, records and reports; ensure timely continuing disclosure filing; monitor revenues collected by SFPUC and expenditures spent through the Trustee; monitor San Francisco's expenditures of proceeds and the purposes or projects financed with such expenditures; and initiate other administrative actions needed to ensure smooth operation over the duration of the bond term (See item 8 in Table 1). These activities can be accommodated within the existing budget.
6. Postpone developing alternative wholesale rate structures that the SFPUC might consider. The original Work Plan did not budget resources for investigating alternative Wholesale Water Rates, or responding to changes in water rate structure that might be proposed by San Francisco (See Item 9 in Table 2). The Work Plan limited this activity to "developing goals and objectives relevant to Wholesale Customers, and facilitating communications with the SFPUC." Given the significant effort directed to preparing for issuance of bonds, no activity has taken place in this area, and none is expected for the balance of this fiscal year. In order to avoid being entirely reactive to ideas put forth by the SFPUC, it would be prudent to budget this work for next fiscal year and begin as soon as possible following July 2013.

Capacity to accommodate potential or unanticipated issues. As always, if potential or unanticipated issues arise during the Spring, they will be brought to the attention of the Committee and the Board with recommendations to further reallocate and/or augment existing resources, if necessary. Potential issues might include the following:

- a. Major legislative effort.
- b. Arbitration to address unresolved cost allocation issues.
- c. Allocation of resources if it is possible to begin work on the water demand projections this fiscal year.

If it were necessary to undertake any of these issues, work during FY 2012-13 would represent only the beginning of the effort. Each of these examples would involve continued work in FY 2013-14.

**Budget modifications needed to complete work expected during FY 2012-13:**

Minor budget reallocations are needed to complete work through the remainder of FY 2012-13 within the currently approved Operating Budget. None of the modifications require Board action. These modifications are as follows:

1. Reprogram a portion of the budget for legal services to cover the additional costs for preparing to issue bonds and the cost of developing an agreement with San Francisco or legislation to protect customers outside San Francisco from potential impacts of efforts to drain Hetch Hetchy Reservoir. A portion of the budget originally provided for participation in FERC relicensing can be reallocated for this purpose due to the slower than anticipated progress of those federal proceedings.
2. Increase the not-to-exceed contract limit for strategic counsel services to support developing an agreement with San Francisco or legislation to protect customers outside San Francisco from potential impacts of efforts to drain Hetch Hetchy Reservoir. The CEO has authority to amend the contract by up to \$25,000. If a greater effort and more resources are needed, the CEO would return to the Board in March with a request for Board consideration and action.

The balance of the General Reserve is sufficient to address all three of the potential issues listed at the end of the prior section. It does not make sense to budget for and commit portions of the General Reserve for those activities at this time. However, it does make sense to leave the General Reserve balance intact until Spring, when a more accurate assessment can be made of the agency's activities and resource needs.

**Work Plan and Funding Alternatives Considered:**

Last year's mid-year review identified significant activities and large expenditures to provide necessary resources. As a result, several Work Plan and funding alternatives were examined.

Given the items already anticipated in this year's work plan, the Work Plan and budget actions approved by the Board in September and November, and ability to perform the recommended work by reallocating portions of the existing budget, no alternatives were examined.

**Projected Year-End Spending and General Reserve Balance as of July 1, 2013**

With the proposed reallocation of funds, the current estimate of year-end spending at this time is that approximately 92% of the Operating Budget will be used by the end of the fiscal year.

This estimate is subject to inherent uncertainties. The "mid-year" assessment necessarily relies on accounting information from July through September plus partial information for October. In addition, there are inherent uncertainties in much of the work being undertaken or proposed, particularly in the areas of protecting water supply reliability.

Using the current estimate, the unspent funds at year-end would be approximately \$200,000. The following table shows approved and estimated adjustments to the General Reserve balance, and an estimate of the balance as of June 30, 2013.

\$916,897	General Reserve balance as of June 30, 2012
<u>+277,943</u>	<u>Unspent budget from FY 2011-12 to be deposited in General Reserve</u>
\$1,194,840	General Reserve balance following deposit
<u>-130,000</u>	<u>Approved use of General Reserve for Water Transfer Plan, Sept 2012</u>
\$1,064,840	General Reserve balance as of December 6, 2012
<u>\$200,000</u>	<u>Estimated unspent budget as of June 30, 2013</u>
\$1,264,840	Estimated General Reserve balance as of July 1, 2013

If next fiscal year's Operating Budget were identical to this year's original Operating Budget, \$2,585,000, the estimated General Reserve as of July 2013 would be equivalent to 49% of the FY 2013-14 Operating Budget, and would exceed the 35% guideline adopted by the Board in September 2011 by approximately \$360,000.

Alternatives that should be considered for managing the General Reserve balance include:

- a. Reducing assessments
- b. Refunding a portion of the excess
- c. Retaining sufficient funds to meet anticipated and highly likely one-time expenses that provide value for water customers.

Estimated costs of the potential activities listed in this memorandum are large enough to consume the entire excess of the General Reserve balance. At this time it would be prudent to postpone taking any action until it is clear how much funding these activities might require. It is recommended that further analysis and discussion of the General Reserve balance take place in the Spring of 2013 during development of the FY 2013-14 Work Plan and budget.

Regardless of whether the Board authorizes uses for the excess balance, a refund to member agencies, or a combination of the two, if the ongoing Operating Budget remains at current levels, the annual assessments should be reduced.

Attachments:

1. Table 1. Results to be Achieved in FY 2012-13: Changes and Progress
2. Table 2. Activities Not Included in Proposed Operating Budget for FY 2012-13

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**Table 1. Results to be Achieved in FY 2012-13**Changes are **highlighted**, progress underlined and in brackets**RELIABLE SUPPLY -- WATER SUPPLY MANAGEMENT PROGRAM****1. Long-Term Supply Solutions: Ensure a reliable, high quality supply of water is available where and when needed.**

- a. Reliable Water Supply Strategy – Complete Phase II A of the Long-Term Reliable Water Supply Strategy to ensure supply reliability through the year 2035, including evaluation of projects to pursue, present policy-decisions for board consideration, review and compilation of projected population and water demands from member agency UWMP. [Phase IIA of Strategy completed July 2012. Strategy on schedule to be completed by December 2014 with Board actions from Sept. 2012.]
- b. Drought Reliability – Pursue projects that would enhance near-term drought reliability for all agencies. [Initiated development of Plan for Pilot Water Transfer.]
- c. Consistent and Defendable Regional Planning – Select a uniform method for projecting future water needs of agencies for development in FY 2013-14. Application of the selected method would be included in the Work Plan for the following year. [RFP released in Oct. 2012. Consultant selection scheduled for January 2013. Work could begin as early as April 2013, which would require Board authorization of contract and additional funding.]

**2. Near-term Supply Solutions: Water Conservation**

- a. Implement Core Water Conservation Programs - Programs that benefit all customers. [Implementing all planned core programs]
- b. Implement Subscription Water Conservation Programs - Rebate and other programs that benefit, and are paid for by, agencies that subscribe for these services. [Implementing all planned subscription programs. Investigating potential pilot subscription program that would provide customers with water use information designed to promote water conservation. May issue RFP in January 2013.]

**3. Facility Reliability: Monitor the SFPUC's Water System Improvement Program**

- a. Monitor WSIP scope, cost, and schedule as San Francisco continues an aggressive construction schedule through 2015. Press the SFPUC and the city's political leadership to meet the city's adopted schedule, satisfy the requirements of AB 1823, and respond promptly to BAWSCA's reasonable requests. Focus resources from technical review to monitoring project and program performance during construction.

**4. Protect Members' Interests in a Reliable Water Supply**

- a. Proponents of draining Hetch Hetchy Reservoir – Assess risks associated with efforts to drain the reservoir and take actions needed to protect water supply reliability for water customers. Pursue agreement with San Francisco or legislation to protect customers outside SF. This will require additional resources available from within the existing budget.
- b. FERC – Ensure resources for legal and technical monitoring and intervention in the FERC Re-licensing of New Don Pedro Reservoir are sufficient to protect the customers' long-term interests in Tuolumne River water supplies. [Delayed. Less than expected activity this year.]
- c. MID/SFPUC water transfer – Protect members' water supply and financial interests. [Suspended. MID transfer terminated by MID.]

**5. Take Actions to Protect Members' Water Supply Interests in the Administration of the 2009 Water Supply Agreement**

- a. Pursue amendment of the Tier 1 drought allocation formula with SFPUC. [Work to be initiated late spring.]
- b. Amend the Water Supply agreement with San Francisco to revise the completion date for the WSIP. [Work to be initiated spring.]

**6. Pursue Grant Opportunities Independently and in Coordination with Regional Efforts**

- a. Implement use of Proposition 84 (Round 1) grant funds awarded for water conservation programs. [Grant funds were available for programs beginning July 1, 2012. BAWSCA working with grant administrator to secure grant reimbursements over the next three years.]
- b. NEW work plan item: Prepare new grant application for conservation funds through Prop 84 IRWMP Round 2. This grant application is due in early 2013. The potential grant request for BAWSCA is roughly \$590,000 for continuation of grant support.

**FAIR PRICE**

**7. Perform Matters that Members Delegated to BAWSCA in the Water Supply Agreement**

Administer the Water Supply Agreement with San Francisco to protect interests of members and their customers in a fair price for water purchased from San Francisco. **Resolve conflicts with SF over cost allocation without arbitration if possible.**

**8. Manage Activities Related to Revenue Bonds Series 2013 A&B to Prepay Capital Debt Owed to San Francisco**

- a. **Price the bonds at appropriate time to ensure the greatest savings to BAWSCA's member agencies, maintain proper records and accounts, and ensure timely continuing disclosure filing.**
- b. **Monitor revenues collected by SFPUC and expenditures spent through the Trustee, and monitor San Francisco's expenditures of proceeds and the purposes or projects financed with such expenditures.**

**HIGH QUALITY WATER**

**9. Support Member Agencies in Receiving Reliable Communication of Water Quality Events**

Coordinate member agency participation in Water Quality Committee established by the 2009 Water Supply Agreement to ensure it addresses Wholesale Customer needs.

**AGENCY EFFECTIVENESS**

**10. Maintain Community Allies and Contacts with Environmental Interests**

- a. Maintain close relationships with BAWSCA's powerful allies (state legislators, business, labor, local government, water customers, and the media) and activate them if necessary to safeguard the health, safety and economic well-being of residents and communities. Respond to requests from local legislators. Maintain a dialogue with responsible environmental and other groups, who will participate in the project permitting and approval process for rebuilding the system.
- b. In conjunction with San Francisco, conduct or co-sponsor tours of the water system for selected participants.

**11. Manage the activities of the agency professionally and efficiently**



**Table 2: Activities Not Included in Proposed Operating Budget for FY 2012-13**

[Highlighted activities have been or may be pursued to some degree in FY 2012-13]

**Reliable Supply**

1. Acquiring and wheeling water to respond to lesson drought reductions in FY 21012-13.
2. Conducting independent analysis of why water use has declined in recent years.
3. Engaging in extended or complex applications for grant funds. Application for water conservation grants will continue to be made through or with the Bay Area Water Agency Coalition, the California Urban Water Conservation Council or other agencies.
4. Introducing new legislation or supporting/opposing legislation initiated by others. If needed, the agency could support major legislative efforts by redistributing resources, using the contingency budget or accessing the general reserve, subject to prior Board approval.
5. Evaluating how sub-metering of mobile home parks or multi-family dwellings could be implemented to encourage conservation.
6. Supporting agencies in forming alliances to comply with Senate Bill 7X (20% by 2020).
7. Estimating the volume of water savings that result from BAWSCA and local agency water conservation activities.

**Fair Price**

8. Evaluating potential economic or water supply impacts of State efforts to fix the Delta and other State water management projects.
9. Developing alternative wholesale rate structures that the SFPUC might consider. Actions will be limited to development of goals and objectives relevant to Wholesale Customers, and facilitating communication with SFPUC.
10. Researching alternative retail rate structures that member agencies might consider to stabilize water rates and water revenues.
11. Arbitrating issues related to the 2009 Water Supply Agreement.

**High Water Quality**

12. Performing technical work related to water quality and San Francisco's treatment of the water it delivers to the BAWSCA agencies.
13. Advocating changes to water quality regulations or the manner in which San Francisco treats water for drinking and other purposes.

**Agency Efficiency**

14. Adding resources to support additional Board, Board committee or technical committee meetings.
15. Conducting tours of the Regional Water System. The Preliminary Operating Budget does not include funds to co-sponsor a tour by the California Water Education Foundation.
16. Conducting tours of member agency facilities to acquaint Board members with potential supply projects and their neighboring jurisdictions.

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## Board of Directors Policy Calendar for FY 2012-13

Board Meeting	Purpose	Issue or Topic
January	R D&A D D D&A	Bond Issuance - Status BAWSCA Mid-Year Review of Progress, Budget and Reserves Budget planning for FY 2013-14 Hetch Hetchy Reservoir – Status of Protecting the Water Users <b>CEO/General Manager Performance Evaluation</b>
March	D D D&A	Discussion of preliminary Work Plan and budget for FY 2013-14 Hetch Hetchy Reservoir – Status of Protecting the Water Users Water Demand Projections – Consultant Selection
May	D&A D&A	Adoption of Work Plan and Operating Budget for FY 2013-14 Approval of annual contracts for FY 2013-14

Key: R=Report, D = Discussion, S = Study Session, A = Action

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