Pre-Council Meeting
Water and Wastewater Rate Study
November 30, 2009

Meeting Began at: 4:00 p.m. Meeting Ended at: 4:20 p.m.

City Council Members Present: Doug Emery, Eugene Carroll, Jayne Snyder, Jon Camp (arrived at 4:08 p.m.), John Spatz (arrived at 4:20 p.m.)

City Council Members Absent: Jonathan Cook, Adam Hornung

Others Present: Public Works & Utilities: Greg MacLean, Fran Mejer, Jerry Obrist, Gary Brandt, Nick McElvain, Gary Thalken, John Miriovsky;
Finance: Don Herz, Steve Hubka;
Mayor's Office: Trish Owen; Law: Steve Huggenberger;
Public Financial Management, Inc. (PFM): Jon Burmeister, Tionna Pooler;
HDR Engineering, Inc. (HDR): Tom Gould

INTRODUCTION:

Doug Emery
Welcome to the Pre-Council of November 30, 2009. A copy of the open meeting laws are in the back. This Pre-Council will be on the Public Works Water and Wastewater Rate Study. I will now turn it over to Greg MacLean.

PRESENTATION:

Greg MacLean
Thank you. I am going to turn it over to Don Herz. He is going to open for us today.

Don Herz
Good afternoon Council Members. My name is Don Herz, Finance Director for the City. Let me introduce the other individuals here. Greg MacLean, Director of Public Works; next to him is Tom Gould, who is the Vice President and National Technical Director for Finance and Rates for HDR; and to my immediate left is Jon Burmeister, Managing Director with Public Financial Management (PFM).

The purpose of our Pre-Council is to discuss the cost of service, rate study, and financial analysis of our Water and Wastewater Systems. It's going to be a fairly extensive endeavor. Some portions of this which have never been done previously. The City went through a selection process, through a RFP process, several months ago and selected PFM/HDR to do this engagement. We had two other proposals and PFM/HDR submitted the proposal we thought was the best. We anticipate that this engagement will take approximately 5 - 6 months. So we are expecting the late spring or early summer to have this project completed.

Greg MacLean
As Don had mentioned, this is an endeavor that is regularly undertaken by public utilities to analyze not only their cost of service, but their rates, and to compare and benchmark against other utilities. It is part of a prudent business plan, its something we would like to make a regular process. This is going to be a little more in depth analysis because its our first time through, but over time we would like to come back and revisit that on a regular basis every couple years or whatever is appropriate. I wanted to basically let you know that this is something that we believe should be part of our regular plan that we engage in and we are very excited to have these two firms engaged to get us started and put on the right track. With that I'm going to turn it over to Jon and let you guys make your presentation.

Jon Burmeister
Thank you. Pleasure to be here today. Again, I'm Jon Burmeister with Public Financial Management. I have next to me Tom Gould. We are very excited to be here. Public Financial Management is a national financial advisory firm and we have worked with several communities throughout the Midwest and on a national basis as well. Tom's group also works with municipalities all over the United States. I bring the financial side of this in terms of the financial analyses, credit analyses, the selling of bonds, and those types of things. We feel that by combining our expertise with Tom's expertise, who is more of digging into the cost of service and the cost allocation; we have a pretty good team here for you, to really analyze your situation and to bring back a report you guys can use.

(Attachment 'A') In front of you, this is a big pie level picture of an overview analysis. We will start off with the financial revenue plan. That is going to be analyzing all of the needs of the utilities. What's your revenues versus your operating expenses, your equipment replacement, how does that affect relative to if you are selling municipal bonds, and your capital improvement plan, what's the correct mix between doing a pay as you go versus a bonding type of a scenario. That then is kind of a foundation that flows into what Tom will do, which is really analyze the cost and what it costs to provide that service to your citizens. And ultimately to review the rates and the design of those rates and how they relate to the ultimate users and what the cost is to serve those users.

(Attachment 'B') Lastly, we listed here for you the steps. As Don pointed out, it's about a 5 - 6 month process. We've highlighted this for the big picture tasks. You can see there are 11 different tasks that we identified here. The scope of services that we developed through this process was actually 6 pages long. It details step-by-step all the various components of these different tasks.

Today we completed our first task. We sat down with City staff and addressed a lot of the issues, the financial performance, we are in the process of accumulating a lot of data. Fran and her staff are busy pulling together audits, budgets, capital improvement plans, comprehensive plans, and different aspects related to your rates and those types of things. So we are in the heavy process of getting that data transferred to us. Tom & I will take a look at that. We anticipate studying that information, researching it, comparing that to other communities that have your similar size, and then probably coming back to staff to provide you with a status report of what we see as some of the concerns and issues that we need to address. At some point in that process we want to be visiting with you folks so we can share with you our initial discoveries of what we learned from your system and also to solicit some of your feedback from you as it relates to policy, directions, and some of those types of things as it relates to the growth issue or impact fees, and those types of things. Throughout this process we want to look at potentially reviewing some financial policies that other communities have put in place and get your feedback on the financial policies and how those relate to what we should be looking at for different financial analyses as we go forward. What kind of debt coverage ratio should we be looking at, what type of bonding versus pay as you go allocation should we be reviewing, what type of cash reserve should we be maintaining, and what's prudent from a business standpoint. After we have your feedback we will come back with an interim status report of what we discovered at that point now that we've pulled everything together. To share that with you, get your feedback, go back and keep crunching the numbers, working with staff, and then finally provide you with a report.

You will see here the overview of our team's approach. From my perspective, the team is Tom and myself as well as Don and staff here at the City. This is going be a team effort, we are going to work with your staff and pull this together on a team effort. We are not going to be out doing our own thing, we will work directly with your staff and putting together a product that fits well with them, fits well with the community, and hopefully fits well with you as well. Tom, I don't know if you had anything else to say, but I guess we will open it up for questions.

Tom Gould
I just wanted to clarify that we are talking about the water and wastewater utility in this exercise.

Greg MacLean
So with that we would be happy to answer any questions that you have or address any concerns.

QUESTIONS & ANSWERS:

Gene Carroll: You are looking at the CIP projects that are listed and say the ones that the City needs to rebuild or redo in the next number of years, balance that against financial cost. Is that what you are going to be looking at? To see which ones made the priority list, financially whether or not the City can or cannot do or should do. Is that part of your study?

Jon Burmeister: Yes. Some of the discussion we had today, we thought about taking your CIP and breaking it down between replacement, regulatory (I kind of think replacement and regulatory is required, you really don't have to much choice on those), and then growth. Breaking those down into those components and see how each one of those components affect your overall impact on utilities. So yes, we did discuss that a little bit today.

Gene Carroll: So you can build that list priority wise as far as financial and as far as regulatory to meet both directions.

Jon Burmeister: Within those categories we want to prioritize within the regulatory and within the replacement. I think we want to prioritize those projects as well, because if we have limited resources we want to make sure we take care of those projects that are high priority for you. If we are looking at different revenues versus the expenditures.

Gene Carroll: That falls into the rate structure after you provide the list. You built your rate structure from that, what your needs are, and then base it on other cities cost wise.

Tom Gould: Let's step back a little bit. One of the first steps is what we call the revenue requirement or financial plan. In essence we look at what's adequate funding to take care of the existing system that you have in place today along with any future growth related improvements and regulatory, as Jon had mentioned. At that point you have some understanding of what has to happen to your overall rates to support that plan. Part of that would be to go through and say so what is it that we think you need in a way of minimum funding for a lot of these areas, because that is maybe one of the questions on the table; what would be an adequate level of funding to take care of the existing system that you have in place today. From that then it goes forward and eventually it gets to what is the rate structure or the rates that would support the financial plan that you had put in place.

Gene Carroll: Thank you.

Jon Camp: In what you are going to be studying will you be doing anything in the standpoint to see if maybe our rates are too high and that we can have a lower rate structure that would support our system?

Tom Gould: At this point what we are going to do is take a look at comparative rates, but the conversation I usually have with City Councils is the problem with that is sort of apples and oranges perspective about rates. What I like to do is talk to City Councils about what is the adequate level of funding that you need to have and it shouldn't be based upon what a neighboring city is, although we understand competitiveness is an important element to this process. So I think we will be taking a look at neighboring utilities, but that shouldn't be the driving criteria that you use to establish your rates.

Jon Camp: I appreciate that, I guess what I'm looking at is in these challenging times when it comes to infrastructure, its almost a bottomless pit so to speak. We can spend a lot of money on that and Lincoln has been very fortunate especially in its water and wastewater and we want to keep it that way. At the same time with the economic stresses we see around the country and all, I just want to be careful that this study doesn't take a predetermined conclusion that it justifies a higher rate.

Tom Gould: We don't walk in the door with any preconceived notions about how this study is going to turn out. I want to look at it truly from a pure analytical perspective, but from a best practices perspective also. We want this to be a study that isn't about this year or next year, but is a framework for long-term rate setting for the City as a whole. If there are anomalies in the short-term because of the economy or whatever, I can accept that; but what I can't accept is a short-term problem that becomes a long-term approach for the City, which is that you artificially set your rates at some level that does not support the infrastructure that you have in place today. So what we want to try and do is work with you through some financial policies or philosophies about how you establish your rates in a way that follow generally accepted principles, how other cities approach this problem. Infrastructure is a huge problem in this country and that we haven't maintained infrastructure in the past and right now we are paying for sort of the sins of the decisions in the past. There is a lot of deferred capital in this country, I'm not talking just about Lincoln. Everywhere I go in terms of the utilities I work with, there are a lot deferred capital. So part of what we are trying to do is catch up with the past, but at least stay even with where we are today. Because every year that you defer capital, its just a decision that somebody else down the road is going to have to make in terms of paying for that infrastructure and properly maintaining it. So that is my philosophical side of how we approach these studies.

Jayne Snyder: I might have missed it, but when do you plan on completing this so we have the final product? Is there a time line?

Tom Gould: We had talked about 5 - 6 months for a time line.

Greg MacLean: At the end of the 5 - 6 months is really the time when we would come back with a draft final report. The report would basically be the basis then that you would be able to make decisions. It's a recommendation. The final decision still lies of course with City Council.

Jayne Snyder: Thank you.

Gene Carroll: Jon, you talked about that during the process you would come back to us in the middle, not just at the end. Is that just an informational meeting?

Jon Burmeister: Both. I think we want to provide you with information and also get feedback from you as to what's important to the City, and what's your future policy decisions. To provide us with some thoughts on how you want this to look going forward. From our perspective the last thing we want is to prepare a report that you look at and you don't have any buy into this report, so you don't want to follow it as the plan. We want to get your feedback so then at that point you feel that there is really some prudent information in here that you can kind of live on as you go on forward and look at the performance of the utility. That's what we hope for during these sessions with you, it will help us get your thoughts and how we can develop this so it gets implemented according to the plan.

Jon Camp: Are we going into this with some dramatic concerns about particular areas of our water or wastewater?

Greg MacLean: I think part of it is that we have not done this exhaustive of a study before. Its never been done, a cost of service, a rate study, and a financial plan, all done at once. So its our hopes that by doing these all at once we can get all of the areas covered and identify any concerns that are there that we don't know about. We believe that there are probably efficiencies that we can find. We don't know what they are,

we don't have a preconceived notion that we are going to find some jewel or some big thing that has been a problem. We also know that there will be some things that we find that could be done better. We are aware of other practices that other communities have used that we are interested in exploring. We would like to see if and how they might fit in our system under the things we can do better. Through this process, not only having the consultant help us review some of those things and make some recommendations, but also some interaction with Council we are hoping that some of these things will rise to the surface and we can select the things that works best for Lincoln's water and wastewater utilities.

Tom Gould: I think the other part of that is I have worked with a lot of communities over the last 30 years and an important part of everything that I do is transition. How do you get from where you are today to where you want to be and how do you do that in a smooth process with as little of impact to customers as possible. So a big part of developing the financial plan will be how do we make sure we have adequate funding and do we need to adjust rates to support that and how do we get to where we need to be. It doesn't all have to be overnight. We can certainly develop a multi-year plan for you to get you where you need to be. The point is again that we want to as part of this process, is to make sure you have a good philosophy in place about how you want to fund certain capital projects and how much should be adequate funding to take care of the existing infrastructure.

Jon Camp: Have you done any work with Omaha?

Tom Gould: I have not personally, no.

Jon Camp: When you come back to us will there be sort of a priority list or some options?

Tom Gould: In my opinion, we always have to provide you with options. I don't think any Council likes to look at one way to do it and this is the only way to do it. We certainly want to look at options. We want to talk about what the pros and cons are, but the thing that I always have to point out to folks is if you don't do something here is what the consequences of that action is, so you make a good informed policy decision.

Jon Camp: Would it be fair to say you would give us a road map then of the future of our wastewater and water system?

Tom Gould: Yes.

Jon Camp: I'm just trying to visualize here what to expect.

Doug Emery: Along with the financial package, it would go along with that road map.

Tom Gould: Each utility should financially stand on their own. Let's just be clear that these are enterprise funds and as enterprise funds they have to financially stand on their own. They should not be subsidized by the General Fund and so if that is the case, then what do we need to do from a financial perspective to be able to adequately fund those utilities and move them forward in a positive way.

Doug Emery: It seems to me like this is the next logical step after what we did during the budget talk. Where we had discussions about what the infrastructure is, there were people who are sitting at this table now, some who are not, who were shocked at what they were told the state of the system is. So at least now we will lay it all out in front of everybody including ourselves and say here it is and now we can either pay for it or don't pay for it or pay for part of it or don't pay for part of it and go forward. We are certainly not in a position where we have to pay for any of it if we don't want to. It becomes a decision based on what we think in best for Lincoln.

Tom Gould: As I mentioned there are consequences to that decision and we will try and lay those out for you. Jon, his background is in public finance, so when you go out to the market place to try and borrow funds those are things that they look at.

Doug Emery: Every decision you make has a consequence.

Tom Gould: Exactly. Some decisions have positive consequences and some have negative. We just want to be fair in a way that we present things to you.

Jon Burmeister: Hopefully at the end of the day, it makes you aware that you can make an informed decision. So if the decision is made, you know what those consequences are or lack thereof and you can be comfortable with that decision.

Doug Emery: That's fair. Any other questions? Anything else we need to bring forward?

Tom Gould: No. We are looking forward to working with you.

Doug Emery: We look forward to something in a couple of months here to see where we are going.

CLOSING:

Doug Emery closed the meeting by thanking those giving the presentation.

ATTACHMENTS:

Attachment 'A' – "Overview of the Comprehensive Rate Study Process"
Attachment 'B' – "Overview of Our Team's Approach"

Prepared By: Chris Koll, Public Works & Utilities
Submitted: December 2, 2009

Overview of the Comprehensive Rate Study Process

Revenue Requirement (Financial Plan)

Compares the revenues of the utility to its expenses to determine the overall level of rate adjustment

Cost of Service

Equitably allocates the revenue requirements between the various customer classes of service

Rate Design

Design rates for each class of service to meet the revenue needs of the utility, along with any other rate design goals and objectives

PFM HDR

CITY OF LINCOLN
NEBRASKA
MAYOR CHRIS BEUTLER

Overview of Our Team's Approach

Planning

Task 1
Initial Project Meeting

Task 2
Data Collection

Task 3
Review Financial/Rate Policies

Analysis

Task 4
Revenue Requirement Analysis (Financial Plan)

Task 5
Cost of Service Analysis

Task 6
Rate Analysis and Design

Task 7
Rate Structure (Final Alternatives)

Communication

Task 8
Pre-rate Design Workshop Session

Task 9
Substantial Completion Workshop Session

Task 10
Written Report

Task 11
Financial Model

Adopted Rates and Fees

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