Finance Committee Meeting

September 12, 2014
3:00 p.m.

Committee Members Present: Chair Larry Dill called the Finance Committee meeting to order at 1:00 p.m. Chair Dill, and Hugh Strom answered present at Roll Call. Laurie Ho was excused.

Staff Present: Kirk Saiki, Eddie Doi, Regina Flores, Kim Tamaoka, Christine Erorita

Guests: Deputy County Attorney, Nick Courson, Clyde Kodani, Shawn Shimabukuro, Grove Farm and Dave Hinazumi, Grove Farm

AGENDA

Chair Dill accepted the Finance Meeting agenda as circulated.

OLD BUSINESS

1. *Manager's Report No. 14-16* – Part 4 Section VII, Facilities Reserve Charge, Proposed Rule Amendments

BACKGROUND:

Acting Manager and Chief Engineer, Mr. Saiki reported that the last Finance Committee meeting discussed Max Day Demand (MDD) which was complicated regarding the legality. Currently the Department is considering a method of assessing the FRC by plumbing fixtures. (Refer to draft Part 4, Page 2 of 5, Schedule 2a & Schedule 2b.)

Problems faced with the numbers developed in the Leidos report was based on the cost per meter (actual unit cost per fixture unit) and that the cost of the meter got lower as the meter size got larger. By getting a 1-1/2" meter, with high fixture units, it would cost more than a 2" meter. There needs to be a way to cap this section in the calculation method. The Department suggested adding a worksheet to determine calculations.

DISCUSSION:

Civil Engineer, Mr. Doi commented that if the meter size is 5/8" to 2" based on the report, the Department had to refigure the meters sizes 3" to 8" by using the report's 2" meter calculation (using multiples of the 5/8" meter) which calculated to $1.13M. This was calculated in the higher unit cost from the previous SAIC report. The Department would determine any meter size above 3".

Leidos Report - Table 4-7, Page 4-11 - Chair Dill asked if the table was determined by the Department on an individual basis, why didn't the Department use the consultant's recommendation in the report.

Mr. Doi explained that the Department was tried to revolve MDD with the applicant. The calculation would clarify the assessment of meter charges vs. MDD. There are no set guidelines to quantity the flow and daily demand.

Honolulu Board of Water Supply uses fixture count and all other counties use flat rate. Previously the Department recommended flat rate but it was not approved.

At 3:10 p.m., Chair Dill recessed the Finance Committee meeting.

At 3:19 p.m., Chair Dill reconvened the Finance Committee meeting.

Chair Dill "Received for the Record" correspondence received from Ms. Shawn Shimabukuro, Grove Farm Company regarding the FRC, Proposed Rules Amendment, dated September 11, 2014 which was addressed to Chair Clyde Nakaya. The correspondence was part of Ms. Shimabukuro's testimony.

.. RECEIVED FOR THE RECORD

14 SEP 11 P3:50

DEPT. OF WATER
COUNTY OF KAUAI

September 11, 2014

Clyde Nakaya, Chairman
Board of Water Supply
County of Kauai
4398 Pua Loke Street
Lihue, Hawaii 96766

Subject: Facilities Reserve Charge, Proposed Rules Amendment

Dear Chairman Nakaya,

We are resubmitting our letter of March 8, 2013 addressed to the then Department of Water Manager who solicited public opinion regarding the proposed change in the Facilities Reserve Charge rules.

While the recently proposed rules have changed since March 2013, we feel that there are still questions and concerns in our letter that are applicable. Furthermore, we respectfully request for additional time to review the leidos *Needs Assessment Study and Facility Reserve Charge Update.*

We appreciate your time and consideration.

Sincerely,

for

Shawn Shimabukuro
Grove Farm Company, Incorporated

Enclosure

March 8, 2013

David Craddick, Manager and Chief Engineer
Kauai Department of Water
4398 Pua Loke Street
Lihue, Hawaii 96766

Dear Mr. Craddick:

Thank you for providing us the opportunity to comment on the proposed changes to the Water Service Development Fee (WSDF). Our comments are as follows:

1) WSDF Increase from $4,600 to $17,160 and SAIC Report:

Any increase, much less one this large, will place a tremendous burden on the island's residents and diminish opportunities for home ownership for current and future generations. Poor economic conditions and increased restrictions on borrowing money mean any increase could be the difference between owning a home or not. Implementing a substantial rate increase would also hinder the island's growth and efforts to move towards a stronger economic footing. For these reasons as well as concerns with the SAIC report, we do not believe that an increase is justified at this time.

We are concerned about the assumptions used in the SAIC and therefore question the validity of the proposed rate for the following reasons:

1. Water use projections. The future water use projections (17.8 MGD in 2020 and 19.4 MGD in 2030), which are based on population growth, are too high. Based on historical data from 1995 – 2009, water consumption has trended down. Water conservation education and improved behaviors are likely to account for this trend, a testament both to the Department of Water and consumers. This shows that future growth alone should not be used for the 2020 and 2030 projections as there certainly was growth from 1995 to 2009. As water consumption projections serve as the basis for the amount of future improvements, these projections need to be revised.

2. Revised water use projections will also lead to a revised projected annual system growth rate, currently stated at 1.1%.

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3. In general, the cost estimates for water system facilities appear to be high. The basis for these costs is not substantiated in the report. Please clarify how the costs were derived? If they were derived from historical cost records, please provide a complete listing.

4. Source capacity

   a. Projected capacity for new growth is 12 MGD.

      i. This does not tie in with and is significantly higher than the current water use projection increase. Assuming current capacity is at least 14.4 MGD (highest water use data from 1995 – 2009), the projected increase to 2030 is only 5 MGD.

      ii. The projected capacity also does not tie in with and is significantly higher than the projected storage capacity for new growth of 8.4 MGD.

   b. Projected capacity increase for Puhi-Lihue-Hanamaulu alone equates to a build-out of 184 homes per year beginning today (2.7 MGD divided by 750 gpd per home divided by 20 years). This is another measure that shows the projections are too high. Our new home absorption studies done a few years ago are significantly less than the 184, at 103 per year. We believe that has also declined given the present economic situation we are currently in.

   c. Cost differentials among projects. Why is Kokolau Tunnel ($8.68/gpd to construct) planned over another alternative such as further SWTP expansion ($2.46/gpd to construct) or another well? Also, why would a project like the Wainiha-Haena Well ($16.93/gpd to construct) be subsidized by consumers outside this water system?

5. Storage capacity

   a. Projected capacity is new growth of 8.4 MGD does not tie in with and is significantly higher than the current water use projection increase.

   b. The cost estimates for the Puhi-Lihue-Hanamaulu storage tanks ($8.31/gpd and $9.08/gpd to construct), even when accounting for planning and land costs are significantly higher than we would expect.

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6. Transmission. It appears that the transmission cost includes new growth projects as well as existing transmission facilities not being abandoned. Our assumption is that the existing facilities can also provide service for new growth. If this is true, then the costs allocated to existing users should be removed. Based on our discussion above regarding source capacity, this would eliminate roughly 75% (14.4 MGD of existing capacity divided by 19.4 MGD projected capacity), or about $150 million, of the cost for existing transmission facilities.

7. Does this list of projects include those contemplated to be constructed by someone other than the Department of Water (DOW)? If so, they should be removed if the non-DOW party decides it is in their best interest to construct the facilities.

8. Do the Water Plan 2020 improvements reduce the demands as listed in the report?

9. This study also assumes that all of the projects listed will be completed by 2030. Is this realistic? If not, perhaps only a percentage of the total projects should be used to factor the rate.

What exacerbates these concerns is the fact that the DOW will not be able to provide immediate water service in all instances. In fact, we understand that only in very limited instances will a consumer receive service upon payment of the WSDF.

After revising the SAIC report, a phasing of improvements and financing plan should be developed. DOW's experience with Water Plan 2020 can lend some guidance. The financial strategy for this was to float bonds to raise the capital and those bond payments will be paid by all users over 30 years.

A theme that resonates throughout these DOW posed questions is how to distinguish between existing and new users, which is a difficult and convoluted issue. A simple response is that it is easier to continue past practices and ease the burden by spreading the cost across all users. If not, why should a user yesterday gain a $13,000 benefit over a user tomorrow when the separation is just days? And wouldn't the 30-year user who has paid into the system for many years feel that recent users should foot a larger bill? If this seems convoluted then we agree that the questions posed are not appropriate unless the proper information is provided.

2) What are the options being considered?

The DOW should continue its mission of water conservation. For example, incentives should be given for developments utilizing water efficient technology or implementing dual water systems whereby irrigation needs are met through non-potable water sources, if available. Incentives could also be provided in terms of lower rates for consumers who use less water.

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The DOW should focus on expanding its customer base to share the burden. Expanding your customer base will allow the cost of system improvements to be shared by a broader base of customers. It seems counterproductive to increase the WSDF that would stifle growth. That model works for regulated entities so why would it be so different for the DOW.

Another consideration is to impose an WSDF assessment by district. It is unfair to burden a ratepayer for other ratepayers who choose to live in a district where the cost of living is much greater.

3) One-time flat fee, or charge per water-using fixture.

We do not think fixture counts can be used in establishing water demand calculations for larger master plan developments.

4) Time of meter installation

If the required fee has been paid to the DOW, then the customer should not have to make-up the deficit at the time a meter is requested. This is especially true where a non-DOW entity has constructed the necessary source, storage and transmission.

Imposing an additional fee is contradictory. DOW is trying to justify the increase in fees for new improvements while at the same time trying to increase the fee for existing customers on a system that has already been built out. There is no basis in trying to exact an additional fee.

5) Future WSDF Increases

DOW having the ability to add an inflationary factor on a yearly basis to the fee is too discretionary. As changes in usage, technology, etc. occur, a new study should be completed.

6) Special considerations for businesses and developers. Should a single developer be granted all the new capacity for a system, or should the water be apportioned in some other way?

Absolutely! The larger the customer base the more secure the financial strength of the water system. If a development could realize water customers sooner than later why wouldn't the DOW grant that capacity? Customers = revenues and the ability to pay for that excess capacity lessens the burden on the current customer base. Why should developers be put at a disadvantage?

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Developers are typically required to develop source, storage and transmission for their projects since there is rarely any additional water. When the construction costs exceed the total FRC liability, the developer never recoups those costs as the DOW doesn't reimburse them for the difference. In fact, the DOW collects additional FRCs from customers who upsize their meters. None of these additional FRCs is shared with the developer. In most cases, developers are credited for only a portion of the value of the constructed facilities. To remedy this situation, the developer should be allowed to transfer the balance

of the credit to another project or carry over the credits and apply them to future upgrades of water meters as discussed in the next section.

7) Should state grant money be used to reduce the WSDF for identified projects, or should the value be spread among all users?

If there are no restrictions on how the grant money may be used, it should be applied to projects based on priority, regardless of whether it assists existing or future customers.

8) If the developer builds and conveys a system that meets their entire needs, should they pay the difference between the system cost and the WSDF?

Absolutely not! If the developer constructed the facilities necessary to service their development, then why should additional fees be collected only to subsidize another project that has no correlation to the project at-hand? As stated above, the DOW does not pay the developer the difference between the FRCs and actual cost of the improvements.

In summary, we recommend that the WSDF is not increased at this time. In addition, to the economic environment, we have serious reservations regarding the SAIC study and believe that it should be revised. Also, our comments listed above are based on the limited questions posed by KDOW in a press release. We are concerned that there are other issues beyond what was published in the press release and ask that KDOW provide more information in regards to the proposed rule changes. The rule changes have far reaching effects and should be thoroughly vetted by the Board of Water Supply and the community. Thank you for your attention to this matter.

Sincerely,

Michael H. Tresler
Senior Vice President

C: Board of Water Supply

Shawn Shimabukuro, Grove Farm Company provided her testimony.

Ms. Shimabukuro stated the letter (dated March 8, 2013) submitted yesterday was in response to the 2013 SAIC study. The figures referenced in the March 8, 2013 letter, no longer are proposed. Recently she became aware of the Leidos report (November 2013) and requested more time to review the report. Ms. Shimabukuro would provide comments to the Finance Committee.

DISCUSSION:
Chair Dill noted that Leidos was SAIC (name change) which is a work in progress. The numbers and values may be different that were reflected from the previously consultant, SAIC. The Department was asked to provide a response to the comments in the March 8, 2013 Grove Farm letter for the Finance Committee to review. The comments would be recommended to the full Board.

Chair Dill thanked Ms. Shimabukuro for her comments relating to the letter.

DISCUSSION:
Page 1 of 5 – #2a, iv. - (This section was provided by the Department.)
"Water service laterals that have failed to install a water meter on the subject property for which the FRC was paid or where water meter has not been in place for a period great than one year will be required to pay the difference of the original FRC paid and the FRC in effect at the time the water meter is installed as described in Part 5 Section III, paragraph 5 of these Rules."

A concern was discussed if someone paid for a meter and does not install it, the Department could ask the applicant to pay an incremental cost of the FRC at installation. But if the meter has been installed, within a year, the FRC charges increase.

Mr. Strom concurred with Chair Dill of not agreeing with the latter portion of the amendment and requested the Department to explain the logic in Part 5 Section III.

The Department will also verify the footer on Part 4 effective date: December 25, 2011.

Page 3-5 - #6 – Calculations:
"Water services with existing meters where additional fixtures unit(s) or water demand is required…"

"FRC $_{(net)}$ = [FRC $_{(existing\ Fixture\ Units\ and\ proposed\ Fixture\ Units)}$] less ***[max. FRC $_{(existing\ water\ meter)}$]"***

Chair Dill posed an example for the Department - If an applicant purchased a 5/8" meter 10 years ago; using the current calculation for the max FRC, the cost is $113,280 or if the charge was $80,000 which the applicant previously paid. This example reflected no FRC was paid in the last part of calculation.

The Department will show more calculations on examples or additional service on the last part of the calculation and to include clarification on the rule.

"The minimum FRC will be $0.00."

The Department will review the last paragraph or delete.

"No FRC refund shall be made for existing meters requiring a decrease in water demand, decrease in meter size or decrease in existing water supply fixture units."

Several examples and options were discussed by the Finance Committee and Department.

- Abandon a 2" lateral and do a 5/8" meter if paid with the current charge.
- There could be no refunds with FRC and the Department's get back the credit. The land owner would benefit from a lower meter rate.

The Department will:

1) Note in the rules that an applicant could be credited to downsize a meter but get credit for a larger meter size.
   Acting Manager and Chief Engineering, Mr. Saiki was concerned that the larger meters may not be priced high enough. There is precedence with the existing rule on how to assess the cost for multi-family resort units but not for an industrial non-residential or non-resort for a larger meter.
2) Provide how the meters will get assessed.
3) Provide worksheets at the next Finance meeting with different scenarios and will adjust the language.
4) Check if the consultant answered Chair Dill's question regarding discrepancies and justification regarding multifamily resort units.

Chair Dill commented he was okay with the tables.

<u>Page 4 of 5, #7a</u> – Last definition -- "and" "or"
The Finance Committee will defer the definition of "and" "or" which is in the existing rules to Deputy County Attorney, Andrea Suzuki regarding.

<u>Page 4 of 5, #7c</u> – (The offset is in the existing rules.)
"*The offsets described in this Paragraph 7 "FRC Offsets" shall not apply to water transmission mains constructed by a subdivider, applicant or consumer which are within or adjacent to a subdivision or lands either 1) owned by the applicant or consumer, or 2) developed by the applicant or consumer for uses such as, but not limited to, residential, agricultural, commercial, resort, industrial, governmental, religious, or educational uses. Where water transmission mains are constructed within, adjacent to, or outside of such subdivisions or lands, the offsets shall apply only to mains constructed outside of an off-site from such subdivisions or lands."*

Chair Dill commented that generally it would be okay for the Department to enter into an agreement with developer for an offset. In other scenarios, the Department needs to be careful not to provide a benefit to a single entity as opposed to the customers.

The Department builds for the future and up sizes for potential development in an area. The FRC is paid by the developer. The Department co-shares the FRC with the developer (Example: A developer puts in a 6" line but with future development, the Department puts in a 10" line with the cost doubles with the Department co-sharing the 10" line.) On individual scenarios, the Department probably would not show that they are covering costs.

Chair Dill agreed with paragraph 7c because the developer would pay for distribution and any upsizing to transmission would be done by a negotiated agreement with the Department.

<u>Page 5 of 5, #8</u>
"*The administrative fees for review of Water Requests and Building Permits shall be assessed as established by Board resolution."*

The Department will check on the status of the administrative fees for review.

Page 5 of 5, #9 - Indexing
"Indexing of the FRC. The FRC shall be determined at the start of each fiscal year according to the percentage increase or decrease based on the Engineering News Record Construction Cost Index percentage on December 31st of the previous year. The Department will inform the Board on the percentage during the fiscal year budget review."

Chair Dill commented that the intent is to establish the FRC at a certain date. Annually the Department updates and adds a factor to apply on what the FRC would be.

Other proposed changes to the value in the rule included:

1) Add the Cost of Goods Index that are posted by the Feds quarterly; if there are adjustments, follow the Fed rate.
2) Annually review the rule to change the numbers.
3) Calculate the FRC but at the end of the calculation add today's CPI over the base CPI. The FRC should be approximately correct.

It was noted that the proposed rules do not allow the Department to update the FRC every time a new facility is built.

The Department will improve the language in paragraph #9.

Leidos Report Page 4-3
"Data sources for the FRC update include the following..."

The data source list was for discussion purposes only. It was noted the material is not updated and would have to be re-evaluated again.

Chair Dill commented that the Rate Study needed to be done quicker.

Page 4-9 Leidos Report – FRC Credit Component
"Because the Average Day design standard is 500 gpd per ERU (Equivalent Residential Unit)..."

DISCUSSION:
Chair Dill questioned when the Department calculates the FRC, the Max Day uses 750 gpd, why is the Department crediting the Average day?

The Department will check why there is a credit on the Average Day.

Leidos Report Page 4-11, Table 4-7 - Comparison of Previous and Updated FRCs
The FRC charge of $2,600 did not represent the actual cost of the 5/8" meter. A question was asked by Chair Dill if the $4,600 charge was the full amount or a discounted amount. He recalled $2,600 was 1/6 of the actual service for 5/8" meter.

In *Acting* Manager and Chief Engineer research, he found that $2,600 was discounted but the Department wanted $5,800 which was cut in half. He did not know how the $4,600 was determined.

Chair Dill referred to Page 4-11 1st sentence: *"A number of factors have been identified as contributing to the increase in the FRC."*

There is a perceived increase in this sentence. On the number of factors that are identified contributed to the increase in the FRC, there needs to be a clear understanding.

The Department will research where the rate study is which reflects and justifies $4,600 and if this was the Department's actual cost of service for the 5/8" meter.

Page 4-11 - Last Paragraph
"There are number of reasons for this change, including the closer correlation between system demand and fixture units…"

Charging customers more appropriately is the goal.

Page 4-13 – FRC Implementation
2nd bullet – re: Phasing
"Consider phasing in the full increase of the FRC so affected parties can appropriately adjust…"

There was no proposal for recommendation from the Department regarding phasing. At the Finance Committee level, they did not want phasing. Chair Dill questioned if phasing was resolved.

The Department will provide phasing for the full Board to consider with a few options.

3rd bullet - re Credit on FRC
Chair Dill requested the Department to recommend to the Board - How to determine the appropriate amount of the transfer from the Water Utility Fund to the FRC fund (the collection of FRC costs through rates). If so, the transfer should be to the FRC fund.

Department will prioritize Part 4 Section VII, Facilities Reserve Charge, Proposed Rule Amendments.

The Assessment of Grove Farm Water Treatment Facility attachment to the Leidos report was not an agenda item which not discussed but will only be used by the Department.

A Finance Committee meeting will be scheduled possibly prior to the Regular Board meeting on Thursday, September 25th.

At 4:40 p.m., Chair Dill adjourned the Finance Committee meeting.

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