F.C. 11/6/14 Agenda Item C-2
(Excerpt - FC 9/10/14 Meeting Minutes)
2 pgs

B. Discussion of Equipment Replacement Reserve for Gen III System

Cassingham said Auditor Maher had provided a memo on General Concepts, Methodologies and an Equipment Reserve Schedule for this discussion. She distributed the Schedule of Member Operating and Service Payments from the FY12-13 Audit. She presented several questions for consideration regarding whether current taxpayers should bear the cost of assets for the benefit of future taxpayers by bearing current debt service while accumulating a reserve for Gen III and the uncertainty of accumulating a reserve for equipment, subject to technology changes. She added a Gen III reserve would be affected by the availability of parcel tax proceeds.

Cassingham said this matter was agendized to begin discussion now and to address why members did not set-aside for Next Gen when financing the current system. Gaffney said he is not aware of agencies setting aside for major future replacement projects while they are replacing systems. While some agencies set-aside for vehicle and other equipment replacement, this would be very unusual. He noted the Fairfield–Suisun Water Treatment Plan replacement in Solano as a rare example. Hymel said we became aware of the need for replacement some time ago but the economic downturn and the effects of asking members to put funds aside for a replacement system in that climate was not possible. There is a higher likelihood now of doing so with a parcel tax. Going forward, we do not want to be paying debt service on a system that has outlived its life. We need to consider how to extend system life so as not to be in this position again. When debt service is retired, we should consider whether this becomes a windfall to members or be used for an extended warranty and for a replacement reserve. Berg noted the example of how the PERS windfall was used. Pearce emphasized creating a Gen III reserve is based on receiving a parcel tax. Hymel said this discussion is about due diligence and developing some scenarios about how a Gen III reserve might be created.

Gaffney said we should have an annual replacement set aside, say up to 10% for system replacement study and design. 100% replacement is not rational since the public would be paying twice. Hymel noted the variation of useful life with current system assets. Continuing some portion of member debt service would permit us to cover certain assets with shorter useful lives, which would give us assurance that those assets will be extended for the life of the replacement system. Pearce agreed with setting aside frontend monies for a replacement system, given how our Reserves have been used in planning for the Next Gen System. Hymel said we want to assure voters that with a parcel tax, we are taking steps to assure the Next Gen System lasts its useful life and we are planning for any uncertainties and at least partial replacement. Gaffney said if we continue current debt service collections beyond retirement, it would generate $2.2M per year. He said we had also discussed using any available funds to add additional sites beyond the 4 budgeted. Tackabery said 7 sites were prioritized, 4 budgeted and with favorable bids, we might be able to add sites. Hymel said he had also hoped the bump in operating costs for Next Gen with additional sites would be covered by maintaining ongoing debt service payments along with setting aside for a replacement reserve.

Item B. Discussion of Equipment Replacement Reserve for Gen III System (continued)

Hymel discussed the Members getting used to the $450,000-per-year payment for a System Upgrade Agreement as part of the useful life extension/system replacement reserve approach. Tackabery and Nelson said a prospective vendor would upgrade the replacement system every 2 years with mostly software and some backbone equipment. Chuck added this does not include mobile support. Tackabery clarified for Gaffney that upgrades over 20 years is dependent on the vendor. Pearce clarified that an SUA may or may not be from day one and may be in increments thereafter based on the vendor. Nelson said there is usually a warranty period followed by the SUA but this is vendor dependent.

Berg asked why there is no drop-off in O&M when Gen I is phased out. Hymel said we are adding more sites with Next Gen. Tackabery said there will be more lease expense, some utilities drop-off and more labor costs. Hymel said what we are trying to achieve is to think about extension of Next Gen useful life, develop scenarios to fund it and set aside for some Gen III replacement costs. In response to Gaffney, he said a policy should drive some offset for increased operating cost while funding useful life extension and some replacement reserve. Gaffney said this policy would have Members understanding and considering such a plan early on versus using retired debt-service for other purposes.

Gaffney said he envisioned project financing with a parcel tax as not having to sell all the bonds right away. We could start with a small bond issue or pay as we go for a year or two to fund design to save interest. We could sell bonds when we start construction. The parcel tax would generate $3.6M per year. Berg said the first order of business would be to reimburse the MERA Replacement Reserve for all related expenses of the Strategic Plan Implementation and Next Gen System planning.