EXECUTIVE COMMITTEE MEETING
FRIDAY, APRIL 9, 2010
ADVISORY BOARD OFFICE
Minutes Approved at the September 10, 2010 Meeting

Present: John Sullivan, BOSTON; John Sanchez, BURLINGTON; Jay Fink, LYNN; Wiff Peterson, NATICK; Lou Taverna, NEWTON; Jeff Zager, READING; John DeAmicis, STONEHAM; Walter Woods, WELLESLEY; Zig Peret, WILBRAHAM.

Also in attendance, Andrew Pappastergion and Joseph Foti, MWRA BOARD OF DIRECTORS; Joseph Favaloro, Cornelia Potter, Matthew Romero and Mary Ann McClellan, MWRA ADVISORY BOARD STAFF.

I. Approval of the March 12, 2010 Minutes of the Executive Committee

In the absence of Chairman Katherine Haynes Dunphy, Jay Fink, Vice-Chairman of Operations, called the meeting to order at 8:38 a.m. A Motion was made **TO APPROVE THE MARCH 12, 2010 MINUTES OF THE EXECUTIVE COMMITTEE**. It was seconded and passed by unanimous vote.

II. Status: Advisory Board Preliminary Budget

MWRA Advisory Board Executive Director Joseph Favaloro gave a preview of the Advisory Board's Preliminary FY11 Budget. Despite the tough economic times and the loss of interest income, staff was able to level fund the Advisory Board's budget based on the ongoing discussion on the rental lease, staggered step increases and personnel matters.

Only a few line items will increase, including printing, to cover the costs of new letterhead, envelopes, business cards, etc. A new line item for Consultant Services will appear. Rent and lease costs will be reduced. The overall budget for the Advisory Board will be nearly level funded at about $452,000. Mr. Fink said that is great because the Advisory Board charged the MWRA to come in at zero as well.

John Sanchez asked what happened with personnel. Mr. Favaloro said as was discussed at last month's meeting, Ms. Potter will be moving to consultant services.

Mr. Favaloro noted that this budget reflects telephone and electrical costs. Staff has been in discussions with the Authority relating to those two line items; because the Advisory Board will be in the same building, it makes sense to tie into the Authority's telephone system. The Authority pays the electricity for the entire building and then receives a credit from the landlord; therefore, the Advisory Board may not take the funds for electricity from the Authority just to give it back.

III. Status: Advisory Board Charlestown Lease

Mr. Favaloro said the Advisory Board has received a commitment letter from Robert Kenney, the landlord in Charlestown, to begin the lease process. Improvements will take between six to eight weeks. The space will be available no later than August 1, 2010.

Staff has also begun to have discussions with Nathan Miller, the landlord of 11 Beacon Street, about leaving earlier than the lease expiration date; we will currently be paying lease costs until the end of September (11 Beacon is now under a purchase and sale agreement). The Advisory Board will have a free month in October in Charlestown and then the $18.50 per square foot goes into effect on November 1.

IV. Preview: Advisory Board CIP and CEB Comments

Matthew Romero, Senior Finance and Policy Analyst, provided the Committee with an update on the Integrated CIP and CEB Comments and Recommendations Review process. For the FY11 CEB, staff took a different approach. Instead of conducting a traditional review after receiving the proposed CEB from the Authority, Advisory Board staff challenged the Authority early on in the process to meet a $0 rate increase.

In October a letter was sent to the MWRA Board of Directors from the Advisory Board requesting the $0 increase. In November, the Board of Directors had their initial discussion on this recommendation. In December, Advisory Board staff made a presentation to the Board on one pathway to achieve this goal and outlined a series of tools for the Authority to use to develop their own pathways come get to a $0 rate increase. In January, MWRA staff provided four options to the Board, which were then voted on. In February, the preliminary assessments, which should be the same as the final assessments, were issued to cities and towns with a 1.49% rate increase, the lowest increase since 1996.

The original planning projections from the FY10 approved budget had 6.41% increases projected for FY11 and FY12. This change to the budget will also reduce the projections for FY11 and FY12 to under 4%.

The new approach the Advisory Board provided in FY10 introduced the concept of a “toolbox” instead of specific recommendations. Several of these tools were used in the FY11 proposed CEB. The tools the Authority used to get to the low rate increase included no COLA increases for FY11. Further, a pension fund expense reduction, which comes on two fronts, was utilized. In the FY10 CEB the MWRA funded its pension based on the actuarial report it had at that time, with an additional $2.8 million optional payment toward the joint Other Post-Employment Benefits (OPEB) and Pension liability as well. That $2.8 million is still in play this year and the Advisory Board has a commitment from Authority staff that they will not make that deposit until June. The Advisory Board is going to push for an active discussion and vote from the Board of Directors to confirm that these funds won’t be deposited because it is $2.8 million that doesn’t necessarily need to be spent and could be providing additional relief to offset expenses in FY11.

This year the Authority made no additional payments to the pension other than what was scheduled, although the amount was taken from an actuarial study that was done at the worst economic time and showed that the Authority was underfunded. In fact, MWRA is now funded in the 80% range due to the slight favorable returns since the actuarial study was done. The Authority agreed to do an interim actuarial study to take into consideration that the Authority is in a slightly better place this year.

The Board has authorized up to $24 million in defeasance using the current year's surplus; the majority of the surplus comes from a favorable interest rate on the variable rate debt. The MWRA had a high interest rate assumption and the market continued to stay low. While the Authority did have some surplus in Direct Expenses, it did have a significant amount of unplanned spending with the wet weather events of March so most of the Direct Expense surplus has been eaten up. The $24 million surplus does not include the $2.8 million optional Pension payment.

Wiff Peterson asked how exposed the Authority is in terms of variable rate debt if it gets into an inflationary period and there is some pressure on government bonds. Mr. Romero said there is always some risk with variable rate debt by its very nature. In the Advisory Board comments, staff breaks out a portion of subordinate debt to be swapped to fixed so that it is synthetically fixed even though it is "variable". As a short-term strategy, MWRA is not taking on any more variable rate debt. Mr. Favaloro added that MWRA's Treasurer will be doing a presentation at the full Advisory Board meeting on the entire debt portfolio and reserves and he could answer questions on how they are dealing with the variable rate portion of the Authority's debt load.

Mr. Romero said at this point the MWRA has budgeted a 3.25% interest rate assumption. While rates have remained low, it is possible that there could be a wide swing within the next year; however, both the MWRA CFO and Treasurer have said they are comfortable with 3.25%.

The largest amount for Direct Expenses is staffing; MWRA has continued to ratchet down on staffing and has maintained its year-end target for next year, with a vacancy rate built in. On Indirect Expenses, if the $2.8 million optional Pension payment and the updated annual contribution based on the interim actuarial study are taken out, it is not surprising that Indirect Expenses went down slightly.

The most important tool the Authority used was what the Advisory Board is calling "targeted rate relief restructuring." MWRA did a major restructuring three years ago and since that time staff has watched for market conditions that lend themselves to any additional restructuring opportunities. The Board has set a policy for a certain amount of savings that must be achieved, or a threshold that needs to be crossed, before they undertake such a restructuring.

This year, in response to the Advisory Board's $0 rate increase challenge, the Authority undertook a restructuring that will cost a bit more over the term of the debt but will provide targeted relief for FY11 principally, with some benefit for FY12 and FY13 as well. This is a dramatic shift. Even in the Advisory Board's recommendations for restructuring it has always been understood that it would be restructuring for savings. While it is not a prudent thing to do all the time, providing direct and targeted relief in these years is actually worth that tradeoff in this instance.

Advisory Board staff regards the less than 4% rate increases for FY12 and FY13 as a starting point and will work to find ways to reduce those increases. The FY11 increase of 1.49% is the lowest rate increase since 1996.

Moving forward to the FY11 CIP, up until now the total capital spending the Authority has undertaken is $7.9 billion; of that, outstanding debt is $5.8 billion, which is essentially 73% that is still outstanding. Moving forward, the Authority and the ratepayers face the challenge of paying this debt without Debt Service Assistance (DSA). The mountain of debt was structured with the assumption that there would be a certain amount of assistance from the Commonwealth through DSA; staff does not know if DSA will be coming back. Debt service climbs until 2022. By FY20, debt service, as projected, is 65% of total expenses; in FY11, it is 59% of the budget, which is already a significant portion of the expenses. By FY20, debt service will be a driver and far more dominant.

Ultimately, Advisory Board staff is saying that you control rates in the future by controlling capital spending now. While reducing capital spending now and in the near years may not necessarily have a direct benefit on debt service expense in the next few years, it will help moving forward.

In the FY10 recommendations, the Advisory Board recommended that the MWRA reduce its capital spending through the remainder of this cap period by $100 million over the four remaining years. There are ways that the Authority can reduce the capital expenses by making realistic projections, rather than utilizing “plug” numbers. In its current proposed CIP, in FY13, MWRA has a level of capital spending that it is not allowed to meet under the provisions of the cap, which states that MWRA can only go plus or minus 20% of the original cap in that year. The Authority is currently at about 30% in FY13, which means some of that will have to be pushed into the FY14-18 cap.

A major recommendation of the *Integrated Comments* is that no future capital spending cap can exceed $1 billion. The Authority needs to challenge itself to ratchet down and tighten up its capital spending. At the end of the current cap period, mandated CSO spending begins to measurably decline. The Ultraviolet Project is still out there, which is mandated, and EPA may come up with further mandated projects in the future, but at this time and moving forward, the majority of projects will be more directly controlled by the Authority.

The Authority has already begun to lay the foundations for updating its Master Plan. The Advisory Board believes that the Authority can get to under $1 billion for each cap period by prioritizing its Master Plan.

Facilitated discussions on system expansion were held. The Advisory Board’s and MWRA’s primary interest for system expansion is to streamline the process to join the MWRA water system for communities that have a demonstrated and measurable need.

The linked components of system expansion are withdrawals (selling the water), downstream releases (which is something that WSCAC and the river associations have been interested in) and holding some of the available consumption in reserve. A safe amount of 36 million gallons per day (MGD) has been identified to be split as 12 MGD for sale, 12 MGD for releases and 12 MGD for reserves.

The state's primary interest is in "smart growth" and that was the genesis of the facilitated discussion.

The hatchery pipeline project is in the FY11 CIP, which will provide oxygenated water to a trout hatchery downstream. It should also be pointed out that it is tied to the releases portion because that is the mechanism whereby the water would be released as well.

Lastly, incentives to join the MWRA were discussed.

The Advisory Board believes the safe yield of 36 MGD should be revisited because this amount was based off of estimates of safe yields and conservative withdrawal amounts from 2006. By the time there is some forward motion on system expansion, it could be five years later and consumption continues to drop, even with the addition of new members.

The Advisory Board would like to underscore to all the players involved that the MWRA will not spend a dime on the hatchery, releases and smart growth until there is some forward motion on streamlining the process. The Advisory Board's suggestion is that MWRA does not fund or undertake the project for the releases (the hatchery) until it sees its first entrance fee under this facilitated system expansion and streamlining process.

Recently, with regard to discussions at the Executive Committee, the Advisory Board's three Board members submitted to the MWRA Board of Directors a request for a personnel study. The Board challenged staff to begin preparations for a new staffing study, similar to the Black & Veatch study that had been conducted in years past.

MWRA has reduced staff by 31% since FY97. Since the MWRA has continually said it is an agency transitioning from construction to maintenance, it is a good time for a look at its staffing to find the right level of staffing for the areas that need it for this core mission, not the core mission that it has undertaken for the past 25 years. The Advisory Board recommends setting and establishing updated levels of staff needed to execute MWRA's core mission.

The MWRA is approaching five years beyond the expiration date of its current NPDES permit. DEP is expecting a new draft permit from EPA sometime before the end of the federal fiscal year. The Advisory Board's principal recommendation is for the MWRA not to co-permittee with the communities because it will allow EPA to come after one big entity that represents all of the communities rather than to go after the individual communities.

By 2020, rate revenue, in the current planning projections, approaches $1 billion and increases 68% over FY10 to FY20. The Advisory Board will push the MWRA over the course of the coming years to find additional sources of funding. Look for opportunities in state and federal funding. With 65% of the MWRA's expenses becoming debt service and a 68% increase in rate revenue, it is incumbent upon this office and the Authority to push for DSA to make a return into the state budget and also to explore any potential avenues from state and federal funds that could also help.

With system expansion there are entrance fees, which provide a one-time benefit and also new members would help to spread the base; since we are seeing drops in consumption on the retail side, the only way to possibly keep up with some of those drops and keep the cost down on the community side is to spread the base more.

Mr. Peterson said having more members is extremely important. Could there be incentives for new members to come in; for example, if half of our costs are fixed and half variable at the time they come in, and the incremental cost of serving a new member is only 50% of the current rate, the other 50% is going toward carrying fixed costs. MWRA could have a period of time for new communities that come in, say three years, in which they start at 50%, then go to 65% and then 85% and then they go to 100% on the rate and that gives incentive to the community to join and it helps them cover some of their transition costs in terms of coming in. It is a different way of structuring the rates for new members but it is in the interest of the current members.

John Sanchez said the issue is the entrance fee as opposed to the rate. The MWRA rate itself is a very competitive rate. It is the entrance fee that is an issue. How is the entrance fee calculated? Mr. Favaloro said the calculation is based on all of the investment in the system and a percent based on millions of gallons is how they calculate the charge out.

Mr. Romero said staff is trying to reframe the words “entrance fee” into something that makes it clear; people think the MWRA is charging a luxury premium, when what it is really doing is recapturing those costs because it is not fair that the other communities have already paid. It is not fair for a new member to come in and benefit from all of those costs that the member communities have paid.

Mr. Peterson said it might be fair because the primary thing that we are focused on is rate stabilization. If we want volume to help stabilize the rates and people to share in the current costs of the system, it is in our interest to incent those people rather than hit them heavily. We want to make it easy for them to transition in so that they are sharing this huge capital cost burden that the system has. When you go back and ask for a retroactive payment that discourages new people from coming in. You hurt your objective, which is to spread those costs over a larger user base. Mr. Romero said one of the things we have done is to allow communities to spread the entrance fee payment over the course of 20 years.

Mr. Romero said an additional potential revenue source could be private advertising. The Norumbega facility is beside the turnpike, why not explore putting billboards up?

The economic landscape is still uncertain. The tight budget is good but it is still important to push the MWRA to tighten it up even more to be able to tackle the mountain of debt through 2022.

V. Update: "March Madness"

Mr. Favaloro said the never-ending rain of last month had significant impacts on the MWRA and the communities. DEP has been invited to come to the Advisory Board meeting next week to talk about notification processes and reporting requirements during events such as these. For example, Stoneham had a discharge going and instead of pumping it into the sewer they took it out by truck, moving it as opposed to doing a direct discharge; they didn't have to do that.

Authority staff will be at the meeting to talk about the overtime costs and diesel fuel costs, which had a significant impact on the Authority's budget, which fortunately had a surplus to deal with these extra costs.

VI. Update: Legislative

The House Budget comes out next week and more than likely will not include DSA. Staff had more success in the House Budget getting earmarked funds for Clinton ($500,000). In reading the sense of the Senate Ways and Means Chairman's comments last week, he was clear there will be no earmarks so staff does not know how this will play out.

VII. Amendment to the Local Water System Assistance Program

At last month's meetings the Executive Committee/Advisory Board approved the Local Water System Assistance Program. At the Advisory Board meeting, Wakefield asked if booster pump stations could be included. After some discussion, it was decided that an Operations Committee meeting would be held; however, staff would suggest that the Program just be amended. Lou Taverna made a friendly amendment for the Advisory Board's next meeting.

Jay Fink asked if Wakefield articulated how the inclusion of a booster pump station would relate to the improvement of water quality. If they were to make the case that they want a booster pump station with the emergency ability to feed chlorine or disinfection in the case that it is needed, then it would qualify for improvement of water quality. Mr. Fink said if everything else is done and pipelines are clean, he has no objection to it.

VIII. Approval of the Advisory Board Agenda for April 15, 2010

A Motion was made **TO APPROVE THE ADVISORY BOARD AGENDA FOR THE APRIL 15, 2010 MEETING.** It was seconded and passed by unanimous vote.

IX. Adjournment

A Motion was made **TO ADJOURN THE MEETING AT 9:55 A.M.** It was seconded and passed by unanimous vote.

Respectfully submitted,

Lou Taverna, Interim Secretary