



TO: Chairman and Board Members
FROM: Mark Foree, General Manager
Jeff Tissier, Chief Financial Officer
DATE: March 4, 2011
SUBJECT: **Status report on the merger of Washoe County Department of Water Resources water utility into TMWA, discussion and possible direction to staff**

RECOMMENDATION

Staff recommends that the Board accept this report on the status of the pending integration/consolidation of DWR's water utility function and TMWA.

DISCUSSION

Overview of the due diligence process

Site/facility, land/easement, water right, and human resource assessments preceded the development and finalization of combined operating plans for the North Valleys, Spanish Springs and the South Truckee Meadows areas. After completion of the operating plans, capital improvement plans (CIPs) were finalized. The last major phase of the due diligence process will be the development of financial models incorporating critical elements of the operating plans and capital improvement plans. Once completed, an informed decision can be made with respect to the feasibility of an integration/merger.

The results of the financial analysis will provide direction on the optimal positioning of both organizations to achieve a successful merger and, to the extent possible, indicate optimal timing of such a merger. Bond market conditions will play a significant role in the timing of the merger since the publicly sold bonds of DWR will have to be refinanced (defeased). Certain other elements that will be necessary, and difficult to place in the merger schedule currently, include transfer of DWR State loans.

The financial analysis is expected to be completed in the March/April timeframe, with next step proposals for consideration by the TMWA Board and the Board of County Commissioners shortly thereafter. Development of the schedules to the Interlocal Agreement (ILA) addendum will be forthcoming in concert with the finalization of financial projections for the independent and combined water agencies. New information or updated assumptions that materially affect the financial analysis will require reiteration of the analysis. All relevant documents will be subsequently amended as necessary.

Status of Merger Activities

The following list summarizes the status of the most critical elements of the integration/merger due diligence process.

- Site/Facility assessments of all DWR facilities – completed and documented. This information was incorporated into the final capital improvement plans (CIPs) by service area.
- System Control and Data Acquisition (SCADA) assessment – evaluation of DWR’s electronic control systems completed. This information is being archived for future reference. This was a major accomplishment because of criticality of SCADA for future operations.
- Land and Easement assessments were completed and title deficiencies identified. DWR is prioritizing corrective measures for the deficiencies.
- Water Rights assessments have been completed with no significant issues noted. Potential increased optimization of the pool of water rights under one agency will be reviewed.
- Operating plans for conjunctive use of water in Spanish Springs, the South Truckee Meadows, and the North Valleys have been completed. These plans provide the framework for staffing requirements and the development of operating costs, as well as anchor the financial projection for the combined entity.
- DWR’s and TMWA’s short term (5-year) CIPs are complete. TMWA has finalized its 2010-2030 Water Facility Plan. This plan provides a preliminary long term (20-year) CIP. This long term CIP describes major facilities that are anticipated over the time period for system rehabilitation (serving existing customers) and new or expanded facilities (serving new customers). The CIP for a combined water entity has been drafted by TMWA and DWR staff; the next step is to assess joint operation risks in order to prioritize facility needs and confirm the estimated timing of construction.
- Human Resources due diligence is virtually complete with the exception of further work on the post-retirement medical (underway), union discussions, and eventually employee transfer matters. Once the financial projections are solidified, it is anticipated that union negotiations can begin.

Financial Activities

Underwriters have been selected for potential future bond sale(s) to defease WC/DWR publicly issued debt and to provide potential funding for high priority capital projects. Continued monitoring of capital market conditions is essential to assess the feasibility of DWR publicly issued debt refinancing, as well as potentially refinancing the remaining 2001A maturities of TMWA debt (\$20 million left in outstanding debt related to the original acquisition bonds). Currently only very limited, and high-risk, refinancing opportunities exist.

The following financial activities have been completed:

- Public Financial Management (PFM) has been retained to develop assumptions for financial forecasting and critical review of financial work being performed by TMWA and DWR finance personnel.
- In February 2011 TMWA provided PFM with its five-year standalone financial projection, which incorporates proposed future developer fee revisions.
- “Start-up” or transition costs for investments associated with the merger have been refined. These include:
 - Cost to transfer customer account records (*finalized*)
 - Of various alternatives, the lowest incremental costs of additional housing of DWR personnel transferred to TMWA (*finalized*)
 - Cost of incremental IT support for transferred personnel (*finalized*)

Merger Activities Underway

Financial Items

The financial analysis being prepared in conjunction with PFM is currently underway. The following specific items continue to be developed or refined:

- Key assumptions for independent and combined agency operations
- DWR revised budget and five-year financial plan as a stand-alone agency
- Financial trend analysis based on actuals through June 30, 2010
- The number and complement of staffing for a combined organization
- Projected operating costs that are consistent with independent and combined operating plans
- Projections of investment income, developer fee collections, and debt payments.
- Cost to serve customers for each independent agency, review adequacy of water rates and developer fees. Water rates and developer fees for the combined agency must also be projected for comparative purposes.
- Identification and quantification of financial exposure / risk to the combined agency of transferred assets and future service commitments

In addition staffs at DWR and TMWA are working on the following:

- Water load analysis (ratio of surface to groundwater use) for the DWR service areas is being analyzed for future demand projections. This analysis feeds directly into the projection of future water sales revenue.
- Outstanding debt-related issues:
 - Washoe County is pursuing creation of a County Bond Bank (which requires changes to the Nevada Revised Statutes) to provide an alternative favorable financing vehicle for water projects, well as other public services.

- Nevada State Treasurer permission to assign the outstanding loans from DWR to TMWA is needed.
- Negotiations to strip the water revenue pledge from the Storm Water Bonds issued by DWR must commence.
- Bond market conditions will continue to be monitored to identify opportunities to defease the outstanding publically sold water bonds issued by DWR in 2005.

Other Items

- Work items that will continue to be of high priority, regardless of the pace of merger, since the goal is consistency in water service to the region, include these:
 - TMWA and DWR personnel are reviewing TMWA's Rules of Service and WC/DWR Ordinances for alignment and harmonization. Development of proposed changes to Rules of Service and Ordinances to minimize changes in service to customers are close to completion. All proposed changes must be brought forth for adoption by both agency governing boards.
 - TMWA and DWR have established joint planning areas for the South Truckee Meadows and for Verdi to promote more efficient water service and protect groundwater sources, which benefits all water customers in the region.
- The South Truckee Meadows General Improvement District (STMGID) Local Managing Board (LMB) has retained a financial consultant to examine the financial implications of service provision options upon the merger of TMWA and DWR.