

**CITY OF PARK RAPIDS  
CITY COUNCIL WORKSHOP  
JUNE 11, 2013, 5:00 PM  
Park Rapids Public Library-Lower Level  
Park Rapids, Minnesota**

**1. CALL TO ORDER:** Acting Mayor Paul Utke called the City Council Workshop for June 11<sup>th</sup>, 2013 to order at 5:00 p.m.

**2. ROLL CALL:** Present: Acting Mayor Paul Utke, Councilmembers Dave Konshok, Rod Nordberg, and Erika Randall. Absent: Mayor Pat Mikesch. Staff Present: Administrator John McKinney, Planner Dan Walker, and Clerk Margie Vik. Others Present: Ulteig Engineer Brian Hiles and Sarah Smith from the Enterprise.

**3. PRESENTATION:**

**3.1. Update on Funding Package for the Well and Water Treatment**

**Facility:** Brian Hiles, from Ulteig Engineers, stated this will be an informal presentation on the updated project costs, and the loan and grant amounts. I have a computerized spreadsheet that I can analysis the city's water rates, where they are now, and what they're projected out to when the project's done. We can plug in different financial scenarios and get instant results to see how changing the rate structure affects usage rates and fees. We'll play with the numbers to see how they interrelate.

Hiles stated we did take the bids on the project with the low bid amount from Di-Mar Construction. The total project cost is \$2,590,000.00. That includes construction, contingencies, engineering, and funding assistance. All of those things are wrapped into the total project cost. Of that amount, we're looking at a PFA loan amount of \$1,315,000.00. The rest of the project costs would be coming from the DEED grant of \$600,000.00. I did get confirmation today that the city is getting the DEED grant. The funds will be available after July 1<sup>st</sup>. PFA principle forgiveness amount is \$677,600.00. Total "free money" (grant, principle forgiveness) is \$1,277,600.00, which comes out to about 49% of the total project cost. It's a very nice funding package. The PFA interest rate is 1%. It's a really low interest rate on the \$1.3 million loan amount.

McKinney questioned is that locked in, or is it subject to when we take it out? Hiles stated it's subject to final project costs. We do have \$100,000.00 for contingencies built into that amount. If there's any change orders that happen throughout the project, whether they increase or decrease costs, that will all be reflected in those numbers. The interest rate is locked in. Utke questioned is that based on a certain term? Hiles stated we can do a fifteen, twenty, or thirty year term, and they're all at 1%. I can show you the differences between those three structures.

Hiles stated the city's current rate structure is a \$14.00 a month base fee, 1-15,000 gallons of water is \$3.15 per 1,000. Anything over the \$3.15 charge, up into the 15,000-30,000 gallons of usage is \$3.47 per 1,000. Those numbers don't show up in the spreadsheet. That number is going to vary from month to month, so everything is based off

of the initial \$3.15. Anything above that ends up being profit for the city, over and above what you need to run the system. Based on your current set up, your yearly base rate of \$56.00, and with the \$3.15 rate, you should be bringing in \$46,000.00 as depreciation expense, which can go into your water reserve.

McKinney stated most of our outstanding loans require us to have some cover allowance. That's optional on our part. Hiles stated right now your water fund has a balance of \$1.7 million. You're sitting pretty good with that. There is one outstanding debt service with principal payments of \$60,000.00 a year for the last water tower project that you did. There's about ten to fifteen years left on that to pay off. The percentage rate on that is 2.57%. That is also a PFA loan. McKinney stated I don't know what the call options are on that money. We can talk about what we want to do with the money we have. The obvious use would be to pay some cash for the project, but we can borrow money to finish off the project at 1% and we have 2.57% money out there. If you're going to use any money you'd want to pay off the expensive debt if you can. The point is we have \$1.7 million, but we have some obligations against that. We couldn't spend it all if we wanted to, you need some reserve. We are in good shape with that reserve.

Hiles stated in the next example we increased the depreciation to \$100,000.00. In order to generate that \$100,000.00 your quarterly base rate would increase to \$22.50 in order to keep that rate at \$3.15. That gives you an idea of an increase of \$54,000.00 in the budget does to your system. McKinney stated that's fully funded depreciation based on present cost. Hiles stated right. McKinney stated there are several factors that go into this. If we were to have a depreciation fund of that order that means when the thing wears out in twenty years, we'd have the cash to replace it, if we could replace it for what we paid for it today. Hiles stated that would be replacing just the working parts, not the building itself. At \$50,000.00, over twenty years you'd have \$1 million set aside to refurbish the plant, if you didn't have any other expenses. McKinney stated assuming that you haven't drawn down on it over the years.

Hiles stated I have a few examples where I used zero in the depreciation. The key to these is to see the differences in the fifteen, twenty, and the thirty year loan repayment. At fifteen years, at 1% interest, we're looking at \$99,000.00 a year. Under that structure, if you wanted to keep the base rate at \$14.00 a quarter, the cost per 1,000 gallons would increase 80 cents. If you kept the \$3.15, you'd have to increase to \$108.00 a year, or \$9.00 a month. So there would be a \$13.00 per quarter increase in the base fee, at zero depreciation. At twenty years at 1% interest, the payment is \$75,000.00 a year, with \$3.71 as your rate per 1,000. It's a dollar a month savings going from the fifteen year to the twenty year.

McKinney questioned what's the total cost of borrowing? Hiles stated for fifteen years of interest it's \$111,400.00, for twenty years it's \$145,600.00, and for thirty years it's \$216,018.00. It doesn't save you a lot going from twenty to thirty years. Based on that my recommendation would be to do the twenty years that gives you the least quarterly impact with a relative interest savings. Plus you're not getting out past the projected life of your facility. McKinney questioned are these callable at any time? Hiles stated I believe they are. McKinney stated but we'd have to pay it all off, not part of it? Hiles stated I believe so.

Hiles presented several scenarios with different annual base rates, and different user fees, and with different levels of depreciation. McKinney questioned from an engineering standpoint the depreciation on the facility, wouldn't that drop down when you reach its maturity if it's set up for a twenty year term. Hiles stated this is set up that it's not

really depreciation, it's more like reserve fund. It's a deposit into a reserve fund. McKinney stated usually a reserve fund is based upon your outstanding debt. After we pay off the existing bonds, the requirement would go down. Hiles stated it could go down. You'd want to leave something in there. McKinney stated if you pay off the old debt, you don't have that reserve requirement anymore. Hiles stated the way your rate structure is set up, is basing everything on a flat \$3.15. When you make an increase, then that's basically profit for the water system and can be put into your reserve account. Your water rates should be an evolving entity. That first year after you adjust them you should go back and look to see how it really affected us. It should be looked at on a yearly basis.

McKinney questioned don't the bond documents for the PFA require an annual rate study? Hiles answered no. You have to provide them with an audit. They're just looking to make sure they are going to get their money back. They don't look at if you're adding to your reserve.

Nordberg questioned what kind of history do we have over the past twenty years? When was the last time we raised the rates? Konshok stated about two years ago. Nordberg questioned was it a necessary thing at the time? Walker stated it was done as a conservation tool. Hiles stated a couple of years ago the DNR said that if you added a conservation scale to your rates that you could decrease your DNR fee. A lot of cities added that portion to their rate structure. It's supposed to be a motivation for people to use less water. Nordberg questioned do we know if it does that? How much are we pumping relative to before it went into effect? Hiles stated I'm sure we could look at the numbers and see. Nordberg questioned how much of our dollars come from those people that are over the minimum? Hiles stated it depends on how detailed the records are of the water sold on a month by month basis. With some digging you could pull those numbers out.

Nordberg questioned how do we compare with comparable cities like Detroit Lakes or Bemidji? Konshok stated we looked at that when we adjusted the rates. Hiles stated part of the PFA process and the reason you are qualifying for the grant money is that they look at an affordability rate. They use the median household income versus comparing you to comparable sizes. They compare you to comparable income towns. They take the median household income and multiple it by a factor that they use and come up with an affordability rate. That's what they say you should be charging the average resident on a monthly basis. Anything that would go above and beyond that qualifies you for grant money. They're saying that you are close to that affordability rate with your rate structure, or where your rate structure will be when you're done with this project. You'll be comparable with any town that's gone through a PFA or Rural Development Project for a water improvement. A town that hasn't had to do this might have lower rates, or they figured out a different way to pay for it. You can either use your rate, an assessment, or a levy. Your water and sewer systems should pay for themselves. You shouldn't be using levy dollars to pay for your water and sewer systems.

Nordberg stated the balance between the base rate and the quarterly usage rate is important too. Hiles stated yes it is. What this spread sheet does is it tries to take all of your fixed amounts and tries to get the majority of your income into the monthly base rate so you're not as dependent on your higher rate structures to make sure you have enough money to cover your operation and maintenance costs. McKinney stated otherwise if they drop down in usage it kills you on income. Hiles stated with the conservation rates the idea is to get the water usage back in line with what you would typically expect from a house.

Utke questioned do we know what the average user/household pays? Hiles stated in design you're usually looking at 100 gallons per person per day. The average house is two and a half people. A house uses about 250 gallons a day. That's a design rate. At that design rate in a month it would be 7,500 gallons, or approximately \$100.00 a quarter.

Nordberg stated I agree with the twenty year term based on my feelings because you'd be spending money on interest after the useful life of the facility. I'd like to limit our discussion to the twenty year term. We still have a lot of variables to go after yet. Utke stated twenty years seems to be the most logical. Hiles stated when you balance out the term versus the interest, versus the payment structure, and the expected life of your filters. Hopefully they last thirty or forty years. But it's designed to be a twenty to twenty-five year facility. That would be just the filters. The building should last as long as a block building will last. Your backwash tank is concrete. That will last a long time. There is also enough room for another filter cell in the building. I've seen some filters last fifty to seventy years with routine maintenance.

McKinney stated we wanted the Council to be able to ask all of the questions that you have. We're going to firm up these numbers and it would be prudent of us to run these past our fiscal agent to make sure there isn't something that we haven't thought of, and in addition to that to weight our options on paying out on the existing debt. Konshok stated we're not bonding for anything, it's all grants or loans. Hiles stated there is a debt service for the new water tower. We are checking out the possibility of paying off that existing debt and if it's feasible. You do a general obligation bond to PFA at the beginning of the project. Once you close your loan with them, then that bond closes.

Hiles stated keep in mind that the first money to get spent is the PFA loan. If we do have some cost savings it comes out of the "free money". That loan will be the loan amount. It's based on the affordability rate. Towards the end of the project and if there is still some contingency money left, we'll look to see if there is anything else we can do with that money, on the water side. We'll look to leverage that for any other approved things in the city instead of having to turn it back. Because it is already grant money that has been approved and set aside for the city. We've done that for some of our other projects.

Hiles stated the main reason for this workshop is for the Council to get an idea of where the funding and rates are going to fall for the project. This is to ease your minds so going into the Council meeting tonight when we ask you to award the project. This is all fluid. We play with the numbers and then re-evaluate it again. McKinney stated the question has been what is this project going to do to the rates. We didn't know that for sure. The numbers are coming together now, and you'll have a sense of how this will impact the people.

Hiles stated the first big payment will be due at the end of 2014. We have a year and a half to plan ahead for it. There has been no rate increase this year. You could look at incremental rates over the years to spread out the financial impact. You have to think about building up your reserves to make that first payment at the end of 2014. March of 2014 is the completion date for the project.

Nordberg stated we should be thinking about when rate changes kick in we need an announcement so it's not a secret to people. Konshok stated stepping the increases will help a little. Hiles stated if you spread it over three increases every six months then it's easier to digest.

Konshok stated I'm looking to balance it. We do have some households that are paying just the standard base rate. You have others that are paying high usage. You don't

want to put the high burden on either one of those. It seems unfair. Hiles stated the way your rates are set up the elderly population is going to be paying a lot less than a family of six. A single widow is not going to use 15,000 gallons of water in three months. Utke stated we want it most fair across the board. Hiles stated you have done a good job of getting to the point where the people that use the most pay the most.

Nordberg questioned do the snowbirds pay the base rate all through the winter? Konshok stated there is no seasonal adjustment. Hiles stated I don't think that they can take the meter out. McKinney stated unless they just discontinue their service entirely as opposed to just turning off the valve. Hiles stated then they'd have a new hookup fee every year. They can turn their water off so there's no water to the house, but they still have that base fee. Because whether they're here or not the water is still available to that house. Utke stated the infrastructure is still there. Hiles stated we had to design the plant to service them during the summer. Konshok stated but their usage drops. Nordberg stated paying the minimum seems like it's sharing the cost.

Konshok questioned do you need any decisions for the grant or loan process. Hiles stated no this is all just on how you need to pay for the project. Utke stated we need to know this first before we decide how to increase rates. Hiles stated you do have the option of having the \$1.7 million in reserves that you could push this out a little bit because you do have some funds there to help pay for it. Nordberg questioned how long have we been building up that reserve from zero? Was there a time when we had no reserves? Konshok stated with an enterprise fund there's always minimums we're expected to have. We've always had reserves on our enterprise funds. The level of it is what we adjust and decide. Hiles stated I think you are required to keep four to six months of operating expenses on hand. McKinney stated there may be other costs to this utility besides this new project as we go through the years.

Hiles stated we are going to ask the Council to award the project tonight at the regular Council meeting. PFA has just added the portion for grant money on the drinking water in the last couple of years. Three years ago the city wouldn't have gotten any of this. PFA didn't have the principle forgiveness funds.

**4. ADJOURNMENT: A motion was made by Nordberg, seconded by Randall and unanimously carried to adjourn the special meeting at 5:45 p.m.**

[seal]

\_\_\_\_\_  
Acting Mayor Paul Utke

ATTEST:

\_\_\_\_\_  
Margie M. Vik  
City Clerk