

OFFICIAL PROCEEDINGS OF THE
BOARD OF WATER, ELECTRIC,
AND COMMUNICATIONS TRUSTEES
OF THE CITY OF MUSCATINE, IOWA
September 29, 2009 - 5:30 P.M.

The Board of Trustees met in regular session at Muscatine Power and Water's Administration/Operations Building, 3205 Cedar Street, Muscatine, Iowa, on Tuesday, September 29, 2009, at 5:30 p.m., CDT.

Chairperson Ingstad called the meeting to order. Members of the Board were present as follows: Trustees Warren Heidbreder, Scott Ingstad, Joan Axel and Gary Carlson. Trustee Doyle Tubandt was absent.

Also present were Sal LoBianco, General Manager of Muscatine Power and Water; Donald W. Kerker, Board Secretary; Duane J. Goedken, Board Attorney; Amy Cahill, Muscatine Journal; Charles Potter, KWPC/KMCS Radio Station; Ray Danz, Gary Wieskamp, Erika Cox, Brandy Dulceak and Brenda Christensen of Muscatine Power and Water.

Chairperson Ingstad asked if there was anyone in attendance who wished to make any public comments. There were no comments.

The minutes of the August 25, 2009, public hearings and regular meeting were presented as previously submitted to all Board members in written form. Trustee Axel moved, seconded by Trustee Heidbreder, that the minutes be approved and placed on file as submitted. Motion carried. All Trustees present voted aye.

The list of August expenditures and transactions was presented as previously submitted in written form to all Board members. After review, Trustee Heidbreder moved, seconded by Trustee Axel, to ratify payments of \$4,913,460.27 for the Electric Utility, \$713,212.85 for the Water Utility, and \$879,037.50 for the Communications Utility for a total amount of \$6,505,710.62. Motion passed. All Trustees present voted aye.

Mr. LoBianco stated that the next agenda item was a recommendation to accept a revised project summary form and contract revision for the West Hill 24" Water Main and Pump Header Modification Project. Mr. LoBianco reminded the Board that at the November 2008 Board meeting, as a part of the annual 2009 budget, this project was approved for a total amount of \$1,176,000. Wet weather and soil conditions have caused significant changes to the original quantities needed for sand and rock that is required to restore sidewalks and roadways. After work began, there were changes to the work scope at the south end of the project, and an overall increase of MP&W labor costs. These changes will put the project in excess of 10% above the approved project amount. Therefore, it is requested that the Board approve the revised project summary form, with the amount changed from \$1,176,000 to \$1,419,635. This is an increase of 20.7% over the original project summary form amount.

During the Board meeting on January 27, 2009, a contract was awarded to Sulzberger Excavating, Inc. for a total of \$1,172,944.75 for the West Hill 24" Water Main Construction and Pump Header Modifications Project. The award was made based upon estimated quantities and unit adjustment prices. Due to reasons detailed above, the contract amount is now above the 10% threshold where the General Manager can approve change orders, as referenced in the Board Policy Manual. Contract Change Order No. 1 was issued on September 22, 2009, for WCDs #1-#3; this change resulted in a net increase to date of \$144,603.94. Therefore, it is requested that the Board approve the change order to adjust the contract total from \$1,172,944.75 to \$1,317,548.69, establishing a new 10% threshold for additional changes. Mr. LoBianco stated that there has also been work requested by the City of Muscatine and the Muscatine School District to accommodate their needs, which will be reimbursed to MP&W upon completion.

Mr. LoBianco continued that due to the nature of this project, and the continued changes required in the field prior to completion, it is anticipated that there may be additional changes to this contract prior to completion, but it is not anticipated that they will exceed the new 10% threshold. Any additional changes, within that limitation, will be presented to the Board with the recommendation for final acceptance of this contract. Final contract costs are projected to run approximately 16.4% over the original contract price. Trustee Axel asked about the progress of the project. Mr. Danz updated the Board on the project progress and expected completion dates.

Trustee Axel moved, seconded by Trustee Heidbreder, that the revised Project Summary Form be approved in the increased amount of \$243,635, resulting in a new project total of \$1,419,635. Motion carried. All Trustees present voted aye.

RESOLUTION 09-24

WHEREAS, the Board of Water, Electric, and Communications Trustees of the City of Muscatine, Iowa, on January 27, 2009, awarded a contract to Sulzberger Excavating, Inc. for the West Hill 24" Water Main Construction and Pump Header Modifications Project in the amount of \$1,172,944.75; and,

WHEREAS, Contract Change Order 1 has been prepared to said contract in the amount of \$144,603.94 and said Contract Change Order 1 was reviewed by the Board and the Board's staff has recommended approval of said Contract Change Order 1; now therefore,

BE IT RESOLVED, by the Board of Water, Electric, and Communications Trustees that said Contract Change Order 1 in the amount of \$144,603.94 be and the same was hereby approved for a new contract price of \$1,317,548.69.

Trustee Heidbreder moved, seconded by Trustee Axel that said resolution be passed, approved, and adopted on this 25th day of September, 2008. Trustees Heidbreder, Axel, Carlson and Ingstad voted aye. Voting nay, none. Trustee Tubandt was absent.

Included with the Board's meeting materials were the Ten-Year Financial Projections for 2010 through 2019. The Board was provided a complete and detailed version of the Ten-Year Financial Projections for the Water, Electric and Communications Utilities in a separate packet, along with a summary version in the Board package. Mr. LoBianco stated that the projections this year were more of a challenge than in past years. The Electric Utility projection is markedly different than the projection of a year ago, and indicates that the Utility faces some significant challenges in order to ensure reasonable cash balances are available to properly sustain and operate the business. As the Board knows, the Utility's retail rates do not generate sufficient income to cover expenses, causing the Utility's cash position to become very dependent upon revenue, and the associated margin, from wholesale energy sales. The margin the Utility has received from wholesale energy sales has, in the past, provided the income necessary to absorb increases in labor and material expenses, significant increases in coal and coal transportation expenses, and fund significant capital expenditures without increasing the rates to our native system customers. Consequently, the Electric Utility has not implemented a rate increase since 2002, when a 4.6% increase was enacted in response to a softening wholesale energy market. MP&W's electric rates are among the lowest in the State. A key assumption in this projection is a 3% annual rate increase, beginning January 1, 2011. The need for and/or the magnitude of annual rate increases is greatly dependent upon the wholesale energy market; a significant recovery in the market would mitigate the rate increase requirements. Scenarios for the Electric Utility include: reduced wholesale sales and purchased power rates, addition of 20 MW's of wind generation, a 2010 rate increase, a 4% annual rate increase beginning January 1, 2011, an annual rate increase needed to achieve minimum cash level by 2015, refinancing debt to extend the payment schedule and from an income statement perspective, adjusting depreciation to better match the useful life of the assets.

Mr. LoBianco told the Board that the Water Utility projection is similar to those of previous years. The Utility revenues deliver a very modest margin and that margin has been preserved by the annual rate increases that have been instituted over the past 5 years. Continued annual rate increases of 3% per year are a base assumption. The Water Utility rates continue to be some of the lowest in the State. The Communications Utility projection indicates a return to positive operating income in 2010 and a positive change in net assets is achieved in 2013. A goal of net subscriber growth in both CATV and Internet services was included in the projections. Continued ongoing rate increases for the various services continue and are necessary to preserve the operating margins necessary to fund debt payments and sustaining capital expenditures. Rate increase amounts are primarily driven by annual CATV programming cost increases, as well as increases in labor and material expenses. Communications services, even with the ongoing rate increases, remain competitive and their value is further enhanced by the exceptional, local customer service that MP&W delivers. Mr. LoBianco told the Board that a number of scenarios have been run to illustrate the sensitivity of the projections to the various assumptions in each of the Utilities.

Mr. LoBianco asked Mr. Kerker to review the primary drivers and highlights for all three Utilities. Mr. Kerker stated that the major financial drivers for each Utility have been identified, along with select operating and financial data, for the Board of Trustees

information. Mr. Kerker reminded the Board that financial projections are used to determine the need for rate adjustments and financing requirements. He explained that this year all three projections also included a recommended cash reserve level. Having reserves in the Electric Utility has provided a cushion so that we did not have to immediately respond with rate increases to adverse economic times and provides funds without the need to borrow for modest capital expenditures. Mr. Kerker reviewed the revenues, expenses, and capital expenditures, along with significant changes, for each utility starting with the Electric Utility

Mr. Kerker stated that although all three Utilities are feeling economic stress, the Electric Utility is the most affected by current economic conditions. Significant changes in the Electric Utility that have influenced this year's projections are that 2009 wholesale revenues are down 60% from 2008, with prices and volumes each down nearly 40% from 2008. Retail sales revenues are down 4% from 2008. Energy efficiency requirements that have been established by the State of Iowa are now in the projections, a target of .83% reduction in retail kWh sales by 2012 and an additional reduction in each year thereafter have been included in the projections, along with the expected annual expenditure of over \$500,000 per year, to accomplish this target. Emissions allowance costs for NOx are also now included along with SO₂ allowance costs. Allowances allocated by the Environmental Protection Agency (EPA) should cover most of the allowances needed for retail sales, but are not expected to cover allowances needed for steam sales and wholesale sales. Pension expense was gradually increased from \$1.7 million in 2009 to \$2.9 million in 2012 due to portfolio losses in 2008 (this addition covers all three utilities). To offset some of these increases, capital expenditures were cut in half through 2012 and a 25% reduction is projected for the remainder of the years, totaling a reduction of \$34.7 million from last year's projections. As a last resort, retail price increases were included beginning in 2011, dependent on wholesale and retail sales recovery.

In review of the major drivers of the Electric Utility projections, Mr. Kerker started with native system sales, which are anticipated to increase 0.9% per year for the projected years and an annual rate increase of 3.0% is projected beginning in 2011. The wholesale electric sales were projected at an eighty percent capacity factor with an average price of \$29 per megawatt-hour (MWH) in 2010, increasing to \$4 per MWH through 2013 and then escalating 3% annually thereafter. Mr. Kerker reminded the Board that due to the fact that MP&W now sells all generated electrical energy into the MISO market and purchases all native system energy requirements from the MISO market, Electric Utility projections for wholesale energy sales and purchased power, both in terms of MWH and dollars, are shown differently than in the past. Steam sales to GPC are projected to continue throughout the ten-year period with the fuel and emissions costs being passed through to GPC. The balance of the revenue, including other revenue and interest income, brings the 2010 total projected revenue dollars to \$88,967,000. The Electric Utility expenses included fuel costs that are projected to have an average annual cost increase of 6.2% from 2009. Purchased power increases of \$4 per MWH per year through 2013 and then escalating 3% annually thereafter are projected. Emission costs of \$1,175,000, and normal operation and maintenance expenses of \$38,051,000, along with depreciation and interest expense, bring the total 2010 expenses to \$101,972,000, resulting in a change in net assets before revenue adjustment of negative \$13,005,000. Capital additions are based on 1% of

plant in service at the beginning of each year for 2010-2012 and 1.5% in the remaining projection years (typically in the past this has been projected at 2% each year), resulting in average annual capital expenditures of \$5,707,000.

Mr. Kerker reviewed a number of the scenarios that were run against the base case Electric Utility Projections. These scenarios included: reduced wholesale sales and purchased power rates, addition of 20 MW's of wind generation, a 2010 rate increase, a 4% annual rate increase beginning January 1, 2011, an annual rate increase needed to achieve minimum cash level by 2015, refinancing debt to extend the payment schedule and, from an income statement perspective, adjusting depreciation to better match the useful life of the assets. An analysis page, indicating the margin derived from native system, wholesale energy, and steam sales, was also included in the Board packet. The analysis clearly illustrates the dependence our native system customers have on the margin delivered by past wholesale energy sales and how the decline of that revenue and associated margin adversely impacts the coverage of expenses and the Utility's cash position.

Trustee Heidbreder asked about the 30% projected increase (vs. 2009) in wholesale sales for 2010 and whether it was realistic with the way things have been going. Trustee Heidbreder also wondered if a price increase before 2011 would be needed. Mr. Kerker stated that Utility projections for 2010 anticipate drawing down on reserves until the impact of joining MISO and the near term future of the wholesale market is better understood. Mr. LoBianco answered that it is hard to tell if the right amount is projected, but that something has to be used and the 30% increase in wholesale sales is a modest increase and the best projection the team could come up with. Mr. Kerker also stated that MP&W is in better shape than most utilities that have had to quickly implement price increases because of having no reserves. Trustee Heidbreder and Trustee Carlson requested that a mid-year 2010 rate increase be looked at during the 2010 budgeting process, keeping in mind the 90 day notice needed. The Trustees would also like management to share with the major industrial customers that MP&W is considering a rate increase.

Mr. Kerker continued with the ten-year projections for the Water Utility, stating that the projection is similar to those of previous years. The Water Utility continues to deliver a modest margin and that margin has been preserved by the annual rate increases that have been instituted over the past five years and a continued annual rate increase of 3% per year is a base assumption. Significant changes from last year's projections are that water pumped over the ten-year period is 9% less and capital expenditures were reduced by \$2.8 million due to lower pumpage, thus reducing well capacity and land needs. A projected borrowing for the Water Utility was deferred until 2014 and 2015 when \$1.3 million is projected for each year to finance a major main extension along Highway 61 Bypass.

In review of the major drivers of the Water Utility projections, Mr. Kerker stated that using 2009 as the base, total gallons of water pumped are projected to increase an average of 1.5% per year. This along with miscellaneous revenues and interest income will give the Water Utility 2010 revenue dollars of \$4,284,000. Normal operation and maintenance expenses make up the bulk of the 2010 expense dollars of \$4,125,000,

leaving the Utility with a positive net income before capital contribution of \$159,000. Annual capital expenditures are projected to be \$989,000.

Mr. Kerker reviewed a number of the scenarios that were run against the base case Water Utility projections. These scenarios included: no rate increase, both 10% higher and 10% lower contract customer consumption, and a 4% annual electric rate increase beginning in January of 2011.

The last Utility projection to be reviewed was the Communications Utility. Mr. Kerker reviewed significant changes from last year's projection, which included that the cost of the digital transition project is now expected to be \$4.5 million instead of \$5.1 million and the external financing needed is now projected at \$1.2 million instead of \$4 million. Improved cash flows due to reduced digital transition's project cost and increased revenues are projected.

In review of the major drivers of the Communications Utility projections, Mr. Kerker stated that CATV subscribers are projected to increase 4% in 2010 and an average of 0.6% per year from 2010 through 2019. A rate increase of 5.5% is projected 1/1/10 and each January 1 after that. Other revenue and interest income will take 2010 total revenues of the Communications Utility to \$11,530,000. Normal operating and maintenance expenses, along with depreciation, amortization and interest expense on the Electric Utility loan make the 2010 total expense for the Utility \$12,771,000, resulting in a 2010 change in net assets a loss of \$1,241,000. Capital additions average \$1,400,000 per year and an additional \$4,545,353 is projected to be spent from 2008 through 2012 on the digital conversion project.

Mr. Kerker reviewed a number of the scenarios that were run against the base case Communications Utility projections. These scenarios included: a 5% reduction of base case CATV subscribers, a 6% instead of 5% programmer charge annual increase, 4.5% instead of 5.5% CATV annual rate increase, no data/internet rate increase, and a 5% reduction of base case data/internet subscribers.

The Board expressed thanks for all the hard work done by management to complete the projections. Trustee Carlson moved, seconded by Trustee Axel, to receive and place on file the 2010 – 2019 Financial Projections for the Water, Electric and Communications Utilities. Motion carried. All Trustees present voted aye.

In the General Manager's report, Mr. LoBianco reviewed his previously submitted memorandum. Mr. LoBianco reminded the Board that the transfer to MISO Energy Market occurred in the early morning hours of September 1. The transition went smoothly. MP&W Management is currently working with our Energy Management and Settlement Services contractor, Tenaska Power Services Company, to identify the appropriate daily and monthly exchange of information concerning unit scheduling and MISO statements and invoices. Tenaska will provide shadow settlements to ensure invoicing by MISO is accurate. Management will continue to monitor the results of our decisions regarding how we offer our generation facilities into the market and our ability to execute MISO directives to optimize the financial performance of our participation in the MISO Energy Market.

Mr. LoBianco also reminded the Board that the closing for the \$494,000 loan to the Water Utility from the Iowa Department of Natural Resources' State Drinking Water Revolving Loan Fund for the Well Motor Control Replacement Project was set for early October and that disbursements from the loan will be made as progress payments. Work is scheduled to begin this fall.

Mr. LoBianco invited the Board to attend the retirement party for long-time employee Connie Thede on Friday, October 2, at the MP&W Administrative Building. This concluded the General Manager's report.

The next item on the agenda was to receive and place on file the August Financial Operating Statements and Balance Sheets for Electric, Water and Communications Utilities. Mr. Kerker stated that the Electric Utility's Change in Net Assets was \$5.3 million below what was budgeted. Native system sales revenues were 8.3% lower than budget, this along with continued softness of the wholesale sales and a lower than average sales price resulted in electricity sales being \$13.2 million less than projected. Steam sales exceeded budget by about \$1.3 million due mostly to a pass through of NOx costs charged to GPC. Production Fuel and Purchased Power Expense showed positive results of over \$3.8 million compared to budget, due mostly to lower than projected coal prices and fewer tons burned. Overall Operation and Maintenance expenses showed better than projected results of \$1.6 million compared to budget.

The Water Utility's Year-to-Date financials showed that water usage is down about 15% among all customer classes, resulting in \$241,849 lower revenue compared to budget. Operating expenses were \$87,540 less than budget, a good portion of that being lower fuel/power purchased and lower labor costs. Maintenance costs were over budget due mostly to costly main repairs on Isett Avenue. The Change in Net Assets for the Water Utility was \$114,571 below budget.

Mr. Kerker stated the Communications Utility Year-to-Date Financials indicated that the data/internet revenue was \$51,449 higher than budget due to more subscribers, this along with greater than budgeted pay-per-view and video-on-demand buys of \$55,211 were able to offset most of the less than budgeted advertising revenue of \$96,369. Lower than budgeted digital conversion expenses, promotional expenses, travel expenses and deferred customer survey and customer service training helped the operating expenses come in at \$63,221 less than budget. Maintenance was close to budget. Overall there was an improvement of \$259,720 to the Change in Net Deficit compared to budget.

Trustee Heidbreder moved, seconded by Trustee Carlson, to receive and place on file the August Financial Operating Statements and Balance Sheets for the Water, Electric, and Communications Utilities. Motion carried. All Trustees voted aye.

The Competitive Quotes for Public Improvements Report was presented as previously submitted to all Board members in written format. There were no items for approval. The report was received and placed on file.

The August departmental reports were presented as previously submitted to all Board members in written form. Trustee Axel moved, seconded by Trustee Heidbreder, to

receive and place on file the August departmental reports. Motion carried. All Trustees present voted aye.

The meeting was adjourned at 7:10 p.m.

BOARD OF WATER, ELECTRIC, AND
COMMUNICATIONS TRUSTEES OF
THE CITY OF MUSCATINE, IOWA



Donald W. Kerker
Board Secretary