

# FINANCE COMMITTEE MINUTES

January 12, 2006

The Finance Committee of the City of Mesa met in the lower level meeting room of the Council Chambers, 57 East 1st Street, on January 12, 2006 at 9:05 a.m.

COMMITTEE PRESENT	COUNCIL PRESENT	STAFF PRESENT
Tom Rawles, Chairman Janie Thom Claudia Walters	None	Christopher Brady Debra Dollar

1. Discuss and consider the District Cooling utility enterprise and rate.

Development Services Manager Jack Friedline reported that the purpose of today's presentation is to recommend a service rate to the Committee that would apply to City and non-City buildings for Mesa's District Cooling Utility. He explained that this would be the first time staff has recommended "a legitimate rate" for the new utility. Mr. Friedline introduced Facilities Energy Management Coordinator Nick DeSantis, who was prepared to address the Committee regarding this matter.

Mr. DeSantis displayed a PowerPoint presentation in the Council Chambers and provided an overview of the City's District Cooling Utility. (The complete PowerPoint presentation is available for review in the City Clerk's Office.) He explained that the District Cooling Plant, which is adjacent to the Mesa Arts Center, has a maximum of 4800 tons of cooling capacity and was constructed to provide chilled water to cool City and private buildings in the downtown area. Mr. DeSantis advised that the primary benefits of District Cooling include reduced capital costs (i.e., eliminates on-site equipment and the equipment is consolidated in the District Plant); reduced operations and maintenance (O&M) costs; energy conservation; revenue generation; and support of Town Center development.

Mr. DeSantis indicated that over the past year, a District Cooling Master Plan was created to determine the proposed phases for extending the chilled-water piping to various buildings in the downtown area. (See Attachment 1.) He commented that in Phases 0-1, such piping has been completed at the Mesa Arts Center, First United Methodist Church, Council Chambers, Information Services Building and Municipal Building (ready for operation once the building remodel is completed). Mr. DeSantis advised that this represents 49% utilization (or 874 tons) of existing plant capacity. He also briefly reviewed the proposed extension of the chilled-water piping in Phases 2 through 4.

Mr. DeSantis explained that staff is recommending a service rate of \$0.160 per ton-hour, plus a pass-through for the price of electricity purchased (similar to the Natural Gas Utility pass-

through) to be applied to City and non-City buildings for the District Cooling Utility. He said that it is further recommended that the rate be reviewed and adjusted after one year. (Note: The initial proposed rate per ton-hour is based on Phase 0-1 only.)

Mr. DeSantis also spoke regarding a document entitled "District Cooling Cost Analysis," which depicts the full cost recovery for District Cooling under the following categories:

- Equipment O&M (including personnel and other resources)
- Capital Equipment Replacement Fund
- Discounted Cooling
- Capital Expansion Fund
- Building O&M Costs
- Plant Construction Capital Recovery

In response to a series of questions from the Committeemembers, Assistant Budget Director Chuck Odom briefly highlighted the "District Cooling Cost Analysis." (See Attachment 2.) He reported that the Plant Construction Capital Recovery category was included as a component of the proposed rate in order to recover the construction costs of the District Cooling Plant, which were funded by Quality of Life monies. (The General Fund would pay back \$3.2 million to the Quality of Life Fund.) Mr. Odom explained that in formulating the rate, staff was asked to look at the rate in such a manner that the City "did not harm itself" on a contribution margin basis to Mesa's Electric Utility, but would also provide a price break to the District Cooling customers. He further noted that staff took a three-year average of electric costs against what the City receives in average sales to obtain the contribution margin, which was then converted from ton-hours (District Cooling Utility) to kilowatt-hours (Electric Utility), and equated what the rate would have to be to hold harmless the Electric Utility. Mr. Odom added that the City would act as any other customer on the District Cooling system, which is consistent with Mesa's other utilities.

Chairman Rawles clarified Mr. Odom's analysis by stating that the General Fund would pay \$0.160 per ton-hour to the District Cooling Utility; that the pass-through for electricity costs would be adjusted as needed; and the District Cooling Utility, in turn, would pay \$0.055 to the General Fund.

City Manager Christopher Brady stated that staff did not want to lose money in contributions to the General Fund, so they converted the Electric Utility contribution from kilowatt-hours into ton-hours in order for the contribution to remain the same.

Mr. DeSantis reported that initially, an interim rate of \$0.10 was established to cover the cost of providing chilled water only and explained that the proposed service rate would achieve an overall goal of District Cooling to cover all expenses and be self-funding. He noted that the fiscal impact for Phases 0-1 to operate the plant is estimated at \$778,920 per year; that the recommended initial rate for District Cooling per ton-hour is \$0.239 (\$0.160 plus \$0.079 pass-through for electricity costs); and that the City would save \$119,708 annually (the difference between the cost of District Cooling and the cost of on-site cooling). Mr. DeSantis added that each additional phase would increase the savings to the City and lower the rate because the Central Plant would be operating at a higher degree of efficiency.

Discussion ensued relative to the fact that in order to make a City building compatible with the Cooling District, staff would tie into the facility's existing system and add coils or a fan in order to

eliminate the need for the building's cooling equipment; and that for an offsite (non-City) building, a piping loop system would be extended to the facility, a plate heat exchanger installed to separate the City's cooling water from the facility's cooling water, and the non-City facility would be required to maintain the system within the structure.

Mr. Brady stated that during his tenure with the City of San Antonio, the community utilized a similar chilled-water system in its downtown area. He explained that the utility was an incentive in attracting large developments to the area including major hotels, the convention center and the Alamo Dome. Mr. Brady added that perhaps Mesa's District Cooling Utility could be used in much the same way to bring new economic development to the Town Center area.

Mr. DeSantis further reported that the District Cooling Enterprise would be fully funded through the proposed rate and said that funds would be set aside for capital equipment replacement and capital expansion. He also said that the District Cooling piping was extended to the First United Methodist Church, the only off-site facility, during the same phase that the piping was installed at the Mesa Arts Center.

Chairman Rawles questioned the necessity of Mesa charging itself the \$0.055 contribution factor that it would eventually pay back to itself. He stated that although from an accounting standpoint staff may prefer such a mechanism, in his opinion, it merely complicates the rate and the process. Chairman Rawles added that the City should not be in the business to make profits, nor to maintain the same profit margin when, in the case of the District Cooling Plant, Mesa has made major technological advances to reduce energy consumption and save money for the customers.

Mr. Odom clarified that the City is required to charge itself the rate it would charge an outside customer, not an artificially low rate. He explained that the City does charge discounted rates to governments, but Mesa does not set itself apart from those entities.

An extensive discussion ensued between Chairman Rawles and staff regarding his concerns and philosophical viewpoints relative to the proposed District Cooling Utility rate recommendations.

Mr. DeSantis concluded his presentation by commenting that the primary benefits of the District Cooling Utility include capital and energy savings, consolidating O&M equipment and overhead into one plant, and offering an opportunity to expand the system to offsite customers.

Chairman Rawles stressed the fact that the District Cooling Plant is a tremendous innovation and said he does not object to its expansion to offsite entities as long as those costs are recovered through a specified rate. He noted, however, that his primary concern is the proposed contribution factor.

Committeemember Walters suggested that because the District Cooling Utility is new, it might be appropriate to develop it as a true enterprise account and include a fixed percentage transfer of its net profits to the General Fund.

Chairman Rawles concurred with Committeemember Walters' suggestion and said that an enterprise account could be developed in such a manner that there would be full cost recovery, including capital replacement and expansion, and, for example, 10% of the profit transferred to

the General Fund on an annual basis. He added that if there were ever a time economically for Mesa to create such an account, the District Cooling Utility would be the entity with which to do so.

Committeemember Walters stated that she would be willing to support staff's recommendation in the interim, but would also like to consider the establishment of the District Cooling Utility as an enterprise fund. She acknowledged, however, that because of Mesa's current budget difficulties, it would be impossible at the present time to accomplish this process with any of Mesa's utilities.

Chairman Rawles commented that he would prefer that the Committee take no action on staff's recommendation today in order for staff to conduct further research in this regard. He requested that staff provide the Committee with an analysis of a complete onsite (City) utilization of the Central Plant (including the First United Methodist Church), and determine how much of the 4800 ton capacity, if any, would remain available. Chairman Rawles said that there might come a time when the cost savings to the City to cool, for example, the Mesa Convention Center may not be as great as the revenue that could be generated by diverting such cooling capacity to a non-City building. He further requested that staff provide the Committee with benchmarking data relative to the rates that other utilities, such as Arizona Public Service (APS), charge their customers.

Additional discussion ensued relative to alternative service rate proposals.

Committeemember Walters stated that she is uncomfortable with "throwing out numbers and percentages" without allowing staff sufficient time to conduct further work regarding this matter.

Committeemember Thom expressed support for the creation of an enterprise fund for the District Cooling Utility, which would ultimately cover all expenses and be self-funding.

Further discussion ensued relative to the fact that the Mesa Tribune, the Marriott, and Mesa Community College have expressed an interest in "tying into the chilled-water system" pending Council approval of a service rate for the District Cooling Utility; and that in the long-term, it may be appropriate for the Council to consider the development of a satellite plant to offer the chilled-water service to additional offsite facilities.

Committeemember Walters noted that the capacity for cost recovery from offsite facilities might be significant and it may be appropriate for the City to bond against future revenues derived from the District Cooling Utility in order to construct a satellite plant more quickly.

Chairman Rawles stated that it is the consensus of the Committee that staff bring back this agenda item as soon as possible. He also acknowledged the complexity of the subject matter and thanked staff for their informative presentation.

## 2 Adjournment.

Without objection, the Finance Committee Meeting adjourned at 10:15 a.m.

I hereby certify that the foregoing minutes are a true and correct copy of the minutes of the Finance Committee meeting of the City of Mesa, Arizona, held on the 12<sup>th</sup> day of January 2006. I further certify that the meeting was duly called and held and that a quorum was present.

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BARBARA JONES, CITY CLERK

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attachments (2)