



COMMISSION
BUDGET WORK SESSION MINUTES
January 28, 2025

No. Topic

[Call to Order](#)

1. [Internal Audit Update](#)
2. [Budget/Compensation Update](#)
3. [Service Area Expansion Policy](#)
4. [Public Comments](#)



COMMISSION
BUDGET WORK SESSION MINUTES
January 28, 2025

The Commission Chair called the meeting to order at 11:16 a.m.

Name	Title	Present for Item Nos.
Rodriguez, Stephen C.	Commission Chair	1-3
Levenston, Jr., Willie	Commission Vice-Chair	1-3
Elofson, Frederick N.	Commissioner	1-3
Glenn, Michael E.	Commissioner	1-3
Lakdawala, Vishnu K.	Commissioner	1-3 (Virtual)
Stern, Nancy J.	Commissioner	1-3
Taraski, Elizabeth	Commissioner	1-3
Templeman, Ann	Commissioner	1-3

In accordance with Virginia Code § 2.2-3708.3 (B) and the HRSD Remote Participation Commission Adopted Policy Commissioner Lakdawala requested approval to participate in today's meeting from Virginia Beach, Virginia due to a business conflict which prevents him from attending in person.

Moved: Willie Levenston, Jr.
Seconded: Frederick Elofson

Ayes: 7
Nays: 0
(Excludes Remote Participant)

1. **Internal Audit Update**

Staff presented the [internal audit update](#) including audit impact, audits in progress, the audit plan for Fiscal Year (FY) 2026, and management action plan progress. The following summarizes SC&H's activity:

Completed Audits:

- Risk Assessment: FY-2025 Audit Plan
- Design and Construction Estimating

Audit in Progress:

- Personnel Investigations
- Operational Technology Security and Resilience
- IT Governance
- Model 3
- Risk Assessment: FY-2026 Audit Plan
- Lab Assessment



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Upcoming Audits:

- Billing, Accounts Receivable, and Aging

Staff also provided an update on the Internal Audit RFP which will be issued in February 2025.

2. **Budget/Compensation Update**

Staff recapped phase 2 of the [Compensation Study](#) including salary structure development, phase-in approach, proposed salary adjustments, and budget impact.

3. **Service Area Expansion Policy**

Staff discussed cost participation agreements for [service area expansion](#). Discussion included background, who pays for expansion, basic approach and critical concepts of cost participation agreements, examples of capital recovery charges, locality credit ratings, examples of cost participation payments, risks, and other utility's approach to expansion.

Staff will present revisions to the Service Area Expansion policy for approval at the February Commission meeting. The first agreement to be issued under the new policy is anticipated in March.

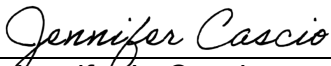
4. **Public Comments**

Public comments were not received during this meeting.

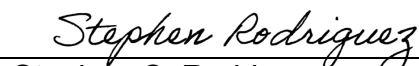
Next Commission Meeting Date: February 25, 2025 at the HRSD South Shore Operations Complex, 1434 Air Rail Avenue, Virginia Beach, VA 23455

Meeting Adjourned: 12:11 pm

SUBMITTED:


Jennifer L. Cascio
Commission Secretary

APPROVED:


Stephen C. Rodriguez
Commission Chair



Commission Budget Work Session

January 28, 2025

- Internal Audit – Update
- Compensation Study – Phase 2
- Service Area Expansion – Cost Participation Agreements
- Closed Session

Completed, In Process, and Planned Audits/Projects

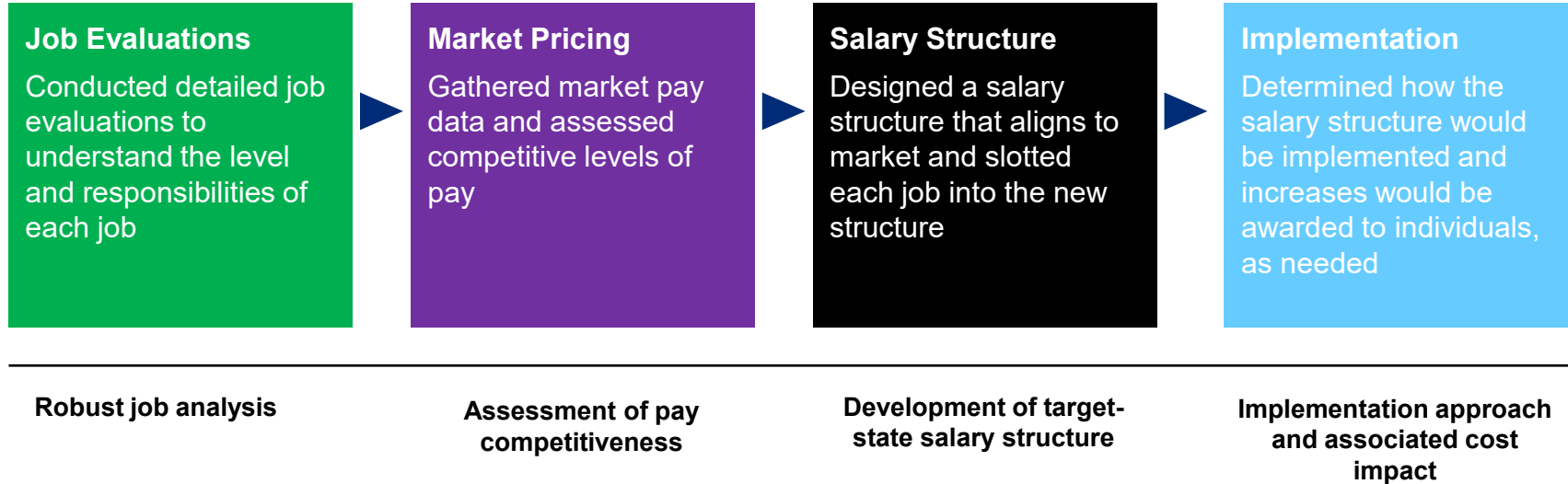
Audit / Project	Status
Risk Assessment: FY25 Audit Plan	Complete
Design and Construction Estimating	Complete
Investigations	In Process: Reporting
Operational Tech Security and Resilience	In Process: Reporting
IT Governance	In Process: Fieldwork
Model 3	In Process: Fieldwork
Risk Assessment: FY26 Audit Plan	In Process: Fieldwork
Lab Assessment	In Process: Planning
Billing, Accounts Receivable, and Aging	Planned: February / March

- Updated Finance Committee October 2024
- Issue RFP February 2025
- Discuss recommendation with Finance Committee April 2025
- Contract to Commission May 2025
- Effective date October 2025

Compensation Study – Phase 2

Salary Structure Development

Process Overview



Salary Structure Development

Methodology Overview



Effective Date

The salary structure is effective as of **7/1/2024**; i.e., the structure has been developed using market data aged to 7/1/2024



Market Data

The midpoints of salary grades are aligned to the **market 75th percentile**, as per the compensation philosophy

Data comes from the *Mercer Benchmark Database* and *American Water Works Association Compensation Survey*

- Mercer scoped data for all jobs to the Virginia market (Source: Economic Research Institute)
- For director-level roles, Mercer scoped market data based on organization size (i.e., revenue)
- Industry data was leveraged for all jobs, in the following order: Utilities, Public sector, General Industry (all data)



Structure Design

The salary structure was developed to align with the **competitive market pay rate** for each job

Overall salary structure design resonates with market best practice (e.g., step increases, midpoint progression)

Recommended Implementation Approach

Phase by Structure Increases over 3 years

Description	<ul style="list-style-type: none">• Discount the entire pay structure in FY 2025 (year 1) by 12%• Move the structure forward annually the next two years:<ul style="list-style-type: none">• Phase 2 - 5.66% + COLA in FY 26• Phase 3 - 6.00% + COLA in FY 27 - At market FY 27
Position in Range	<ul style="list-style-type: none">• Maintains equitable position in range
Impact to Employees	<ul style="list-style-type: none">• Organization-wide strategy (vs. targeted individualized strategy)

Salary Adjustments

	Market Level Adjustment + COLA	Merit	Training Level Increase	Above Range (x'ers)
% Increase	8.56% (5.66% MA + 2.9% COLA)	3%	2.2%	2.9% (COLA)
Date	July 1	On Merit Date	Usually, Summer	July 1

Year 2 Comp Phase-In Budget Impact

	FY26		% Increase
Standard Market/COLA Adjustment	\$ 3,981,266	Average	6.94%
Merit Adjustments	\$ 426,632	Max	10.9%
Training Adjustments	\$ 199,691	Min	2.9%
COLA(off table) Adjustments	\$ 651,815	Most frequent	8.56%
Total	\$ 5,259,404		

- Standard Market Adjustment includes 5.66% planned phase in plus 2.9% COLA for EE on table
- COLA adjustment includes 2.9% for EE “off table”
 - 71 EE enter back on table in FY26, leaving 256 over market
 - EE entering back on pay table have an increase ranging from 3.2% to 5.4%
- Apprentices also receive a training increase of 2.2% bringing their total max increase to 10.9%
- Data set is for active EE as of 1/24/25
- Year 2 Comp adjustments are in line with budget projection



HRSD

Service Area Expansion Cost Participation Agreements

Budget Work Session



- HRSD's
 - Territory is 4,998 square miles
 - Service area is 766 square miles
- Growing the service area is a “Service Area Expansion”

Background (continued)

- Service Area Expansion Policy
 - Adopted 2019; amended 2023
 - Service area is established through coordination with localities
 - Infrastructure cost for infrastructure capacity expansions within an existing service area are the responsibility of HRSD
 - Service Area Expansions (SAE)
 - No infrastructure/capacity deficiencies – recommend approval to Commission
 - Infrastructure/capacity deficiencies or extensions of the system – develop Cost Participation Agreement

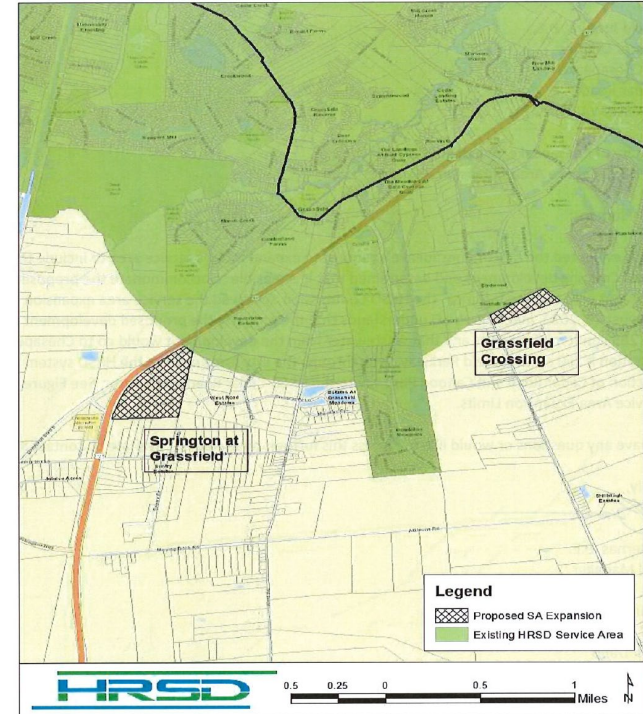


Figure 1 – Service Area Expansion Limits

Cost Participation Agreements – Basic Questions

- Who pays for what recognizing that HRSD is a governmental utility/partner with sister jurisdictions?
- At what extent should HRSD participate in expansionary and/or speculative development?
- How do we preserve rate payer equity given that different jurisdictions have differing development philosophies/strategies?
- If HRSD does participate in a monetary way, how do we
 - Minimize risk?
 - Defer risk?

- Developed with the concept that “*Growth must pay for growth*”
 - Revenues from SAE must pay for needed infrastructure improvements
 - When new revenues are insufficient to pay for capital improvements, the sponsoring jurisdiction must make up the difference
- Establish a concept of a “*TIF-like*” area where new revenues in the designated area are earmarked and used to pay for capital improvements

Critical Concepts of Cost Participation Agreement

HRSD Infrastructure Improvements	All infrastructure must be owned and operated by HRSD and designed to HRSD standards
New SAE Revenues	New revenues (excludes Facility Charges) received from new connections will be used to pay for Infrastructure Improvements.
Capital Recovery Charge	<p>Charge based on an estimation of debt service costs for infrastructure Improvements.</p> <p>Charge is equal to debt service multiplied by 1.4 and is offset by new SAE Revenues.</p> <p>1st payment due 6 months after facilities are placed in service.</p>

Example Capital Recovery Charge

Example of Payment Required	
Semi-Annual Debt Service Calculation	\$2,000,000
Capital Recovery Charge ($\$2,000,000 * 1.4$)	\$2,800,000
Less: New SAE Revenues Received	(\$1,500,000)
Net Due from Locality	\$1,300,000

Critical Concepts of Cost Participation Agreement (continued)

Term	30 years from substantial completion
Locality Participation	Will only execute with localities with at least a AA credit rating
Security Pledge	<p>Payments from the Locality will be:</p> <p>(a) secured by a revenue pledge (e.g., sewer revenue, water and sewer revenue); or</p> <p>(b) absolute and unconditional, subject to and contingent upon the annual appropriation of funds by the governing body for such purposes.</p>
Downstream Improvements	Separately negotiate another CPA

Service Area – Credit Ratings

- Over 60% of the population served is within a triple-A-rated locality

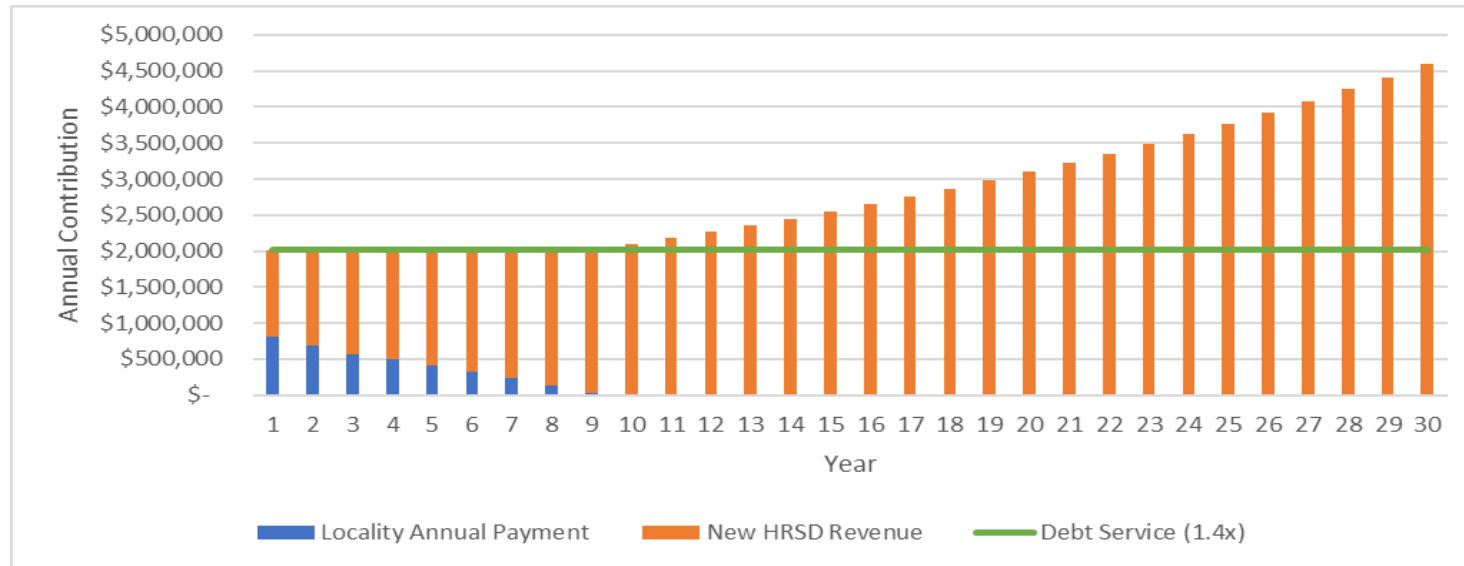


Locality Served	2022 Population	Ratings (M/S&P/F)
Accomack County	32,926	-
City of Chesapeake	251,959	Aaa/AAA/AAA
City of Hampton	136,387	Aa1/AA+/AA+
City of Newport News	183,504	Aa1/AA+/NR
City of Norfolk	237,770	Aa2/AAA/AA+
City of Poquoson	12,624	Aa2/AAA/NR
City of Portsmouth	96,700	Aa2/AA/AA
City of Suffolk	99,179	Aaa/AAA/AAA
City of Virginia Beach	455,385	Aaa/AAA/AAA
City of Williamsburg	16,224	Aa1/AAA/NR
Gloucester County	38,799	-
Isle of Wight County	39,950	Aa2/AA+/AA
James City County	79,488	Aa3/AA+/AAA
King & Queen County	6,663	-
King William County	18,107	-
Mathews County	8,446	-
Middlesex County	10,779	-
Surry County	6,492	-
York County	71,491	-

Sources: Population estimates as of July 1, 2022 from the Weldon Cooper Center.

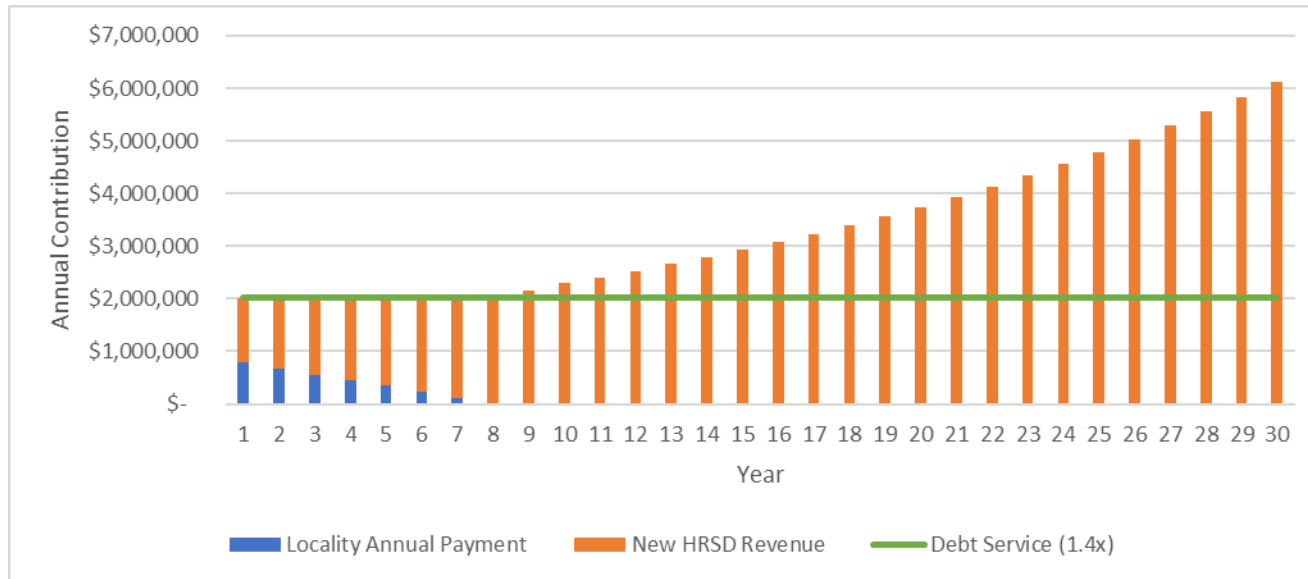
Some Examples

Principal	\$25M
Interest	4%
Initial ADF (gallons)	300,000
Growth Rate	0%
Debt Service w/ Coverage	\$2,013,758
Revenue Credit	100%



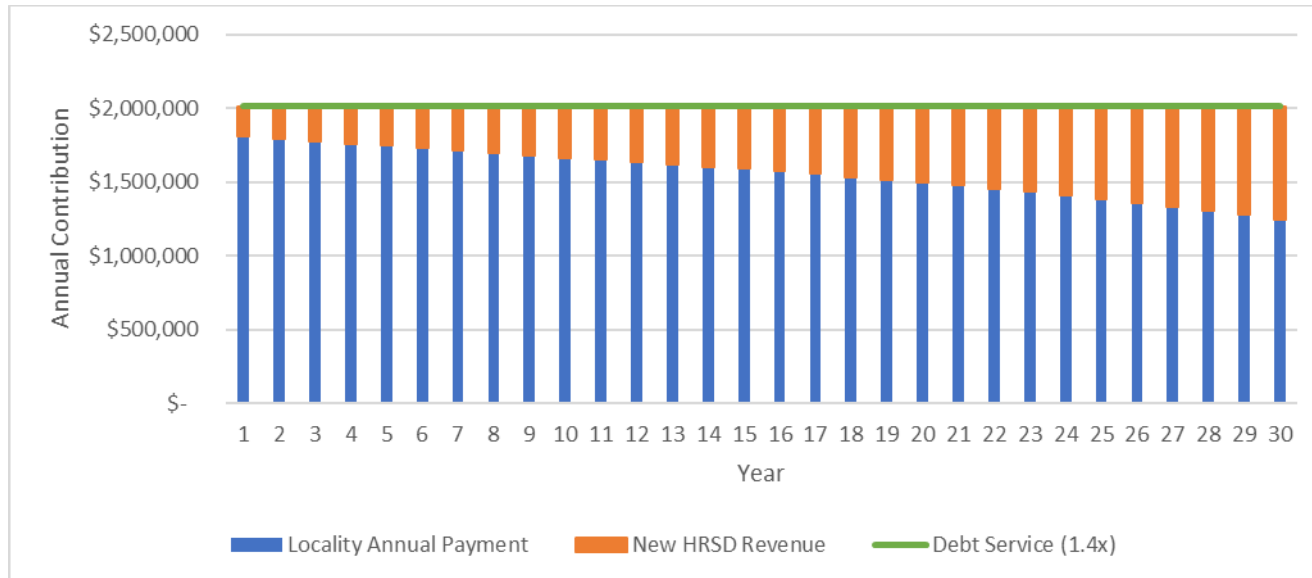
Some Examples

Principal	\$25M
Interest	4%
Initial ADF (gallons)	300,000
Growth Rate	1%
Debt Service w/ Coverage	\$2,013,758
Revenue Credit	100%



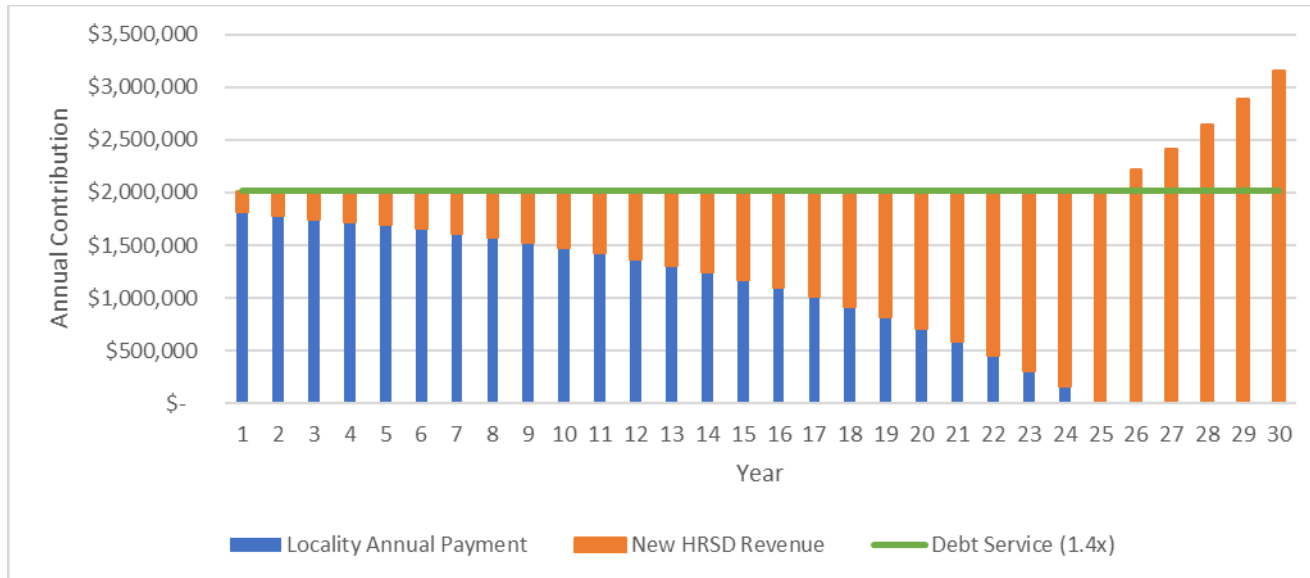
Some Examples

Principal	\$25M
Interest	4%
Initial ADF (gallons)	50,000
Growth Rate	0%
Debt Service w/ Coverage	\$2,013,758
Revenue Credit	100%



Some Examples

Principal	\$25M
Interest	4%
Initial ADF (gallons)	50,000
Growth Rate	5%
Debt Service w/ Coverage	\$2,013,758
Revenue Credit	100%



- **Locality Participation/Risk**
 - Locality carries the burden of initial capital cost offset by New Revenues
 - By offsetting new revenues, Localities share in upside of expansion
- Provides an avenue for expansion/development that does not put HRSD in the role of determining development priorities for a Locality
- **HRSD Participation/Risk**
 - Finances the capital for needed expansion
 - Some interest rate risk relative to payment from the Locality
 - Target debt service coverage requirements (2x DS) are not met
 - Operation and Maintenance costs may not be fully covered by payments
 - HRSD pays for renewal of the new infrastructure as it ages
 - Risk is offset by
 - Payment guarantee from the Locality for initial capital costs
 - Potential upside in New Revenues that extend beyond the term of the agreement
- Provides an avenue for expansion that is fair and does not unduly burden existing ratepayer

- Des Moines Metropolitan Wastewater Reclamation Facility (WRA)
 - Expansion at the cost of one or more participating communities
 - Community pays a surcharge over 30 years that matches SRF rate at time of agreement
- Commonly in Virginia, generally a utility will require a developer to fund the capital costs associated with an expansion
 - The utility may fund additional improvements the utility requires, beyond what is necessary for the development
 - Some policies allow for additional cost participation from the utility, upon explicit Board approval
 - Some policies allow for some type of offset to the availability fees based on new revenues, for a limited time (e.g., up to five years) or up to a cap (e.g., up to 50% credit)

- Recommendation
 - Proceed with development of Cost Participation Agreement format
 - Amend our existing policy if necessary
 - February – present changes to Commission for consideration