Board Of Water Works
REGULAR CALLED MEETING MINUTES
March 20, 2018

Board Members Present:
Mr. Creighton Mershon, Chair
Dr. Sundeep “Sunny” Dronawat
Mr. Paul Esselman
Dr. Sharon Kerrick
Mr. Craig Willman

Not Present:
Mayor Greg Fischer
Ms. Tierra Kavanaugh Wayne

Others Present:
Mr. Spencer Bruce, President and Chief Executive Officer
Mr. Daniel Frockt, CFO, Louisville / Jefferson County Metro Government
Mr. Dave Vogel, Executive Vice President, Customer Service and Distribution Operations
Ms. Kelley Dearing Smith, Vice President, Communications and Marketing
Mr. Tim Kraus, Vice President, Production Operations and Chief Engineer
Dr. Tom Luckett, Vice President and Chief Information Officer
Ms. Lynn Pearson, Vice President, Finance and Treasurer
Mr. Terrence Spence, Vice President, Human Resources and Labor Relations
Mr. Michael Tigue, Vice President, Compliance, General Counsel and Corporate Secretary
Ms. Kim Reed, Director, One Water Liaison
Ms. Jenni Schelling, Director, Internal Audit
Mr. Matthew Griffith, Strategic Planning and Performance Specialist
Ms. Beverly Soice, Paralegal

Visitors:

The regular called meeting of the Board of Water Works (“BOWW”) was held on Friday, February 16, 2018 at the Louisville Water Company (“Louisville Water” or “Company”) located at 550 South Third Street, Louisville, Kentucky. Chair Creighton Mershon called the meeting to order at 11:00 a.m.

Minutes of the Previous Regular BOWW Meeting Approved

Mr. Paul Esselman moved to approve the Regular Called Meeting Minutes of February 16, 2018, seconded by Mr. Craig Willman and the motion was unanimously carried.

Report Provided by the President/Chief Executive Office

Mr. Spencer Bruce stated the recent opening of the Omni Louisville Hotel highlighted Louisville Water’s history and product. The hotel was constructed on the site of our company’s second corporate office.

Since we began in 1860, Louisville Water has always had an office on Third Street. The first corporate building was adjacent to where the Omni stands today. It housed the Company’s business operations until a larger facility opened in 1910. Louisville Water remained in that building until we moved to our current address in 1998.

Last year, we began working with Omni Hotels to highlight our history at that location. The hotel has named the pool area "The Water Company" and will serve Louisville's drinking water throughout the venue. In 1938, Louisville Water produced a movie about the company's operations that includes a film of the 1910 office building. As part of the opening, Omni projected the film near the pool area. The hotel also gave a nod to our history with a large "Louisville Water Company" detail hanging near the hotel lobby.

First Quarter 2018 Dividend Declared

Ms. Lynn Pearson advised section 508 of the Series 2009 Water System Revenue Bond Resolution provides that the Louisville Water Company will pay to the Louisville / Jefferson County Revenue Commission an annual dividend on the Louisville Water Company stock owned by Louisville / Jefferson County Metro Government, Kentucky. The dividend declared for 2017, based upon estimated net income, is required to be adjusted after completion of the annual audit to reflect any difference between estimated and actual net income. The amount of such adjustment is to be paid with or deducted from the regular quarterly dividend payments in 2018.

The annual audit has not been completed, and as a result, there will be no adjustment to the first quarter 2018 dividend. The adjustments will occur in subsequent quarters of Louisville Water's 2018 calendar year as directed by Louisville Metro Office of Management and Budget.

The 2018 Annual Budget provides for a budgeted annual dividend of $21,453,700. Dr. Sharon Kerrick moved to declare the first quarterly 2018 dividend in the amount of $5,363,425.

> **WHEREAS**, it has been the long established policy of the Louisville Water Company to pay a dividend on its common stock related to its net earnings, after giving consideration to any requirements for debt amortization and bond reserve requirements, and
> **WHEREAS**, a covenant written into the 2009 Water System Revenue Bond Resolution sets forth a formula for determining the amount of any such dividend, and
> **WHEREAS**, such covenant requires payment of a dividend each year based on estimated annual adjusted net income, with adjustment upon completion of the annual audit to reflect any difference between estimated and actual net income, such adjustment to be made in the quarterly dividend payments of the following year, and
> **WHEREAS**, an estimated dividend of $20,827,200 was paid in 2017 based on estimated adjusted net income of $43,740,600 and
> **WHEREAS,** the annual audit for 2017 is not yet completed, no adjustment will be made to the first quarter 2018 dividend and adjustments will occur in subsequent quarters of LWC's 2018 calendar year as directed by Louisville Metro, and
> **WHEREAS**, the 2009 Bond Resolution requires that the Board of Water Works pay a quarterly dividend based on the formula contained therein, such quarterly payments to be as nearly equal in amount as possible, and
> **WHEREAS**, the 2018 Louisville Water Company Annual Budget reflects the 2018 annual dividend to be $21,453,700, it would be in order at this time to declare a regular first quarter dividend of $5,363,425; therefore, be it
> **RESOLVED**, the regular first quarter 2018 dividend of $5,363,425 is hereby declared, and further
> **RESOLVED**, that the President of the Company hereby is authorized and directed to pay $5,363,425 to the Louisville / Jefferson County Revenue Commission on March 30, 2018, this being the first quarterly dividend for 2018.

Mr. Willman seconded and the motion unanimously carried.

Contract Awarded for Project 14321 – Eastern Parkway 48-inch Water Main Rehabilitation Project Phase 2B

Mr. Tim Kraus advised the Eastern Parkway 48-inch transmission main extends from the Crescent Hill Water Treatment Plant, down Stilz Avenue, to Lexington Road, to Grinstead Drive, to Cherokee Parkway, to Willow Avenue, to Eastern Parkway, to Third Street and ends at the intersection of Third Street and Winkler Avenue for a total length of 33,400 feet. The original 48-inch main was installed in the 1920's and is composed of cast iron pipe with leadite joints. In recent years, Louisville Water has experienced a series of failures of this main and, as a result, we have initiated a project to rehabilitate it in a phased approach. Eastern Parkway 48-inch Water Main Rehabilitation Project, Phase 1 began in 2016 by sliplining a 42-inch outer diameter spiral welded steel pipe inside the existing 48-inch inner diameter cast iron main from Grinstead Drive to Beargrass Creek near Goss Avenue. Phase 2A extended the 42" outer diameter sliplining project on Eastern Parkway from Beargrass Creek to I-65.

Phase 2B of the project begins at I-65 and ends at the intersection of 3rd Street and Winkler Avenue and includes sliplining 1,440 feet of 42-inch outer diameter welded steel pipe inside the existing 48-inch inner diameter cast iron main. An additional 3,400 feet of 42-inch inner diameter ductile iron main will be installed in open cut excavation through parts of the University of Louisville campus.

On March 7, 2018, Louisville Water received bids from three (3) prequalified contractors for construction of Phase 2B of the project. The Project Manager's estimate for the project was $5,700,000. The low bidder was MAC Construction & Excavating, Inc. with a bid price of $4,919,000.

Mr. Esselman moved to award the contract to MAC Construction & Excavating, Inc. for construction of Phase 2B of the Eastern Parkway 48-inch Water Main Rehabilitation Project for $4,919,000. Dr. Kerrick seconded and the motion unanimously carried.

Compensation and Benefits Committee Report Given

Dr. Kerrick reported the Compensation and Benefits Committee met on March 7, 2018 at which time staff presented detailed results of the 2017 Executive Shared Operating Goals, Management Incentive Goals and Corporation Performance Goals, as well as the proposed Merit Matrix for Non-Union Employees.

Dr. Kerrick advised staff provided background regarding merit increases and the compensation structure movement. The Committee recommends approval of the merit matrix with an overall 3.0% increase and a 2.0% market movement. Mr. Bruce advised that the increase is a 3.0% overall, but that the actual raise for each employee is based on the results of their individual performance goals.

Dr. Kerrick advised that the Committee that there were five goals that make up a total of 25% of all Executives performance rating; all goals were achieved at a successful or superior performance. These goals included: (1) Capital Implementation expended $83 million of the Capital Program; (2) Operation and Maintenance Expense Cost Control was $2 million under budget; (3) Top-Line Growth – Regionalization, Economic Development and Partnerships Increased non-operating revenue by over $700,000 per year as well as further partnerships with Greater Louisville Inc. (GLI), Louisville Forward and the Kentucky Economic Development Cabinet; (4) MBE Construction Spend at 8.2% exceeded goal of 6.5% and (5) the best safety performance in the history of the Company at a 1.74 Occupational Safety and Health Administration (OSHA) Recordable Rate.

Additionally, there were four goals associated with the Management Incentive Plan with a Level I and Level II performance for each goal or a total of 8 possible incentives. Performance on these goals included: (1) for Net Income, neither the Level I or Level II goal was met so there was no performance incentive; (2) for Customer Service, the Total Customer Satisfaction Index (CSI) survey was 837 and Service CSI was 881 achieving a

Level I performance incentive; (3) all targets for water quality were met achieving a Level II performance incentive; and (4) and other Operating Revenue was $11.9 million achieving a Level I performance incentive

Finally, Dr. Kerrick reviewed the Corporate Performance Award for non-union/non-management employees. There are five incentive goals with a Level I and Level II performance available for each goal or a total of 10 possible incentives. Performance on these goals included: (1) for Water Quality, all distribution water quality goals were met. The Customer Service Index (CSI) fell 27 points short of the stated goal; however, the Compensation Committee recommended award of the incentive to employees because the result of this portion of the goal is in part determined by factors outside the control of front-line employees. Since this has also been one of the best water quality years in the history of the Company, it was recommended that a Level II incentive should be awarded to front-line employees; (2) for the Service component of the Customer Satisfaction Index, a score of 881 was achieved allowing for a Level II performance incentive; (3) for Safety, there was only one injury allowing for a Level I performance incentive; (4) for Health and Wellness, neither of the goals were met so no performance incentive was achieved; (5) for Cost Control, Operational and Maintenance expenses were $2 million under budget allowing for a Level II performance incentive.

Dr. Kerrick moved to approve and Mr. Willman seconded the Committee's motion to approve a 3.0% overall merit increase for non-union employees and the 2.0% market movement. The motion unanimously carried.

Dr. Kerrick moved to approve and Mr. Willman seconded the Committee's motion to approve the Management Incentive Plan awards and the Corporate Performance Awards including the Level II performance for the Water Quality CSI goal for employees. The Motion unanimously carried

Mr. Daniel Frockt congratulated everyone on the Company's impressive safety and water quality goal results for the year.

Mr. Esselman inquired into how the Company incentive goals compare to other utilities. It was noted that most other utilities are predominantly governmental whereas the Company operates primarily as a private utility so the governance and metrics are somewhat different. Nevertheless, the Company's consultants do comparative analysis of other utilities metrics when making recommendations for the Company's corporate and management goals.

Discussion occurred regarding whether the Company should permit part-time employees to participate in the Company's incentive awards as current policy does not allow part-time employee participation. It was generally observed that given the part-time employee contribution toward the Company's successful performance that it would be appropriate to permit part-time employees to participate in and benefit from the Company's incentive programs on a pro-rate basis moving forward.

Mr. Mershon moved to approve part-time employees in the Company's performance award. Dr. Kerrick seconded and the motion unanimously carried.

Ms. Dearing Smith stated an announcement will be sent to all employees today.

The Board took a break for lunch at 12:00 p.m.

<u>Closed Session</u>

Mr. Dronawat moved to go into closed session at 12:15 p.m. pursuant to KRS 61.810(1)(f) and (m) to discuss personnel matters. Dr. Kerrick seconded and the motion unanimously carried.

Resume Open Session

Dr. Kerrick moved to return to open session at 1:27 p.m., seconded by Mr. Dronawat and the motion unanimously carried. No action was taken in closed session.

Mr. Mershon stated the Board is very complimentary with regard to the professionalism and efforts of the executives on behalf of the Company.

Dr. Dronawat moved to approve a salary increase of 3.5% for Mr. Bruce, seconded by Dr. Kerrick, and the motion unanimously carried.

Dr. Kerrick moved to authorize Mr. Bruce to determine the appropriate salary increases within Mr. Bruce's recommend ranges for the following executives: Dave Vogel, Tom Luckett, Lynn Pearson, Kelley Dearing Smith, Terrence Spence, Michael Tigue, and Tim Kraus. Seconded by Mr. Willman, the motion unanimously carried.

Financial Report Given

Ms. Pearson summarized the Financial report for February 2018 and provided an update on December 2017.

The Company's audit and the year-end financial statements cannot be completed until the GASB 68 report is received from the Kentucky Retirement System. We expect to receive preliminary, unaudited information in the near future based on prior year's timing.

Water revenue and other operating revenue both came in slightly under budget for the month, while operating and maintenance expenses are over budget. These unfavorable variances were partially offset by other operating expenses and non-operating income and expense all of which performed favorably to budget. As a result, net income for the month is $136,000 or 4.6% lower than budgeted. Details of the Company's financial performance as compared to budget and prior year follows.

Consumption of 2.4 billion gallons for February 2018 is 58 million gallons higher than budget, and 128 million gallons more than February 2017. Consumption for all customer classes is over budget with the exception of residential and irrigation. Year-to-date consumption is over budget and prior year, both by 3.9%. Through February, all customer classes are over budget except for irrigation, with wholesale accounting for close to half of the overall favorable budget variance.

Water Revenue for February 2018 is $151,000 lower than budget and $666,000 higher than the prior year. Water revenue through February is $183,000 higher than budget and $1.2 million higher than last year.

Other Operating Revenue for February is $26,000 lower than budget but is $41,000 higher than year-ago levels. For the period-to-date, other operating revenue is $53,000 below budget and $60,000 over prior year. The variance compared to budget for both the month and the year-to-date period is primarily due to revenue from late fees and disconnect fees running lower than anticipated. The variance to prior year is driven by higher service line protection and sewer billing revenue, offset by lower late fees and disconnect fees.

Operating and Maintenance Expenses for February of $6.3 million are $148,000 higher than budget and $717,000 higher than February 2017. The February variance from budget is primarily due to higher power costs, overtime, and contractual services. Power costs are higher than anticipated due to increased pumping resulting from main breaks and leaks in the system and increased facility heating costs. Elevated main break activity also resulted in budget overages in overtime and contractual services. Additional overtime was also incurred at Zorn Avenue as a result of the recent flooding. February year-to-date operations and maintenance expenses are $208,000 over budget and $1.5 million over year-ago levels. The majority of the year-to-date unfavorable budget variance is in labor and labor related costs, contractual services, bad debt and insurance reserves. Increased main break activity resulted in a higher portion of labor charged to O&M vs. capital than anticipated. Overtime and contractual services are also higher due to main breaks. Bad debt is over budget for the year-to-date period, though for the month it was lower than budget.

Total Operating Expenses for February of $10.8 million are $31,000 higher than budget and $773,000 more than February 2017. Year-to-date total operating expenses are 0.7% higher than budget and 9.4% over year-ago levels. The year-to-date budget variance is due to higher operating and maintenance and depreciation costs, which were mostly offset by lower losses recognized from disposition of property.

Non-Operating Income through February is $284,000, which is $22,000 higher than budget and $110,000 more than same period through February 2017. The variance to prior year is due to funds reinvested in treasury securities at a substantially higher effective rate than those which matured late in 2017. The variance to budget is due to receiving a higher rate on the new treasuries than anticipated.

Non-Operating Expense through February of $1.2 million is $117,000 less than budgeted and $212,000 less than year-ago levels. Interest expense is less than prior year and budget due to higher amounts of interest capitalized. Principal payments made on bonds during 2017 also reduced interest expense as compared to prior year levels.

Net Income before Distributions and Contributions for February is $2.8 million, $136,000 less than budgeted. In comparison between years, net income for February is $117,000 more than February 2017. February year-to-date net income of $6.9 million is $123,000 over budget but is 3.8% less than the two months ended February 2017.

Contributions through February of $670,000 are $520,000 lower than budgeted and $424,000 less than prior year.

Cash, Cash Equivalents and Short-term Investments totaled $77.3 million at the end of February 2018, well in excess of 250 days of estimated Operations and Maintenance expense of $51.7 million.

Communications and Marketing Report Given

Ms. Smith summarized the Communications and Marketing report for January.

Each year, Louisville Water visits over 100 schools with its education program. Typically, the majority of the programming is delivered in elementary and middle schools. This year, through a partnership with Teach Kentucky and the Louisville Water Foundation, we began a focus in high schools. Two teachers in Jefferson and Oldham counties are piloting curriculum on environmental issues and career opportunities. Based on initial feedback, we plan to expand this effort in the 2018-2019 school year.

Louisville Water continues to create partnerships with local distilleries to highlight our connection to this signature industry. Recently, Louisville Water participated in “Beyond the Beam, Grain and Steam.” Guests met with a local farmer who supplies a majority of the corn for Beam Suntory’s distilleries and then learned how Louisville’s water is part of the entire bourbon process. Jim Beam is one of 12 distilleries in our service area that use Louisville Water in their production and/or visitor experiences.

As construction begins on a back-up generator facility for the Crescent Hill Water Treatment Plant, staff met with the public for a final project overview. We visited with the Crescent Hill Community Council and the Frankfort Avenue Business Association and then hosted a community conversation. Overall, the Crescent Hill neighborhood is pleased with the facility design.

We kicked off the 2018 Louisville pure tap® season on a cold Saturday morning with the Anthem 5k. Louisville Water coordinates the water stops for the Triple Crown of Running series as well as over 100 other community events. For the runs and walks, our crews are out early to provide connection points for volunteers who fill cups with Louisville pure tap®. The pure tap program is at the center of our customer outreach, reaching nearly one million people annually.

Customer Service and Distribution Operations Report Given

Mr. Vogel summarized the Customer Service and Distribution Operations report for January.

The Call Center operations had an outstanding month in February. For the month, 27,738 calls were received with an abandonment rate of 5.9%. Year-to-date our abandonment rate is running at 10.9%, which is significantly lower than last year (14.8%) and the five-year average (18.4%). The average speed of answer came in at 3:00 m:s for the month, which is an improvement from last year (3:50 m:s) and the five-year average (4:07 m:s).

The Customer Service organization closed its offices on Presidents Day holiday (February 19th) for training. The entire group participated in an all-day training session that focused on metering Services Q&A, goal setting and accountability, business process training, rates (both LWC and MSD), main break and sewer operations, and interview skills and resume building. There were also several teambuilding activities throughout the day and the feedback on the session was very positive.

Inclement weather hindered our productivity in meter reading which put us slightly behind schedule. In spite of this, we maintained a low level of estimations for the month. The percentage of estimated bills in February came in at 1.88%, which is lower than last year and significantly lower than the five-year average. Billing accuracy for the month finished at 99.91% versus 99.96% last year and 99.74% for the five-year average. The team is preparing for four retirements from our union workforce in the coming months.

Bad debt for February came in below budget at $111K assisted by a provision adjustment of $36K. This is significantly lower than last year and our aged receivables are trending favorably. Staff continues to focus on tactics to lower the bad debt levels. We had a conference call with the Phoenix water department to review their bad debt and collections practices, and we also received tags that will go in the meter vault to dissuade customers from tampering with our valves upon shut off. We will begin using these tags in March.

We finished with 46 main breaks for the month of February, which is in line with last year (47) and significantly lower than the five-year average (72). Significant clean up and restoration work continued in February as a result of the higher than normal break activity in January. As a result, we have performed limited Capital work for the month. Distribution is also preparing for several union retirements as well as one management retirement in the coming months.

Engineering and Production Operation Report Given

Mr. Kraus summarized the Engineering and Production Operations report for February.

2018 capital program expenditures through February totaled $8,415,796, which is $128,521 or 1.50% lower than the same period last year. These expenditures equate to 7.58% of the 2018 total capital program of $110,955,773.

The amount of water produced and delivered to the system in February 2018 was 111.8 MGD, which was 10.0% higher than February 2017 and 3.8% higher than the February five-year average. For year-to-date, the amount of water delivered to the system is 13.5% higher than 2017, and 8.5% higher than five-year average.

There was a total of four chemical spills reported by ORSANCO during the month of February; all four were upstream of Louisville Water's Zorn intake. There were no impacts on water quality and treatment.

Water Quality (WQ) staff monitored 1,154 water quality parameters of a required 994 per federal and state regulatory requirements with zero violations.

Staff collected 280 compliance distribution samples. There were zero total coliform and zero *E-Coli* results. All internal water quality goals were met. Staff also collected 104 main break samples on 52 repairs in the month, of which six localized boil water advisories were issued due to field conditions and none were issued due to water quality monitoring results. There were a total of 24 water quality customer complaints, the same as the five-year average.

Human Resources Report Given

Mr. Spence provided a summary of recent and current activity between the Louisville Water's Labor Management and Local Union 1683 of the American Federation of State, County and Municipal Employees, AFL-CIO (the Union).

Currently, there are ten active grievances; all are in various stages of the contractual process for resolution.

Union and Company leadership agreed to and signed a proposal statement directing the Company's Decision Partnership Team to review and recommend a strategy to establish an internal workforce development initiative to address current and future staffing needs.

The Union and Company representatives jointly established the Healthcare Incentive goals for the 2018 benefit plan year.

The Company posted one temporary full-time classified position for union employee's internal bidding process.

Information Technology Report Given

Mr. Tom Luckett summarized the Information Technology Report for February.

Testing continues on the Oracle Work and Asset Management (WAM) implementation. IT is currently working with the mobile technology vendor to set up a server outside of the Louisville Water Company secured firewall network. IT is also working with the Ernst & Young implementer on integration support.

Staff is currently evaluating the responses to our Request for Proposal for support of the Louisville Water Oracle software suite. We received thirteen proposals.

Staff is evaluating proposals for security services and network services that include monitoring and maintenance.

Phase 1 of the Oracle Identity Management Implementation has been completed with integration between Active Directory and Oracle Database technologies. It also includes a self-password reset portal. Phase 2 has started, which will expand the integration to include PeopleSoft HR and E-Business Suite Financials along with on-boarding and off-boarding workflows.

There being no further business for the Board, Mr. Dronawat moved to adjourn at 1:50 p.m., seconded by Mr. Willman and the motion unanimously carried.

Respectfully submitted,

Michael F. Tigue
Vice President, Compliance, General Counsel
and Corporate Secretary