

Sewerage & Water Board Privatization at a Critical Stage

June 2002



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Executive Summary

Over the past year and a half, the Sewerage & Water Board of New Orleans (“S&WB”) has actively pursued a procurement for the private management, operation, and maintenance of the S&WB’s water and wastewater systems. The procurement process has now advanced to the critical stage of contractor selection.

The Bureau of Governmental Research (“BGR”) has been closely following the S&WB’s procurement. In June 2001, BGR issued a detailed analysis of the proposed privatization and the draft procurement documents. In that study, it concluded that the S&WB’s procurement suffered from serious shortcomings that could, individually and in the aggregate, seriously impact competition and the ultimate cost to the S&WB’s ratepayers.

Some of the troubling issues originally identified by BGR in its June 2001 study remain unresolved. Additional problems have surfaced since the study was issued. Given the scope of the proposed privatization and its implications for all citizens, BGR engaged Raftelis Financial Consulting, PA (“Raftelis”) to reassess the S&WB’s evaluation and selection process in light of developments over the past year.

Raftelis identified a number of serious flaws in the procurement process and the draft service agreement (the “Service Agreement”) that could prevent the S&WB from maximizing the benefits of its procurement. Some of the flaws are procedural deficiencies that could adversely affect the S&WB’s ability to identify and select the proposal offering the greatest total value to the S&WB and its customers. Others are structural ones that could significantly impact the total cost of the privatization, regardless of which proposer is chosen.

Fortunately, the S&WB still has an opportunity to remedy deficiencies. This can be done by:

- amending the Request for Proposals (“RFP”) and the Service Agreement,
- providing proposers with an opportunity to revise their pricing, and

- reconvening the S&WB’s Special Evaluation Committee (“SEC”) or appointing a new evaluation committee to evaluate proposals pursuant to a detailed, rigorous process.

BGR realizes that amending the procurement process at this late date involves risk, inconvenience, and additional expense. However, BGR believes that, regardless of the risk and expense, corrective action is preferable to continuing with a flawed process that could result in twenty years of unnecessary expense for the S&WB and its ratepayers.

We urge the S&WB to implement promptly the recommendations set forth in this report. Determined action to address the flaws in the current procurement would both greatly improve its quality and send a strong message that New Orleans is focused on delivering services in an efficient, businesslike manner.

Cost Issues

A review of the S&WB’s procurement documents and process uncovered several issues that could limit the financial advantages of the proposed privatization. These include the following:

1. **Baseline.** The S&WB has not established a credible economic baseline against which the cost of the various proposals can be compared. Without a baseline, the S&WB cannot determine savings and make a responsible determination as to whether to proceed.
2. **Electricity Costs.** The S&WB’s RFP does not provide for the consideration of electricity costs in the evaluation of proposals. Because electricity is a major expense that could vary significantly depending on a contractor’s approach to operations and maintenance, the true cost of a proposal cannot be ascertained without an analysis of the associated electricity costs.
3. **Electricity Pass-through.** The pass-through provision for electricity does not promote responsible energy consumption by the operator. This could result in unnecessary expense for the S&WB.
4. **Residuals Disposal Pass-through.** The baseline for the pass-through of cost increases associated with the transportation and

disposal of water and wastewater residuals is not established until after the contract is executed. As a result, the number is subject to manipulation.

5. **Insurance Pass-through.** The RFP inappropriately classifies insurance costs as a pass-through item. These costs are more in the control of the system operator than of the S&WB.
6. **Flow and Loadings Adjustments.** Adjustments to the Annual Service Fee based on changes in flow and loadings could act as a disincentive to the repair of the water pipes. In addition, the proposed adjustment thresholds could require immediate adjustments to the Annual Service Fee.

Additional Contract Issues

1. **Termination for Convenience.** Although the Service Agreement provides for termination for convenience, the termination right is illusory due to an unusually steep penalty schedule. The S&WB has not provided a reasonable explanation or supporting numbers to justify penalty payments to the contractor that could be as high as \$30 million—an amount that is equal to one-third of the 2002 sewer and water systems' operating budgets and exceeds current assets.
2. **Termination for Uncontrollable Circumstances.** The Service Agreement imposes similar penalties on the S&WB for terminating a contractor whose ability to perform has been negatively impacted by a natural disaster or other uncontrollable event.
3. **Approval of Professional Service Subcontracts.** Although the S&WB has indicated that it intends to seek elimination of a contract provision requiring S&WB approval of certain professional services contracts, the revision has not yet been made.
4. **Legality of Contract.** The S&WB has invested millions of dollars in a procurement that raises significant issues under Louisiana law, while steadfastly refusing to have it reviewed by independent legal counsel for compliance with the public bid, civil service, and other state laws.

Process Issues

The evaluation process established for the SEC lacked critical elements. Partially as a result of these procedural shortcomings, the SEC's review is of limited use to the S&WB.

1. **Inadequate Information.** The S&WB has not requested sufficiently detailed information with respect to electricity consumption and demand, the cost of residuals disposal, the cost of the letter of credit required of private proposers, and other components of the Annual Service Fee. Without this information, the S&WB cannot conduct a thorough financial analysis of the proposals.
2. **Definition and Direction.** Neither the RFP nor the S&WB's financial advisors provided adequate definition and direction for the evaluation process. There were no procedures for calling and conducting meetings or for documenting, collecting, and consolidating the evaluations by the individual members of the SEC. This contributed to a haphazard, undisciplined evaluation by the SEC.
3. **Superficial Analysis.** Neither the S&WB nor its financial advisors provided the SEC with the type of detailed guidance and analysis needed to determine the cost effectiveness of the proposals. As a result, the SEC conducted a simplistic cost analysis that did not take into account the long-term economic impact of the proposals.
4. **Committee Autonomy.** Evaluation committees are established to provide the utility owner with independent, third-party advice. The SEC weakened its ability to function independently by allowing a representative of the S&WB, rather than one of its own members, to chair its meetings.
5. **Assessment of Monetary and Customer Value.** The evaluation protocols did not adequately separate the consideration of monetary and customer values. Objectivity can be compromised if these two values are not considered independently.
6. **Clarification Process.** The S&WB did not establish a process for obtaining clarification of proposals. As a result, the SEC based its evaluation on ambiguous proposals.

7. **Ambiguities with Respect to the Sub-criteria.** The ability of the SEC to evaluate proposals thoroughly and objectively was negatively impacted by ambiguities in the evaluation sub-criteria. The sub-criteria under the Disadvantaged Business Enterprise criterion are particularly unclear and, based on the proposals submitted, were interpreted differently by the different bidders.
8. **Allocation of Scoring Points.** Although the S&WB assigned values to the major criteria for evaluating proposals, it did not allocate them to the sub-criteria. This unnecessarily decreased objectivity.
9. **Inadequate Time for Review.** The schedule set forth in the RFP did not allow adequate time for the SEC's review of proposals. Although the over-all time period was extended *de facto*, inadequate time was allowed for critical steps in the process, such as the review of the SEC's draft evaluation report.
10. **Superficial Report.** The SEC's report is too general and subjective to provide meaningful guidance to the S&WB.
11. **Scoring.** The SEC did not utilize the scoring system defined in the RFP.
12. **Misplaced Emphasis.** The SEC placed undue emphasis on non-binding pledges.

Recommendations

To Maximize Financial Benefits

1. The S&WB should prepare a credible economic baseline that includes an analysis of the direct and indirect costs incurred to manage, operate, and maintain the water and wastewater systems.
2. The RFP should be amended to factor future electricity costs into the evaluation of the cost of the proposals. The amendment should require proposers to provide the information needed to analyze the impact of their operating plans on electricity costs.

3. The S&WB should amend the pass-through provisions by:
 - establishing the electricity pass-through caps and the residuals disposal baseline cost before the contract is executed,
 - capping energy consumption in terms of energy per unit of water and wastewater treated (e.g., kilowatt hours/million gallons), and
 - eliminating the pass-through of insurance.
4. The S&WB should amend the Service Agreement to eliminate the provisions for water flow adjustments. Wastewater Base Demand Range and the Wastewater Loadings Range for adjustments should be changed to reduce the probability that those adjustments will be required.
5. The S&WB should obtain more detailed information on the components of the Annual Service Fee, including the base cost for residuals disposal and the cost of letters of credit.

To Improve the Contract

1. In accordance with its resolution dated April 24, 2002, the S&WB should take all necessary action to eliminate from the Service Agreement the requirement for board approval of certain professional service contracts.
2. The S&WB should reduce the penalty schedule for Termination for Convenience to amounts that would discourage termination without making it impossible.
3. The S&WB should amend the Service Agreement to eliminate the penalty for Termination for Uncontrollable Circumstances.
4. The S&WB should hire independent legal counsel to review the contract for compliance with the public bid, civil service, and other applicable laws.

To Provide an Objective Evaluation

The S&WB should take the following steps to ensure an independent, thorough evaluation of the proposals:

1. The S&WB should reconvene the SEC or appoint a new evaluation committee to prepare a thorough, independent evaluation of the proposals.
2. In order to enable the evaluation committee to conduct such a review, the S&WB should provide it with a detailed, professional analysis of the proposals that, at a minimum:
 - analyzes the cost effectiveness of the proposals based on net present value,
 - takes into account the differences in the scope of the obligations imposed on the private companies and the Managed Competition Employees Committee (“MCEC”), and
 - discusses in detail the strengths and weaknesses of the proposals under the criteria established by the S&WB.
3. In order to enable the evaluation committee to conduct a thorough and objective review, the S&WB should provide it with an evaluation guide that:
 - clarifies the existing evaluation criteria and sub-criteria, particularly those relating to Disadvantaged Business Enterprises,
 - allocates scoring points to the sub-criteria set forth in the RFP,
 - establishes a process for obtaining clarification of proposals,
 - establishes procedures for calling and conducting meetings,
 - provides for, and emphasizes the importance of, an independent consideration of the monetary and customer values, and
 - provides protocols for documenting, collecting, and consolidating the evaluations of the individual members of the evaluation committee.

4. To encourage independence, the evaluation committee should select one of its own members to act as chairperson.
5. The evaluation committee should prepare an evaluation in accordance with the requirements of the RFP and the evaluation guide. As part of that process, the evaluation committee should:
 - request clarification of ambiguities in the proposals, and
 - assign scores to the proposals based on the weights specified in the RFP and the evaluation guide.
6. The S&WB should allow the evaluation committee adequate time to conduct a thorough evaluation.
7. After the evaluation committee conducts its evaluation on the basis set forth above, the S&WB should either (i) accept the evaluation committee's recommendation, or (ii) conduct its own evaluation on the basis set forth above and provide detailed explanations of variations from the evaluation committee's scoring.

I. Introduction

A. Background

Early in 2000, the S&WB, faced with the cost of significant capital improvements and attendant rate increases, initiated a procurement for the private management, operation, and maintenance of its water and wastewater systems. The procurement was for the largest water/wastewater privatization in the United States, with a term of 10 to 20 years and an estimated value of \$1 billion.

The procurement was structured as a managed competition, meaning that both private firms and employees of the S&WB were invited to submit proposals. In February 2001, the S&WB released, but did not formally issue, a draft Request for Qualifications/Request for Proposals soliciting proposals.

After extensive public hearings, the S&WB in August 2001 issued a Request for Qualifications accompanied by a draft Request for Proposals. Four potential proposers responded and qualified.

On January 2, 2002, the S&WB issued a final Request for Proposals, with a deadline for submitting proposals of February 13, 2002. The MCEC and two private companies, USFilter Operating Services, Inc. and United Water New Orleans LLC, submitted proposals.

From February 25 to 27, 2002, the SEC met to hear presentations by the proposers and to consider the proposals. On April 8, the SEC met to finalize its report to the S&WB. The report was submitted to the S&WB at its board meeting on April 24, 2002. The S&WB has not indicated when it will consider the proposals.

BGR in June 2001 issued a study of the proposed privatization entitled *Privatization of Water and Wastewater Systems in New Orleans: An Analysis of the Sewerage and Water Board of New Orleans' Proposal*. In that report BGR concluded that the proposed procurement had serious shortcomings that could, individually and in the aggregate, seriously impact competition and the ultimate cost to the S&WB's ratepayers.

Some of the troubling issues originally identified by BGR in its June 2001 study remain unresolved. Additional problems have surfaced since that study was issued. Given the scope of the proposed privatization and its implications for all citizens, BGR decided to reassess the S&WB's evaluation and selection process in light of developments over the past year.

To assist it in preparing an impartial evaluation, BGR engaged Raftelis, a Charlotte, North Carolina, consulting firm with expertise in water and wastewater management and privatizations, to do the following:

1. review and evaluate the S&WB's evaluation and selection process to identify factors that could negatively impact the S&WB's ability to select the proposal that would maximize the potential benefits of the procurement, and
2. identify other aspects of the procurement process and the Service Agreement that might negatively impact the privatization.

This report sets forth the results of their evaluation and recommendations.

B. Purpose of the Evaluation and Selection Process

The procurement process is the mechanism that both promotes competition among qualified parties in an effort to increase value and allows for the selection of the party that will provide the greatest total value. The evaluation and selection component of the procurement should be structured in a way that allows for a thorough and objective evaluation of the total value offered by each proposal. That evaluation should serve as the basis for the selection of the proposal that offers the greatest total value.

It is important to recognize that total value is comprised of two separate components. The first component is the monetary value associated with the transaction. In the S&WB procurement, monetary value is referred to as Cost Effectiveness.

The other component of total value is the value intrinsic in high quality services. That component will be referred to in this report as customer value. In water and wastewater privatization transactions, customer value is

typically measured using factors such as customer satisfaction, drinking water quality, environmental stewardship, employee well-being, and regulatory compliance. In the S&WB procurement, this component is determined by evaluation under the following criteria: Technical Approach; Disadvantaged Business Enterprise Plan; Employee Compensation and Benefits Package, Employee Relations and Career Development; Quality of Management Team; and Employee Transition Plan.

C. S&WB Evaluation and Selection Process

The evaluation and selection process defined in the RFP consists of two steps. The first step involves an evaluation of proposals by the SEC, a thirteen-member panel comprised of individuals with expertise in various disciplines. The RFP states that the SEC is to perform its evaluation based on criteria described in the RFP. It also sets forth sub-criteria under each of the primary criteria. The SEC is to assign a score to each of the proposals based on the scoring system set forth below and provide the S&WB with an executive summary of each proposal, including the strengths and weaknesses of each.

Cost Effectiveness

250 points

- Total costs to manage, operate, and maintain the systems
- Financial viability of the proposals
- Completeness, clarity, and correctness of the cost proposal

Technical Approach

250 points

- Operation and management plan and proposed practices
- Maintenance management plan
- Suggestions for the board's capital improvement plan
- Plan for Consent Decree compliance
- Plan for interaction with regulatory agencies
- Understanding of contract performance and compliance requirements
- Customer service plan
- Proposed plan for emergencies
- Staffing plan
- Transition of services

Disadvantaged Business Enterprise	175 points
Management opportunities afforded to DBE firms	
Types of functions to be performed by DBEs	
Identification of DBE firms	
Ability to meet or exceed DBE participation goals	
Employee Compensation and Benefits Package; Employment Relations and Career Development Program	175 points
Proposed employee compensation and benefits package	
Scope of training programs	
Breadth of human resource plans	
Responsiveness to employee career development objectives	
Quality of Management Team	100 points
Management team	
Current and previous experience	
Financial strength of proposer and guarantor	
Employee Transition Plan	50 points
Overall efficiency of transition plan	
Proposed schedule for employee interviews	
Plans for job assignments and responsibilities	
Employee training objectives and plans	
Total	1,000 points

The second step in the S&WB evaluation and selection process involves a review by the S&WB of the SEC's evaluation and scoring of the proposal. The S&WB may rely on the SEC's evaluation or it may perform its own evaluation, using the same criteria and the scoring system, if it deems such an evaluation is necessary. The S&WB will then select the proposal with the highest score based on either its evaluation or the evaluation of the SEC.

II. Factors Negatively Impacting Cost Effectiveness

Certain aspects of the selection process may have compromised the ability of the SEC and the S&WB to identify the most cost effective proposal. The deficiencies relate to both inadequate requests for information and inadequate guidance for the evaluators.

In addition, a review of the Service Agreement revealed several issues that, while not directly related to the evaluation and selection process, could potentially prevent the S&WB from maximizing the benefits that it hopes to receive as a result of the procurement.

A. Failure to Establish an Economic Baseline

In many water and wastewater contract operation procurements, an economic baseline is established to provide a basis for judging the true economic benefits of the proposals. An economic baseline is basically a detailed estimate of the long-term costs associated with continuing the status quo, assuming that the activities included in the calculation are being funded at an appropriate level.

While a utility's current budget is the starting point for developing an economic baseline, a simple projection of the current budget does not provide an adequate baseline. This type of analysis fails to consider whether the current funding levels are appropriate. If the activities included in the baseline are not being funded at an appropriate level, the projection must be adjusted to reflect an appropriate level of investment. The baseline should not be adjusted to reflect any benefits from optimizing operating processes, unless it is absolutely certain that these benefits will be realized.

In the case of the S&WB's proposed privatization, the determination of the baseline would start with the current budget for the continued management, operation, and maintenance of the water and wastewater systems by the S&WB. The budget numbers would be adjusted to include additional annual investment needed to maintain and repair the system at the level required of the contractor under the Service Agreement.

The resulting capital and operating costs would be projected for a period equal to the term of the contract using economic assumptions identical to the assumptions used to evaluate the cost implications of each of the proposals. The projected costs would then be discounted back to the present to determine the net present value ("NPV") of costs associated with the status quo. The baseline NPV of costs would then be compared with the NPV of costs for each proposal in order to develop an understanding of the economic value offered by the proposals. If the proposals do not represent significant savings with respect to the baseline, the S&WB must consider whether contract operations will provide the desired combination of monetary and customer values.

It should be noted that the baseline would not include all the costs of repairing and replacing the water and wastewater systems. In particular, it would not take into account the cost of capital repairs and replacements for which the contractor does not assume responsibility. While the baseline comparison is a useful tool for developing an understanding of the economic value offered by the proposals, it would not necessarily reflect differences in the level of service and customer value under the status quo and the contract operation.

In conjunction with the economic baseline, an indirect cost analysis should be performed. This type of analysis is particularly important with respect to managed competition in that it provides insights into the total costs, both direct and indirect, associated with both the draft Memorandum of Understanding (the "MOU") for the MCEC and the Service Agreement for the private company proposers.

Since the MCEC will still be a division of the S&WB if it is selected as the operator, it is likely that the S&WB will continue to incur certain indirect costs that it might not incur if a private firm were selected. These costs, which are reflected in most municipal utility budgets as indirect cost allocations or inter-fund transfers, are associated with functions that are not explicitly related to providing water and sewer service but are necessary to the day-to-day operation of the utility. Typical indirect costs include purchasing, human resources, risk management, legal services, and administration.

Under the scenario where a private firm is selected, the S&WB will continue to incur some of these indirect costs. It is highly probable, however, that they will not be of the same magnitude as they would be under the status quo or an MOU with the MCEC. For instance, it is conceivable that under the MOU the S&WB's legal department will incur costs related to the review of third-party contracts on behalf of the MCEC, while under a contract with a private firm such costs would not be incurred.

In addition, new indirect costs will be incurred by the S&WB if a private firm is selected. The most obvious new indirect cost will be for oversight of the contract operator and contract administration.

In order to fully understand the way in which these indirect costs will differ under the two possible scenarios resulting from this procurement, each of these functions and their associated costs must be carefully examined.

B. Failure to Consider Electricity Costs

Electricity costs are a significant part of any utility's operating budget, and energy consumption can vary significantly depending upon the way in which facilities are operated and maintained. Because the RFP treats electricity as a pass-through cost, the cost remains with the S&WB and is not included in the proposers' prices. Unfortunately, the RFP does not factor this significant cost component into the evaluation.

Electricity costs are influenced by three variables: rates, consumption, and a demand component. In water/wastewater privatizations, the rate risk is usually absorbed by the utility owner. The responsibility for controlling consumption is usually placed with the operator. This is done either by (i) obtaining from the proposers guarantees as to electricity consumption, or (ii) including in the Service Agreement a carefully crafted cap establishing the maximum electricity consumption. The cap, by imposing an upward limit on pass-through costs, makes it possible to measure the impact of the proposals on the system's electricity costs. Requiring proposer guarantees has the added benefit of introducing a competitive element into the realm of electricity costs.

In order to allow for an evaluation of the impact of the proposals on the utility's energy costs, the cap should be based on historic energy

consumption. This is not the case in the RFP, which bases the Maximum Utility Utilization on electricity consumption during the first year of operation under the new contractor. Because the cap is not established until after the operation of the S&WB has changed, cost increases attributable to increased consumption during that first year of private operation escape the cap and become the responsibility of the S&WB.

The S&WB might have opted for an after-the-fact determination of the consumption component because of the difficulty of reconstructing the historical costs of the water and wastewater systems. This difficulty in estimating the historical electricity requirements stems from the fact that energy consumed by some of the drainage system pumps is not segregated from energy consumed by the water and wastewater system. While it is understood that historic energy requirements of the systems are uncertain, it is apparent from review of the S&WB's 2001 Comprehensive Annual Financial Report ("CAFR") that the historic energy requirements of the wastewater treatment plants are known. Commitments or caps based on historic usage could easily be established for these.

Although it would be more difficult and less exact, the costs associated with the other portions of the water and wastewater system could also be calculated by subtracting the amount of electricity consumed by the drainage system pumps. The energy requirements of the drainage system pumps could be estimated based on known characteristics of the pumps such as horsepower and historical pumping time. Alternatively, temporary metering devices could be installed on the drainage pumps for the purpose of measuring the pumps' energy consumption per unit of time. This information, in conjunction with historic pumping time, could then be used to estimate the annual energy requirements of these pumps. The estimated energy requirements of the drainage system pumps could then be subtracted from the overall energy requirements with the remainder being the energy requirements of the systems.

As noted above, the demand for electricity can also significantly impact electricity costs. Most electric bills have a demand component, i.e., a charge for the capacity that the electric utility must have available in order to meet a customer's peak demand. The peak demand is determined by the maximum utilization of electricity by a customer during a given period of time. Obviously, the S&WB's peak demand, and hence its electricity costs, can be

significantly increased depending on how the system is operated and maintained. Because the S&WB does not require any type of commitment related to electricity demand, these costs cannot be addressed during the evaluation and selection process.

The RFP should have required proposers to provide information relating to (i) energy consumption required by each proposer's proposed operating approach, and (ii) their plans to limit the energy requirements of the water and wastewater systems. In addition, the S&WB should have capped the pass-through of electricity costs by either (i) defining the maximum electricity consumption by reference to the S&WB's historic electricity consumption, or (ii) requiring the proposers to provide guarantees relating to electricity consumption. Preferably, the energy consumption guarantees would be expressed in terms of energy per unit of water or wastewater treated (e.g. kilowatt hours/million gallons) as this approach would take into account variations in energy consumption related to variations in flow. The RFP should also have required a commitment with respect to electricity demand costs. The information, combined with the limitations, would have enabled the S&WB to estimate the electricity cost associated with each proposal.

By not obtaining pertinent information and requiring proposers to commit to maximum electricity consumption and demand prior to selection, the RFP limits the SEC's and S&WB's ability to perform a thorough assessment of the cost implications of each proposal. This limitation could result in the selection of a proposal that does not maximize total value to the S&WB. Depending on the energy implications of a particular operating plan, the lowest priced proposal might not provide the best over-all monetary value to the S&WB.

C. Pass-through Costs

Pass-through costs are costs for which the owner retains responsibility; they are not included in the proposed Annual Service Fee. The primary reason for the owner retaining responsibility for pass-through costs is a belief that the owner can more efficiently manage the risks associated with them. In the case of electricity, bearing the risk of electricity rate fluctuations would

require the private contractor to add a risk premium to its Annual Service Fee. As a result, most utility privatization transactions include electricity costs as a pass-through.

Schedule 13 of the Service Agreement lists the following costs as pass-through costs:

1. Electricity costs up to the Maximum Utility Utilization,
2. Insurance premium costs for insurance coverage set forth in Section 13,
3. Pass-through taxes,
4. Direct incremental cost increases associated with the transportation and disposal of water and wastewater residuals, and
5. Activated carbon costs up to a maximum of \$20,000 per year (escalated).

The pass-through cost provisions of the Service Agreement contain several flaws.

1. Electricity Cost Pass-through

The current electricity pass-through provisions might reduce the economic benefits that the S&WB ultimately realizes as a result of this procurement. As discussed on page 15, the current provisions are deficient in two respects. First, because the Maximum Utility Utilization is determined by reference to electricity utilization during the first year of private operation (as opposed to historic utilization), any increases in electricity consumption attributable to changes in operation and maintenance practices during the first year of private operation will be passed through. Second the pass-through provisions do not take into consideration the demand component of electricity costs.

As described earlier, the S&WB could either (i) require that proposers provide guarantees relating to electricity consumption, or (ii) define the maximum electricity consumption allowed at these facilities. Either of these approaches would help to ensure that the S&WB's electricity costs are not

increased as a result of the contractor's method of operating or maintaining the S&WB's facilities. Including in the Service Agreement provisions that promote responsible energy demand management practices could potentially reduce the S&WB's total electricity costs related to this project.

In the absence of these suggested modifications to the Service Agreement, the Maximum Utility Utilization that is eventually determined should be expressed in terms of the amount of electricity required per unit of water or wastewater treated. While this modification will not impact the selection process, it will help to ensure that the S&WB does not pay excessive electricity costs during periods of low flow.

2. Residuals Transportation and Disposal

As noted above, the current pass-through provisions give the S&WB responsibility for cost increases associated with the transportation and disposal of water and wastewater residuals. However, since the RFP does not require the proposers to disclose the portion of their Annual Service Fees related to residuals transport and disposal, they do not provide a basis for estimating the cost.

The contractor's original residuals transportation and disposal costs may not be easily ascertained and are subject to manipulation. Conceivably, a contractor could negotiate an artificially low price for residuals transportation and disposal during the first year. If subsequent residuals transportation and disposal contracts were not based on the same artificially low price, the S&WB would be responsible for the difference.

The pass-through for residuals costs may be an attempt to reduce the risk to the contractor associated with changes in law relating to residuals transport and disposal. If this is the case, it may be more appropriate to address this issue within the Service Agreement's existing uncontrollable circumstances provisions.

3. Insurance Costs

The inclusion of insurance premium costs as a pass-through cost on Schedule 13 conflicts with Section 13.01(a), which states that the contractor "shall secure or cause to be secured, and maintain through the term of this Agreement, at its sole cost and expense, including premium payments the

following insurance coverages...” As a result of this apparent contradiction, it is unclear whether the cost of maintaining the required insurance coverage is a pass-through cost or not.

Regardless of the contradictory statements relating to the responsibility for insurance costs, insurance costs should not be considered a pass-through cost. The company has as much, if not more, control over the costs of its insurance coverage as does the S&WB. In fact, negligent actions on the part of the company can actually cause their insurance premiums to increase. If mitigation of insurance rate risk on the part of the contractor is the primary driver behind including insurance as a pass-through cost, this risk could be more effectively mitigated by adjusting the insurance cost component of the Annual Service Fee using a separate index based on actual fluctuations in insurance rates.

D. Adjustments for Changes in Flow and Loadings

1. Motivational Conflicts

The Service Agreement provides for adjustment of the Annual Service Fee upward or downward to reflect changes in costs resulting from:

1. the requirement to produce drinking water in amounts above or below the Drinking Water Base Demand Range,
2. the requirement to treat wastewater volumes above or below the Wastewater Base Demand Range, and
3. the requirement to treat wastewater with strength characteristics above or below the Wastewater Loading Range.

Fee adjustments to recognize cost changes related to increases or decreases in the amount of water that private operators are required to produce and/or the amount and strength of wastewater that they are required to treat are common in water and wastewater operating contracts. These types of adjustments help to ensure that the contractor is being adequately compensated for services performed and that the owner is not paying for services that the contractor is not required to perform. However, in most of

these contracts the contract operator does not have responsibility for the operation, maintenance, repair, and replacement of the water transmission/distribution system or the wastewater collection system.

Where the contractor has the responsibility for maintaining the physical integrity of the transmission/distribution and collection network, fee adjustments of this type may provide a disincentive for the contractor to meet the owner's networks maintenance objectives. Under the S&WB's adjustment formula, if the contractor reduces physical water loss such that water production is reduced by more than 5%, the Annual Service Fee would be reduced by the proposed flow adjustment.

The same is true with wastewater. If the contractor reduces infiltration and inflow of water into the wastewater collection system such that flows to the wastewater treatment plants are reduced by more than 5%, its Annual Service Fee would be reduced by the proposed wastewater flow adjustment.

The Consent Decree among the S&WB, the Environmental Protection Agency, and the City of New Orleans has specific requirements that will help ensure proper maintenance, repair and replacement of the wastewater collection system. However, unless the Service Agreement includes physical water loss reduction guarantees or provides the contractor with economic incentives for reductions in physical water loss, the contractor's decisions related to these issues could be driven more by its economic self-interest than by what is in the best interest of the S&WB and its customers.

2. Basis for Adjustment

The provisions for flow adjustments provide for an adjustment by a fixed amount for each 5% increment that actual flows are above or below a defined threshold. It could be argued that it would be more appropriate for the adjustments to be based on a per-unit-of-flow basis. This would result in adjustments being made for each million gallons per day that the annual average daily flows are above or below the thresholds. The same approach should be used for wastewater loading adjustments.

Based on these issues related to the flow and loadings adjustments, the S&WB may wish to reconsider whether the Service Agreement should include the provisions for water flow adjustments. Considering the fact that

the water and wastewater systems are relatively mature and the demand for water treatment is not anticipated to increase dramatically during the term of the contract, it may be appropriate to eliminate the flow adjustment for water and revise the Drinking Water Base Demand Range so that flows resulting from anticipated increases in demand fall within the revised range. Depending on how much the new range differs from the original range, it may be necessary to allow the proposers to revise their proposed Annual Service Fee in reaction to this change in the Service Agreement provisions.

3. Improperly Set Thresholds

It should also be noted that water flows for the past two years were approximately 140 and 125 MGD, both of which are below the lower threshold (142 MGD) of the Drinking Water Base Demand Range. In addition, in year 2000 both wastewater nutrient loading measures were in excess of the upper wastewater loadings ranges. In 2001, one of the wastewater nutrient loading measures was very close to, but within, the lower threshold. It has been Raftelis' experience that flow and loadings ranges related to flow and loading adjustments are typically based on current flows and loadings, with current flows and loadings being close to the mean of the upper and lower thresholds.

III. Additional Contract Provisions

A. Termination for Convenience

The Service Agreement provides that, if the S&WB terminates the contract for convenience, the S&WB will pay liquidated damages according to a schedule with amounts of up to \$30 million. This payment is in addition to reimbursement for unamortized capital investments and demobilization costs.

The amount payable as liquidated damages seems to be inordinately high. In transactions of this type, the convenience for termination payment is set at an amount that is high enough to prevent the owner from arbitrarily terminating the contract, but not so high as to prevent the owner from realistically being able to exercise its right to terminate for convenience. Since the amount that the S&WB would be required to pay if it terminated

the contract for convenience in years two through four equals one-third of the 2002 budget for water and wastewater and exceeds the value of the S&WB's current assets, it is unclear how the S&WB could realistically exercise its right to terminate for convenience in those years.

In addition, it is unclear why the payment to be made upon termination for convenience increases during each of the initial three contract years. Typically, the termination payment decreases on an annual basis from the amount set for the first year in which termination for convenience is an option.

B. Termination for Uncontrollable Circumstances

The Service Agreement's provision for Termination for Uncontrollable Circumstances is somewhat unclear, but it seems to place an inordinate amount of financial risk associated with Uncontrollable Circumstances on the S&WB. Under the current provision, if the contractor is unable to perform as a result of an Uncontrollable Circumstance (including hurricanes and rainfalls of specified severities), the S&WB and the contractor are supposed to meet to agree on a course of action that will restore the contractor's ability to perform. If they cannot reach agreement, the S&WB has no option but to terminate the contract. As a result, the S&WB would not only be responsible for any capital costs associated with addressing the Uncontrollable Circumstance, but would also be required to pay the contractor for demobilization costs, unamortized capital investments, and a termination payment that could be as high as \$30 million.

In most long-term operating contracts, upon termination for Uncontrollable Circumstances the owner is only required to compensate the contractor for any investment for which it has not already received compensation and for the costs associated with demobilization. No other termination payment is usually required.

C. Approval of Professional Service Subcontracts

One of the major drivers of the economic benefit that can result from privatization is the increased efficiency and cost effectiveness that result from the contractor's ability to sub-contract with the firms that offer the greatest value. In order to realize this efficiency, the contractor must be given the freedom to select sub-contractors without being unduly influenced or restricted by the owner.

The Service Agreement restricts this freedom by giving the S&WB the right to approve professional services contracts valued at more than \$150,000 or with businesses that do not have a principal place of business in New Orleans. The provision reduces the efficiency of the contractor by forcing it to become involved in the bureaucracy associated with an approval process.

The S&WB recently adopted a resolution to ask the winning proposer to agree to the elimination of the contract approval provision. While this is a positive step, the issue will remain on BGR's list of contract flaws until the revision has been made.

D. Legal Clouds

The S&WB's procurement raises significant issues under Louisiana's public bid law. For example, a provision in the Service Agreement requiring the contractor to make repairs and replacements, other than repairs and replacements exceeding \$25,000, appears to conflict with a law requiring that repair and construction contracts costing more than \$10,000 be awarded by the S&WB to the lowest bidder.

The Civil Service Commission ("CSC") claims considerable power over privatizing or restructuring the S&WB. Although the CSC rules provide that no proposal to privatize shall be binding or effective until approved by the CSC, the S&WB's procurement makes no mention of such authority or approval. It merely contains a condition precedent that the CSC shall have approved the compensation and benefit package for transferred employees. The CSC filed a suit asserting its approval authority.

Another suit was filed challenging the authority of the S&WB to privatize the water and wastewater systems. The suit was settled before the court decided the issue.

The S&WB has invested millions of dollars in a procurement that raises significant issues under Louisiana law, while steadfastly refusing to have it reviewed by independent legal counsel for compliance with the public bid, civil service, and other state laws.

IV. Weaknesses in the Selection Process Established by the S&WB

An effective evaluation and selection process must allow for a thorough and objective evaluation of the total value offered by each proposal. Total value includes two components: monetary value, referred to as Cost Effectiveness in the RFP, and customer value (i.e., the quality of the services offered by a proposer).

In order to perform a thorough and objective evaluation, the evaluators must be provided with adequate information, sufficient time, and an appropriate level of direction. To the extent that a selection process does not provide these, it will be compromised and may not lead to the selection of the best overall proposal.

Unfortunately, certain aspects of the evaluation and selection process defined in the RFP could potentially compromise the final selection. Several of these relate specifically to the determination of the cost effectiveness of the proposals. Others impact the evaluation of cost effectiveness and/or customer value. This section summarizes the more significant shortcomings in the process as defined in the RFP.

A. Inadequate Guidance for Evaluating Cost Effectiveness

The RFP provides the SEC with very little direction with respect to evaluating total costs. Although it states that “[t]otal cost to manage, operate and maintain the System will be considered”, it neither describes how total

cost will be determined nor indicates how much weight total cost will be given. This lack of definition with respect to total cost allows for a great deal of subjectivity and is particularly troubling because total cost is the criterion that best lends itself to complete objectivity.

The evaluation of the total cost associated with a long-term operating contract can be a very complicated process. A proper evaluation involves economic projections and financial modeling to develop an understanding of the long-term financial implications of each proposal.

Although the RFP failed to request adequate information relating to the proposed Annual Service Fee, it did require a significant amount of information relating to total cost. Cost information required of the private firms included:

1. Proposed annual service fees associated with managing, operating, and maintaining each major component of the systems (water, wastewater, billing, collection, and customer service) for three different contract terms and two different employee retention commitments for each of the three contract terms;
2. Cost information concerning certain portions of the Annual Service Fee that relate to the differing requirements of the Service Agreement and the MOU; and
3. Proposed increases or decreases in each of the proposed Annual Service Fees to reflect changes in costs associated with major fluctuations in water and wastewater flows and wastewater strength.

The MCEC was required to provide similar cost information; however, it was only required to provide proposed Annual Service Fees for three different contract terms.

The private companies provided 108 cost related values. Although each of these values could impact the total cost of that proposal, the RFP did not provide the SEC with any direction as to how to factor each of these values into the determination of total cost. It is difficult to imagine how a volunteer committee could determine the method for analyzing all the information and perform the analysis within the nine-day evaluation period provided in the RFP.

Typically, RFPs for procurements of this type provide a description of the method for analyzing and evaluating the proposers' cost information, as well as the method for comparing one proposer's cost information with that of the others. This type of description was not included in the RFP.

In procurements where this type of description is not provided in the RFP, the procurement advisors typically either (i) perform a detailed analysis of the cost information and provide the results of their analysis to the evaluators, or (ii) provide direction to the evaluators as to how the analysis and evaluation should be performed. The analysis typically consists of a calculation of the NPV of costs associated with each proposal. The NPV of costs for each proposal is calculated by first projecting the annual costs resulting from each proposal over a period equal to the term of the contract. These cost projections are based on a set of economic assumptions that are the same for each proposal. Once the annual costs have been projected, they are discounted back to the present using a discount factor based on the owner's weighted average cost of capital. The resulting NPV of costs for each proposal provides a relatively simple and objective point for comparison of the long-term cost implications of proposals.

Based on a review of the documentation provided to the SEC by the S&WB's financial advisors, the financial advisors neither performed and provided to the SEC an analysis of the cost information nor provided the SEC with any direction regarding the analysis and evaluation of the cost information.

B. Inadequate Information

1. Line Item Budget

The RFP should have required the proposers to provide additional detail relating to their proposed Annual Service Fees. In many procurements, this additional detail takes the form of a line item budget that shows the specific costs associated with specific components of the Annual Service Fee (salary and benefits, maintenance, chemicals, laboratory services, residuals disposal, repair and replacement, etc.).

While these cost details are typically not binding, they provide the evaluators with an opportunity to assess the reasonableness of the proposed Annual Service Fees and to determine whether the proposers fully comprehend the

costs associated with each component of the scope of services. For instance, detailed cost information with respect to maintenance and capital repairs can provide useful insights into each proposer's approach to ensuring the long-term performance of a system's assets.

2. Break-out of Certain Costs

To facilitate an equitable comparison of the private firms' proposals with the MCEC proposal, the RFP required that the private firms provide information regarding certain portions of their Annual Service Fee that relate to requirements that apply only to private firms. The RFP failed, however, to require the private firms to indicate the portion of their Annual Service Fee that is related to the provision of a \$10 million letter of credit, which the MCEC is not required to provide. By requiring the private firms to provide this information on letter of credit costs, the S&WB could have developed a better understanding of the cost implications of this extra level of security. Requiring letter of credit cost information would have also allowed for a more equitable comparison of the private proposals with the MCEC proposal.

C. Evaluation Schedule

The schedule set forth in the RFP allowed only nine business days for the SEC to perform its evaluation of proposals. Given that the evaluation of proposals for a project of this magnitude is an incredibly complex process, this is an insufficient amount of time for the SEC to perform a complete evaluation of the proposals. Raftelis' experience indicates that the SEC should have been allowed at least three weeks to perform its evaluation of the proposals.

Although the time period was in fact extended, the schedule indicated a lack of understanding of the process and conveyed the message that a thorough review was not expected. In addition, SEC members were not provided adequate time to perform important tasks within the review period. For example, SEC members were not given time to review the copy of the SEC's draft report that was prepared on their behalf by the S&WB's financial advisors. Although the S&WB's financial advisors had more than five weeks

to prepare the draft report, it was not distributed to the committee members until the start of their meeting to review and approve it. This impeded thoughtful consideration of the contents.

Invariably, proposals for a project with a scope of services as complex as that requested by the S&WB will require clarification. The schedule in the RFP did not allow sufficient time for the clarification process to occur.

D. Ambiguities

1. Ambiguous Criterion

Certain aspects of the Disadvantaged Business Enterprise (“DBE”) criterion are unclear. Specifically, the sub-criterion addressing management opportunities was neither adequately defined in the RFP nor was it discussed in the Service Agreement or the MOU. The responses of the proposers suggest that they had difficulty interpreting the meaning of this sub-criterion.

Discussions during the proposer’s presentations to the SEC indicated that there was also some uncertainty relative to the S&WB’s DBE requirements. The RFP refers to the minimum requirements for DBE participation as outlined in Section SC16.4 of Schedule 16 of the Service Agreement. Some clarification is needed however, as to how these percentages are to be applied.

There are four possible interpretations of the minimum requirements outlined in the RFP:

1. The participation percentages simply relate to the total cost of each type of contract;
2. The minimum requirements must be met for each separate contract;
3. A weighted average of DBE participation for all contracts can be used to meet the minimum requirements; or
4. An average of DBE participation for all contracts can be used to meet the minimum requirements.

The S&WB should clarify the DBE requirements and require the proposers to submit additional information in response to the S&WB's clarification.

2. Clarification Process

The RFP does not specifically address the proposal clarification process. It should have defined the mechanism for seeking clarification and provided specific dates for making and responding to clarification requests. Absent a clarification process, the evaluation must be performed without complete information. This can decrease the objectivity of the evaluations by forcing the SEC and the S&WB to make assumptions relative to aspects of the proposals that may not be completely clear.

E. Evaluation Process: Definition and Direction

In order to perform a thorough and objective evaluation of the proposals, the parties responsible for performing the evaluation must have a clear understanding of the evaluation process and the objectives of the process. This understanding can either be derived from the definition of the evaluation process in the RFP or provided by advisors with special expertise in the field of water and wastewater contract operations.

It is not uncommon for the evaluation process defined in an RFP to allow some flexibility with respect to the way in which the proposals are evaluated. This flexibility allows the evaluators to respond to the information provided in the proposals. However, flexibility should be limited in situations where stakeholders have the perception that the evaluation process is being influenced by agendas other than the selection of the proposal offering the greatest total value. Because the S&WB's procurement falls into this category, the RFP should have provided a more detailed definition of the evaluation process.

The lack of definition with respect to the evaluation of cost effectiveness was discussed above. There are other areas that would have profited from greater definition.

1. Allocation of Scoring Points to Sub-criteria

The RFP should have allocated maximum points to the sub-criteria within each of the primary criteria used to assess customer value. A more detailed allocation of scoring points would have given the SEC a better understanding of the S&WB's priorities and would have helped to eliminate subjectivity in the assignment of scores for each primary criterion.

2. Committee Autonomy

Evaluation committees are established to provide the utility owner with an independent, third-party evaluation of proposals. In order to encourage independence, the committee should function autonomously.

The SEC's meetings were conducted by the mayor's executive counsel, operating as a representative of the S&WB, rather than by a committee member selected by the other members. The lack of an independent chair may have compromised the SEC's ability to operate autonomously. It is a matter that should be remedied if the SEC is reconvened or if a new evaluation committee is established.

3. Procedures for Conducting Meetings and Coordinating Evaluation Efforts

Neither the S&WB nor the SEC established procedures for convening and conducting meetings. In addition, the RFP failed to address the way in which the members of the SEC would coordinate their evaluation efforts. This issue is particularly important in the current S&WB procurement. Since the SEC is comprised of people from a variety of different backgrounds, many of whom have no direct relation to the water and wastewater industry, it is likely that each member of the SEC approached the evaluation of proposals in a slightly different way. For example, a member of the SEC with a civil engineering background might have placed much greater emphasis on the technical aspects of the proposal, while an SEC member who is a former S&WB employee might have considered aspects of the proposals that relate to the Affected Employees to be of primary importance.

While it is not inappropriate for each member of the SEC to focus his evaluation efforts on components of the proposals that fall within his area of expertise, it is critical that a mechanism for consolidating the input from each member be defined prior to the evaluation process. Establishing protocols in this area helps to ensure that all components of each proposal are given the appropriate consideration in the final evaluation.

In other procurements, the parties responsible for the evaluation of proposals have assigned responsibility for the evaluation of specific criteria to members of the evaluation committee with expertise relevant to the specific criteria. After these members have completed their evaluations under the assigned criteria, they have presented the results to the rest of the committee for discussion. Based on this discussion, the committee as a whole has reached agreement on the score it assigned to each proposal with respect to each criterion.

In the absence of a more detailed definition of the evaluation process in the RFP, the SEC should have, and the S&WB should, develop evaluation protocols that specify the method for coordinating their evaluation efforts.

4. Expert Evaluations

Because the proposals submitted for a transaction of this magnitude are extremely complicated and deal with complex technical, financial, and legal issues, many utility owners rely on their procurement advisors to perform expert evaluations of proposals. An expert evaluation usually includes detailed analysis of the strengths and weakness of the technical approach and of the long-term financial implications of each proposal. The resulting information is compiled into a report that the evaluators can use as the basis for their evaluation or as a source of information. It is our understanding that the only information provided to the SEC by the financial advisors with respect to the proposals is a brief summary describing in general terms the contents of each proposal.

F. Independent Assessments of Monetary and Customer Value

As discussed previously, the total value offered to the S&WB by the proposers is comprised of two separate components, monetary value and customer value. In order for the procurement to be a success, the evaluation process must allow for the objective evaluation of each of these components of total value.

Objectivity can be lost if each component of total value is not assessed independently. This is particularly the case in procurements where economic benefit is the primary driver of the decision to pursue privatization. If the evaluators develop an opinion of the monetary value offered by a proposal prior to their assessment of the proposal's customer value, this opinion could prejudice their evaluation of the customer value offered by the proposal.

Many procurements require that the evaluators assess customer value prior to viewing the cost information provided by each proposer. However, because the cost information submitted by the proposers is available to the public under the Louisiana public records law and has been reported in the press, it was not feasible to withhold this information from the SEC and S&WB until after they had reviewed the technical volume. Although it was not possible as a practical matter to withhold the cost information, the S&WB should have designed protocols that separated the consideration of the monetary and customer value to the extent possible. The independence of the two factors should have been stressed to the SEC.

G. Weaknesses in the SEC's Report

Raftelis identified several aspects of the SEC's report that lead it to question whether the SEC's evaluation was indeed thorough and objective.

1. Scoring

The SEC did not utilize the scoring system defined in the RFP. One purpose of a scoring system is to allow an objective assessment of the benefits offered by each proposal with respect to each individual evaluation criterion.

Another is to provide some assurance that the evaluators are evaluating the proposals with the priorities of the S&WB in mind. Neither of these objectives has been satisfied.

2. Cost Evaluation

As discussed above, cost evaluation is an extremely complex process with respect to which the SEC did not receive adequate guidance. As a result of the lack of guidance, the SEC did not attempt to determine the long-term cost implications of each proposal, nor did it attempt to evaluate the financial implications of the flow and loadings adjustments that proposers were required to provide. In performing the cost evaluation, the SEC simply compared the proposers' Annual Service Fees.

The SEC's report also failed to make price adjustments that would have allowed the SEC to compare more equitably the costs of the MCEC against those of the private companies. Because the latter were asked to assume additional costs and provide a higher level of performance guarantees, certain of those costs should have been backed out.

3. Generality

The SEC's report is of a very general nature. It simply provides a summary of each evaluation criterion and then a brief subjective statement regarding the way in which each proposal addressed the criterion. The report provides neither details with respect to each proposal nor a clear indication of why one proposal should be considered to be more favorable than the others.

Presumably, the SEC evaluation and report is intended to serve as the basis for the S&WB's scoring and selection of the most advantageous proposal. Unfortunately, as a result of its generality, the SEC report does not provide the S&WB with sufficient information to make an objective selection.

4. Reliance on Pledges

The SEC's report places a great deal of emphasis on proposers' "pledges" to exceed the requirements of the Service Agreement. Unless the proposers have committed to incorporating the pledges into the Service Agreement, they should be given little weight during the evaluation process.

Recommendations

To Maximize Financial Benefits

1. The S&WB should prepare a credible economic baseline that includes an analysis of the direct and indirect costs incurred to manage, operate, and maintain the water and wastewater systems.
2. The RFP should be amended to factor future electricity costs into the evaluation of the cost of the proposals. The amendment should require proposers to provide the information needed to analyze the impact of their operating plans on electricity costs.
3. The S&WB should amend the pass-through provisions by:
 - establishing the electricity pass-through caps and the residuals disposal baseline cost before the contract is executed,
 - capping energy consumption in terms of energy per unit of water and wastewater treated (e.g., kilowatt hours/million gallons), and
 - eliminating the pass-through of insurance.
4. The S&WB should amend the Service Agreement to eliminate the provisions for water flow adjustments. Wastewater Base Demand Range and the Wastewater Loadings Range for adjustments should be changed to reduce the probability that those adjustments will be required.
5. The S&WB should obtain more detailed information on the components of the Annual Service Fee, including the base cost for residuals disposal and the cost of letters of credit.

To Improve the Contract

1. In accordance with its resolution dated April 24, 2002, the S&WB should take all necessary action to eliminate from the Service Agreement the requirement for board approval of certain professional service contracts.
2. The S&WB should reduce the penalty schedule for Termination for

Convenience to amounts that would discourage termination without making it impossible.

3. The S&WB should amend the Service Agreement to eliminate the penalty for Termination for Uncontrollable Circumstances.

4. The S&WB should hire independent legal counsel to review the contract for compliance with the public bid, civil service, and other applicable laws.

To Provide an Objective Evaluation

The S&WB should take the following steps to ensure an independent, thorough evaluation of the proposals:

1. The S&WB should reconvene the SEC or appoint a new evaluation committee to prepare a thorough, independent evaluation of the proposals.

2. In order to enable the evaluation committee to conduct such a review, the S&WB should provide it with a detailed, professional analysis of the proposals that, at a minimum:
 - analyzes the cost effectiveness of the proposals based on net present value,
 - takes into account the differences in the scope of the obligations imposed on the private companies and the MCEC, and
 - discusses in detail the strengths and weaknesses of the proposals under the criteria established by the S&WB.

3. In order to enable the evaluation committee to conduct a thorough and objective review, the S&WB should provide it with an evaluation guide that:
 - clarifies the existing evaluation criteria and sub-criteria, particularly those relating to Disadvantaged Business Enterprises,

- allocates scoring points to the sub-criteria set forth in the RFP,
 - establishes a process for obtaining clarification of proposals,
 - establishes procedures for calling and conducting meetings,
 - provides for, and emphasizes the importance of, an independent consideration of the monetary and customer values, and
 - provides protocols for documenting, collecting, and consolidating the evaluations of the individual members of the evaluation committee.
4. To encourage independence, the evaluation committee should select one of its own members to act as chairperson.
 5. The evaluation committee should prepare an evaluation in accordance with the requirements of the RFP and the evaluation guide. As part of that process, the evaluation committee should:
 - request clarification of ambiguities in the proposals, and
 - assign scores to the proposals based on the weights specified in the RFP and the evaluation guide.
 6. The S&WB should allow the evaluation committee adequate time to conduct a thorough evaluation.
 7. After the evaluation committee conducts its evaluation on the basis set forth above, the S&WB should either (i) accept the evaluation committee's recommendation, or (ii) conduct its own evaluation on the basis set forth above and provide detailed explanations of variations from the evaluation committee's scoring.

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